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[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 14, 1994

RECENT DEVELOPMENTS

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

DOMESTIC NONFINANCIAL DEVELOPMENTS

The economy shows every sign of continued brisk growth. Payroll employment surged in November and manufacturing output posted another substantial gain. Consumer spending has remained robust, and consumer sentiment moved up to the highest levels since before the last recession. Business investment in both equipment and nonresidential structures appears to be rising at a rapid clip. Despite substantial ongoing inventory accumulation, firms do not thus far appear to be overstocked.

Although prices of industrial materials and intermediate supplies have continued to post large increases, recent increases in the "core" CPI have been quite moderate. In addition, tighter labor markets have yet to generate a substantial firming of wages.

Labor Market Developments

Nonfarm payroll employment jumped 350,000 in November, following a gain of 164,000 in October. Although the average workweek of private production or nonsupervisory workers fell back in November from a high October level, total hours look to be headed toward a growth rate of around 4-1/2 percent (annual rate) in the fourth quarter. In the household survey, the unemployment rate fell another 0.2 percentage point in November, to 5.6 percent.[1] Since January, the jobless rate has fallen 1.1 percentage points, the largest ten-month drop since 1984.

Private payrolls expanded 324,000 in November, with more than one-third of the increase in the goods-producing sector. Manufacturing recorded another sizable advance, showing widespread production gains throughout both durable and nondurable goods

1. The Bureau of Labor Statistics recently reported that its research suggests that the introduction of the new Current Population Survey and new weights based on the 1990 Census raised the unemployment rate 0.2 percentage point beginning in January 1994.

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

	1992	1993	1994 Q1	1994 Q2	1994 Q3	1994 Sept.	1994 Oct.	1994 Nov.
	-----------Average monthly changes---------							
Nonfarm payroll employment[2]	96	194	229	345	284	272	164	350
Private	76	179	222	320	240	208	180	324
Manufacturing	-14	-11	13	21	17	1	42	51
Durable	-14	-7	12	21	18	16	30	40
Nondurable	0	-4	0	0	0	-15	12	11
Construction	-1	19	23	40	15	30	4	71
Trade	10	42	44	96	79	81	49	34
Finance, insurance, real estate	4	10	4	6	-1	-7	-11	8
Services	78	116	133	146	124	102	100	147
Health services	22	23	23	22	20	8	26	11
Business services	31	46	61	57	59	55	35	93
Total government	20	15	8	26	44	64	-16	26
Private nonfarm production workers	86	164	211	300	199	186	152	228
Manufacturing production workers	-3	-1	22	24	19	7	39	34
Total employment[3]	127	209	459	131	399	462	608	372
Nonagricultural	120	219	349	195	341	497	522	307
Memo:								
Aggregate hours of private production workers (percent change)	.1	.3	.4	.4	.2	.6	1.1	-.5
Average workweek (hours)	34.4	34.5	34.6	34.7	34.5	34.6	34.9	34.6
Manufacturing (hours)	41.1	41.5	41.7	42.1	42.0	42.0	42.1	42.1

1. Average change from final month of preceding period to final month of period indicated.
2. Survey of establishments.
3. Survey of households. Data for 1994 are not directly comparable with earlier years because of a redesign of the CPS in January 1994.

SELECTED UNEMPLOYMENT AND LABOR FORCE PARTICIPATION RATES[1]
(Percent; based on seasonally adjusted data)

	1992	1993	1994 Q1	1994 Q2	1994 Q3	1994 Sept.	1994 Oct.	1994 Nov.
Civilian unemployment rate (16 years and older)	7.4	6.8	6.6	6.2	6.0	5.9	5.8	5.6
Teenagers	20.0	19.0	18.0	18.4	17.4	17.0	17.3	15.3
20-24 years old	11.3	10.5	10.6	9.6	9.8	9.5	8.9	9.1
Men, 25 years and older	6.4	5.8	5.3	4.8	4.8	4.6	4.6	4.4
Women, 25 years and older	5.7	5.4	5.3	5.0	4.8	4.8	4.6	4.6
Full-time workers	7.4	6.8	6.7	6.2	6.0	5.9	5.9	5.6
Labor force participation rate	66.3	66.2	66.6	66.5	66.5	66.6	66.8	66.8
Teenagers	51.3	51.5	52.7	53.6	52.2	51.1	52.6	51.7
20-24 years old	77.1	77.1	77.0	77.0	76.7	76.9	77.4	77.1
Men, 25 years and older	76.6	76.2	76.3	75.8	75.8	75.9	76.2	76.3
Women, 25 years and older	57.0	57.1	58.0	57.9	58.2	58.6	58.4	58.5

1. Data for 1994 are not directly comparable with earlier years because of a redesign of the CPS in January 1994.

industries. In construction, employment was up 71,000 in November, reflecting increases in all three major components.[2] According to the BLS, some of the employment growth in construction likely reflected a bounceback from a level that had been depressed by heavy rains in the Southeast during the survey week in October. In addition, the November survey week came relatively early in the month, so the estimates for November may incorporate fewer seasonal construction layoffs than usual.

The private service-producing sector added 204,000 jobs in November, following an increase of 137,000 in October. Gains last month were uneven. Hiring in retail trade was sluggish, perhaps because the early survey week missed some temporary Christmas-season workers who normally are picked up in the November survey. At service establishments, net hiring increased a bit in November; rapid growth in personnel supply resumed in November after a pause in October. Elsewhere, renewed hiring in trucking and warehousing boosted transportation payrolls by 18,000 in November.

Employment as measured by the household survey rose 372,000 in November, and the unemployment rate fell to 5.6 percent. Jobless rates declined for men and for teenage women. In addition, the number of long-term unemployed dropped noticeably. On net, the labor force rose 100,000, and the participation rate was unchanged at 66.8 percent.

Other indicators are also consistent with robust labor market activity. The Conference Board's help-wanted index jumped 11 points in October to its highest level since July 1990,[3] and weekly initial claims for unemployment insurance have remained in the

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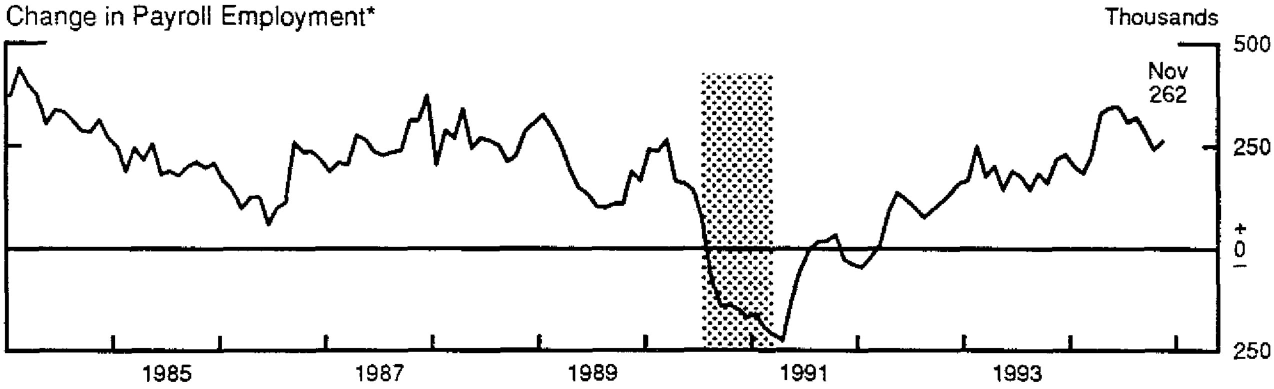
2. General building contractors, heavy construction, and special trades.

3. Adjusted for the increased use of temporary help, the help-wanted reading approached the high levels that prevailed in 1988 and 1989.

Labor Market Indicators

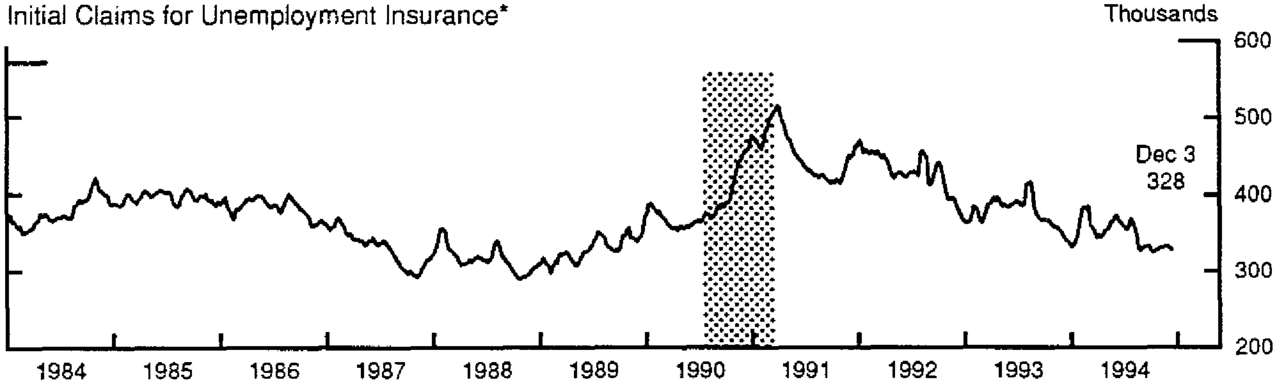
(Seasonally adjusted data)

Change in Payroll Employment*



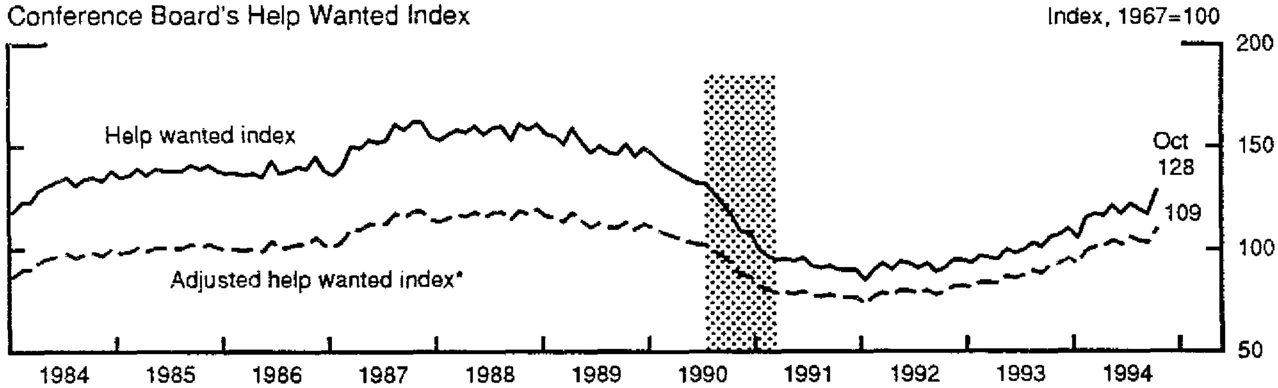
* Three-month moving average.

Initial Claims for Unemployment Insurance*



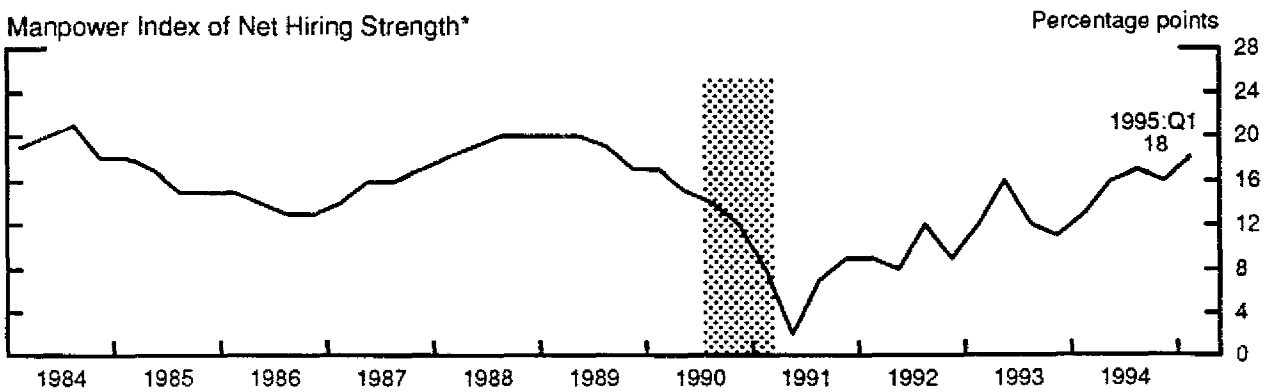
* Four-week moving average of initial claims including EUC adjustment.

Conference Board's Help Wanted Index



* Help wanted index adjusted for personnel supply services employment.

Manpower Index of Net Hiring Strength*



* Percent planning an increase in employment minus percent planning a reduction.

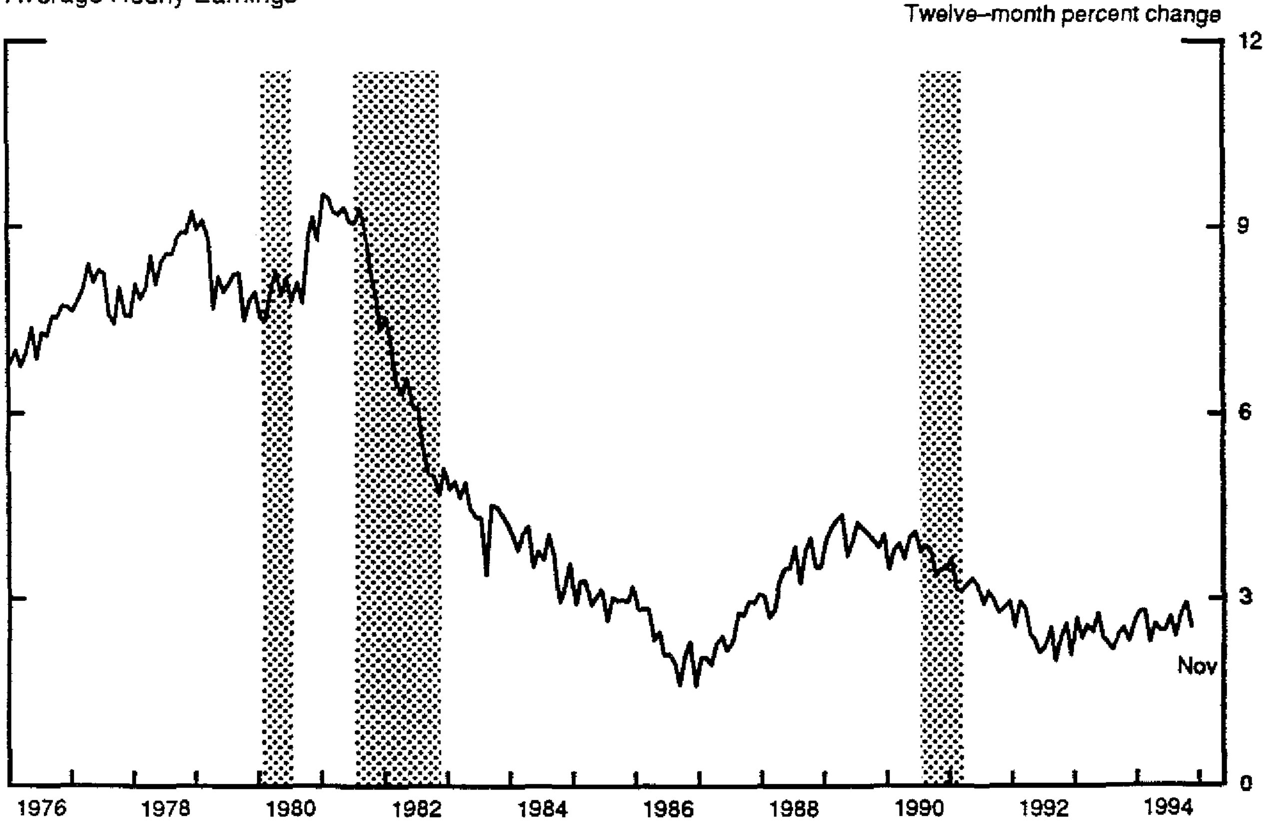
Wage Rates of Production or Nonsupervisory Workers

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

			1994			1994		
	1992	1993	Q1	Q2	Q3	Sept.	Oct.	Nov.
			-Annual rate-			-Monthly rate-		
Total private nonfarm	2.1	2.6	2.2	2.2	3.3	.4	.6	-.2
Manufacturing	2.2	3.2	2.4	1.0	3.0	.3	.2	.2
Durable	2.1	3.4	2.6	.0	3.5	.4	.1	.3
Nondurable	2.4	2.5	2.9	1.4	2.5	.4	.4	.0
Contract construction	1.2	1.2	1.7	5.6	4.2	.7	.5	-.6
Transportation and public utilities	1.6	1.3	1.8	-.3	3.2	.1	1.1	.1
Finance, insurance, and real estate	3.6	5.5	2.8	1.7	5.2	.8	1.3	-.8
Total trade	2.0	2.3	2.4	2.3	2.3	.2	.8	-.3
Services	2.4	2.2	2.2	3.0	3.3	.4	.9	-.5

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

Average Hourly Earnings



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

	Proportion in total IP 1993:Q4	1994			1994		
		Q1	Q2	Q3	Sept.	Oct.	Nov.
		----Annual rate-----			----Monthly rate----		
Total index	100.0	7.1	6.0	5.0	-.1	.5	.5
Previous		7.1	6.0	5.0	.0	.6	
Major Market Groups:							
Products, total	60.7	6.7	4.9	4.0	-.2	.4	.5
Consumer goods	28.2	6.8	2.1	2.0	-.6	-.2	.6
Business equipment	14.7	10.4	8.2	11.1	.2	1.3	.7
Defense and space equipment	2.8	-10.2	-7.9	-16.1	-.6	-.3	-.1
Construction supplies	5.4	4.6	11.4	9.6	.2	.6	.8
Materials	39.3	7.9	7.7	6.6	.2	.6	.6
Major Industry Groups:							
Manufacturing	86.0	7.2	7.3	5.5	.0	.6	.8
Manufacturing excluding motor vehicles and parts	80.5	5.7	9.3	5.6	.0	.6	
Motor vehicles and parts	5.6	30.2	-17.8	4.9	-.7	.8	2.
Mining	6.4	3.7	5.7	-2.3	.2	-.4	-.6
Utilities	7.6	11.7	-6.7	4.3	-1.1	-.7	-1.6

CAPACITY UTILIZATION
(Percent of capacity; seasonally adjusted)

	1988-89	1967-93	1993	1994		1994		
	High	Avg.	Avg.	Q2	Q3	Sept.	Oct.	Nov.
Total industry	84.9	81.9	81.7	83.8	84.3	84.3	84.5	84.7
Previous				83.8	84.3	84.3	84.6	
Manufacturing	85.2	81.2	80.9	83.1	83.6	83.6	83.9	84.4
Previous				83.1	83.6	83.6	84.0	
Primary processing	89.0	82.3	84.6	87.6	88.1	88.2	88.5	8[illegible]
Advanced processing	83.5	80.7	79.4	81.3	81.8	81.9	82.1	82[illegible]

320,000 to 340,000 range, a level consistent with another sizable gain in employment in December. Moreover, the Manpower Inc. index of net hiring plans for the next quarter rose to its highest level since 1989, with notable strength evident in construction, manufacturing, and trade.

Despite increasing anecdotal reports of labor shortages, recent aggregate measures of wage growth have remained in the moderate range that has prevailed for some time. Average hourly earnings of production or nonsupervisory workers fell 0.2 percent in November, partly offsetting the October gain of 0.6 percent. This measure of wage growth has picked up somewhat in a few sectors, notably construction and services. For the economy as a whole, hourly earnings rose 2.6 percent over the past twelve months--1/4 percentage point faster than the pace over the twelve months ending in November 1993.

Industrial Production

Led by continued increases in manufacturing output, the industrial production index rose 0.5 percent in November, following a revised gain of 0.5 percent in October. With output growth running faster than the pace of capacity expansion, the rate of industrial capacity utilization moved up 0.2 percentage point, to 84.7 percent.[4]

Motor vehicle assemblies rose to 12.3 million units at an annual rate in November, somewhat below planned output at the beginning of the month but still well above October's rate. Moreover, current schedules show a sizable increase in assemblies at

4. Utilization rates have been marked down slightly since the last Greenbook because of the annual revisions to the production, capacity, and capacity utilization indexes.

the turn of the year;[5] even assuming a typical production shortfall, the motor vehicles and parts industry should make a solid contribution to overall IP gains in coming months. The ramp-up in motor vehicle output may be motivated in part by the current low level of dealer stocks of automobiles and light trucks relative to the recent sales pace. Days' supply for automobiles and light trucks remained somewhat short of the level of sixty-five days that the industry considers "comfortable."

PRODUCTION OF DOMESTIC AUTOS AND TRUCKS
(Millions of units at an annual rate; FRB seasonal basis)[1]

	1994			1994	1995
	Oct.	Nov.	Dec.	Q4	Q1
			--------scheduled--------		
U.S. production	11.9	12.3	12.8	12.3	13.3
Autos	6.4	6.5	7.1	6.7	7.4
Trucks	5.5	5.8	5.7	5.7	5.9
Days' supply					
Autos	60.8	58.0			
Light trucks	62.6	62.5			

1. Components may not sum to totals because of rounding.

Unlike October's widespread output gains, last month's production increases were concentrated in durable goods industries, where output climbed 1.1 percent Among nondurable industries, petroleum and rubber posted large advances.

Capacity constraints do not appear to be leading to much slowing in manufacturing activity. The following table reports recent production growth rates in three manufacturing groups. The first group includes those two-digit SIC industries for which factory operating rates had, by August, exceeded their 1988-89

5. General Motors has indicated to us that Wards' schedules for production at GM may be overstated for the first quarter by about 0.3 million units. If this is correct, total schedules for the first quarter of 1995 would be 13.0 million rather than the 13.3 million that appears in the table.

cyclical peaks.[6] The second group comprises those industries for which August rates remained below their last cyclical peaks but above their 1967-93 averages.[7] The third group includes those for which August rates were below their long-term averages.[8] The first column reports the average growth rate of production over the past year; the next three report growth rates in the last three months. The table shows that those industries with high operating rates in August have continued to grow at a robust pace.

RECENT PRODUCTION GROWTH RATES

	Past 12 mos.[1]	Sept.	Oct.	Nov.
Manufacturing	.5	.0	.6	.8
Above peak capacity	.9	.4	1.0	1.4
Above average capacity	.4	-.2	.7	.5
Below average capacity	.2	-.1	.5	-.4

1. Compounded average monthly growth rate from November 1993 to November 1994.

Outside of manufacturing, activity has declined in the past couple of months. Mining production fell another 0.6 percent in November, after a 0.4 percent retreat in October. Utilities output dropped 1.6 percent in November, the fifth straight monthly decline. However, short-run movements in utilities output often follow the weather, which was unusually mild over the past few months.

Owing to the run-up in manufacturing production, the factory operating rate rose one-half point, to 84.4 percent, in November. The utilization rate was reduced about one-half percentage point in

6. The reference month of August was chosen to allow a substantial time period after the reference month over which to examine growth patterns.

The above-peak group includes petroleum, fabricated metals, machinery, electrical machinery, and motor vehicles and parts.

7. Food, textiles, lumber, furniture, paper, chemicals, rubber, leather, stone, clay and glass, primary metals, and miscellaneous manufactures.

8. Tobacco, apparel, printing, other transportation equipment, and instruments.

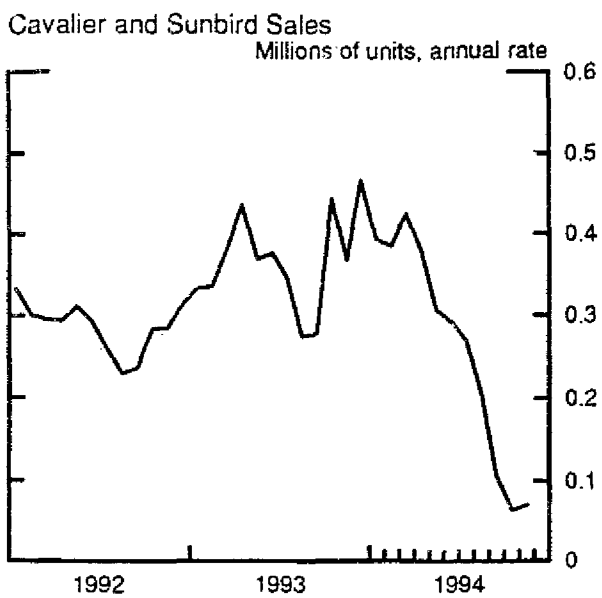
SALES OF AUTOMOBILES AND LIGHT TRUCKS[1]
(Millions of units at an annual rate; FRB seasonals)

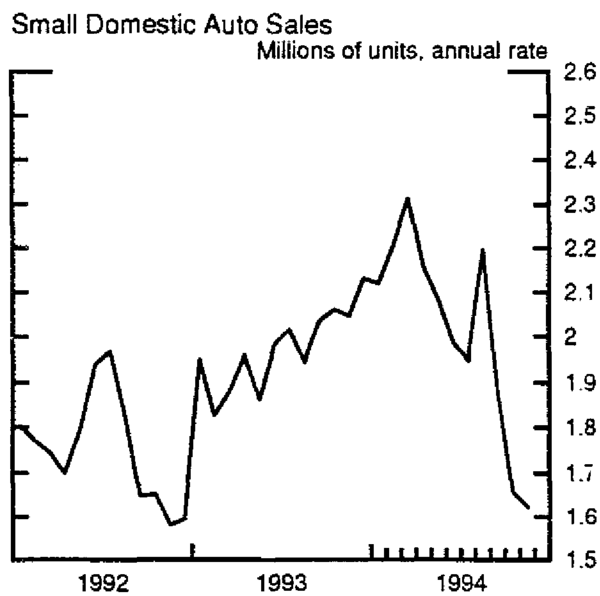
			1994			1994		
	1992	1993	Q1	Q2	Q3	Sept.	Oct.	Nov.
Total	12.9	13.9	15.0	14.8	15.1	15.4	15.4	15.2
(BEA seasonals)	12.9	13.9	15.5	14.8	14.6	14.9	15.3	15.4
Autos	8.4	8.7	9.2	9.1	9.3	9.5	9.1	9.1
Light trucks	4.5	5.2	5.8	5.7	5.8	5.9	6.2	6.1
North American[2]	10.5	11.7	12.9	12.6	12.8	13.2	13.2	13.3
Autos	6.3	6.7	7.3	7.2	7.2	7.6	7.2	7.3
Big Three	5.1	5.5	5.9	5.7	5.6	6.0	5.6	5.8
Transplants	1.2	1.3	1.4	1.5	1.6	1.6	1.6	1.6
Light trucks	4.2	5.0	5.6	5.5	5.6	5.7	6.0	5.9
Foreign produced	2.3	2.1	2.1	2.1	2.2	2.1	2.2	1.9
Autos	2.1	2.0	2.0	2.0	2.0	1.9	1.9	1.8
Light trucks	.2	.2	.1	.2	.2	.2	.2	.2
Memo: Domestic name-plate market share								
Total	.72	.74	.74	.73	.71	.73	.73	.75
Autos	.63	.65	.65	.63	.61	.64	.62	.64

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

1. Components may not add to totals because of rounding.

2. Excludes some vehicles produced in Canada that are classified as imports by the industry; before January 1994, some vehicles produced in Mexico were also excluded.





the recent revision, in large part reflecting data showing that manufacturing investment, and thus growth of the net capital stock, was stronger than previously thought. Still, the primary processing utilization rate, at 89.2 percent, is now above its peak in the late 1980s, while the advanced processing utilization rate, at 82.5 percent, is only one percentage point below its peak.

Motor Vehicles

Sales of new light vehicles in November held near the strong pace that has prevailed since August. Sales were 15.2 million units at an annual rate (FRB seasonals), as a slight gain among North American-produced vehicles mostly offset small declines in sales of imports.

Several factors that have affected recent sales in selected segments of the light vehicle market are likely to prevail through the turn of the year. Within light trucks, an ongoing year-end sales race between GM and Ford has boosted light truck sales since September. And although sales of sport-utility vehicles continue to rebound in the wake of last summer's availability problems, the pace of production since August may not have been sufficient to eliminate the pent-up demand that accumulated while these vehicles were in short supply.

For automobiles, both industry sources and the November data suggest that GM's production problems continue to hold down sales of small cars. Since last March, sales of GM's popular Cavalier and Sunbird models have plunged about 400,000 units as an extended changeover and slow ramp-up have curtailed supply. Although a substantial incentive program for Toyota's small cars in August siphoned off some of the pent-up demand for GM's small vehicles, sales of small cars have continued to decline since then. GM's auto

RETAIL SALES
(Percent change; seasonally adjusted)

	1994			1994		
	Q1	Q2	Q3	Sept.	Oct.	Nov.
Total sales	1.6	1.1	2.0	.8	1.3	1.2
Previous estimate			1.9	.5	1.1	
Retail control[1]	1.1	1.2	1.9	.6	.3	.7
Previous estimate			1.9	.5	.5	
Total excl. automotive group	.8	1.5	2.1	.6	.5	.9
Previous estimate			2.1	.5	.6	
GAF[2]	.8	1.8	2.4	.8	.9	.6
Previous estimate			2.3	.7	.8	
Durable goods stores	2.4	1.5	2.5	1.3	2.8	2.3
Previous estimate			2.2	.6	2.3	
Bldg. material and supply	-1.4	4.0	3.5	.7	1.5	2.9
Automotive dealers	4.5	-.2	1.5	1.4	4.0	2.0
Furniture and appliances	.1	4.0	4.6	2.1	1.1	2.3
Other durable goods	.2	4.4	3.1	.3	.5	2.6
Nondurable goods stores	1.1	.8	1.6	.5	.3	.4
Previous estimate			1.6	.5	.4	
Apparel	-1.0	.2	.9	-.6	2.2	.6
Food	1.0	-.1	1.2	.7	.5	.6
General merchandise[3]	1.9	1.4	1.9	.8	.3	-.1
Gasoline stations	2.4	.6	3.1	.0	-1.6	.9
Other nondurables[4]	.7	1.5	1.5	.5	.3	.5

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. Excludes mail-order nonstores; mail-order sales are also excluded from the GAF grouping.
4. Includes sales at eating and drinking places, drug stores, and proprietary stores.

assembly plans for the first quarter show a sharp rebound in small-car production.

Personal Income and Consumption

The latest data on retail sales point to a large gain in consumer spending in the fourth quarter, supported by strong employment and income growth and substantial recent gains in consumer sentiment.

Total nominal retail sales increased 1.2 percent in November, following an upward-revised gain of 1.3 percent in October. Spending in the retail control group, which excludes sales at automotive dealers and at building material and supply stores, rose 0.7 percent in November; revisions to previous months were small and offsetting. Within the retail control category, nominal sales at most types of stores were up in November. The retail sales data and the available information about prices suggest that the November level of real spending on goods other than motor vehicles was 1.9 percent above the third-quarter average, not at an annual rate.

Consumer spending on services has also advanced solidly, growing 0.4 percent in October. Outlays for energy services rebounded somewhat from their September level, which was held down by unusually mild weather. Gains were widespread among other services, with the largest increases occurring in transportation and personal business services; as a whole, spending on non-energy services was 0.6 percent higher in October than the third-quarter average.

Real disposable personal income grew rapidly in October, advancing 1.3 percent and pushing the personal saving rate up to 4.7 percent in that month. Roughly two-thirds of the growth in disposable income was attributable to a sizable gain in wages and salaries, including large bonuses paid to workers in the motor

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

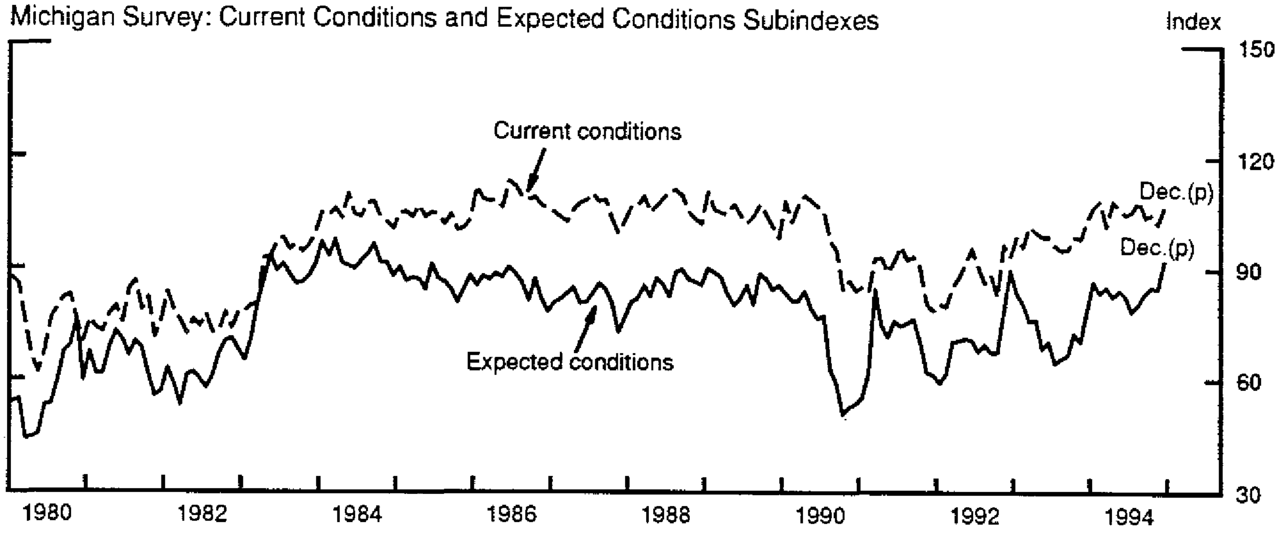
	1993	1994 Q1	1994 Q2	1994 Q3	1994 Sept.	1994 Oct.
Total personal income	.1	30.3	22.5	28.7	34.1	80.5
Wages and salaries	-8.8	19.8	15.6	13.9	19.8	47.7
Private	-10.2	17.0	14.0	12.7	18.5	45.5
Other labor income	2.5	1.8	1.7	1.8	1.8	1.9
Proprietors' income	2.9	.5	-4.0	1.1	2.1	20.0
Farm	.7	-1.7	-5.5	-.8	.4	16.5
Rent	1.9	2.3	-1.9	.2	.2	-.9
Dividend	.8	.9	2.1	1.8	1.8	2.0
Interest	-2.7	3.2	7.5	6.7	7.0	7.3
Transfer payments	4.6	4.9	2.8	4.2	2.8	5.7
Less: Personal contributions for social insurance	1.1	3.1	1.3	1.0	1.4	3.2
Less: Personal tax and nontax payments	.1	5.2	4.1	2.6	3.6	11.5
Equals: Disposable personal income	.0	25.1	18.4	26.0	30.4	69.1
Memo: Real disposable income	-6.4	11.8	5.9	11.2	16.6	49.2

REAL PCE SERVICES
(Percent change from the preceding period)

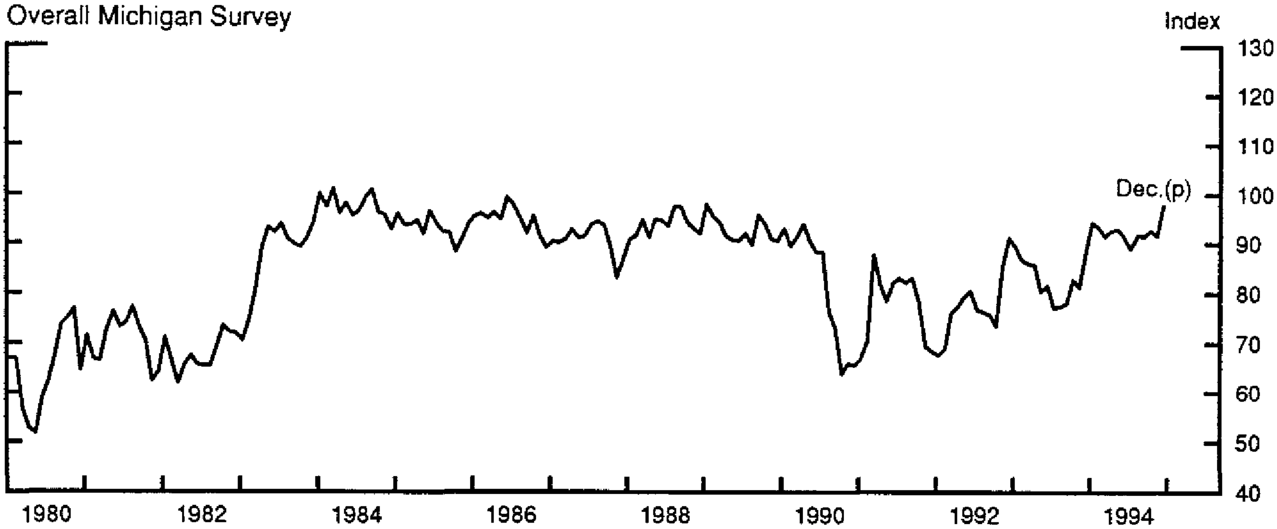
	1993	1994 Q1	1994 Q2	1994 Q3	1994 Sept.	1994 Oct.
		------Annual rate-----			Monthly rate	
PCE services	2.5	4.0	1.1	2.4	.1	.4
Energy	2.2	5.9	-3.4	-11.9	-5.2	2.9
Non-energy	2.5	3.9	1.3	3.3	.4	.2
Housing	1.6	1.9	1.9	2.0	.3	.2
Household operation	1.1	1.2	4.1	6.5	.5	.3
Transportation	4.8	3.4	2.8	2.1	.6	.4
Medical	2.5	2.4	3.6	2.7	.3	.3
Personal business	3.5	8.1	-6.7	-1.7	.6	.4
Other	3.1	7.4	2.5	9.7	.4	.0

Consumer Sentiment

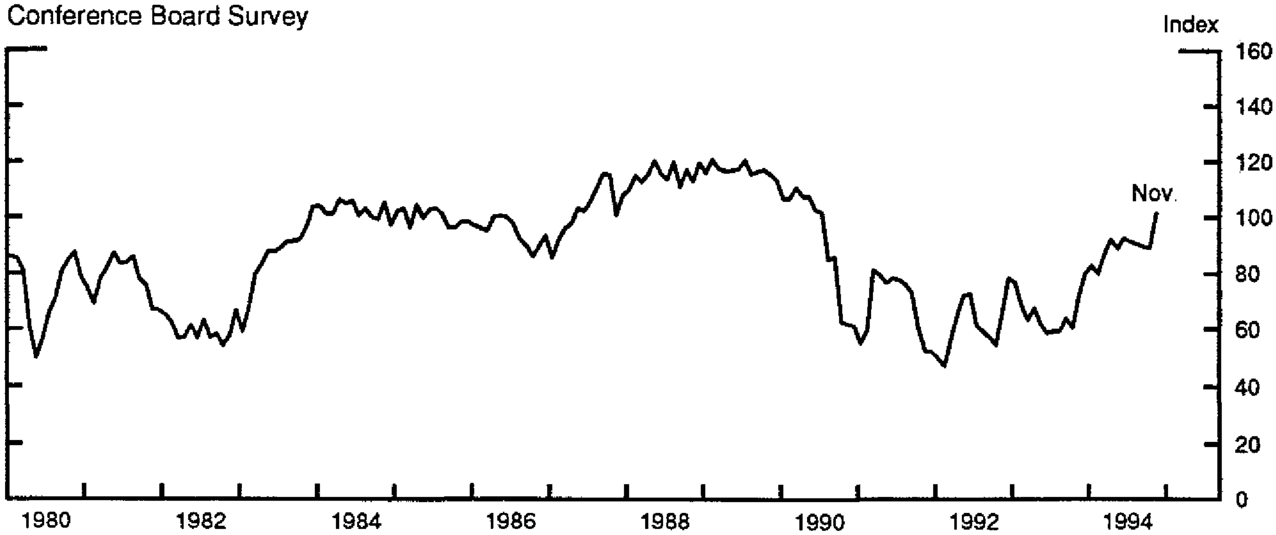
Michigan Survey: Current Conditions and Expected Conditions Subindexes



Overall Michigan Survey



Conference Board Survey

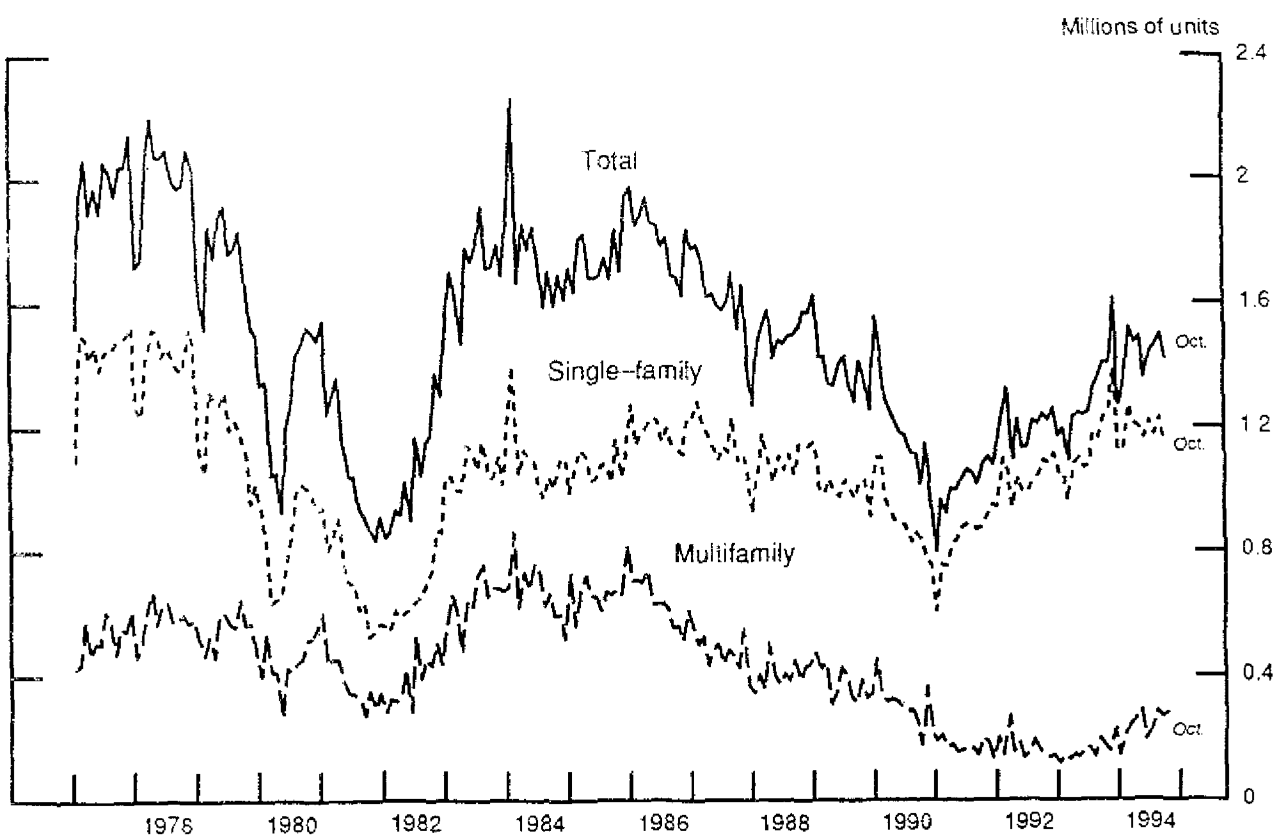


PRIVATE HOUSING ACTIVITY
(Millions of units; seasonally adjusted annual rates)

	1993		1994					
	Annual	Q4	Q1	Q2	Q3[r]	Aug.[r]	Sept.[r]	Oct.[p]
All units								
Starts	1.29	1.48	1.37	1.44	1.47	1.46	1.50	1.42
Permits	1.20	1.38	1.29	1.35	1.37	1.35	1.43	1.40
Single-family units								
Starts	1.13	1.29	1.17	1.19	1.21	1.18	1.23	1.14
Permits	.99	1.13	1.06	1.07	1.04	1.05	1.05	1.05
New-home sales	.67	.77	.69	.66	.68	.68	.72	.73
Existing-home sales	3.80	4.17	4.05	4.06	3.93	3.93	3.89	3.91
Multifamily units								
Starts	.16	.19	.20	.25	.26	.29	.27	28
Permits	.21	25	23	.29	.33	.31	.37	.35

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

Private Housing Starts
(Seasonally adjusted annual rate)



vehicles industry. In addition, October income was boosted by large government payments to farmers who had voluntarily put farmland in the Conservation Reserve program. In November, farm proprietors' income should drop back, and the most recent labor market data suggest that wages and salaries will be little changed. Nonetheless, real disposable income appears likely to register a gain in the neighborhood of 6 percent (annual rate) in the fourth quarter.

The Michigan Survey Research Center's index of consumer sentiment increased sharply in the first part of December. Consumers' assessments of current conditions improved solidly, and the expected future conditions index jumped up sharply; if its early-December level is maintained for the remainder of the month, it will be the most favorable reading since 1984. The latest Conference Board report indicated a sharp improvement in sentiment in November. Before November, the Conference Board index of consumer sentiment had been depressed relative to its pre-recession values; the November increase put the series in line with its readings in the first half of 1990.

Housing Markets

The fundamental determinants of housing activity have weakened substantially since late last year, but indicators of sales and production have not yet shown a commensurate drop. The most recent readings gave mixed signals about the current direction of activity in the housing market.

Single-family starts fell 7 percent in October, to 1.14 million units, the lowest figure since February, and the strong initial estimate for September was revised down moderately. However, the level of single-family permits, which are measured with considerably less statistical error than are starts, has been essentially

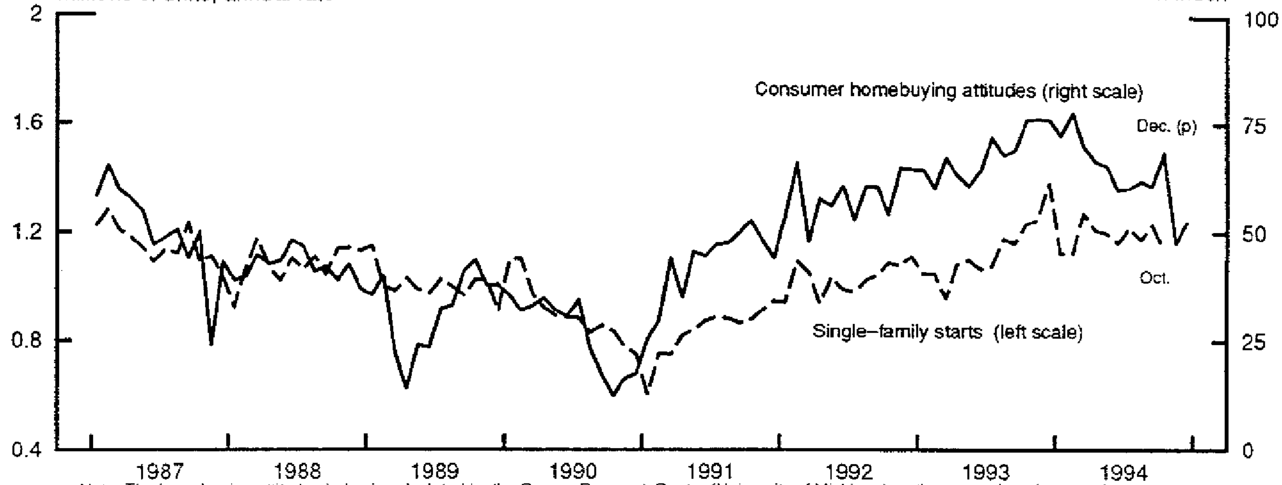
Indicators of Housing Demand

(Seasonally adjusted)

Consumer Homebuying Attitudes

Millions of units, annual rate

Diffusion index

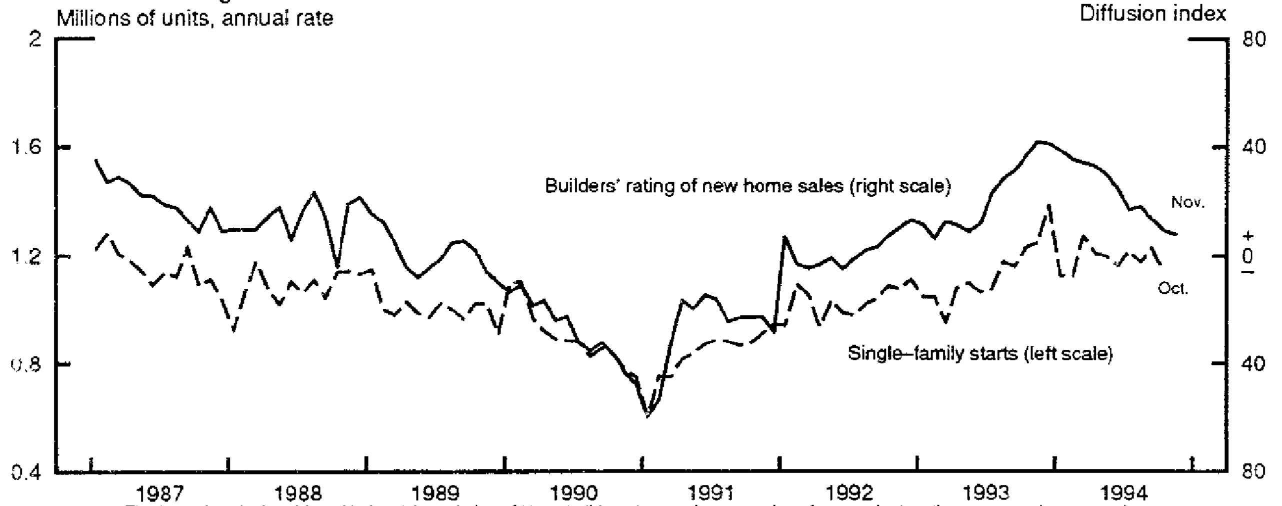


Note. The homebuying attitudes index is calculated by the Survey Research Center (University of Michigan) as the proportion of respondents rating current conditions as good minus the proportion rating such conditions as bad.

Builders' Rating of New Home Sales

Millions of units, annual rate

Diffusion index

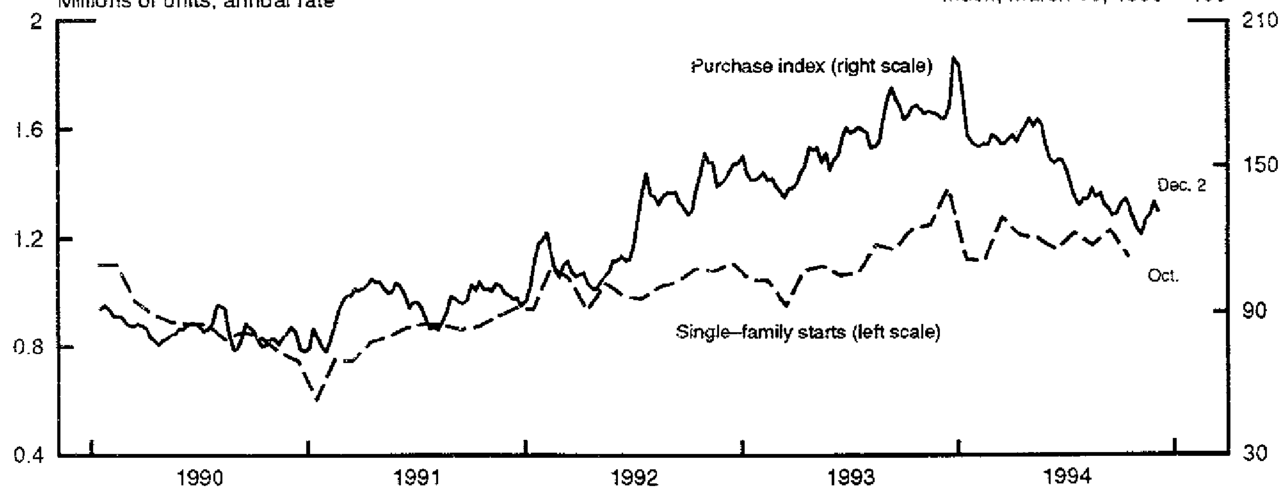


Note. The index is calculated from National Association of Homebuilders data as the proportion of respondents rating current sales as good to excellent minus the proportion rating them as poor.

MBA Index of Mortgage Loan Applications

Millions of units, annual rate

Index, March 16, 1990 = 100



unchanged in recent months, and at its current level suggests that the October level of starts may understate the true volume of construction activity.

Sales of new homes rose 1.3 percent in October, to 726,000 units at an annual rate, the highest level since December 1993. The September-October data on sales and single-family construction, on average, placed the two series in a typical alignment after a period when sales were unusually low relative to starts. Sales of existing homes edged up in October, but the September-October average sales level stood below the pace in months before September.

The survey indicators of housing activity have been mixed recently, but all remain substantially below the favorable readings registered early this year. Consumer attitudes about homebuying conditions improved slightly in early December after a sharp drop in November, while builders' assessments of new home sales continued to worsen in November. Applications for home mortgage financing rose somewhat on a month-average basis in November, after dropping sharply earlier in the year.

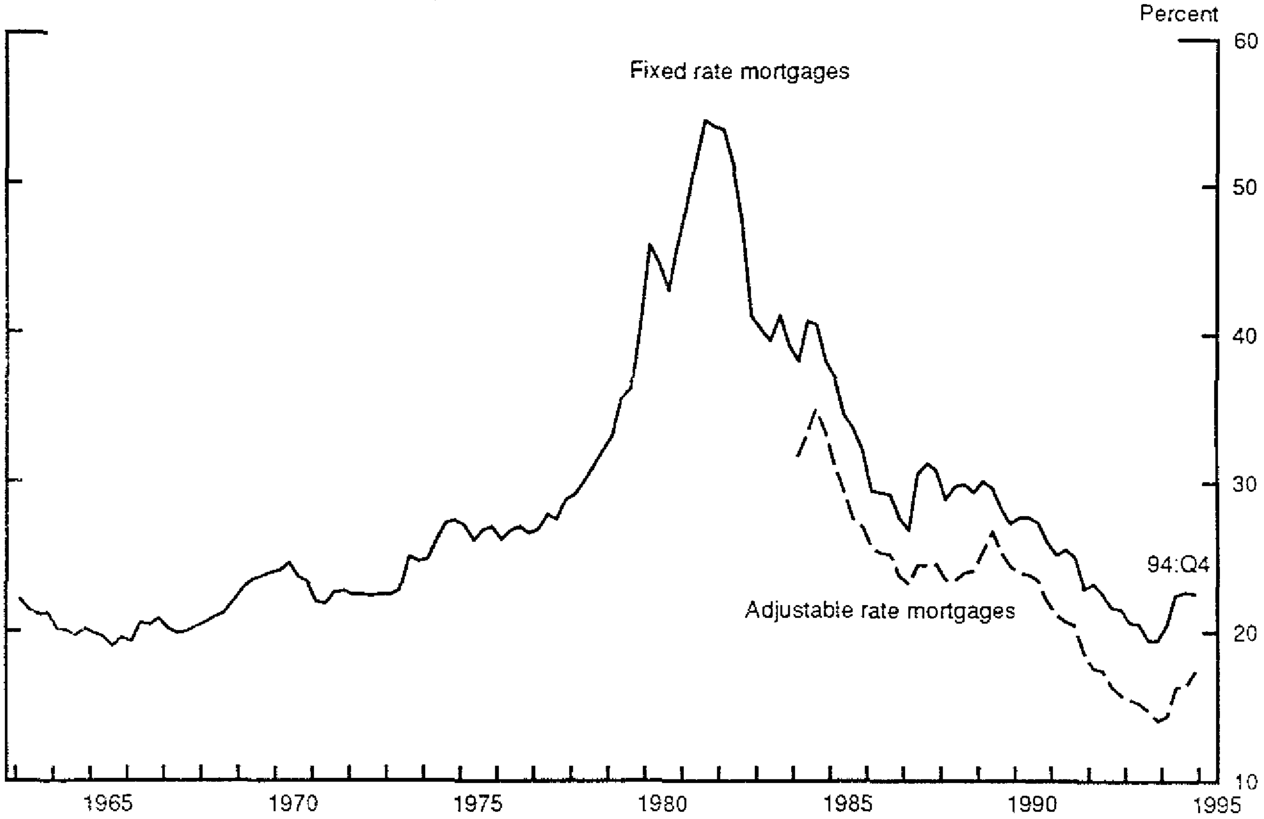
After approaching a 28-year low early this year, the cash-flow burden of fixed-rate mortgage (FRM) financing has risen noticeably in recent months, although the effect of the higher FRM rates may have been cushioned somewhat by a shift toward adjustable-rate mortgages (ARMs), which depository institutions have offered with large initial rate discounts. According to the Federal Housing Finance Board, the ARM share of newly originated conventional home mortgages rose in October to 49 percent, the highest proportion since May 1989.

Since the last FOMC meeting, however, typical ARM rates have increased about 55 basis points, while rates on FRMs have fallen

12-13-94

Mortgage Financing

Cash-flow Burden of Homeownership



Note. Cash-flow burden is defined as the financing cost of a constant-quality new home as a percentage of average household disposable income.

FRM AND ARM RATES AND CORRESPONDING TREASURY RATES
IN THE INTERMEETING PERIOD
(Percent except as noted)

Series	Week ended: Nov. 11	Week ended: Dec. 9	Change (basis points)
Treasury securities			
10-year	8.00	7.79	-21
1-year	6.42	7.09	67
Mortgages			
FRM	9.37	9 33	-4
ARM	6.01	6.56	55

Note. FRM rate is on a bond-equivalent yield basis. ARM rate is the average initial contract rate on new commitments for thirty-year adjustable rate mortgages that are indexed to the yield on one-year Treasury securities.

4 basis points.[9] This narrowing FRM-ARM spread may prompt more homebuyers to opt for the less-risky fixed-rate alternative--and it likely will disqualify some would-be buyers who can qualify for loans only if the monthly payments are lower in the early years.

Multifamily housing starts rose 4.8 percent in October, to 282,000 units. In general, multifamily starts have been trending up recently, reflecting emerging demand pressures in some markets.

Business Fixed Investment

Investment in producers' durable equipment evidently has continued to expand rapidly this quarter. Shipments of nondefense capital goods excluding aircraft were up a bit in October after advancing sharply in the two previous months, yielding an October level that was 2-1/4 percent above the third-quarter average. Nominal shipments of computing equipment have been very strong in recent months, rising in October to a level 5-1/2 percent above their average for the third quarter. Reports in the trade press suggest that both business and consumer demand for PCs, workstations, and related equipment is surging.[10] Shipments of other capital goods were also at a very high level in October. Moreover, the continuing strength in new orders for both computers and other capital equipment, along with growing backlogs for computers and office equipment, suggests that shipments will rise further in coming months.

9. The majority of ARMs are linked to the one-year Treasury rate.

10. Intel announced recently that under certain conditions its Pentium microprocessor might malfunction. This problem has received a great deal of attention in the press, but our industry contacts do not believe that, thus far, it has had much of a depressing effect on computer purchases, owing to the small share of Pentium machines in total business computer purchases. However, as a result of its own research showing that the problem is more severe than Intel has indicated, IBM announced that it will suspend shipments of machines with the defective chips. These developments have caused uncertainty, which may lead some customers to postpone purchases for a few months until the situation is clarified.

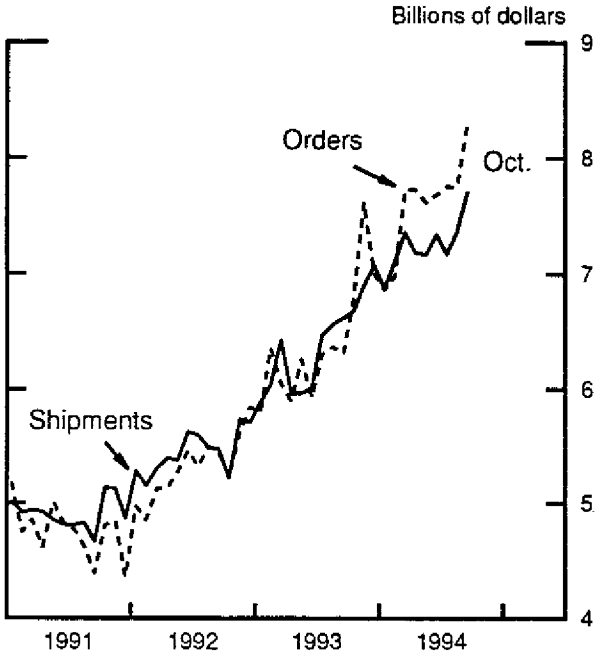
BUSINESS CAPITAL SPENDING INDICATORS
(Percent change from preceding comparable period;
based on seasonally adjusted data, in current dollars)

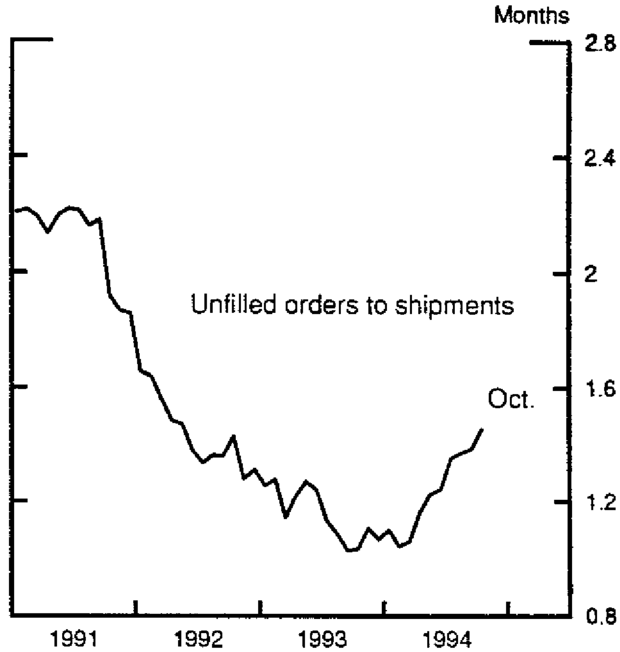
	1994			1994		
	Q1	Q2	Q3	Aug.	Sept.	Oct.
Producers' durable equipment						
Shipments of nondefense capital goods	1.0	2.3	3.4	3.3	1.6	-.8
Excluding aircraft and parts	1.2	4.6	3.2	3.3	1.4	.2
Office and computing	3.3	1.7	2.5	2.6	4.6	1.5
All other categories	.5	5.4	3.4	3.5	.5	-.2
Shipments of complete aircraft[1]	9.6	-33.1	-4.5	68.4	11.6	-40.0
Sales of heavy trucks	-1.0	5.3	1.3	17.2	-6.7	4.8
Orders of nondefense capital goods	6.2	.2	3.3	3.5	3.9	-2.3
Excluding aircraft and parts	1.7	4.2	3.4	2.1	3.5	.1
Office and computing	.8	6.7	3.3	-.1	7.0	2.8
All other categories	1.9	3.5	3.5	2.7	2.5	-.7
Nonresidential structures						
Construction put-in-place	-3.1	3.6	2.0	.3	3.1	1.6
Office	-.3	3.7	2.6	4.0	.7	-.6
Other commercial	-6.0	11.9	2.0	-3.4	5.2	.5
Institutional	-6.7	7.4	-1.2	-3.0	2.8	3.6
Industrial	1.0	6.6	3.4	5.2	2.7	.8
Public utilities	-2.2	-4.5	4.4	1.0	2.1	3.7
Lodging and miscellaneous	-2.7	-.6	-7.3	2.3	6.3	.1
Rotary drilling rigs in use	.8	2.2	-.8	-1.6	3.1	-4.9
Memo:						
Business fixed investment[2]	10.9	9.2	14.4	n.a.	n.a.	n.a.
Producers' durable equipment[2]	18.6	6.1	18.0	n.a.	n.a.	n.a.
Nonresidential structures[2]	-11.8	20.6	2.9	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. Based on constant-dollar data; percent change, annual rate.
n.a. Not available.

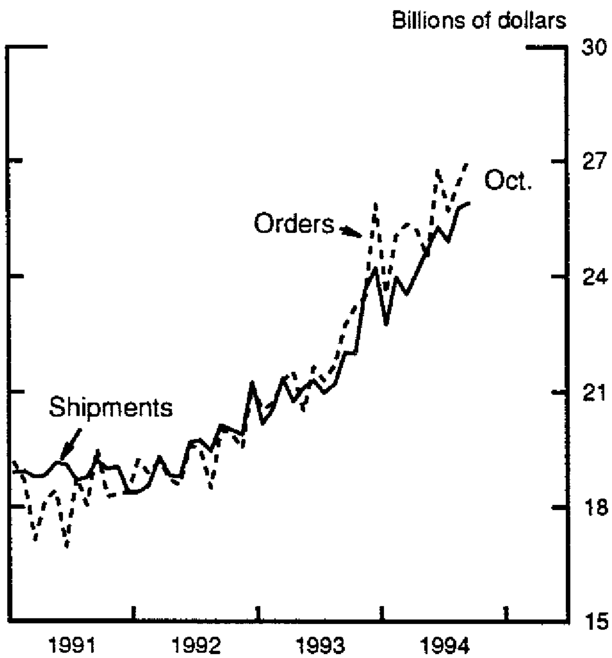
Orders and Shipments of Nondefense Capital Goods

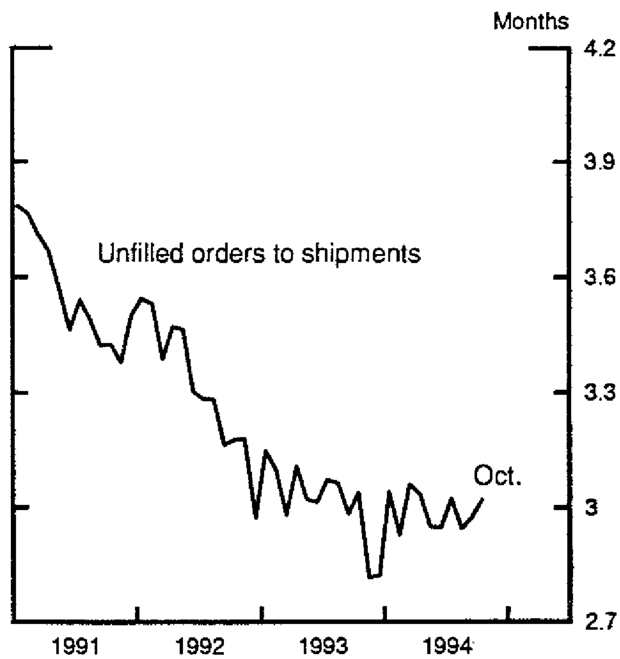
Office and Computing Equipment





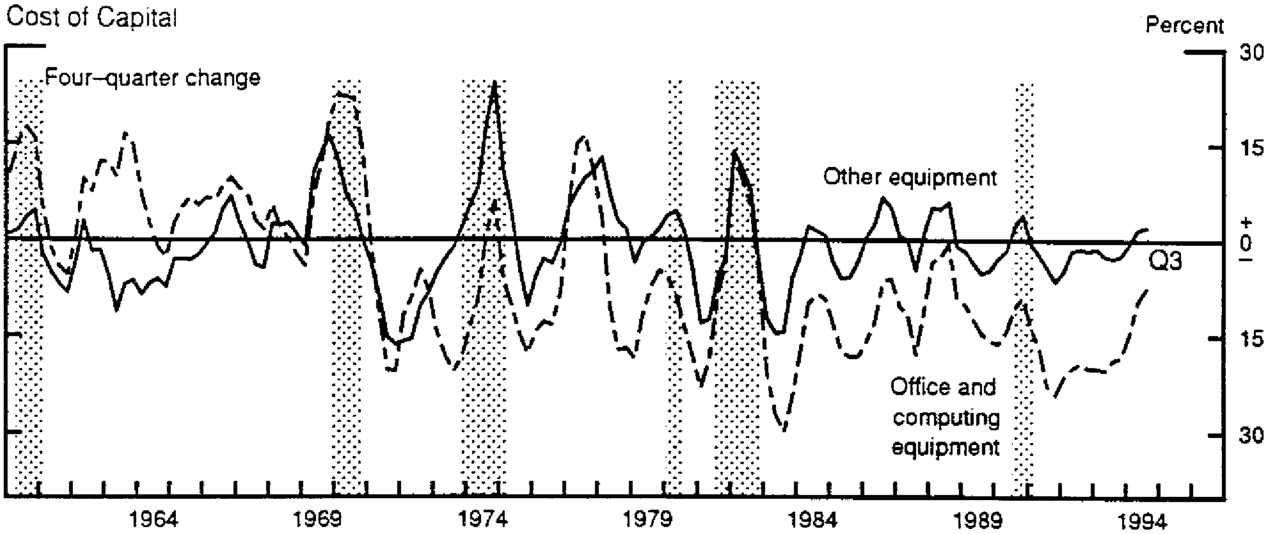
Other Equipment (Excluding Aircraft and Computing Equipment)



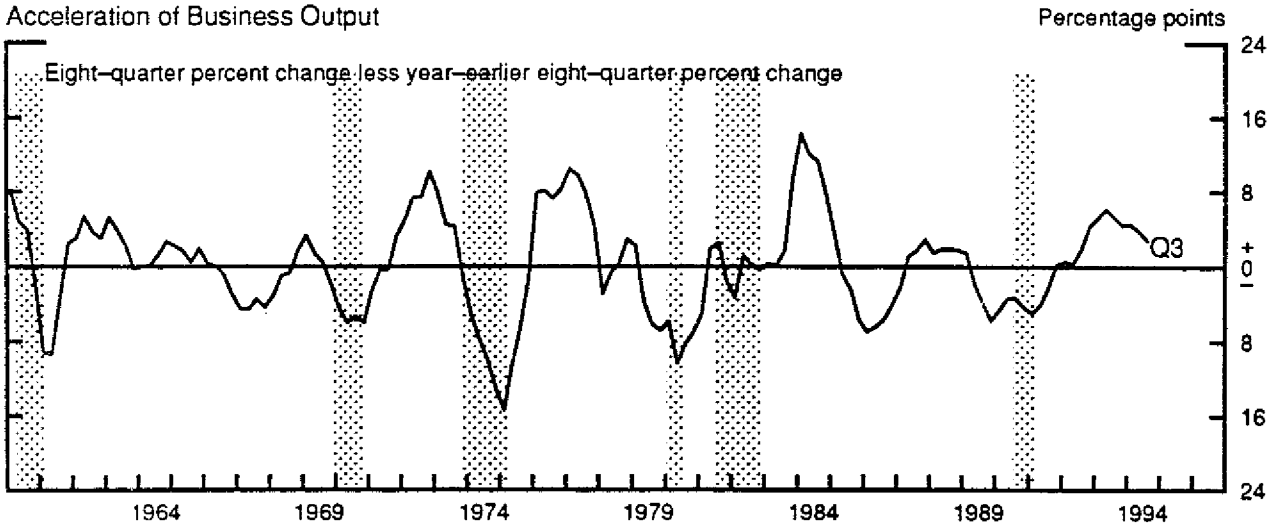


Fundamental Determinants of Business Fixed Investment

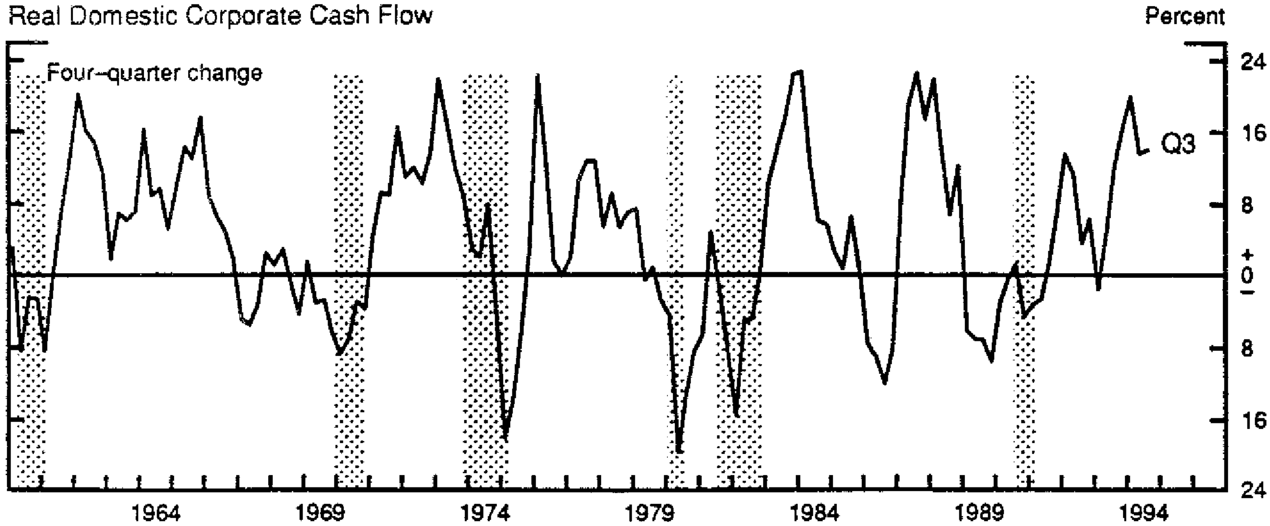
Cost of Capital



Acceleration of Business Output



Real Domestic Corporate Cash Flow



As for transportation equipment, healthy business demand helped push up light vehicle sales in October and November. In addition, heavy truck sales shot up in October and November, putting the average pace in the two months roughly 10 percent (not annual rate) above their third-quarter rate. The demand for heavy trucks has been very high throughout 1994, but capacity constraints have slowed deliveries, and orders have backed up considerably. Several truck manufacturers report that new capacity is coming on line in the fourth quarter, which should help them whittle away at the large backlog. Aircraft outlays and backlogs have continued to fall. Domestic shipments dropped 35 percent from December 1993 to September 1994, and this downtrend has continued into the fourth quarter. Boeing's domestic orders, which were very slow in 1993, have remained weak so far this year.

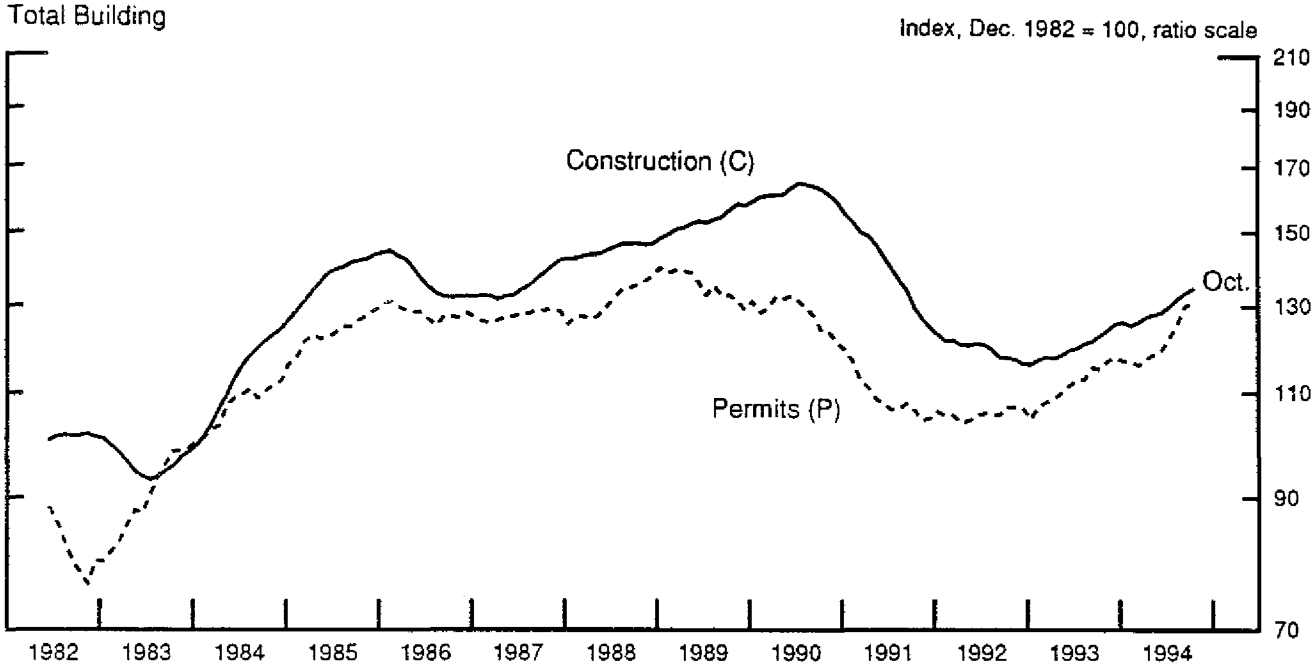
The continued strength of spending on producers' durable equipment is broadly consistent with recent readings on several fundamental determinants of investment. Despite higher interest rates, the cost of capital continues to be quite favorable for equipment, primarily because prices for capital goods have not increased very rapidly on average--owing importantly to the drop in computer prices. In addition, the acceleration of business output continues to provide a positive, albeit diminishing,[11] stimulus to investment, and corporate cash flow has been growing rapidly.

Outlays for nonresidential structures have continued to advance strongly. Construction put-in-place for buildings increased 1-1/2 percent in October and has been on a modest but steady uptrend for almost two years. The strength is concentrated in the "other commercial" sector (which includes retail outlets) and, to a lesser

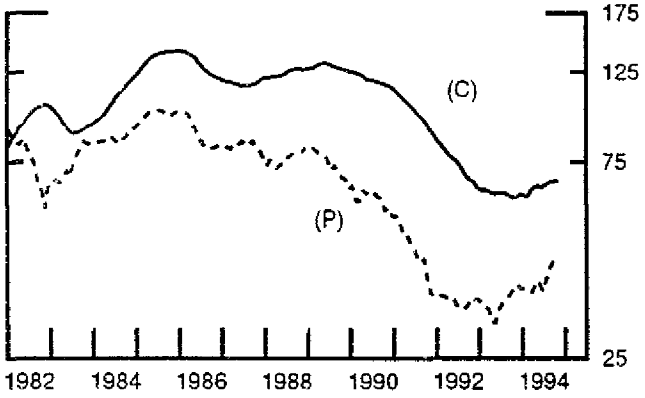
11. The accelerator effect relates the lagged change in growth rates to investment. While growth in nonfarm business output excluding housing (called "Business Output" in the chart) has continued strong, the <u>change</u> in growth rates has declined.

Nonresidential Construction and Permits
(Six–month moving average)

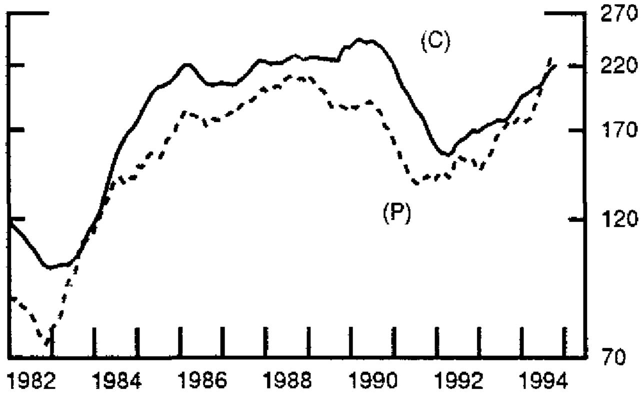
Total Building



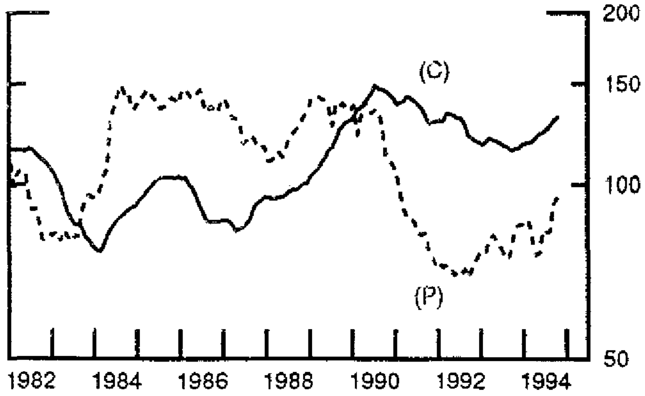
Office



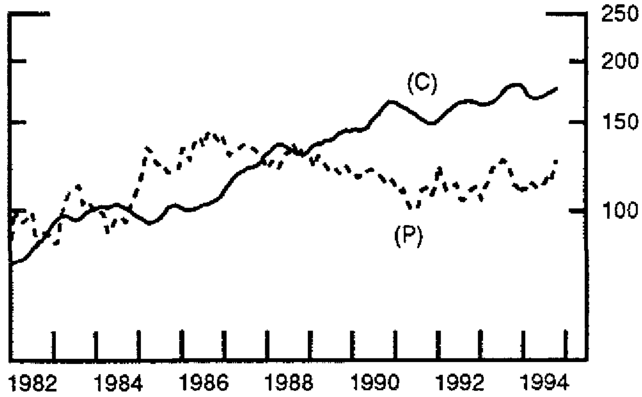
Other Commercial



Industrial



Institutional



extent, in the "industrial" category; office and institutional construction (which includes structures related to health care and private educational buildings) have been only inching up. In the aggregate, leading indicators of future construction have also been solid. Although permits for nonresidential construction dropped back in October, after smoothing through the monthly volatility they still appear to be on a healthy uptrend.

Drilling and mining is one sector where investment has been declining, as relatively low natural gas prices and substantial inventories have depressed drilling activity. The slowdown in activity in this sector may well be intensifying. Rotary drilling rigs-in-use dropped about 5 percent in October, after declining 1 percent in the third quarter. In addition, the Baker-Hughes index of footage drilled registered a large drop in October.

Inventories

The recent robust business inventory expansion may have continued into October. Census data available at this point show that inventories in manufacturing and wholesale trade rose in October at a $33.7 billion annual rate, only a bit less than the rapid $36.4 billion pace posted during the third quarter. The brisk rise in stocks appears to reflect desired accumulation in light of favorable sales expectations and concerns about prompt availability of supplies.

In manufacturing, the pace of stockbuilding picked up again, with an accumulation of $17.5 billion (annual rate) in October following little net change in the preceding two months. The pattern of manufacturers' inventory investment in October was quite similar to that observed through much of this year; a sizable portion of the increase was in stocks at producers of capital goods, reflecting the continued strength in demand for business equipment.

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

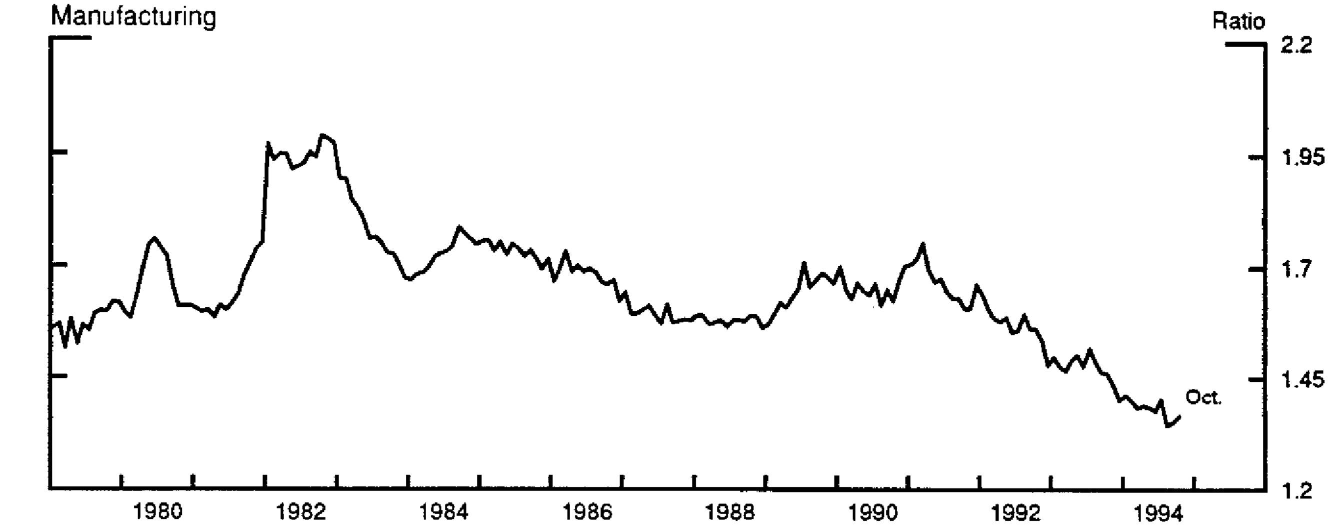
	1994			1994		
	Q1	Q2	Q3	Aug.	Sept.	Oct.
Total	18.4	75.6	74.8	93.9	63.5	n.a.
Excluding wholesale and retail motor vehicles	21.1	58.9	55.6	57.0	34.3	n.a.
Manufacturing	9.4	13.3	13.7	4.4	-5.8	17.5
Defense aircraft	-4.4	-4.7	-2.3	-4.9	-2.9	.2
Nondefense aircraft	-1.4	3.7	-.8	2.0	-4.7	-2.5
Excluding aircraft	15.2	14.4	16.8	7.3	1.8	19.7
Wholesale	3.1	23.0	22.7	11.5	14.1	16.2
Excluding motor vehicles	8.3	16.6	23.0	18.7	11.7	11.9
Retail	5.9	39.4	38.4	78.0	55.1	n.a.
Automotive	2.6	10.4	19.5	44.0	26.7	n.a.
Excluding auto dealers	3.4	29.0	18.9	34.0	28.4	n.a.
Constant-dollar basis						
Total	9.9	39.0	38.4	34.5	8.2	n.a.
Excluding motor vehicles	11.8	35.6	31.2	36.2	7.2	n.a.
Manufacturing	9.9	.7	3.6	-1.6	-16.4	n.a.
Wholesale	-2.0	16.0	14.0	5.8	4.2	n.a.
Excluding motor vehicles	3.0	10.8	14.5	12.5	2.0	n.a.
Retail	2.0	22.3	20.7	30.2	20.4	n.a.
Automotive	2.5	-1.9	6.9	4.3	-2.3	n.a.
Excluding auto dealers	-.5	24.2	13.8	25.9	22.7	n.a.

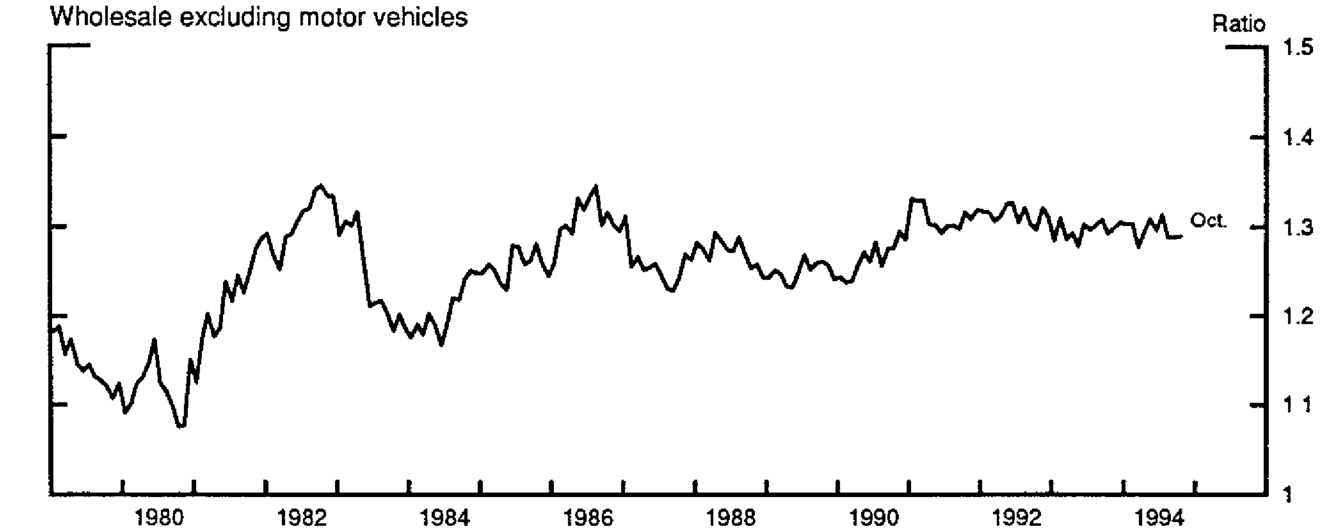
INVENTORIES RELATIVE TO SALES[1]
(Months supply; based on seasonally adjusted data at book value)

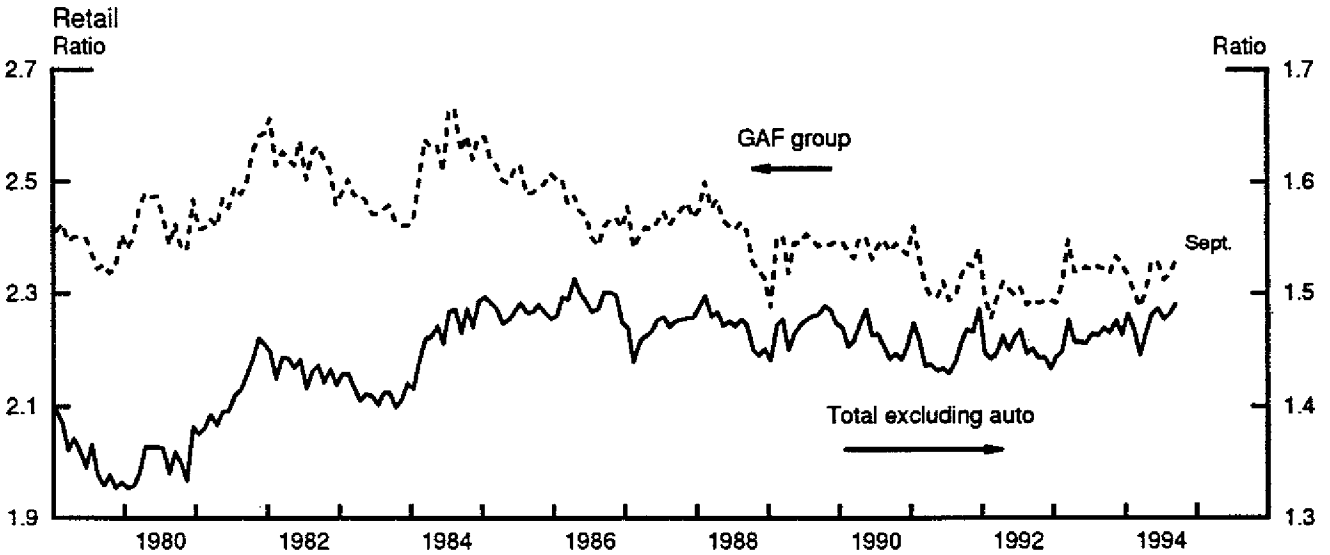
	1994			1994		
	Q1	Q2	Q3	Aug.	Sept.	Oct.
Total	1.41	1.41	1.41	1.39	1.40	n.a.
Excluding wholesale and retail motor vehicles	1.39	1.39	1.38	1.36	1.37	n.a.
Manufacturing	1.40	1.39	1.36	1.34	1.35	1.37
Defense aircraft	4.80	4.85	4.69	4.49	4.95	4.79
Nondefense aircraft	5.00	5.84	5.54	5.62	5.38	5.76
Excluding aircraft	1.28	1.26	1.25	1.23	1.23	1.25
Wholesale	1.31	1.33	1.32	1.30	1.31	1.32
Excluding motor vehicles	1.30	1.30	1.30	1.29	1.29	1.29
Retail	1.50	1.54	1.56	1.53	1.54	n.a.
Automotive	1.61	1.67	1.76	1.70	1.73	n.a.
Excluding auto dealers	1.47	1.50	1.50	1.48	1.49	n.a.
Constant-dollar basis						
Total	1.46	1.46	1.46	1.44	1.44	n.a.
Excluding motor vehicles	1.52	1.51	1.51	1.49	1.50	n.a.
Manufacturing	1.44	1.43	1.41	1.40	1.40	n.a.
Wholesale	1.39	1.41	1.40	1.39	1.39	n.a.
Excluding motor vehicles	1.39	1.39	1.39	1.38	1.38	n.a.
Retail	1.53	1.56	1.57	1.56	1.56	n.a.
Automotive	1.56	1.57	1.62	1.62	1.61	n.a.
Excluding auto dealers	1.52	1.55	1.56	1.54	1.55	n.a.

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

Ratio of Inventories to Sales
(Book value)







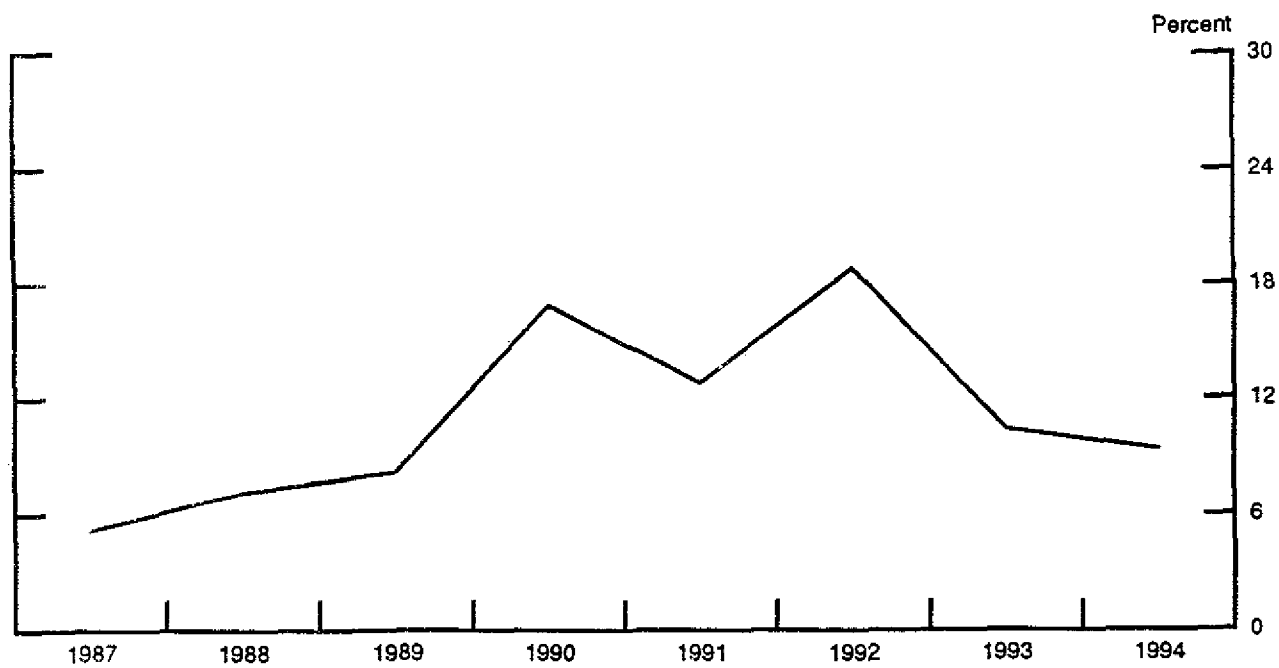
FEDERAL GOVERNMENT OUTLAYS AND RECEIPTS
(Unified basis, billions of dollars, except where otherwise noted)

	Oct. 1993	Oct. 1994	Dollar change	Percent change
Outlays	124.1	121.5	-2.6	-2.1
Deposit insurance (DI)	.1	-.7	-.7	---
Outlays excluding DI	124.0	122.2	-1.9	-1.5
National defense	24.3	18.8	-5.5	-22.6
Net interest	17.1	18.7	1.6	9.3
Social security	25.5	26.7	1.2	4.6
Medicare and health	20.0	19.7	-.3	-1.6
Income security	17.4	15.3	-2.1	-12.0
Other	19.7	23.0	3.3	16.5
Receipts	78.7	89.0	10.4	13.2
Personal income taxes	37.7	43.2	5.6	14.8
Social insurance taxes	30.8	32.7	1.9	6.0
Corporate income taxes	2.2	3.5	1.3	60.8
Other	8.0	9.6	1.6	20.3
Deficit(+)	45.4	32.4	-13.0	-28.6
Excluding DI	45.4	33.1	-12.2	-27.0

Details may not add to totals because of rounding.

Federal Unified Budget Outlays for Health Programs

(Percent change from previous fiscal year)



In particular, inventories at producers of computers and computer accessories, office machinery, and telecommunications equipment--industries where bookings have been robust for much of this year and the backlog of unfilled orders has been relatively high--accounted for the bulk of the October buildup. By stage of processing, investment in stocks of materials and supplies posted another sizable rise in October following a string of increases since January. In contrast, factories have seen little net accumulation in inventories of finished goods since July.

Merchant wholesalers continued to build their inventories at a brisk pace in October; excluding motor vehicles, wholesale stocks expanded at a $12 billion annual rate in October, about the same pace as in September. The pattern of accumulation was similar to that of the manufacturers, with a significant part of the buildup in the categories of machinery, professional and business equipment, and metals.

Non-auto retail inventories seemed well in line with sales at the end of September, as a sharp August-September rise in inventories was matched by sales gains, leaving the overall inventory-sales ratios near trend. Moreover, some of retailers' stockbuilding in recent months may reflect optimistic expectations regarding holiday sales.

Federal Sector

Continuing spending restraint combined with rising tax revenues have contributed to substantial shrinkage of the federal budget deficit. On a unified basis, the deficit was $32 billion in October compared with $45 billion a year ago. However, October outlays were artificially depressed this year by about $6 billion because the October outlays for defense payrolls, veterans benefits, and SSI benefits were paid in September. (October 1 fell on a Saturday.)

After adjusting for this special factor, the October deficit was down $7 billion from last year, with adjusted outlays up 3 percent and receipts up 13 percent. Falling payroll-adjusted defense spending, which was down 12 percent, contributed more than any other category to the overall spending decline. The strong growth in receipts was due primarily to a surge in personal withheld taxes and social insurance taxes, and likely reflected the robust growth in wages and salaries.

Defense spending for operations and maintenance was a bit below trend in October after surging in September.[12] The September-October military operations in Haiti were likely sustained primarily by September spending and by inventories; additional operations and maintenance expenditures will probably show up in future months as inventories diminish. Nonetheless, the low operations and maintenance expenditures in October could signal lower levels of expenditures for Haiti than were projected by OMB.[13] In addition, OMB sources indicate that the Persian Gulf buildup will be reflected primarily in future defense purchases as fuel supplies are replenished and equipment is returned to storage.[14]

OMB and CBO reportedly will lower their estimates of future federal spending for health programs in their respective fiscal year 1996 budget documents due to be released in early 1995 Last summer, the average annual growth rate of health spending between

12. Timing of procurement spending also contributed to the year-over-year decline in payday-adjusted October defense spending. This year, high procurement spending in September was offset by low procurement spending in October.

13 OMB estimates that outlays for Haiti were $514 million in FY1994 and $148 million for October. Estimates for the remainder of FY1995 are not yet available. In addition, costs associated with the retention of Cuban refugees are estimated at $119 million for FY1994 and $243 million for FY1995.

14. Arab countries are expected to finance most or all of the costs of the Persian Gulf operations via a special defense account, so that the resource costs will be reflected in offsetting NIPA purchases and transfers, but not in unified outlays. (Payments into the special defense account will be scored as a negative outlay.)

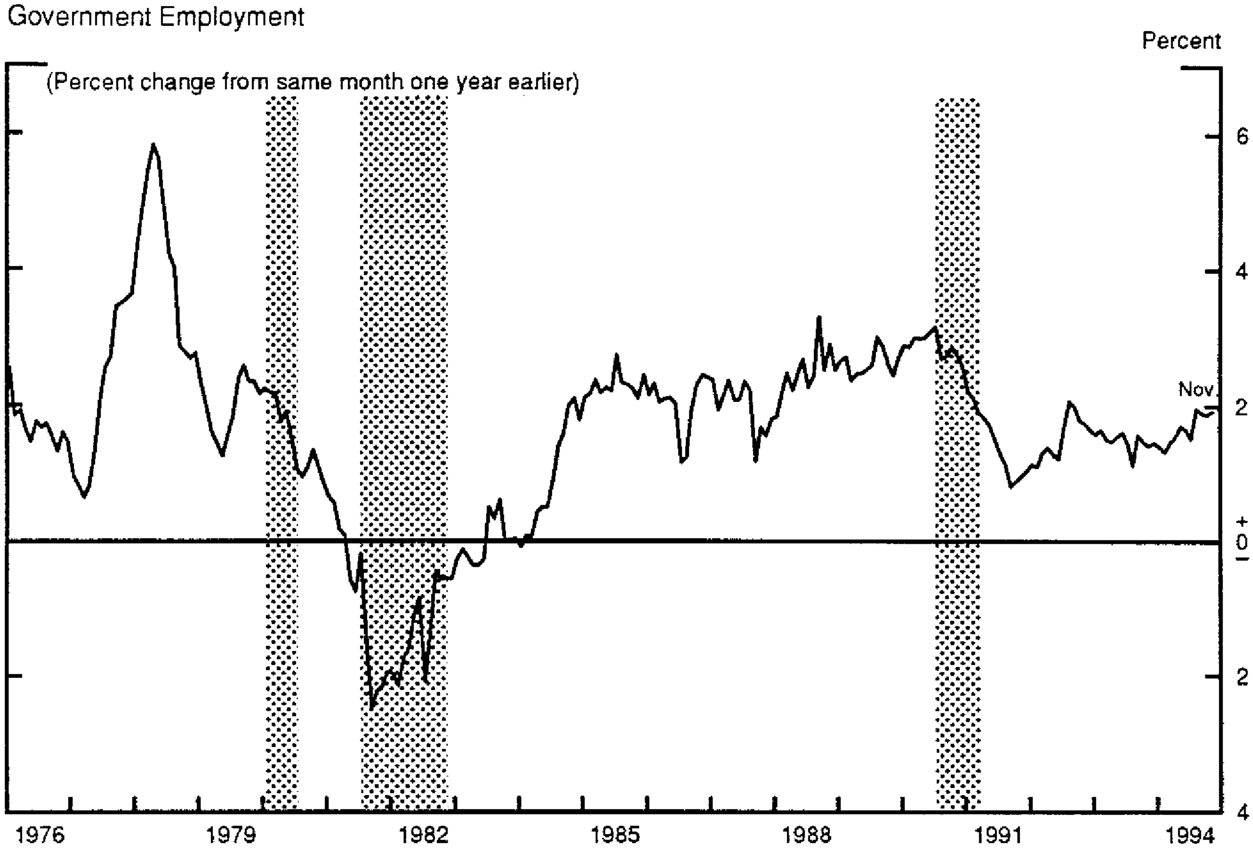
fiscal years 1994 and 1996 was estimated at 10 percent by OMB and 12 percent by CBO, somewhat higher than the 9 percent growth rate experienced in fiscal 1994 (see chart).[15]

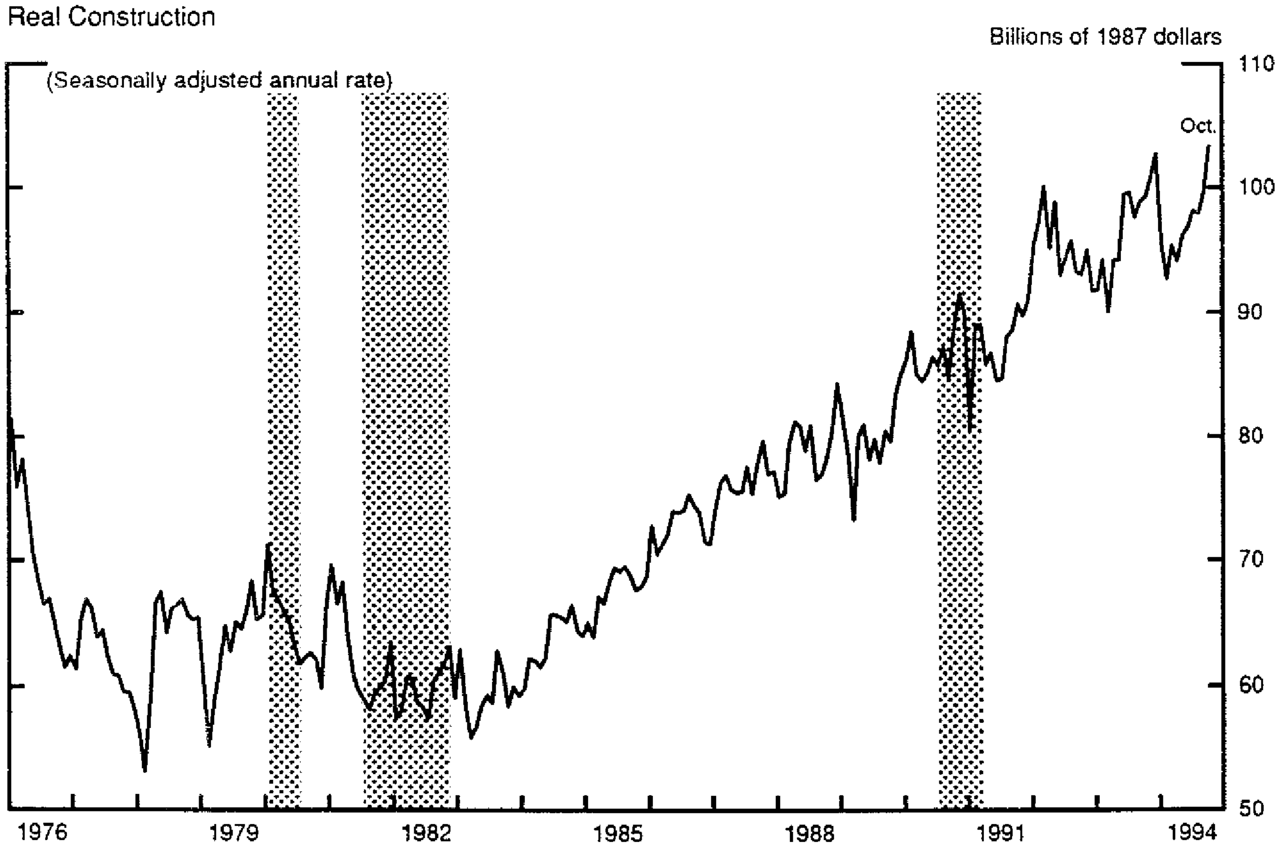
President Clinton recently proposed a $2 billion emergency supplemental appropriation for the Defense Department for fiscal year 1995 to offset the costs of military operations in Haiti and Bosnia, the setup of a migrant camp for Cuban refugees at Guantanamo Bay, and the buildup and builddown in the Persian Gulf. Under OBRA-93 budget rules, emergency spending need not be offset by other spending reductions. In addition, the President announced that his fiscal year 1996 budget will request $25 billion more defense spending over the next five years than was requested in last year's budget. Increases in non-emergency defense spending through fiscal year 1998 must be offset by reductions in other discretionary spending under OBRA-93 budget rules.

Both houses of Congress have approved legislation implementing the Uruguay Round of the General Agreement on Tariffs and Trade (GATT) and providing for offsetting revenue increases and spending cuts necessitated by the OBRA-93 budgeting rules. The five-year financing legislation includes $1 billion from spending cuts, $4 billion from increased tax compliance and changes in the timing of tax payments, $1 billion from reforms to the operations of the Pension Benefit Guarantee Corporation, $2 billion from surpluses attributable to previous legislation, and $4 billion from other miscellaneous sources. The President signed the legislation on December 8.

15. OMB revised down its estimates of health spending this past August but CBO, for the most part, did not. CBO chose to remain consistent with the assumptions used to cost out the various health care reform proposals put forward during the 1994 legislative season.

State and Local Sector





The President's Commission on Entitlements and Tax Reform, chaired by Senator Kerrey, was scheduled to have voted its recommendations on December 14. The commission's options, which were set out in a staff report, include more than seventy-five measures to restrain entitlement spending or increase federal revenues. Which options will be chosen and the net impact remain quite uncertain.

State and Local Government Sector

Available indicators suggest that purchases of goods and services by state and local governments will post another solid gain in the fourth quarter. Although the increase in employment in November largely represented temporary election workers, trend employment growth in the state and local sector appears to have firmed a bit in recent months. In addition, real outlays for structures jumped in October, boosting construction to a level nearly 5 percent above the third-quarter average. Most categories of construction spending saw advances in October, with the largest increase in outlays for educational facilities.

With many states having ended fiscal year 1994 in reasonably good shape, pressures to raise taxes have abated. Although the changes in state tax laws made last spring raised revenues, on net, the increase is forecast by the National Council of State Legislatures to be only about 1 percent of total collections in fiscal 1995, the smallest increment since 1988. This development reflects both a drop in the amount of money raised from tax hikes and a step-up in tax cuts.

Further reductions in taxes are likely during the 1995 legislative sessions. Four states just elected governors with ambitious tax-cutting agendas, and a number of others have similar plans. However, in light of the recent fiscal difficulties in many

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

	Relative importance, Dec. 1993	1992	1993	1994 Q1	1994 Q2	1994 Q3	1994 Oct.	1994 Nov.
				-----Annual rate------			-Monthly rate-	
All items[2]	100.0	2.9	2.7	2.5	2.5	3.6	.1	.3
Food	15.8	1.5	2.9	-1.1	2.8	5.1	.0	.2
Energy	7.0	2.0	-1.4	4.7	-4.9	10.9	-.7	.7
All items less food and energy	77.2	3.3	3.2	2.9	3.1	2.6	.2	.2
Commodities	24.4	2.5	1.6	.6	4.2	.6	.0	.1
Services	52.8	3.7	3.9	4.2	2.4	3.6	.2	.3
Memo:								
CPI-W[3]	100.0	2.9	2.5	2.5	2.5	3.6	.1	.3

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.

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

	Relative importance, Dec. 1993	1992	1993	1994 Q1	1994 Q2	1994 Q3	1994 Oct.	1994 Nov.
				-----Annual rate------			-Monthly rate-	
Finished goods	100.0	1.6	.2	3.6	-.3	2.6	-.5	.5
Consumer foods	22.9	1.6	2.4	-.6	-5.5	3.9	-.2	.2
Consumer energy	13.3	-.3	-4.1	15.4	-1.0	3.2	-1.2	2.1
Other finished goods	63.7	2.0	.4	3.0	2.1	2.1	-.5	.1
Consumer goods	40.3	2.1	-.4	2.0	1.5	2.0	-.3	.2
Capital equipment	23.4	1.7	1.8	4.3	3.0	2.4	-1.0	.1
Intermediate materials[2]	95.2	1.1	.8	2.8	3.1	5.9	.4	1.1
Excluding food and energy	82.3	1.2	1.6	1.9	3.9	6.2	.7	.9
Crude food materials	44.1	3.0	7.2	-4.5	-20.6	-12.9	-2.0	1.5
Crude energy	34.4	2.3	-12.3	10.1	21.0	-20.5	.0	-1.0
Other crude materials	21.5	5.7	10.7	22.7	-.8	18.8	.9	3.4

1. Changes are from final month of preceding period to final month of period indicated.
2. Excludes materials for food manufacturing and animal feeds.

of these states, most recent tax-reduction proposals have been relatively small.

Prices

Although inflation has picked up smartly at the early stages of processing, thus far this acceleration has not been paralleled in prices for final goods.[16] The PPI for intermediate materials excluding food and energy increased 4.8 percent in the past twelve months--more than three percentage points faster than its pace in the year-earlier period. In contrast, for commodities excluding food, energy, and tobacco, the PPI for finished goods accelerated just 0.1 percentage point in the past year, while the corresponding CPI decelerated about 0.8 percentage point. Nor do the recent data give a hint of a change in direction. The core PPI rose just 0.1 percent in November, while the CPI excluding food and energy was up only 0.2 percent.

PRICES EXCLUDING FOOD AND ENERGY
(Percent change from November to November)

	PPI			CPI ex. tobacco	
	Crude	Intermediate	Finished ex. tobacco	Commodities	Total
1992	3.0	1.1	1.8	2.2	3.3
1993	11.6	1.6	1.4	2.1	3.3
1994	15.4	4.8	1.5	1.3	2.8

Intermediate goods prices excluding food and energy advanced at a 7-1/2 percent annual rate in the past six months--considerably faster than during the previous six months. The increases were led by a variety of materials purchased as inputs to manufacturing. Crude prices have been increasing even faster, and have also picked

16. Logically, there are three possible explanations for the lack of a pass-through: either producers' margins must have declined, some other costs (e.g., labor costs) must have declined, or their productivity must have risen. It is not possible at this stage to determine the relative importance of these possibilities.

INFLATION RATES EXCLUDING FOOD AND ENERGY

	Percent change from twelve months earlier		
	Nov. 1992	Nov. 1993	Nov. 1994
CPI	3.4	3.1	2.8
Goods	2.5	1.6	1.5
Alcoholic beverages	2.9	1.2	1.3
New vehicles	2.6	3.2	3.4
Apparel	0.9	1.1	-1.8
House furnishings	1.4	1.2	0.4
Housekeeping supplies	0.5	1.3	0.5
Medical commodities	5.1	3.3	3.1
Entertainment	1.8	1.6	2.2
Tobacco	7.7	-4.7	3.2
Services	3.9	3.7	3.5
Owners' equivalent rent	3.0	3.0	3.6
Tenants' rent	2.5	2.0	2.6
Other renters' costs	5.9	3.1	2.9
Airline fares	9.0	14.5	-5.6
Medical care	7.3	5.9	5.2
Entertainment	2.8	3.7	3.0
Auto financing	-14.0	-5.7	17.5
Tuition	8.2	7.3	5.9
PPI finished goods	2.0	0.3	1.6
Consumer goods	2.2	-0.5	1.5
Capital goods, excluding computers	2.7	2.3	1.9
Computers	-15.7	-12.6	-7.2
PPI intermediate materials	1.1	1.6	4.8
PPI crude materials	3.0	11.6	15.4
Factors affecting price inflation			
ECI hourly compensation[1]	3.4	3.7	3.3
Goods-producing	3.9	4.0	3.3
Service-producing	3.1	3.6	3.2
Civilian unemployment rate[2,3]	7.3	6.5	5.6
Capacity utilization[2] (manufacturing)	80.3	81.4	84.4
Inflation expectations[4,5]			
Michigan Survey	3.3	3.8	3.7
Conference Board	4.6	4.3	4.2
Non-oil import price[6]	2.8	0.3	3.2
Consumer goods, excluding autos, food, and beverages	4.0	0.6	0.7
Autos	2.3	1.6	3.5

1. Private industry workers, periods ended in September.
2. End-of-period value.
3. Data for 1994 are not directly comparable with earlier values because of a redesign of the CPS in January 1994.
4. One-year-ahead expectations.
5. Latest reported value: December.
6. BLS import price index (not seasonally adjusted), periods ended in September.

up their pace in the past six months from that of the previous half year.

Meanwhile, the PPI for finished goods rose 0.5 percent in November--a sizable increase, but one that only partially offset a 1 percent decline registered over the previous two months. Gasoline prices increased 4-1/2 percent, likely reflecting temporary disruptions to supplies from the pipeline rupture in Texas in late October. Food prices were little changed. Excluding food and energy, the PPI edged up 0.1 percent after a drop of 0.5 percent in October. Truck prices declined again in November after a sharp drop a month earlier, the fallout of an end-of-year sales contest between Ford and GM. November producer prices were also soft for apparel and tobacco.

Consumer energy prices rose 0.7 percent in November, led by increases in gasoline prices as well as gas and electric utility rates. Although crude oil prices were generally flat over the past couple of months, retail gasoline prices in November probably were boosted by temporary supply disruptions following the pipeline ruptures in the Houston area. For natural gas, consumer prices had been declining for several months before November, reflecting pervasive weakness in spot wellhead prices through much of this year. The November increase in natural gas prices in the CPI retraced only part of the previous declines.

The prices paid by gasoline wholesalers and consumers are expected to increase in the near term, reflecting government mandates for gasoline designed to reduce emissions of carbon monoxide, benzene, and other pollutants. The reformulated gasoline had to be stocked at the wholesale level by December 1, and at the retail level by January 1. The mandate is expected to add six cents per gallon to wholesale prices and nine cents per gallon to retail prices in the approximately one-third of the national market that is affected; as a result, the mandate is expected to add two and three cents per gallon respectively to the national averages of wholesale and retailer prices. The price increase will not appear in the PPI or CPI, because (contrary to our earlier expectation) the BLS has ruled that the mandate is a quality improvement.

Consumer food prices were unchanged in October and rose only slightly in November. Meat and poultry prices were down a bit, on net, over the two months, and prices of fruits and vegetables rose moderately. Prices for other foods increased about a tenth of a percent per month, on average. The twelve-month rise in food prices held steady at 2.4 percent.

Unlike prices at the earlier stages of processing, price increases for consumer commodities other than food and energy slowed a bit over the past year. In November, they increased 0.1 percent after showing no change a month earlier. Apparel prices continued to fall, while car prices decreased 0.2 percent and truck prices were off 0 7 percent. In the past year, however, new car and truck prices have increased slightly faster than other consumer prices, while used car prices have well outpaced the consumer market basket, increasing 1 4 percent in November to a level 6-3/4 percent above a year ago

Over the past twelve months, non-energy service prices increased 3.5 percent, compared with a 3.7 percent rise over the preceding twelve-month period. Owners' equivalent rent and residential rent increased 0.3 percent in November, about in line with the pace over the past year. Medical service prices increased 0.3 percent in November and are up 5 2 percent over the past twelve months- compared with a 5.9 percent increase during the year-earlier period. In contrast, auto finance charges have increased sharply in recent months, reflecting the rise in interest rates.

The increase in materials prices has been most notable among industrial commodities. In the past month, prices of industrial materials increased sharply, with the *Journal of Commerce* Index of Industrial Commodities up 1.1 percent. In the past year, this index has moved up 22 percent. Among industrial metals, particularly large increases have been registered for copper and steel scrap. Although prices of tin and zinc fell in the past month, they had posted large increases in earlier months. Cotton and rubber prices have risen rapidly in recent months. Plywood prices have declined 6-1/2 percent in the past month but had increased rapidly in earlier months. In contrast, gold and silver have traded lower in the past month and are down from their year-earlier levels. Agricultural prices have shown no clear direction in the past month, but they had generally fallen over the summer and early fall, reflecting bumper harvests of corn and soybeans and sizable increases in livestock production. Coffee prices have weakened substantially of late, reversing some of the earlier run-up.

SPOT PRICES OF SELECTED COMMODITIES

	Current price ($)	Percent change[1] 1992	1993	To Nov. 08[2]	Nov. 08[2] to Dec. 13	Memo: Year earlier to Date
	INDUSTRIAL COMMODITIES					
Metals						
Copper (lb.)	1.390	4.1	-19.0	50.9	7.8	66.5
Steel scrap (ton)	143.500	1.1	46.8	-4.3	7.5	3.2
Aluminum, London (lb.)	.816	9.9	-10.7	66.7	-2.1	61.7
Lead (lb.)	.415	-4.3	3.0	18.4	1.5	23.8
Zinc (lb.)	.570	-10.3	-7.5	26.3	-3.4	22.2
Tin (lb.)	3.996	6.5	-14.1	25.6	-2.8	20.1
Textiles and fibers						
Cotton (lb.)	.800	-3.2	19.6	14.5	12.6	34.9
Burlap (yd.)	.292	-9.6	8.2	9.2	.9	10.2
Miscellaneous materials						
Hides (lb.)	.905	11.4	1.3	17.7	-2.7	13.1
Rubber (lb.)	.773	12.3	-7.3	58.7	8.8	72.6
	OTHER COMMODITIES					
Precious metals						
Gold (oz.)	379.100	-5.9	16.6	-.8	-1.4	-2.0
Silver (oz.)	4.750	-5.7	38.8	4.3	-9.6	-6.5
Platinum (oz.)	414.000	5.5	8.0	6.4	1.0	7.1
Forest products						
Lumber (m. bdft.)	287.000	47.5	75.8	-32.1	-8.9	-34.0
Plywood (m. sqft.)	365.000	53.5	-6.3	20.0	-6.4	18.5
Petroleum						
Crude oil (barrel)	15.650	1.4	-25.0	28.5	-9.8	14.2
Gasoline (gal.)	.469	-2.9	-31.0	49.1	-15.2	30.9
Fuel oil (gal.)	.488	21.9	-22.4	16.4	-4.1	15.7
Livestock						
Steers (cwt.)	70.000	10.6	-7.3	-3.4	.0	-3.1
Hogs (cwt.)	32.000	10.4	.6	-31.3	14.3	-23.8
Broilers (lb.)	.516	-5.3	6.1	-6.0	6.4	-.8
U.S. farm crops						
Corn (bu.)	2.170	-16.1	41.7	-29.8	7.7	-21.9
Wheat (bu.)	4.190	-11.7	5.8	10.4	-3.0	5.5
Soybeans (bu.)	5.540	1.1	24.5	-20.9	.9	-18.0
Other foodstuffs						
Coffee (lb.)	1.465	17.9	-2.3	182.9	-19.7	132.5
Memo:						
Exchange value of the dollar (March 1973=100)	89.663	10.1	3.4	-9.6	4.1	-6.5
Yield on Treasury bill, 3-month[3]	5.780	-68	-14	217	55	274

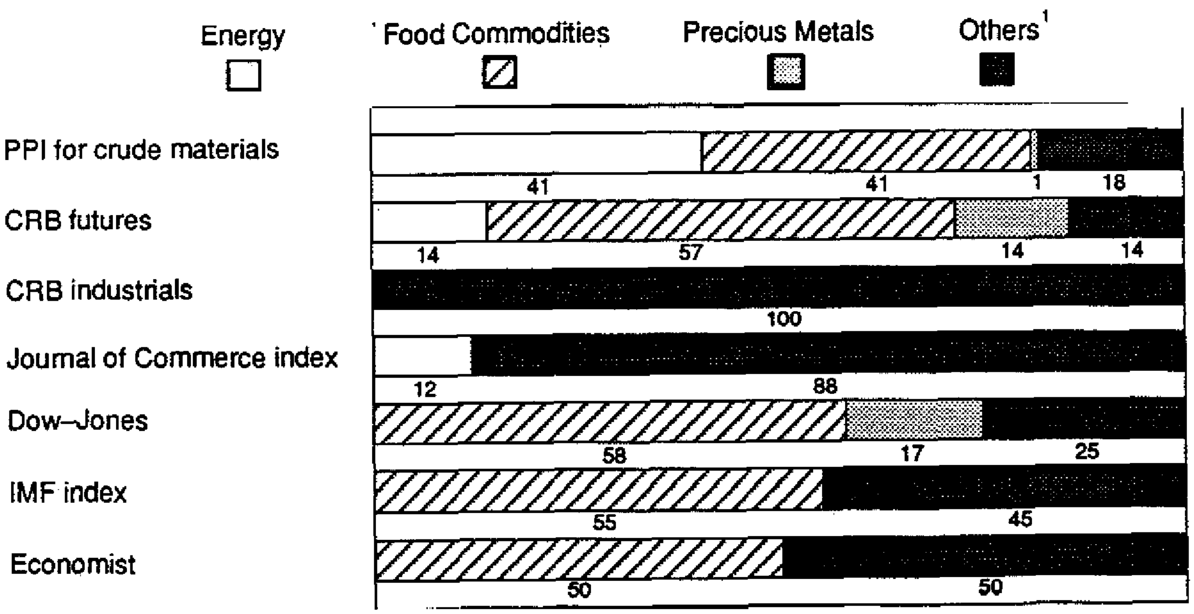
1. Changes, if not specified, are to the last week of the year indicated and from the last week of the preceding year.
2. Week of the November Greenbook.
3. Changes are in basis points.

COMMODITY PRICE INDEXES

PPI for crude materials[3]	Nov.	n.a.	n.a.	-1.6	n.a.	-2.7
Foods and feeds	Nov.	n.a.	n.a.	-10.6	n.a.	-9.1
Energy	Nov.	n.a.	n.a.	0.4	n.a.	-5.5
Excluding food and energy	Nov.	n.a.	n.a.	13.9	n.a.	15.4
Excluding food and energy, seasonally adjusted	Nov.	n.a.	n.a.	14.4	n.a.	15.7
Commodity Research Bureau						
Futures prices	Nov. 29	n.a.	n.a.	3.8	-1.4	5.8
Industrial spot prices	Nov. 22	n.a.	n.a.	22.7	2.4	28.6
Journal of Commerce industrials	Nov. 29	n.a.	n.a.	20.3	1.3	23.4
Metals	Nov. 29	n.a.	n.a.	29.0	1.2	38.8
Dow-Jones Spot	Nov. 29	n.a.	n.a.	14.0	-0.4	18.5
IMF commodity index[3]	Oct.	-2.6	2.4	n.a.	n.a.	18.5
Metals	Oct.	-3.1	-14.4	n.a.	n.a.	30.3
Nonfood agricultural	Oct.	2.4	0.2	n.a.	n.a.	12.7
Economist (U.S. dollar index)	Dec. 06	1.6	9.1	30.7	-1.6	30.7
Industrials	Dec. 06	4.5	4.4	31.3	3.6	39.4

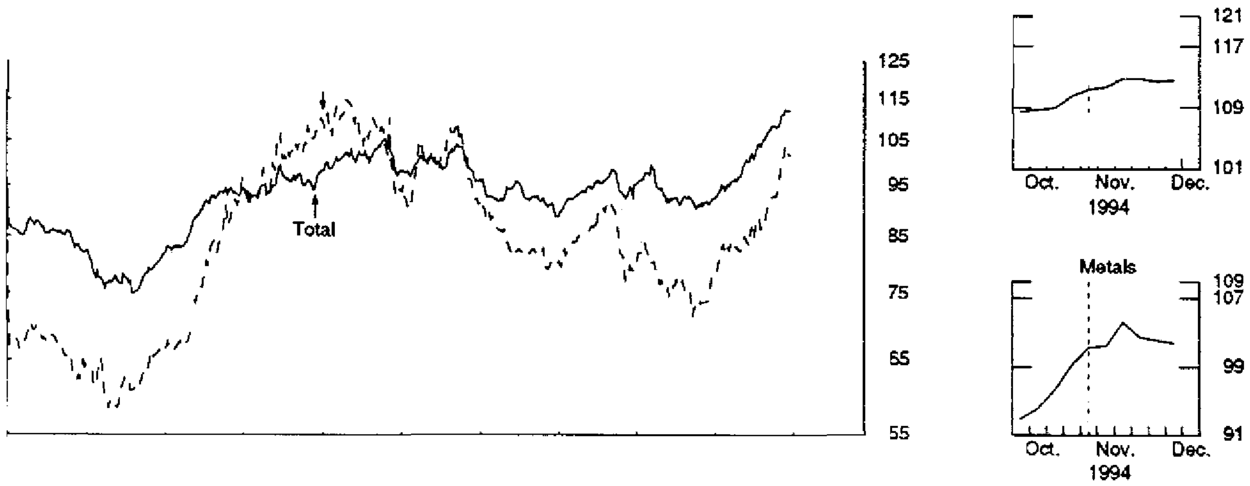
Note. Not seasonally adjusted. Copyright for Journal of Commerce data is held by CIBCR, 1994.
1. Change is measured to end of period, from last observation of previous period.
2. Week of the November Greenbook.
3. Monthly observations. IMF index includes items not shown separately.
n.a. Not available.

INDEX WEIGHTS

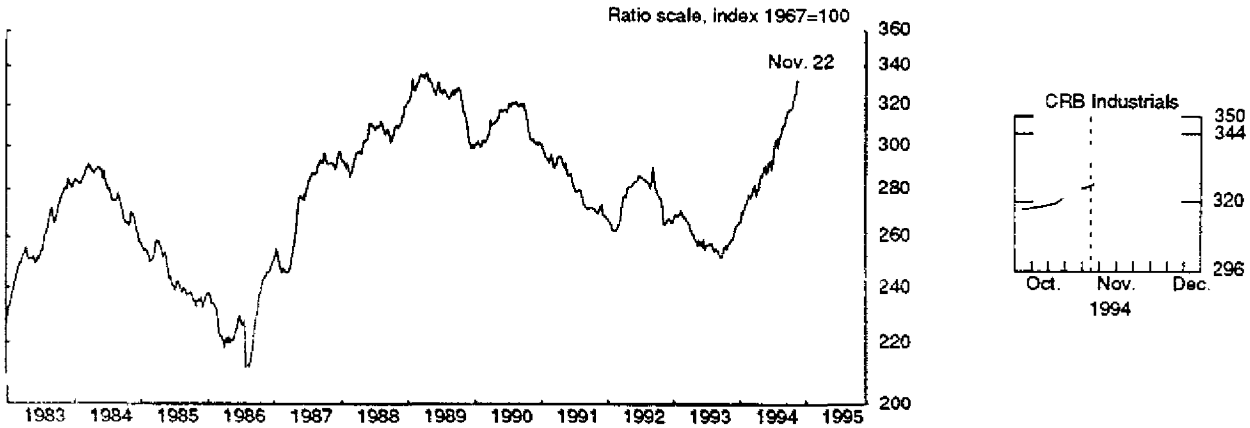


1. Forest products, industrial metals, and other industrial materials

Commodity Price Measures



CRB Spot Industrials



CRB Futures

Note. Weekly data, Tuesdays. Vertical lines on small panels indicate week of last Greenbook. The Journal of Commerce index is based almost entirely on industrial commodities, with a small weight given to energy commodities, and the CRB spot price index consists entirely of industrial commodities, excluding energy. The CRB futures index gives about a 60 percent weight to food commodities and splits the remaining weight roughly equally among energy commodities, industrial commodities and precious metals. Copyright for Journal of Commerce data is held by CIBCR, 1994.

DOMESTIC FINANCIAL DEVELOPMENTS

SELECTED FINANCIAL MARKET QUOTATIONS[1]
(Percent except as noted)

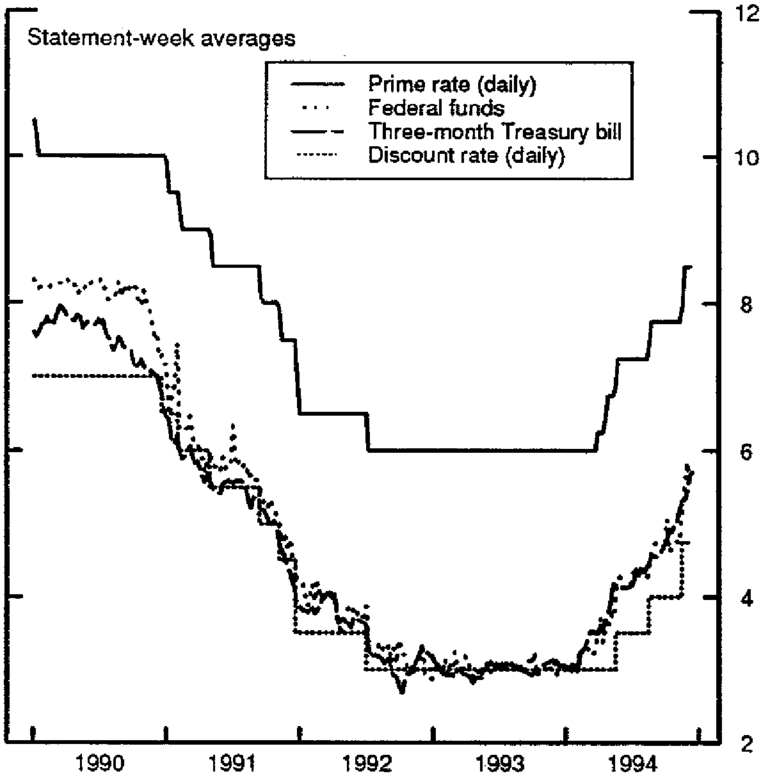
Instrument	1993 Oct lows	1994 Feb 3	1994 FOMC,* Nov 15	1994 Dec 13	Change to Dec 13, 1994: From Oct 93 lows	From Feb 3	From FOMC,* Nov 15
SHORT-TERM RATES							
Federal funds[2]	3.07	3.07	4.75	5.48	2.41	2.41	.73
Treasury bills[3]							
3-month	3.01	3.13	5.28	5.78	2.77	2.65	.50
6-month	3.09	3.27	5.69	6.38	3.29	3.11	.69
1-year	3.23	3.52	6.11	6.84	3.61	3.32	.73
Commercial paper							
1-month	3.13	3.16	5.32	6.13	3.00	2.97	.81
3-month	3.23	3.25	5.76	6.32	3.09	3.07	.56
Large negotiable CDs[3]							
1-month	3.08	3.11	5.27	6.08	3.00	2.97	.81
3-month	3.22	3.25	5.71	6.33	3.11	3.08	.62
6-month	3.23	3.41	6.01	6.85	3.62	3.44	.84
Eurodollar deposits[4]							
1-month	3.06	3.06	5.25	6.06	3.00	3.00	.81
3-month	3.25	3.25	5.75	6.31	3.06	3.06	.56
Bank prime rate	6.00	6.00	7.75	8.50	2.50	2.50	.75
INTERMEDIATE- AND LONG-TERM RATES							
U.S. Treasury (constant maturity)							
3-year	4.06	4.60	7.37	7.80	3.74	3.20	.43
10-year	5.19	5.81	7.94	7.83	2.64	2.02	.11
30-year	5.78	6.31	8.09	7.86	2.08	1.55	.23
Municipal revenue[5] (Bond Buyer)	5.41	5.49	7.23	7.17	1.76	1.68	.06
Corporate--A utility, recently offered	6.79	7.35	8.89	8.78	1.99	1.43	.11
Home mortgages[6]							
FHLMC 30-yr. fixed rate	6.74	6.97	9.19	9.15	2.41	2.18	.04
FHLMC 1-yr. adjustable rate	4.14	4.12	6.01	6.56	2.42	2.44	.55

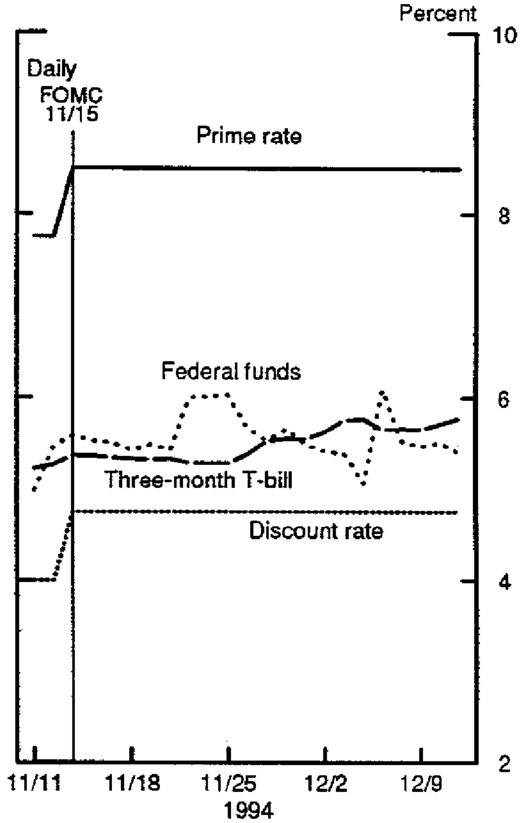
Stock exchange index	Record high Level	Record high Date	1989 Low, Jan. 3	1994 FOMC,* Nov 15	1994 Dec 13	Percentage change to Dec 13: From record high	From 1989 low	From FOMC,* Nov 15
Dow-Jones Industrial	3978.36	1/31/94	2144.64	3829.73	3715.34	-6.61	73.24	-2.99
NYSE Composite	267.71	2/2/94	154.00	254.84	245.72	-8.21	59.56	-3.58
NASDAQ (OTC)	803.93	3/18/94	378.56	768.14	719.49	-10.50	90.06	-6.33
Wilshire	4804.31	2/2/94	2718.59	4611.07	4416.93	-8.06	62.47	-4.21

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 Dec 21, 1994.
3. Secondary market.
4. Bid rates for Eurodollar deposits at 11a.m. London time.
5. Most recent observation based on one-day Thursday quote and futures market index changes.
6. Quotes for week ending Friday previous to date shown.
* Figures are as of the close on Nov. 14, 1994.

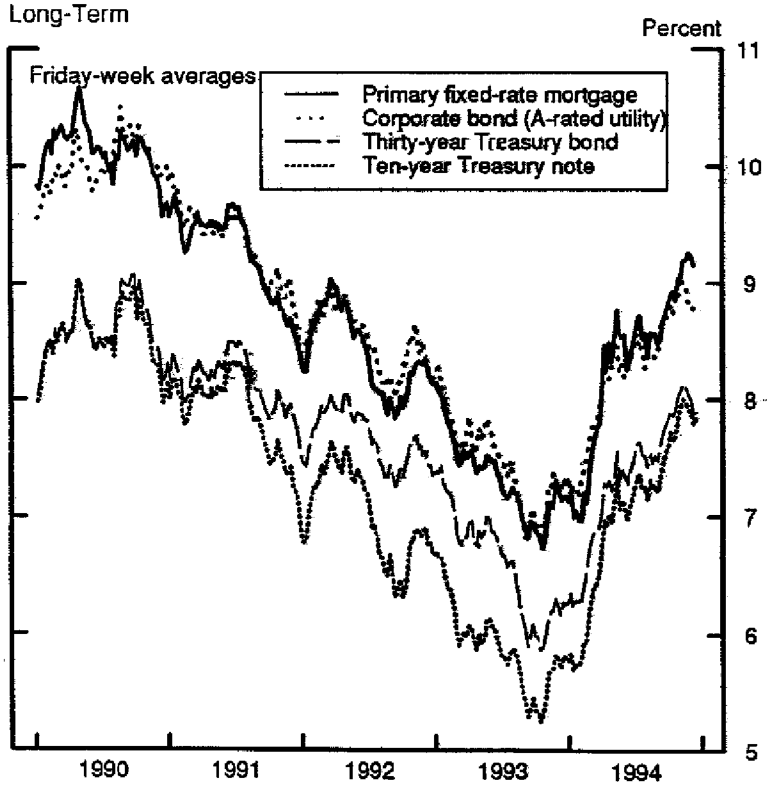
Selected Interest Rates

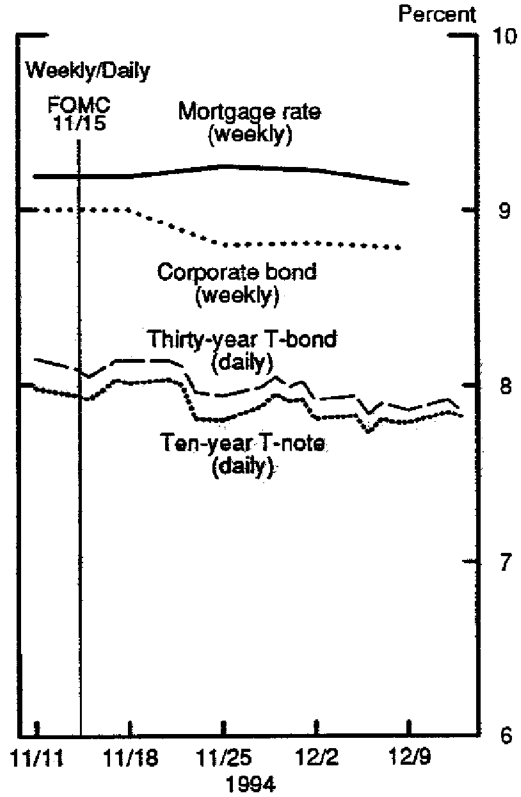
Short-Term





Long-Term





Note. Statement weeks are plotted through Dec. 7 , Friday weeks through Dec. 9.

The System action announced after the November FOMC meeting--a 75 basis point increase in the discount rate that was fully passed through to the federal funds rate--was more forceful than generally anticipated in the markets. Other money market yields firmed in response, and major commercial banks promptly raised their prime rates by an equal amount, to 8-1/2 percent. But the large move--and the unanimous discount rate vote--evidently was taken as a signal that the Federal Reserve was firmly committed to taking such steps as might be needed to contain inflation: Rates further out the yield curve increased only a few basis points, and the thirty-year Treasury bond yield actually fell on the day of the policy action.

Bond yields continued to move down over the balance of the period, despite surprising and persistent strength of incoming data. These data were read as suggesting that considerably tighter policy was likely to be needed, and short-term rates rose considerably. In early December, financial markets were disrupted for a time by the news of Orange County's difficulties. Municipal bond markets were affected by concerns that other issuers might have similar problems and that tax-exempt mutual funds would experience accelerated redemptions. Spreads on federal agency securities widened somewhat in response to sales of agency issues held as collateral by Orange County creditors, and the equities of such agencies fell sharply. After a period of several days, however, as only scattered reports of other such situations emerged, markets settled down. Mutual funds generally reported little change in investor interest, with reports of unusual redemptions limited to money funds that specialized in California paper. By December 13, both agency and municipal spreads had returned to levels prior to the Orange County problems, although individual tax-exempt borrowers, especially those associated with the Orange County pool investors, continued to experience difficulties. Gross issuance in tax-exempt markets also was disrupted only briefly.

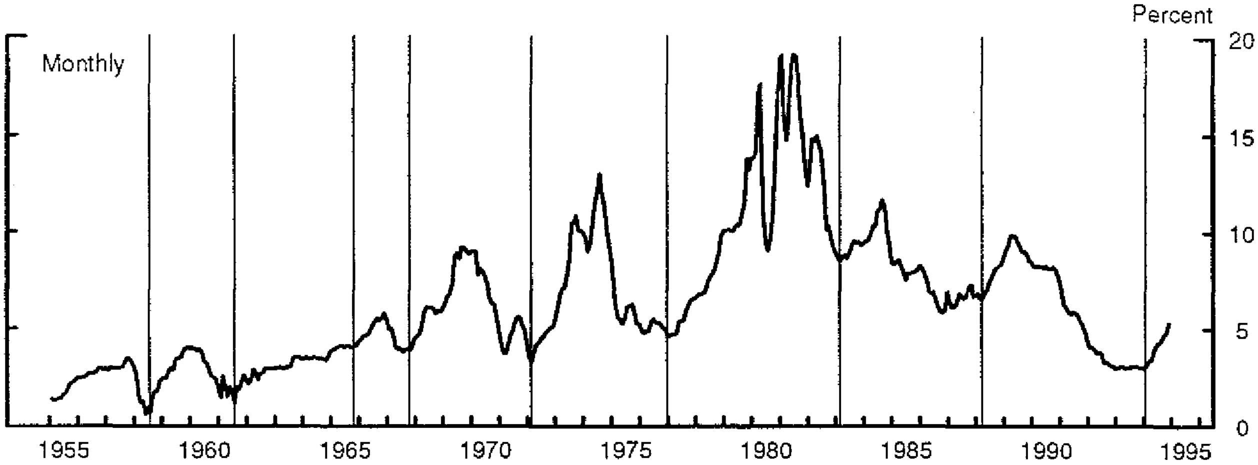
More broadly, borrowing by businesses and households has continued at a brisk pace. Long-term bond offerings by nonfinancial firms remained fairly weak, as these firms have continued to display a preference for short-term financing; the latter was reflected in further solid growth of business loans at banks and in commercial paper issuance. Mortgage lending is estimated to have proceeded near its third-quarter pace, supported by the firmness of home sales through October. Consumer credit recorded double-digit growth again in October.

Bank credit expanded at an annual rate of 3-1/4 percent in November, as robust loan growth once again was partly financed by run-offs of security holdings. M3 growth continued to be supported by rapid expansion of large time deposits to help fund bank credit. M2 rose a little in November, the first monthly increase since July, lifted by the rapid growth of small time deposits and retail money funds.

Interest Rates

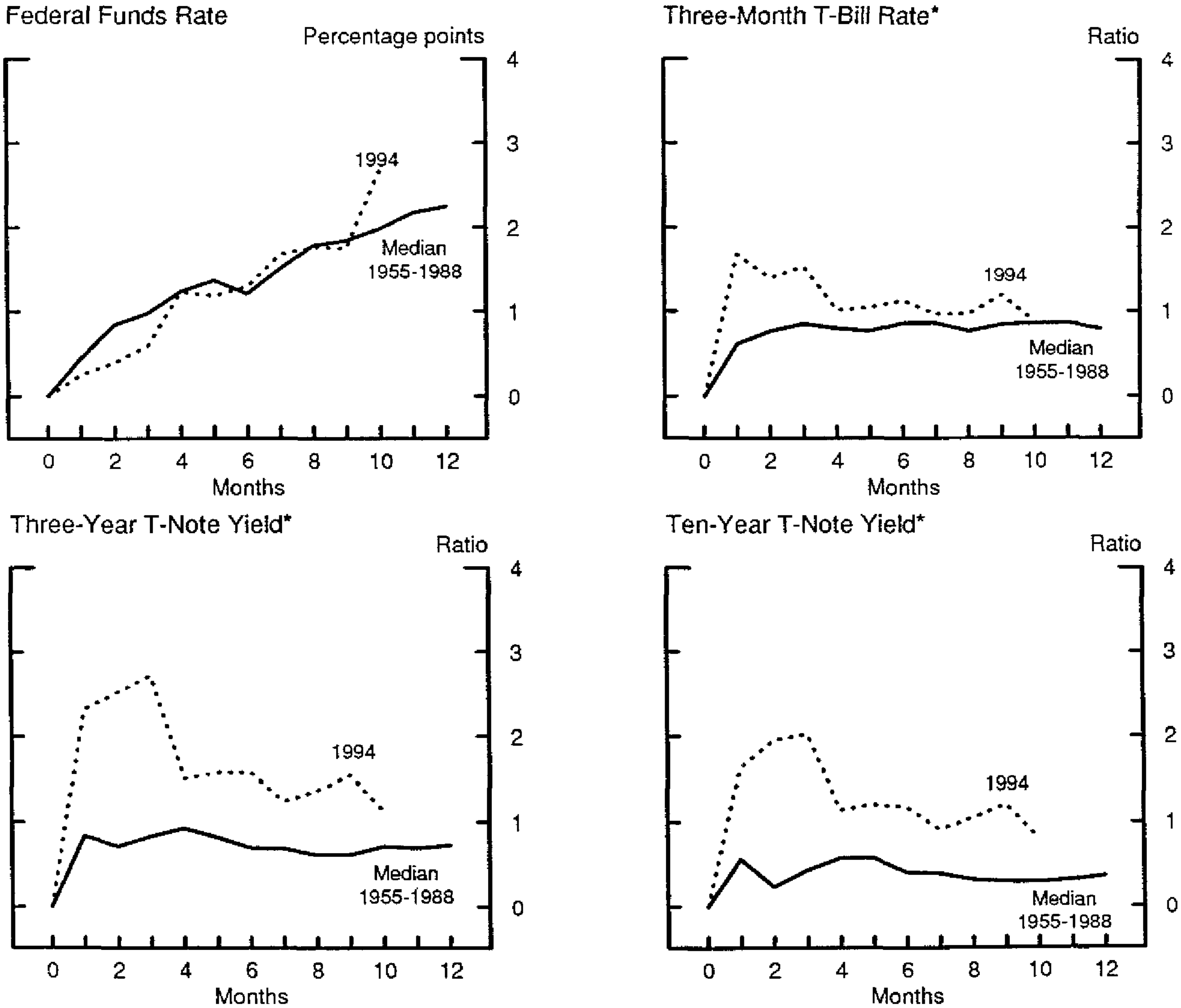
The rise in short-term rates and drop in bond yields combined to produce the flattest yield curve (thirty-year minus three-month rate) since December 1991. Contributing to the upward pressure on very short-term rates was the approach of year-end. One-month commercial paper rates, for example, jumped 34 basis points on the day that maturity first fell in 1995, implying a turn-of-year premium of almost 3 percentage points. Orange County's chapter 9 bankruptcy filing may have added upward pressure on Treasury yields; in particular, dealers' efforts to sell the collateral they claimed when Orange County ran dry of funds may have affected the three- to

Upward Turning Points in the Federal Funds Rate



Note. Vertical lines mark the onset of sustained increases in the federal funds rate.

Movement of Market Rates Following Upward Turning Points in the Federal Funds Rate



* As a ratio to the cumulative change in the federal funds rate.

five-year sector, where rates are up 20 to 40 basis points over the intermeeting period.

With the November move, System actions in 1994 have slightly outpaced the median increase in the federal funds rate in episodes of policy tightening since 1955 (chart). In those eight prior periods, the federal funds rate rose just over 2 percentage points in the first ten months of rising short-term rates, compared with the 2-1/2 percentage point increase since February 1994. It is the market reaction in the wake of those policy moves that stands out more. Short-term market rates rose by a larger amount in the early stages of tightening this year than the historical record would suggest. This pattern may partly reflect the System's announced intention to move to policy "neutrality" early this year, enabling markets to anticipate further actions. In addition, the incoming news suggested that aggregate demand was especially strong and the margin of slack was dwindling rapidly. More recently, though, the pass-through to the three-month Treasury bill rate, at about 75 percent of the total change in the policy rate, has been similar to the average experience over the 1955-to-1988 period. Three- and ten-year note yields have about followed that same pattern: More of the market response came sooner this time around, but the reaction looks less anomalous ten months after the onset of tightening.

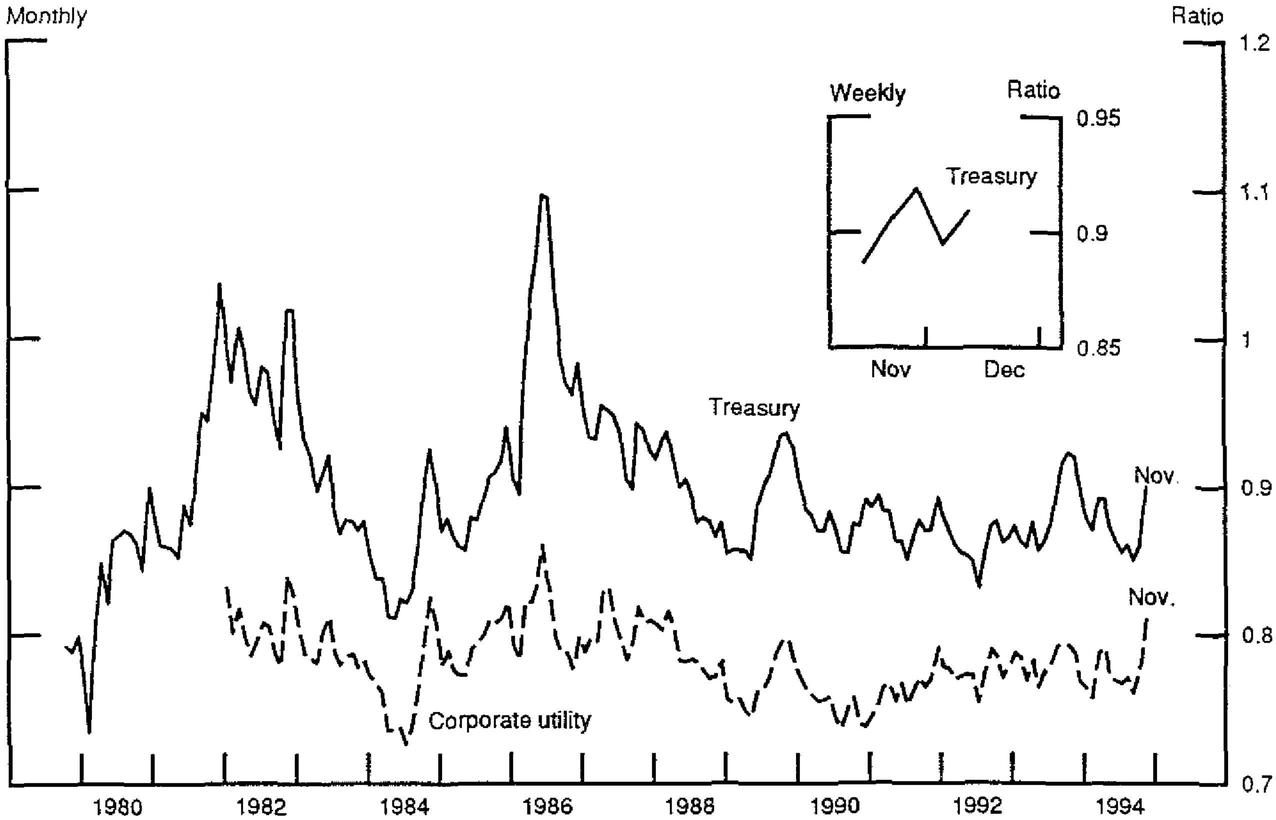
Municipal Markets

Revelation of the financial difficulties of Orange County dominated municipal and other financial market news in early December. The Orange County investment pool managed commingled assets of 187 municipalities and other agencies, including Orange County. The fund engaged in repurchase agreements to lever its $7-1/2 billion in capital into $20 billion in securities, mostly debt of federally sponsored agencies (specifically, Fannie Mae and the Federal Home Loan Banks). With the fund's management betting in 1993 and throughout 1994 that rates would fall (or at least would not rise much), most of those securities had maturities of five to twenty years. More than 40 percent of the fund's assets were structured notes with coupons that vary inversely with short-term market rates. With interest rates rising fast and the fund deep in the red, the county and its fellow investors added to their bets last summer by issuing nearly $1 billion in short-term taxable notes.

On December 2, the county released to the public an estimate that its investment fund had lost $1-1/2 billion, or about one-fifth, of its value. More recent estimates place the size of the loss at upwards of $2 billion. On December 6, when dealers became reluctant to roll over maturing repurchase agreements, or demanded additional collateral, and concerns grew that its own pool investors would clamor for their funds, Orange County filed for chapter 9 bankruptcy protection; it actually defaulted on $110 million of taxable notes on December 8. With few exceptions, dealers, who held $13 billion of collateral provided by Orange County for money lent to the investment pool under RP agreements, sold off those securities in the secondary market, although their right to do so under chapter 9 remains unclear. Standard & Poor's lowered its rating of the county to CCC from AA-, and Moody's suspended ratings on all noninsured Orange County bonds.

The reaction to these developments was widespread. Municipal bond prices fell; dealers bid for uninsured Orange County debt at deep discounts, although no trading has been reported, and its insured debt traded for a while at a spread of 40 basis points over other municipal securities, but such spreads have now dissipated. Much of the debt issued by California municipalities is uninsured,

Ratio of Tax-Exempt Yields to Yields on Treasury and Corporate Utility Securities



Note. Weekly data from Nov. 10 to Dec. 8.

GROSS OFFERINGS OF MUNICIPAL SECURITIES[1]
(Monthly rates, not seasonally adjusted, billions of dollars)

	1992	1993	1994 Q2	1994 Q3	1994 Sept.	1994 Oct.	1994 Nov.
Total tax-exempt	22.2	27.2	17.0	16.1	9.1	12.0	12.0
Long-term	18.9	23.3	13.3	11.1	7.8	10.5	10.8
Refundings[2]	10.4	15.7	3.9	1.9	1.7	1.6	1.4
New capital	8.5	7.6	9.4	9.2	6.1	8.9	9.4
Short-term	3.3	3.9	3.7	5.0	1.3	1.5	1.2
Total taxable	.6	.7	.4	.3	.5	2.4	.4

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

leaving mutual funds, households, and other holders to bear the brunt of any losses stemming from defaults. But the county may still decide to make its investors whole, and some recoveries may be made through lawsuits against brokers who sold securities to Orange County.

With the price of municipal securities down, the net asset value of tax-exempt money market funds declined. Reports of unusual outflows from these funds, however, have been limited to funds that specialize in California paper. Several fund advisors have requested SEC permission to shore up their funds' portfolios in order to prevent them from "breaking the buck."

Earlier in the intermeeting period, the ratio of tax-exempt to taxable yields had risen above 91 percent amid a large amount of muni bond fund redemptions. Subsequently, large purchases by insurance companies led to a rally in municipals, which pushed the ratio below 90 percent. The Orange County developments reversed that rally, sending the ratio back up to 91 percent. The ratio is at its highest level in five years, apart from a few months in late 1993 when heavy volume boosted municipal bond rates (chart). In the first week of December, tax-exempt bond funds experienced modest inflows, but reports from a number of funds suggest that outflows may have resumed more recently.

Gross issuance of long-term tax-exempt debt remained light in November, owing to a continued low level of refunding activity. Retirements probably roughly offset gross issuance last month, leaving the stock of long-term tax-exempt debt about unchanged. The level of such debt outstanding is estimated to have fallen about $5 billion since the beginning of the year. Heavy retirements scheduled to occur in December ensure a further run-off of long-term debt this month.

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

Item	1994 Q3	1994 Q4[p]	1994 Oct.	1994 Nov.[p]	1994 Dec.[p]
Total surplus/deficit (-)	-53.4	-75.2	-31.4	-43.4	-0.4
Means of financing deficit:					
Net cash borrowing/repayments (-)	37.1	52.2	27.1	35.9	-10.8
Nonmarketable	-3.4	-0.9	-0.6	-.7	0.3
Marketable	40.5	53.1	27.7	36.6	-11.2
Bills	-1.2	29.3	20.2	20.2	-11.2
Coupons	41.7	23.9	7.5	16.4	.0
Decrease in the cash balance	15.0	11.2	-0.5	9.8	1.9
Other[2]	1.2	11.7	4.8	-2.3	9.3
Memo: Cash balance, end of period	35.9	24.7	36.4	26.6	24.7

1. Data reported on a payment basis.
2. Includes checks issued less checks paid, accrued items, and other transactions.
p--projected.

Note: Details may not add to totals because of rounding.

NET CASH BORROWING OF GOVERNMENT SPONSORED ENTERPRISES[1]
(Billions of dollars)

Agency	1994 Q1	1994 Q2	1994 Q3	Oct.
FHLBs	5.7	13.5	13.6	11.5
FHLMC	12.9	10.4	10.6	5.62
FNMA	15.3	11.5	11.4	2.67
Farm Credit Banks	-0.7	1.3	0.6	-1.41
SLMA	5.9	2.3	1.8	.10

1. Excludes mortgage pass-through securities issued by FNMA and FHLMC.

Treasury and Sponsored Agency Financing

Yield spreads for federally sponsored credit agencies widened considerably over the intermeeting period. Some market participants estimated that the bankruptcy filing by Orange County may have caused spreads on short-term instruments to increase 10 to 15 basis points, as dealers sold collateral backing Orange County's repurchase agreements. But spreads had been widening for unrelated reasons throughout November. The value of the stock of major agencies fell; the stocks of Fannie Mae and Freddie Mac, in particular, dropped more than 2 percent on December 7, the day after the bankruptcy filing. These agencies, which grew rapidly in 1994, may feel compelled to scale back the aggressive expansion of their balance sheet if the spreads remain wide.

The staff anticipates that the Treasury will finance the projected $79 billion fourth-quarter fiscal deficit partly by borrowing $55 billion from the public and by drawing down its cash balance by $9 billion. With no long-term bond in its midquarter refunding, the Treasury has relied heavily on bills, which are expected to raise $31 billion this quarter. Since September, the Treasury has increased the size of the weekly bill auctions, from $23 billion to $27 billion, while the sizes of the coupon auctions have been kept unchanged. It also auctioned three cash management bills, raising $35 billion, to help cover seasonal financial needs.

Monetary Aggregates and Bank Credit

M2 grew at a 1 percent annual rate in November--the first monthly increase since July. From the fourth quarter of 1993 to November, M2 increased at that same rate, leaving it at the lower bound of its growth cone.

The rise in M2 last month was mostly accounted for by rapid increases in small time deposits and retail money funds, whose rates

MONETARY AGGREGATES
(Based on seasonally adjusted data, except where noted)

Aggregate or component	1993	1994 Q2	1994 Q3	1994 Sept	1994 Oct	1994 Nov (pe)	1993:Q4 to Nov 94 (pe)	Level (bil $) Oct. 94
Aggregate	Percentage change (annual rate)[1]							
1. M1	10.5	1.9	3 0	1.0	-3.6	-1	2¼	1148 5
2 M2	1 4	1 9	0.8	-0.4	1.1	1	1	3593 4
3. M3	0 7	0.7	1.7	1.5	3.5	2	1¼	4261.2
Selected components								
4 Currency	10.3	10 6	9.1	6 6	9.0	10	10½	349 9
5. Demand deposits	13 3	-2.5	1 1	1 5	-6.5	-7	½	385 9
6. Other checkable deposits	8.4	-1 1	-0.4	-4.7	-11.2	-5	-2¼	404 4
7 M2 minus M1	-2 3	2.0	-0 3	-1.1	0.1	1	½	2444 9
8 Savings deposits	2 9	-2.1	-6.6	-8.2	-13 3	-14	-4¼	1173.4
9. Small time deposits	-10 5	-2.9	4.4	8.5	15.6	19	2	793 4
10. Retail money market funds	-2.1	17.8	1 0	-2.0	8.9	16	6¾	365 0
11. Overnight RPs, n.s.a.	21.2	16.9	22.2	25.2	17 8	-1	21	88 9
12 Overnight Eurodollars, n s.a.	-15 5	31.5	122.9	-9.6	115 7	53	49	27 3
13 M3 minus M2	-3.3	-6.2	7.1	12 1	28.9	12	2¾	667 9
14 Large time deposits, net[4]	-6 9	-3.2	9 2	21 8	28.0	22	6½	355 0
15. Institution-only money market mutual funds	-5.4	-22.8	-5 8	-9 9	52.9	2	-10	175 3
16. Term RPs, n s.a.	18 8	24.6	10.6	13.2	-1.2	5	5¾	101 2
17. Term Eurodollars, n s a	0 0	16 1	23.7	11.6	18.4	43	16¾	53 0
Memo								
18 Monetary base	10 4	8 3	7 4	5 3	6 7	9	8½	413.3
19 Household M2[2]	0 1	1 7	-0 7	-1 1	-0.6	2	¼	3084.9
	Average monthly change (billions of dollars)[3]							
Memo								
20 Managed liabilities at commercial banks (lines 22 + 23)	5.5	12.2	16.8	20.8	-4.2	-3	. .	982 7
21 Large time deposits, gross	-2.3	1.6	4.3	5.5	5.8	7	.	357 2
22. Nondeposit funds	7.8	10.7	12.4	15.3	-10.0	-10	. . .	625 5
23. Net due to related foreign institutions	4.5	8.7	10.3	4 4	-1 6	-5	. . .	214 0
24. Other[5]	3.3	2.0	2.1	10 9	-8.3	-4	. .	411 6
25. U.S. government deposits at commercial banks	0.2	-0.4	-1.1	3.3	-1.2	2	. . .	17 3

1. For the years shown, fourth quarter-to-fourth quarter percent change. For the quarters shown, based on quarterly averages.
2. Sum of seasonally adjusted currency, retail money funds, and other checkable, savings, and small time deposits.
3. For years, "average monthly change" is based on the dollar change from December to December For quarters, it is based on the dollar change across the last months of quarters.
4 Net of holdings of money market mutual funds, depository institutions, U S. government, and foreign banks and official institutions.
5. 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 estimate
pe Preliminary estimate n.s.a Not seasonally adjusted.

kept pace with increases in market rates in recent months, at least until the mid-November tightening. In addition, small time deposits have probably been buoyed by banks' increased issuance of brokered CDs, as indicated by Call Report data through September. Market sources suggest that rates on brokered deposits have risen more than those on nonbrokered CDs this year. Security dealers may be using these instruments to lure customers moving out of mutual funds, and banks can bid up rates on brokered CDs without raising the structure of rates on their core retail deposit business.

In contrast, rates on OCDs and saving deposits have moved up only slightly in recent months, considerably widening the opportunity costs of such deposits. In consequence, these liquid deposit components of M2 continued to contract in November.

A portion of the growth in M2 in November may mirror the net redemptions of bond and stock mutual funds (chart). Outflows from bond funds apparently accelerated in November, while inflows to equity funds slowed early in the month and briefly turned to outflows around Thanksgiving. Investors may have channeled some of these mutual funds outflows into direct holdings of securities, consistent with heavy net noncompetitive tenders at Treasury auctions of bills and notes again in November.

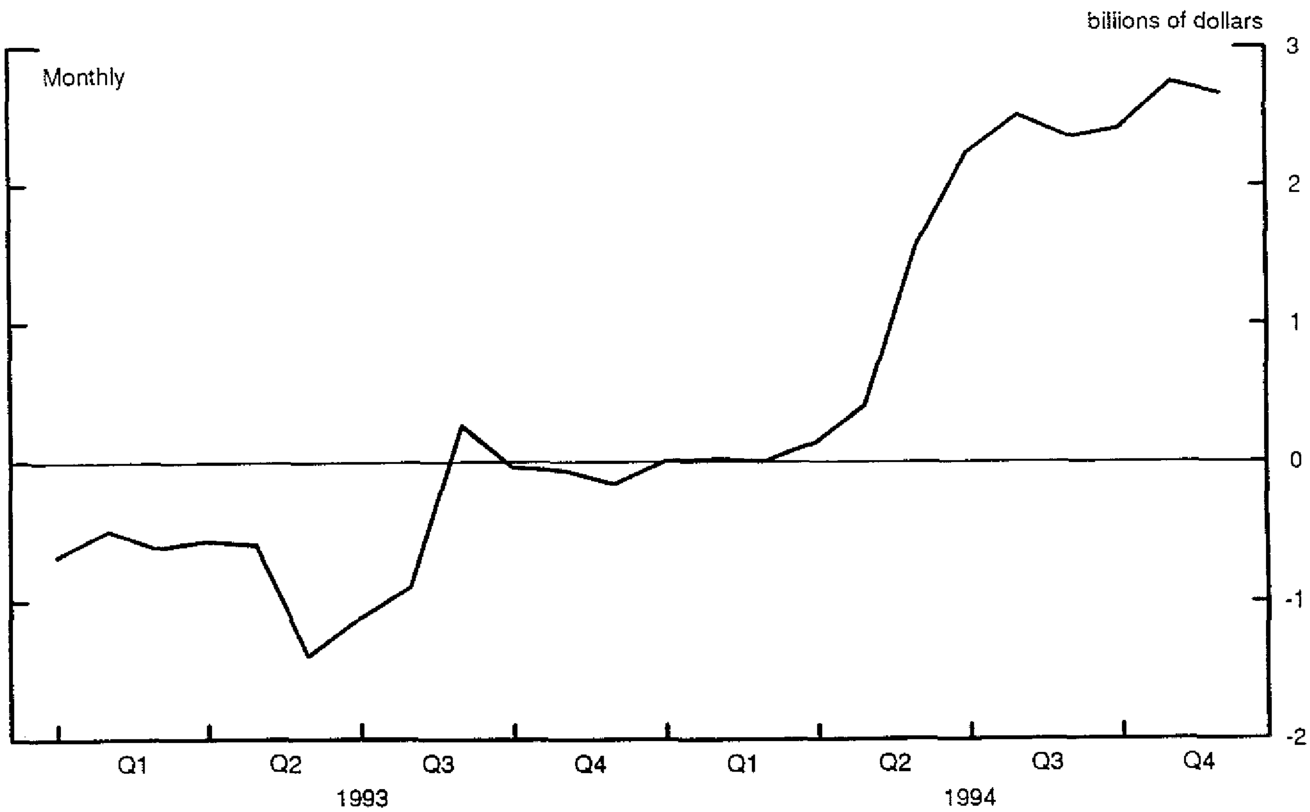
M3 grew at a 2 percent annual rate in November, a bit slower than in October. The continued expansion of this aggregate has positioned it well within its annual range. Growth in the non-M2 component of M3 slowed from its exceptional October pace, as institution-only money market mutual funds, which had spurted in October, were about flat for the month. Yields on these funds lag market rates, inducing some investors to shift into direct holdings of the underlying instruments after the mid-November tightening. Growth of large time deposits, while slowing slightly from October's

NET SALES OF MUTUAL FUNDS CLASSIFIED BY TYPE
(Billions of dollars, monthly rate, NSA)

	1994							Memo: Oct.
	Q1	Q2	Q3	Aug.	Sept.	Oct.	Nov.[e]	assets
Total stock	13.7	10.9	11.2	14.5	9.4	9.5	2.2	891.0
International	6.2	3.0	3.9	5.5	2.8	3.3	1.0	170.1
Domestic	7.6	8.0	7.3	8.9	6.6	6.2	1.2	720.8
Total bond	3.7	-0.8	-1.3	-0.8	-2.1	-6.0	-12.0	746.4
GNMA	-1.6	-1.4	-1.0	-0.9	-1.0	-1.3	-1.8	56.6
Government	-1.1	-1.6	-1.5	-1.3	-1.5	-2.1	-2.4	91.5
High-yield	0.0	0.5	0.1	0.3	0.1	-0.3	-0.5	46.0
Tax-exempt	1.0	-0.3	0.0	-0.2	-1.0	-2.0	-4.7	236.4
Income	4.9	2.2	1.7	1.7	2.1	0.3	-1.2	219.0
Other	0.5	-0.2	-0.6	-0.5	-0.9	-0.7	-1.4	61.3
Total money fund	5.7	-1.9	3.2	-10.6	11.4	11.2	7.5	597.4
Taxable	1.9	-0.7	3.4	-10.3	12.0	10.5	4.9	486.2
Tax-exempt	3.8	-1.2	-0.2	-0.2	-0.5	0.7	2.6	111.2

e Estimate.
Source: Investment Company Institute.

Net Noncompetitive Tenders



Note. The series is a 3-month moving average of total net noncompetitive tenders.

brisk pace, nevertheless proceeded at an annual rate exceeding 20 percent for the third consecutive month. The strength in large time deposits over the last few months has contributed to the funding of rapid loan growth in the face of weak retail deposits, compensating for the weakness in other managed liabilities. To fund credit growth over much of 1994, banks had been relying heavily on managed liabilities; although credit growth continued, these liabilities declined in both October and November.

Bank credit grew at an annual rate of 3-1/4 percent in November. Following the same pattern since August, robust loan growth offset runoffs in security holdings. Consumer loans decelerated to an annual rate of 7-1/2 percent from more than twice that pace in October, partly because of increased securitization, while the growth of real estate loans accelerated to 7-3/4 percent. About half of the pickup in real estate loans was accounted for by the purchase of a thrift by a large commercial bank and half by a slowing of the run-off in real estate loans at branches and agencies of foreign banks.

Growth in business loans remained robust, at a 9-1/2 percent annual rate in November. In addition to a shift from longer-term sources of funds owing to relatively high bond yields, this growth may be due in part to a continued easing of terms and standards for commercial and industrial loans, as reported by respondents to the November senior loan officer opinion survey. Recently available data on loan rates from the November survey of terms of bank lending, conducted the week before the most recent tightening, show a narrowing of spreads for small loans, while spreads remained narrow for larger loans (chart).

In the last several senior loan officer surveys, banks have attributed their easing of terms and standards to increased

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

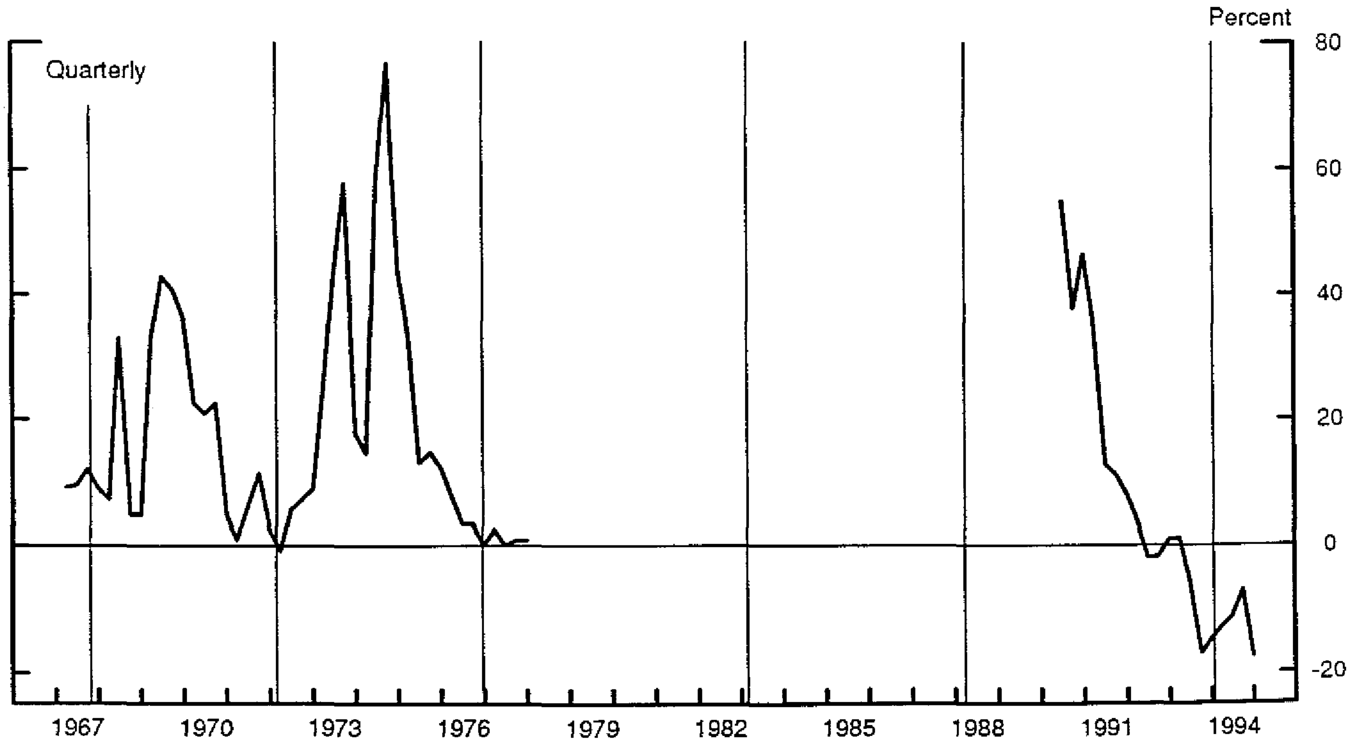
Type of credit	Dec. 1992 to Dec. 1993	1994 Q2	1994 Q3	1994 Sep	1994 Oct	1994 Nov	Level, Nov 1994 ($billions)
	Commercial bank credit						
1. Total loans and securities	5.3	5.8	6.8	3.4	2.8	3.2	3,294.9
2. Securities	8.6	6.3	-3.4	-5.2	-12.0	-9.2	949.9
3. U.S. government	9.6	2.6	-6.1	-9.8	-19.9	-13.7	719.5
4. Other	4.8	19.3	5.9	10.7	13.2	5.8	230.5
5. Loans	4.0	5.5	11.2	6.9	9.0	8.3	2,345.0
6. Business	-1.8	10.1	11.5	8.5	11.3	9.5	638.7
7. Real estate	4.5	5.4	9.6	9.3	5.8	7.7	989.9
8. Consumer	9.0	13.4	18.2	13.7	19.0	7.6	444.6
9. Security	35.8	-34.5	-36.7	-92.8	50.3	20.0	73.3
10. Other	-.7	-7.0	21.8	15.1	-18.5	4.9	198.5
	Short- and intermediate-term business credit						
11. Business loans net of bankers acceptances	-2.1	9.7	11.6	8.6	12.6	10.8	630.2
12. Loans at foreign branches[2]	-12.1	18.8	17.9	21.0	-36.1	5.3	22.7
13. Sum of lines 11 and 12	-2.5	10.0	11.7	8.9	10.9	10.6	652.9
14. Commercial paper issued by nonfinancial firms	4.4	-9.2	11.0	15.8	32.8	22.8	160.7
15. Sum of lines 13 and 14	-1.2	6.2	11.7	10.4	14.9	12.8	813.5
16. Bankers acceptances, U.S. trade-related[3,4]	-12.2	-13.3	-3.9	-11.8	-35.8	n.a.	19.5[5]
17. Loans at finance companies[4]	1.3	13.5	7.2	22.0	17.0	n.a.	343.9[5]
18. Total (sum of lines 15, 16, and 17)	-.7	7.9	10.1	13.2	14.8	n.a.	1,168.3[5]

1. Except as noted, levels are averages of Wednesday data and percentage changes are based on averages of Wednesday data; data are adjusted for breaks caused by reclassification; changes are measured from preceding period to period indicated.
2. Loans to U.S. firms made by foreign branches of domestically chartered banks.
3. Acceptances that finance U.S. imports, U.S. exports, and domestic shipment and storage of goods.
4. Changes are based on averages of month-end data.
5. October 1994.
n.a. Not available.

competition. This relatively more aggressive lending behavior may reflect the improved quality of bank balance sheets. The September Call Report data show continued sharp declines in delinquency and charge-off rates for all three major loan types (chart, page 16), as well as a preservation of comfortable capital ratios. Indeed, this relaxation of standards on business lending stands in contrast to previous episodes of monetary tightening (chart, below).

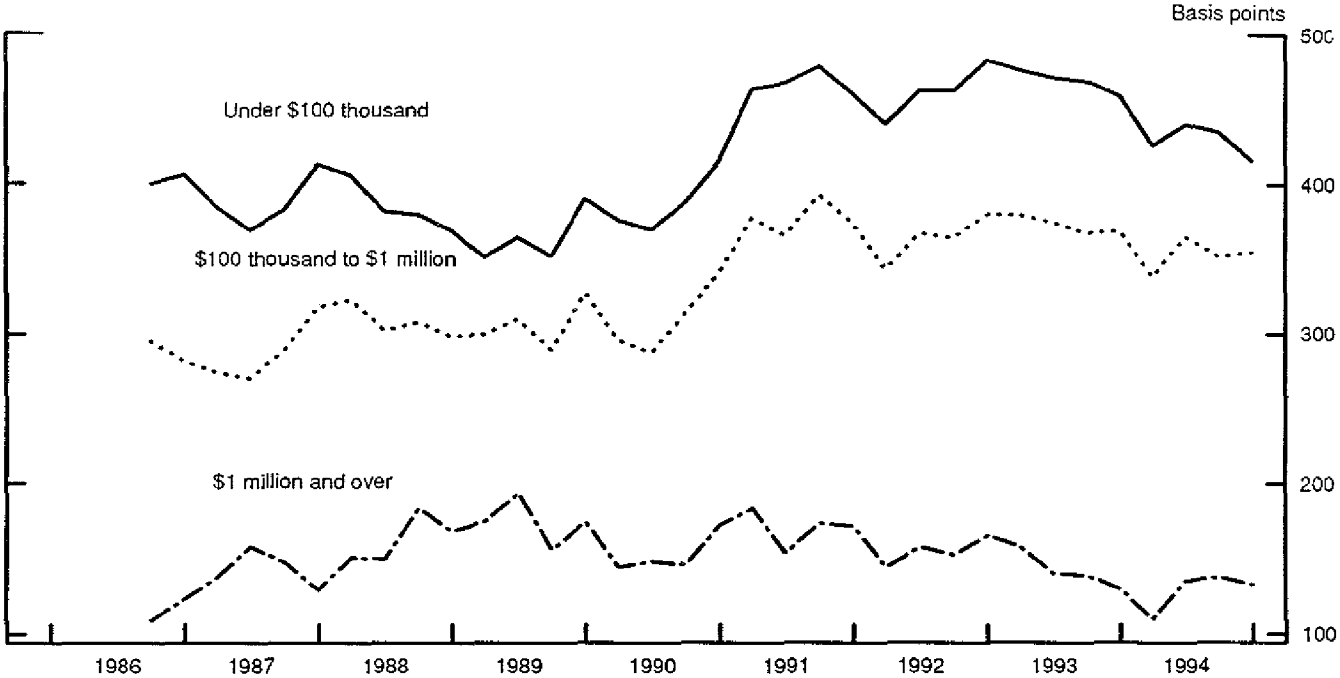
Banks' holdings of securities declined at a 9-1/4 percent annual rate in November after having fallen at a rate of 12 percent in October. In both months, a significant part of the drop reflected declines in the market value of securities that banks mark to market. A little over half of securities at domestic banks are marked to market--all of those held in trading accounts, plus those held in investment accounts that are classified as available for sale.

Net Percentage Tightening Standards For C&I Loans



Note. Vertical lines mark the onset of sustained increases in the federal funds rate.

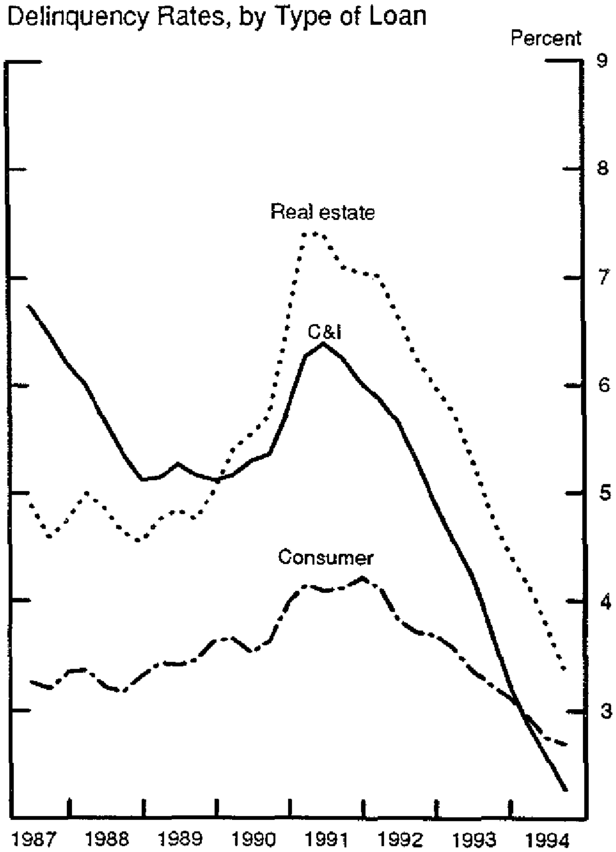
Loan Rate Spreads, by Loan Size
From the Survey of Terms of Bank Lending



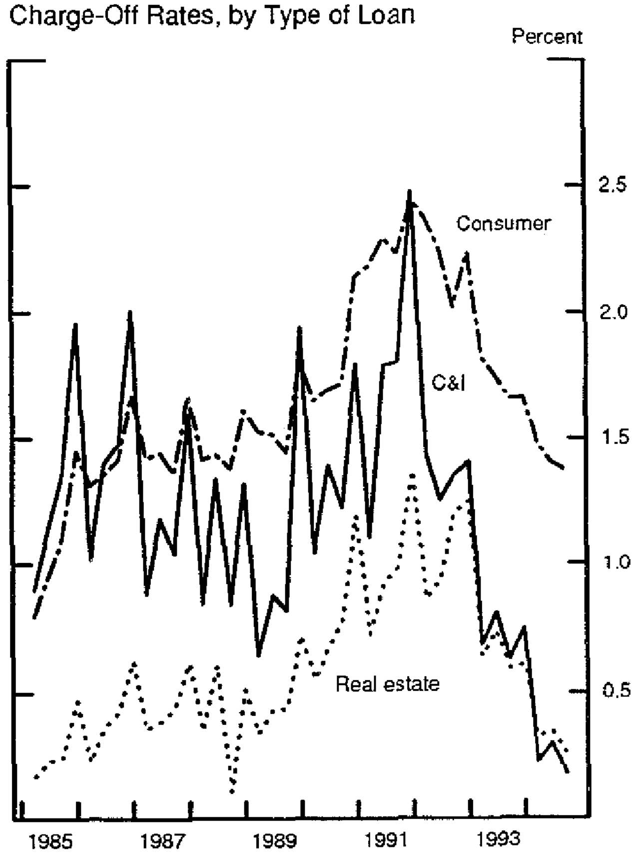
Note. Spread over intended federal funds rate, Q4 data are preliminary.

Call Report Data on Delinquency and Charge-Off Rates

Delinquency Rates, by Type of Loan



Charge-Off Rates, by Type of Loan

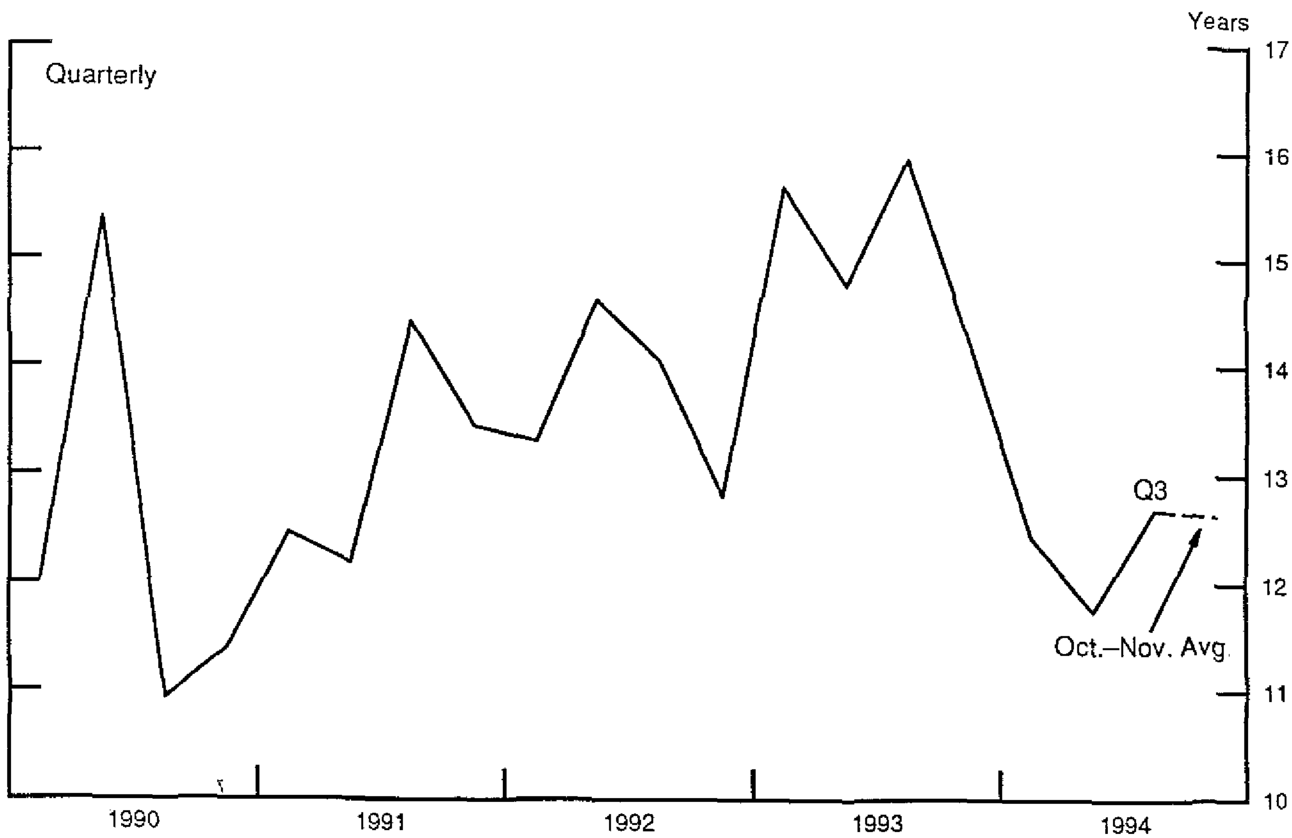


Business Finance

While lending by banks and commercial paper issuance was brisk in November, public bond issuance by nonfinancial firms remained fairly subdued. The $6-3/4 billion pace of bond issuance last month was more than 50 percent below the average monthly rate in 1993, when many firms satisfied their long-term funding needs by locking in relatively low interest rates. The rise in bond rates has depressed bond issuance this year and has reduced considerably the average maturity of nonfinancial bond issues (chart).

Although yields on most corporate bonds, from investment grade to junk, have remained close to those on Treasuries, spreads on junk bonds of the lowest quality widened considerably in November.

Weighted Average Maturity of Domestic Nonfinancial Corporate Bond Issuance*



Source: Securities Data Corp.
* Excludes medium-term notes.

GROSS OFFERINGS OF SECURITIES BY U.S. CORPORATIONS[1]
(Billions of dollars; monthly rates, not seasonally adjusted)

Type of security	1992	1993	1994 Q2	1994 Q3	1994 Sept.	1994 Oct.p	1994 Nov.p
All U.S. corporations	40.84	53.20	43.29	33.22	31.00	29.98	34.65
Stocks[2]	7.04	9.43	5.50	4.15	4.42	3.38	5.85
Bonds	33.80	43.77	37.79	29.07	26.58	26.60	28.80
Nonfinancial corporations							
Stocks[2]	4.42	5.18	3.36	1.79	2.33	1.81	4.53
Sold in U.S.	4.03	4.91	3.17	1.65	2.03	1.77	4.03
Utility	.87	1.05	.44	.20	.30	.08	.67
Industrial	3.16	3.82	2.73	1.45	1.73	1.69	3.36
Sold abroad	.39	.27	.19	.14	.30	.04	.51
Bonds	13.67	16.19	6.91	5.82	5.78	6.33	6.67
Sold in U.S.	12.83	15.55	5.96	5.01	5.38	5.00	5.80
Utility	5.33	7.34	1.90	1.08	1.46	1.20	2.20
Industrial	7.50	8.21	4.06	3.93	3.92	3.80	3.60
Sold abroad	.84	.64	.96	.81	.39	1.33	.87
By quality[3]							
Aaa and Aa	2.18	2.56	.59	.41	.98	.80	1.88
A and Baa	7.74	8.70	3.33	3.59	3.33	3.66	2.40
Less than Baa	2.86	4.17	1.99	.93	1.07	.54	1.53
Unrated or rating unknown	.09	.09	.01	.00	.00	.00	.00
Financial corporations							
Stocks[2]	2.62	4.31	2.14	2.36	2.09	1.57	1.32
Sold in U.S.	2.51	4.06	1.98	1.80	1.32	1.52	1.30
Sold abroad	.11	.25	.15	.56	.77	.05	.02
Bonds	20.13	27.58	30.87	23.25	20.81	20.27	22.13
Sold in U.S.	18.67	25.02	26.79	20.27	17.95	17.00	18.20
Sold abroad	1.46	2.56	4.08	2.98	2.85	3.27	3.93
By quality[3]							
Aaa and Aa	1.55	1.78	6.12	2.56	1.26	1.85	1.65
A and Baa	6.77	9.01	9.66	7.44	7.39	6.21	7.10
Less than Baa	.31	.49	.17	.14	.20	.20	.00
Unrated or rating unknown	.04	.08	.11	.00	.00	.00	.00

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.
3. Bonds categorized according to Moody's bond ratings, or to Standard & Poor's if unrated by Moody's. Excludes mortgage-backed and asset-backed bonds.
p Preliminary.

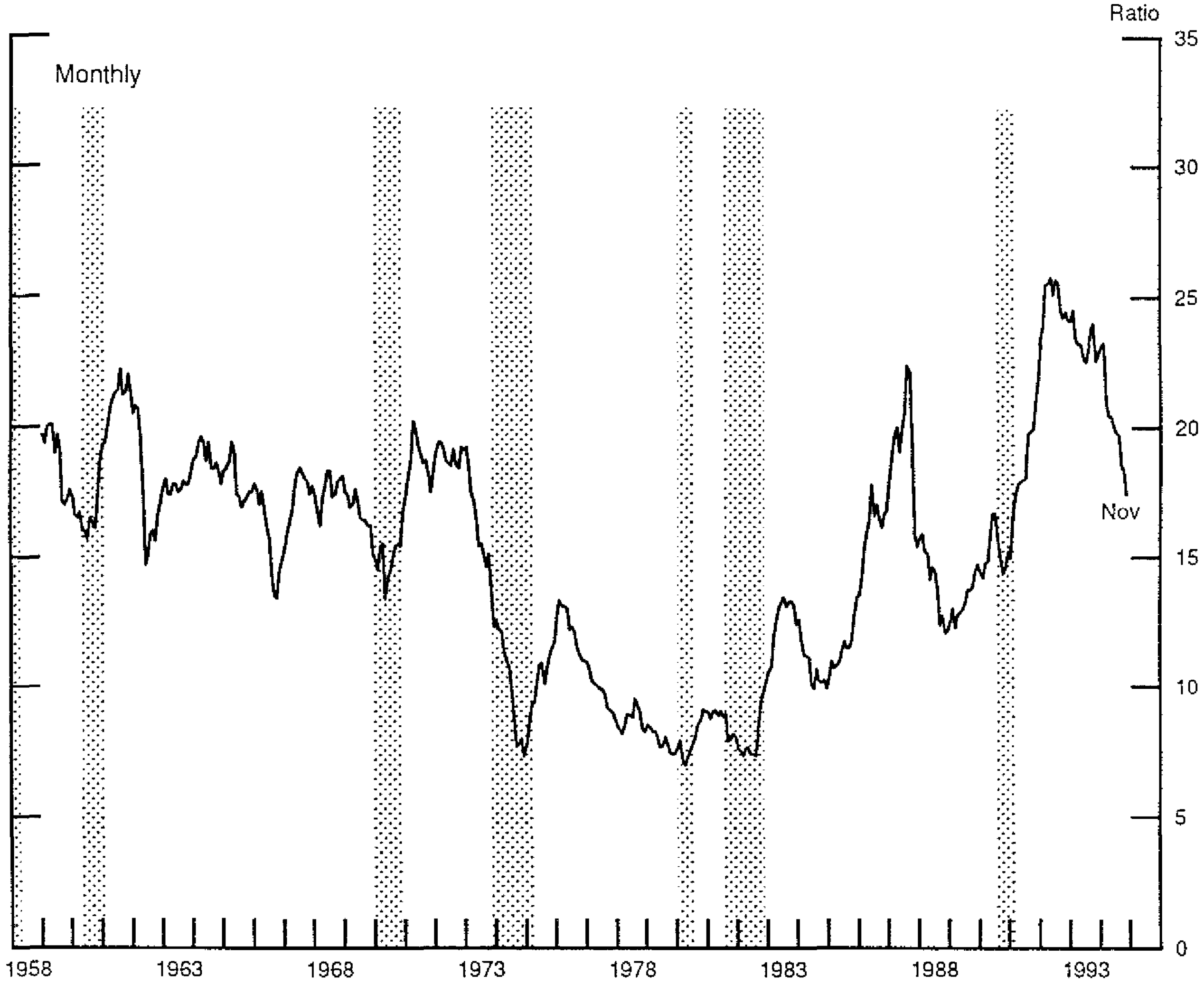
Several planned issues of junk bonds have been withdrawn in recent weeks, and the deals that were completed generally required higher coupons than first anticipated or additional equity to attract investors. The high-yield market remains particularly wary of unseasoned and lower-quality issuers.

Gross public equity issuance by nonfinancial corporations increased to $4-1/2 billion in November, up sharply from the anemic pace that had prevailed since midsummer, and the issuance thus far in December has slackened only slightly. Despite this pickup in gross issuance, spurred by increases in both initial public offerings and seasoned issues, net equity issuance is expected to be negative again in the fourth quarter, reflecting another slug of merger-related share retirements.

Merger activity has continued heavy in recent weeks. Since the November FOMC meeting, eight mergers of nonfinancial firms have been announced in which the target company was valued in the neighborhood of $1 billion. Three of these transactions are structured as stock swaps, and the other five involve equity retirements, which will be debt financed to some degree. So far this year, $70 billion of large nonfinancial mergers (those with targets valued at $1 billion or more) have been completed, and deals valued at another $30 billion have been announced for later this year or early next year. By comparison, only $22 billion of large nonfinancial mergers were completed in 1993.

Issuance of commercial paper by nonfinancial companies has continued to be robust on net, largely to provide funding for merger activity. Nevertheless, strong corporate profits reportedly enabled some firms to pay down outstanding paper--including paper that was issued earlier to finance acquisitions. Further, cash from balance

S&P 500 Price–Earnings Ratio



sheet restructurings and asset sales reportedly was used to reduce commercial paper outstanding.

Recently released reports on corporate earnings for the third quarter have been strong on the whole and generally have come in above analysts' forecasts. Nonetheless, over the intermeeting period, broad indexes of stock prices moved down 3 to 6-1/2 percent, as investors apparently were lured away from equities by the higher rates on fixed-income instruments and by the potential for some slowdown in the growth of corporate earnings. At the end of November, the ratio of the Standard and Poor's 500 price index to the earnings of companies in the index over the previous twelve months stood at about 16-1/2, the lowest level during the current expansion (chart).

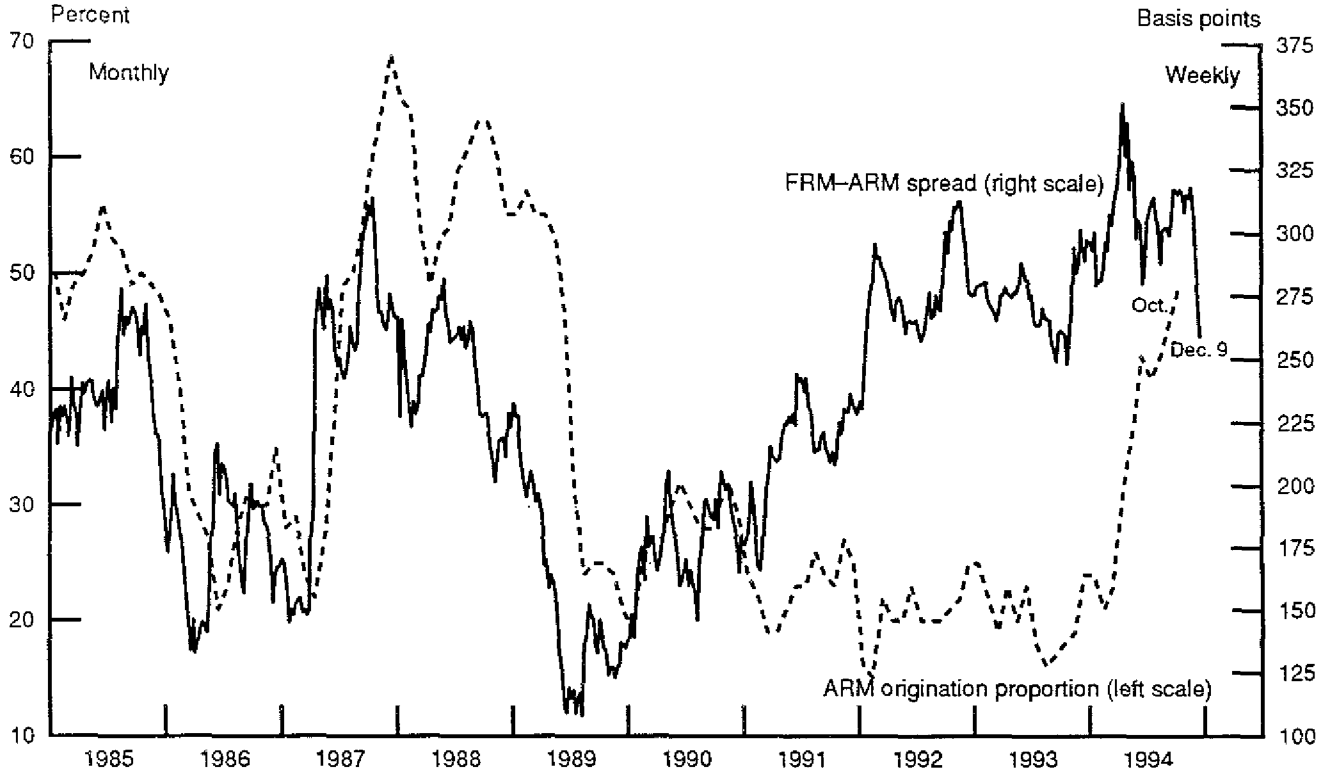
Mortgage Markets

Contract rates on thirty-year fixed-rate conventional mortgages climbed to their highest levels since late 1991 after the November FOMC meeting but subsequently edged down and, on net, are little changed from the November meeting. Initial rates on adjustable-rate mortgages indexed to the one-year Treasury constant maturity yield are up about 55 basis points, somewhat less than the one-year Treasury benchmark and adding to the already large teaser discounts. As a result, the FRM-ARM initial rate spread has narrowed to 260 basis points, around the levels prevailing in September 1993. The ARM share of new conventional loan originations moved up to 49 percent in October, which was the highest ARM share since May 1989 (chart).

Upward adjustments to ARM rates this year are estimated to have added less than $5 billion, on net, to annual household mortgage interest costs, while interest rate adjustments on home equity lines contributed about half as much to these costs. The increase in

FRM–ARM Spread and ARM Origination Proportion

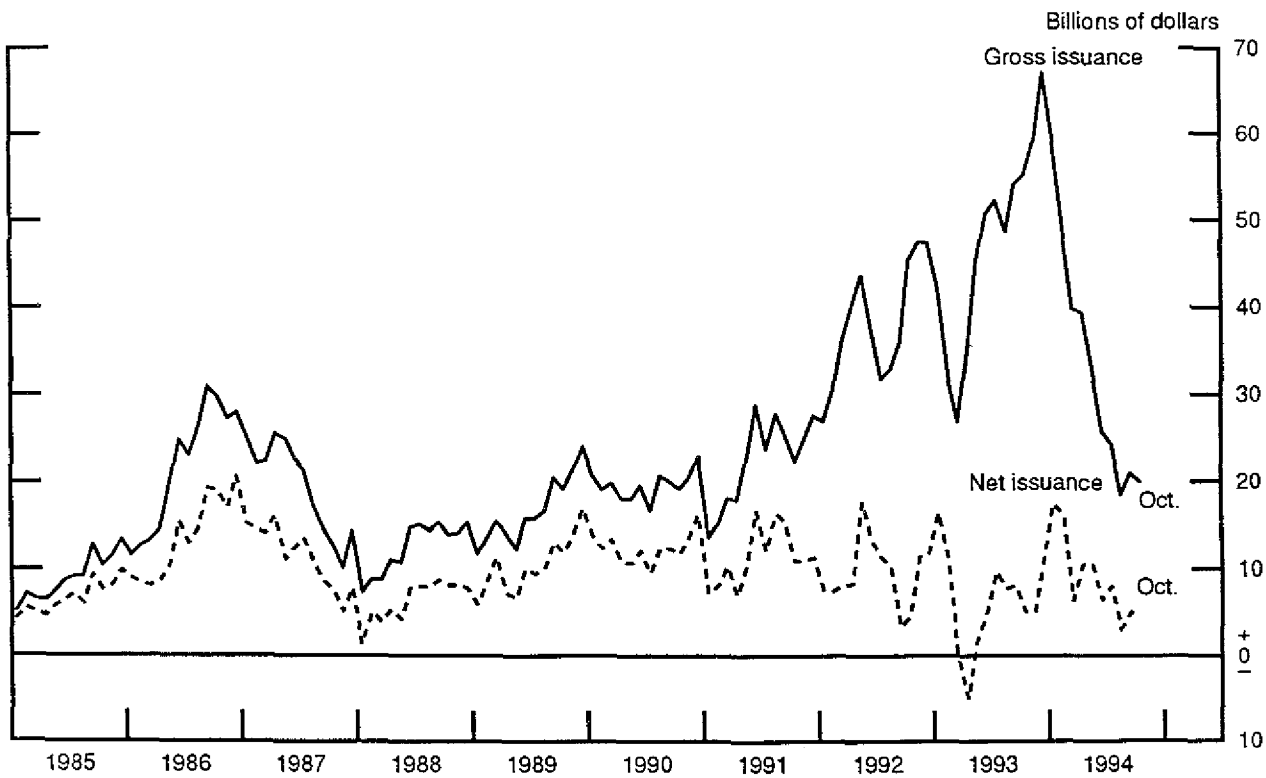
(Not seasonally adjusted)



Note. ARM origination proportion data from Federal Housing Finance Board.

Issuance of Agency Mortgage Pass–Through Securities

(Monthly; not seasonally adjusted)



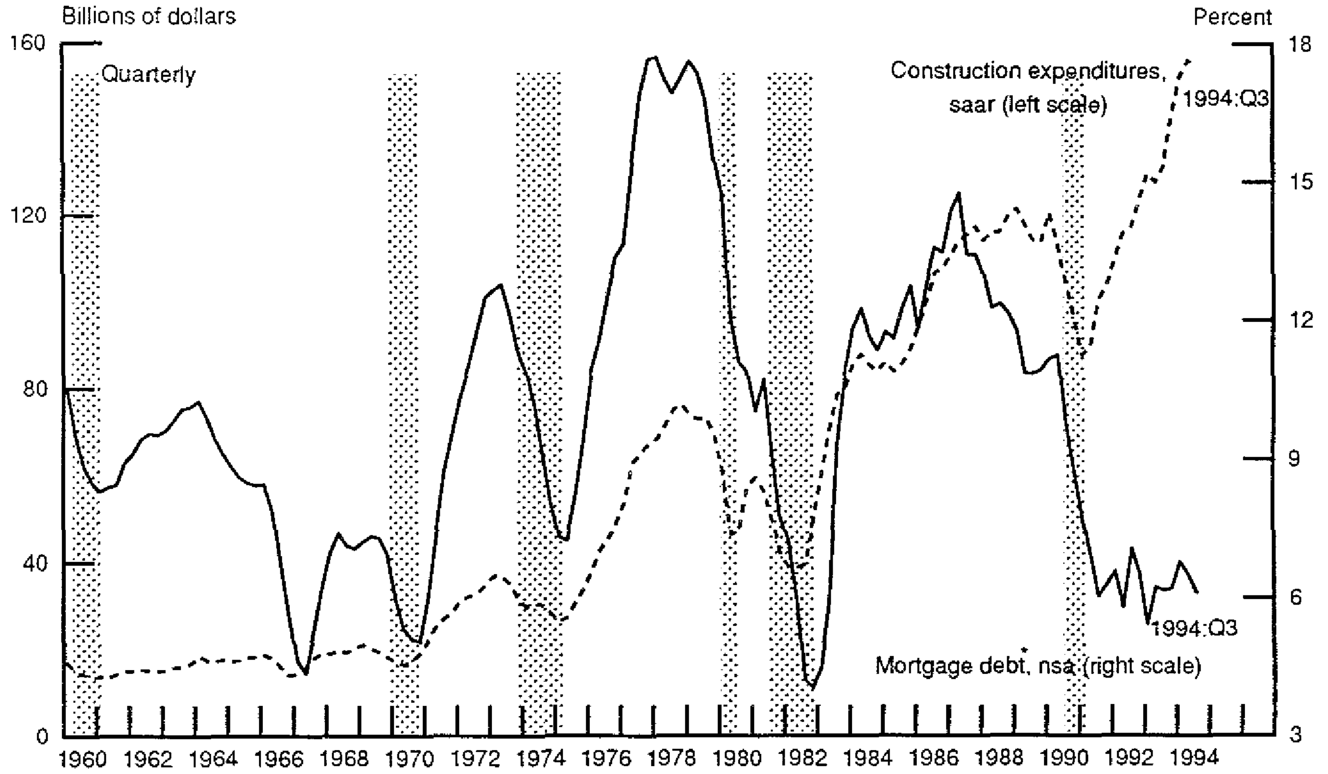
these interest costs has been partly offset, however, by further savings on FRMs in 1994, something over $3 billion, associated with the large volume of refinancings earlier this year.

In the secondary mortgage market, gross issuance of pass-throughs by the agencies slipped to about $20 billion in October, and net issuance totaled $4.8 billion, near September's pace but substantially below January's peak of $17 billion (chart). Spreads of newly originated fixed-rate mortgage pass-through securities over Treasuries have increased in recent weeks, owing to the flatter yield curve and uncertainty surrounding the Orange County developments.

Total mortgage debt outstanding grew at an estimated 5-1/4 percent annual rate in the third quarter, as all four property categories registered positive growth. Residential mortgage debt outstanding on single-family dwellings grew at an annual rate of roughly 6-1/4 percent, while the comparable figure for multifamily dwellings is 2-1/2 percent. Farm mortgage debt outstanding increased at about a 4-1/2 percent annual rate, and outstanding debt on nonfarm, nonresidential properties expanded at 1-1/4 percent, the second consecutive quarter of growth after 3 years of decline.

Compared with previous cycles, growth in total mortgage debt in the current expansion has been weak, owing both to the runoff in debt outstanding on income properties and to the sluggish growth in single-family mortgage debt outstanding. Historically, growth in the latter debt category has tended to rise sharply after cyclical troughs, reach a local peak around mid-cycle, and then decline, usually bottoming out around the end of each economic downturn (chart). In the most recent cycle, however, single-family mortgage debt has failed to register the spurt in growth that has characterized previous expansions, despite relatively strong housing

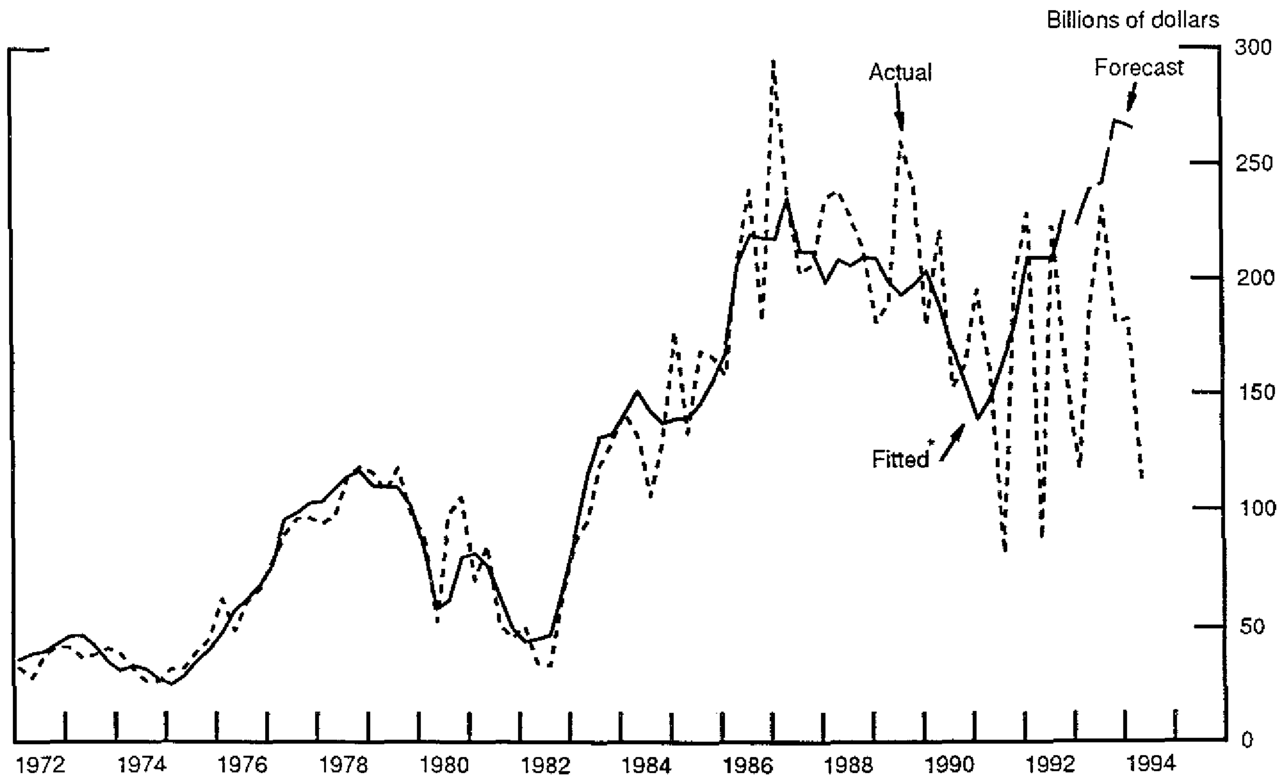
Growth of Single–Family Mortgage Debt Outstanding and Single–Family Housing Construction Expenditures



* Four–quarter percent change.

Change in Household Mortgage Debt

(Quarterly; seasonally adjusted annual rate)



* Fitted through 1992:Q4.

activity, and has consistently fallen short of model-based forecasts (chart). Anecdotal reports of a pickup in the number of borrowers making additional principal payments on their outstanding mortgages may provide part of the explanation for the unusually slow growth of home mortgage debt.

The Federal Housing Finance board announced last month that the national average single-family house price was $141,900 for October 1994, down from $144,000 a year earlier. Normally, the percentage change in the national average home purchase price as reported in the FHFB's October interest rate survey is used by Fannie Mae and Freddie Mac to determine the conforming loan limit; that is, the maximum size of home loans that they will purchase or securitize. But, despite the 1.5 percent drop in the home price index, both agencies have announced that the current limit of $203,150 will be retained. This would be only the second time since the statutory formula was established in 1973 that the conforming loan limit remained the same for three consecutive years; the first such episode occurred in the 1975-1977 period, when the limit remained at $42,000.

Consumer Installment Credit

Growth in consumer installment credit remained brisk in October, at an annual rate of 16 percent, slightly above the third-quarter average. Revolving credit registered an 18 percent annual rate of increase, and the large "other" category also expanded rapidly. After a very strong September, growth in auto credit moderated to an annual rate of 11 percent.

Interest rates on consumer loans at banks rose between the August and November surveys, as they have throughout 1994, but by considerably less than yields on Treasury securities of similar

GROWTH OF CONSUMER CREDIT
(Percent change: seasonally adjusted annual rate)

Type of credit	1992	1993	1994 H1	1994 Q3 r	1994 Sept. r	1994 Oct. p	Memo: Outstanding Oct. 1994 (Billions of dollars)
Installment	.4	8.6	13.5	15.2	14.3	15.8	891.6
Auto	-.7	9.5	15.2	15.3	21.1	11.1	318.1
Revolving	4.9	11.9	15.0	17.3	5.4	18.2	327.7
Other	-3.3	3.8	9.2	12.4	17.3	19.0	245.8
Noninstallment	6.4	-4.9	-1.8	-8.7	16.1	.8	51.6
Total	.8	7.7	12.5	13.8	14.4	15.0	943.2

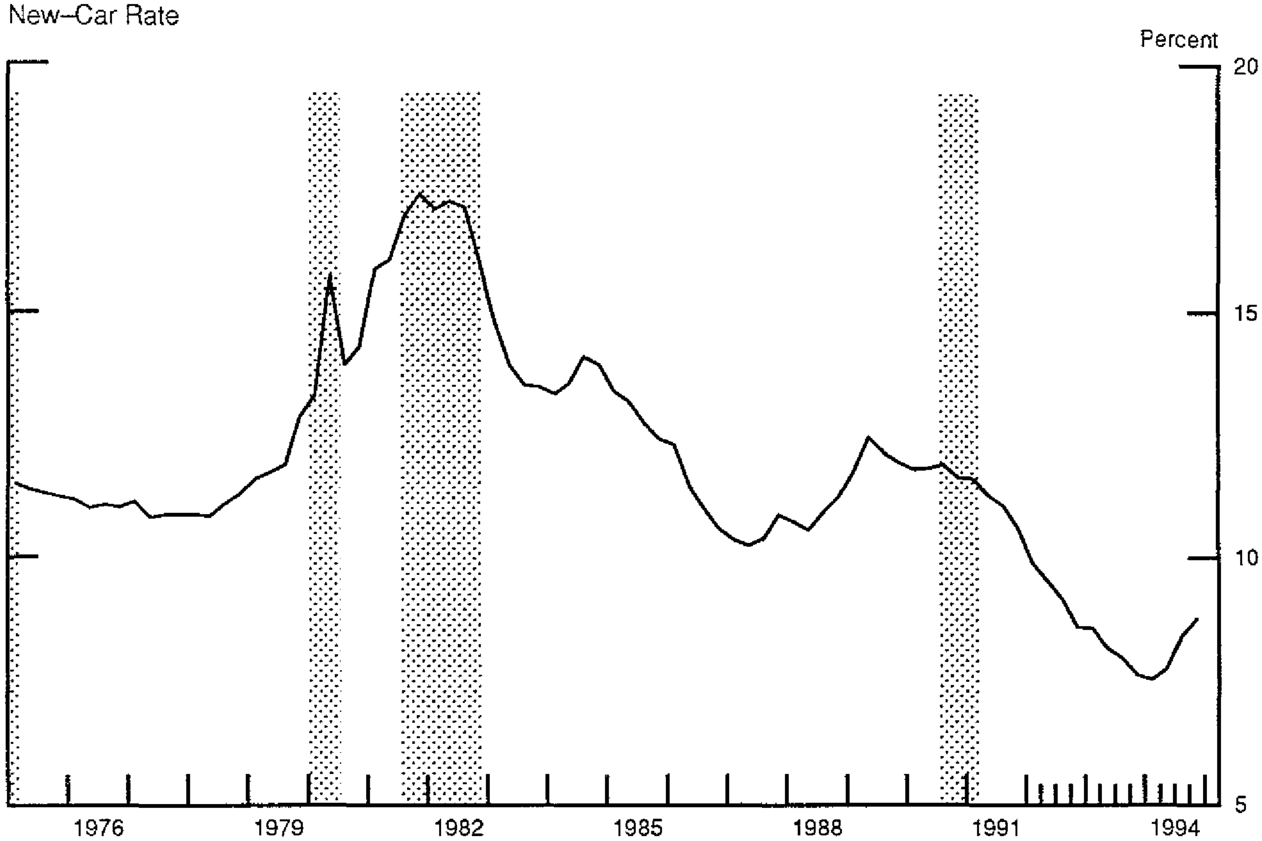
r Revised.
p Preliminary.

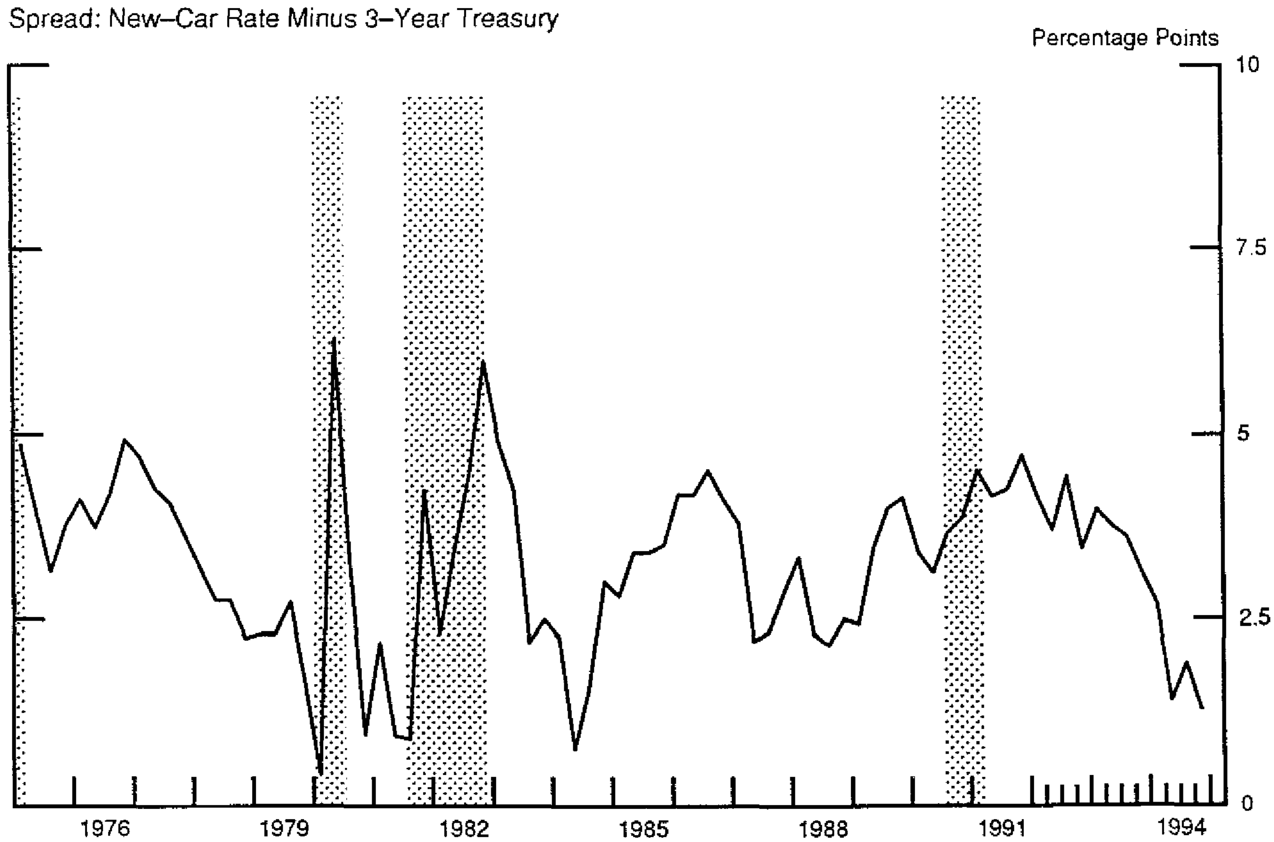
INTEREST RATES ON CONSUMER LOANS
(Annual percentage rate)

Type of loan	1991	1992	1993	1994 May	1994 Aug.	1994 Oct.	1994 Nov.
At commercial banks[1]							
New cars (48 mo.)	11.1	9.3	8.1	7.8	8.4	...	8.8
Personal (24 mo.)	15.2	14.0	13.5	13.0	13.3	...	13.6
Credit cards	18.2	17.8	16.8	16.2	16.3	...	...
At auto finance cos.[2]							
New cars	12.4	9.9	9.5	9.9	10.3	10.4	...
Used cars	15.6	13.8	12.8	13.5	13.9	14.0	...

1. Average of "most common" rate charged for specified type and maturity during the first week of the middle month of each quarter.
2. For monthly data. rate for all loans of each type made during the month regardless of maturity.
Note: Annual data are averages of quarterly data for commercial bank rates and of monthly data for auto finance company rates.

New-Car Loan Interest Rates and Spreads





maturity, and they remain low by historical standards. Rates on 48-month new-car loans were up 34 basis points to 8.75 percent, and rates on unsecured personal loans rose 26 basis points to 13.59 percent, while yields on three-year Treasury securities climbed 94 basis points over the same period.[1] The spread between rates on newly originated new-car loans and yields on three-year Treasuries has dropped from 400 basis points early last year to 130 basis points most recently (chart). The narrowing spreads between consumer and Treasury market rates reflect, in part, a typical lag in consumer rates, which tend to track the more sluggish movements in lenders' costs of funds but are also consistent with an easing of banks' lending standards.

1. Credit card rates were not reported in the latest survey. A new survey for credit card rates was initiated in November that will better reflect the broader spectrum of rates offered than the previously reported "most common rate." Results of the new survey are expected to be available in mid-January.

APPENDIX

GROWTH OF THE CREDIT AND MONETARY AGGREGATES IN 1994

Summary

Growth in M1 and M2 slowed in 1994 while growth in M3 and the broad credit aggregates rose this year at least as rapidly as in 1993. Of particular note were changes in the composition of asset flows which were greatly affected by the rise in interest rates this year. Higher long-term interest rates induced borrowers to shift into shorter-term or floating rate obligations; lenders, concerned about future capital losses, seemed eager to reduce their exposure to long-term market instruments thereby accommodating, and perhaps even encouraging, the change in borrowers' preferences. A byproduct of the rise in market interest rates and the deceleration of M1 was a sharp weakening of reserve aggregates.

Total debt of nonfinancial sectors increased 5-1/4 percent through November--the same as in 1993--leaving it in the lower half of its monitoring range. A slower expansion of federal debt this year offset a pickup in the debt growth of nonfederal sectors from 4 percent in 1993 to 5 percent in 1994.

Business borrowing was boosted by a rising financing gap and a surge in merger and acquisition activity. However, the weakness in bond and equity markets led firms to shift their credit demands toward shorter-term debt such as commercial paper and bank loans. Households, in turn, redirected mortgage borrowing into adjustable rate loans, and mortgage debt continued to expand at a moderate pace despite the backup in rates. Households also greatly increased usage of consumer credit. The change in business and household borrowing may have been encouraged by bank behavior: Survey evidence indicated continued relaxation of standards and nonprice terms of credit for business loans, and rates on consumer credit lagged the rise in market rates. Bank credit overall grew at a 6-1/2 percent pace through November, with bank loans advancing 7-1/4 over the same period.

Depositories elected to meet increased loan growth primarily through sales of government securities and reliance on wholesale funds. The shift toward wholesale funding in the form of large time deposits helped push M3 growth up to 1-1/4 percent through November. This was in the lower half of the Committee's range, and somewhat faster than in 1993. Banks were reluctant to raise retail deposit rates, however, and the resulting rise in the opportunity cost of holding money constrained M2 growth to 1 percent this year--a bit below the pace in 1993 and at the lower bound of its target range. The sluggish expansion of M2 was quite consistent with long-run historical relationships and, in contrast to 1992 and 1993, was not a consequence of unusually large portfolio shifts into mutual funds. Higher opportunity costs produced a sharp deceleration in M1 growth from 10-1/2 percent in 1993 to 2-1/4 percent through November of this year.

Domestic Nonfinancial Debt Growth

Although changes in the growth of the broad debt aggregates were rather modest, rising long-term interest rates produced some notable shifts in the underlying pattern of credit flows. Falling bond prices and greater market uncertainty led households to scale back their holdings of bond mutual funds in favor of investments that posed less risk of capital loss. Outflows from bond mutual funds began in February and continued at a rapid pace through November. A portion of the outflow from bond funds likely helped bolster inflows to money funds and bank retail certificates of deposit in M2. In addition, short-term Treasury securities appeared to be a popular safe haven for investors fleeing bond mutual funds. Indeed, net noncompetitive tenders for Treasury bills averaged $1.2 billion per month through November, the highest level in more than a decade.[1]

Households made adjustments on the liability side of the balance sheet as well. The pace of mortgage refinancing fell sharply toward the end of 1993 and was further depressed by the increase in long-term rates this year. Nonetheless, total household mortgage debt continued to expand; ARMs became increasingly popular, rising to nearly half of originations, with many mortgage lenders offering attractive terms relative to those on fixed-rate mortgages. Consumer credit accelerated as household spending on consumer durables strengthened. In addition, convenience usage of credit cards likely increased with the proliferation of cards offering incentives tied to transaction volumes.

In the business sector, declines in bond and stock prices sparked a change in funding patterns. Bond and equity issuance fell off sharply during the year from the extremely heavy pace in 1993. In the face of weak investor demand and higher interest rates, junk bond offerings, in particular, were depressed. Stronger earnings allowed many firms to finance a large portion of their capital outlays with internal funds. In addition, many firms turned to shorter-term instruments for their external financing needs. Commercial paper grew rapidly in the second half of the year, while bank loans to businesses increased for the first time since 1990, in part reflecting a more accommodative stance by bank lenders. A portion of the rise in commercial paper and business loans was associated with a resurgence of merger activity during the year. In addition, lending by finance companies accelerated sharply over the year, paced by auto-related loans and equipment leasing.

In the state and local sector, tax-exempt bond issuance was also depressed by the rise in interest rates. Much of the proceeds of new tax-exempt bonds in recent years had been targeted to refinance higher-cost debt issued in 1980s. Refunding offerings subsided early this year, as the amount of bonds eligible for advance refunding dwindled and borrowing costs rose. The moderate pace of new offerings, coupled with an unusually large volume of bond retirements, will result in a contraction in outstanding long-term tax-exempt debt is projected to decline this year.

Depository Credit Growth

Bank credit expanded at a 6-1/2 percent pace from the fourth quarter of 1993 through November--the fastest rate of growth since 1989. Indeed, through October, a little more than 30 percent of the

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1. Individuals can purchase Treasury securities at auction by submitting a noncompetitive tender through a Federal Reserve Bank at no cost. In addition, they can buy Treasury securities through a bank or brokerage firm for a modest fee. The data on noncompetitive tenders thus measure only a portion of the total retail demand for Treasury securities.

increase in total domestic nonfinancial debt was intermediated through the banking sector--the largest share since the 1970s.

Business and consumer loans were the fastest growing components of bank credit, with the increase in business loans especially striking following the previous three years of runoffs. Responses to survey questions throughout the year indicated that many banks were easing underwriting standards and nonprice terms for such loans. Moreover, data on bank loan pricing indicate that spreads of bank loan rates over Treasuries held roughly constant over the year despite the strength of loan demand, remaining well below levels prevailing earlier in the 1990s. Continued declines in delinquency and chargeoff rates for all major loan categories likely contributed to banks' renewed interest in lending. Banks were also eager to book consumer loans as suggested by historically low spreads of rates on such loans over benchmark rates. Through November, growth of consumer loans at banks strengthened to about 14-1/2 percent at an annual rate--comparable to the growth of overall consumer credit --even as securitization of consumer loans picked up.

The measured change in bank securities during the year was significantly affected by two changes in accounting standards, which on net added perhaps three-quarters of a percentage point to the growth of bank credit.[2] Aside from these accounting changes, banks appeared to rely on liquidations of U.S. Treasury securities to make room for new business and consumer loans, especially in the second half of the year. Through November, growth of total bank securities slowed to 5 percent compared with 8-1/2 percent last year. Growth of Treasury securities was slightly negative through November.

The long-running contraction of the S&L industry drew to a close in the first quarter, tending to buoy growth of depository credit.

<u>M3 Growth</u>

Helping to fund the pickup in depository credit, M3 expansion picked up this year to 1-1/4 percent, comfortably within its 0 to 4 percent annual target range. With M2 deposits weak, domestic banks issued large time deposits to fill a portion of their funding gap. Growth of large time deposits for the year is expected in the neighborhood of 6-1/4 percent, marking the first yearly increase in this component since 1989. In an effort to avoid deposit insurance premiums, much of the past year's large time deposit issuance took the form of senior bank notes. Another substantial portion of domestic banks' funding gap was filled by borrowing from (or reducing lending to) their foreign offices--an item not included in M3. The reasons for this trend are not clear, but may be related to

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2. A new accounting rule implemented at the start of this year (FIN 39) limited banks' ability to net their gross positions on certain items that are included in "other securities." This rule change, which inflated both sides of banks' balance sheets, substantially boosted the growth of securities early in the year and may have added as much as 1-1/4 percentage points to bank credit growth for the year through November. A second accounting rule change (FAS 115) required banks to begin marking-to-market securities held in "available-for-sale" accounts. Estimates suggest that revaluations of securities under FAS 115 pared perhaps 1/2 percentage point from the growth of bank credit during the year.

the profitability of investment opportunities at banks' domestic offices relative to those overseas. In addition, borrowing from foreign affiliates is not included in the deposit insurance assessment base and, since December 1990, has not been subject to reserve requirements.

<u>M2 Growth</u>

M2 hovered at or near the 1 percent lower bound of its target range throughout the year, with banks not bidding very aggressively for retail deposits. As noted, banks evidently found wholesale funding less expensive than mounting a campaign to attract retail deposits with attendant advertising, administrative, and deposit insurance costs. On balance, though, M2 growth was more in line with the historical relationships embodied in the staff's money demand models than in recent years.

In part, weaker-than-expected adjustments of retail deposit rates help explain why outflows from bond mutual funds and reduced inflows into stock funds did not translate into faster M2 growth. Indeed, with households evidently favoring direct holdings of Treasury securities, M2 plus stock and bond funds grew at about the same 1 percent pace as M2.

<u>M1 Growth</u>

Consistent with its historical behavior, M1 growth slowed sharply in 1994 in response to widening opportunity costs. From the fourth quarter of 1993 through November, M1 grew only 2-1/4 percent at an annual rate--down substantially from the double digit growth recorded over the previous two years. Following the typical pattern, demand deposits and other checkable deposits (OCDs) were especially responsive to the rise in short-term interest rates. On balance, demand deposits edged up only 1/2 percent through November compared with growth of 13-1/4 percent in 1993. OCDs were depressed early in the year by a reserve avoidance program introduced by in which customers' OCD balances are swept into MMDA accounts at the end of each day. In addition, a holding company with affiliates operating in many of the same markets implemented a version of the sweep account program in September, further depressing OCD growth. More important, the sluggish adjustment of interest rates offered on OCD accounts throughout the year encouraged households to shift funds into higher-yielding assets.

In contrast to transaction deposits, the currency component of M1 continued to register strong growth. Through November, currency advanced at a 10-1/2 percent pace, a bit faster than last year and close to the record annual currency growth rate of 1990. As in 1990 and subsequent years, much of this year's currency growth was associated with strong demands from abroad. In 1994, foreign demand appeared to be heavily concentrated in Russia and the other former Soviet republics.

The downturn in transaction deposits during the year led to a decline in required reserves. Given the strength of currency growth, however, the monetary base expanded at a 8-1/2 percent rate through November, down only a little from the 10-1/2 percent pace recorded last year.

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

Growth rates or flows	1990	1991	1992	1993	1994[1]	Memo: Recent 1994 levels ($ billions)[1]
Growth Rates (percent)						
M1	4.2	7.9	14.3	10.5	2-1/4	1,147.6
M2	4.0	2.9	1.9	1.4	1	3,595.4
M3	1.7	1.2	.5	.7	1-1/4	4,269.4
Domestic nonfinancial debt	6.5	4.6	4.7	5.2	5-1/4	12,925.4
Bank credit	5.6	3.5	3.7	4.9	6-1/2	3,294.9
Thrift assets	-9.8	-10.8	-5.4	-2.5	-1/4	1,309.8
Flows ($ billions, December to December)						
M1	31.7	71.3	127.1	103.6	19.2	1,147.6
Currency	24.1	20.4	25.1	29.2	31.5	352.9
Demand deposits	-1.9	12.1	49.6	45.2	-1.3	383.5
Other checkable deposits	8.6	38.8	52.1	29.4	-11.4	402.9
M2	113.2	102.2	53.8	58.9	27.5	3,595.4
Nontransactions M2	81.5	30.9	-73.3	-44.7	8.3	2,447.8
Savings & MMDAs	29.4	120.7	142.5	31.9	-55.6	1,159.9
Small time deposits	20.8	-107.1	-196.9	-84.8	20.0	805.7
General purpose and broker/dealer money market mutual fund assets	35.1	14.9	-18.4	-3.2	21.0	369.8
Overnight RPs, net (NSA)	-8.1	.2	1.5	15.2	14.4	88.9
Overnight Eurodollars, net (NSA)	5.2	3.1	-1.5	-3.5	8.4	26.2
M3	58.4	54.7	2.6	49.0	37.4	4,269.4
Non-M2 component	-54.8	-47.5	-51.2	-9.9	9.9	674.0
Institution-only money market mutual fund assets	26.5	46.0	20.5	-4.5	-21.4	175.6
Large time deposits	-59.6	-63.7	-65.5	-21.3	22.5	361.5
Term RPs, net (NSA)	-9.4	-17.1	8.6	15.7	4.8	101.6
Term Eurodollars, net, NSA)	-10.8	-11.1	-11.9	1.3	7.6	54.6

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

INTERNATIONAL DEVELOPMENTS

U.S. International Trade in Goods and Services

The U.S. trade deficit in goods and services was a bit larger in September than in August (exports declined marginally and imports increased slightly) and the deficit for the third quarter as a whole was substantially greater than in the second quarter. Data for October will be released by the Commerce Department on December 20.

NET TRADE IN GOODS & SERVICES
(Billions of dollars, seasonally adjusted)

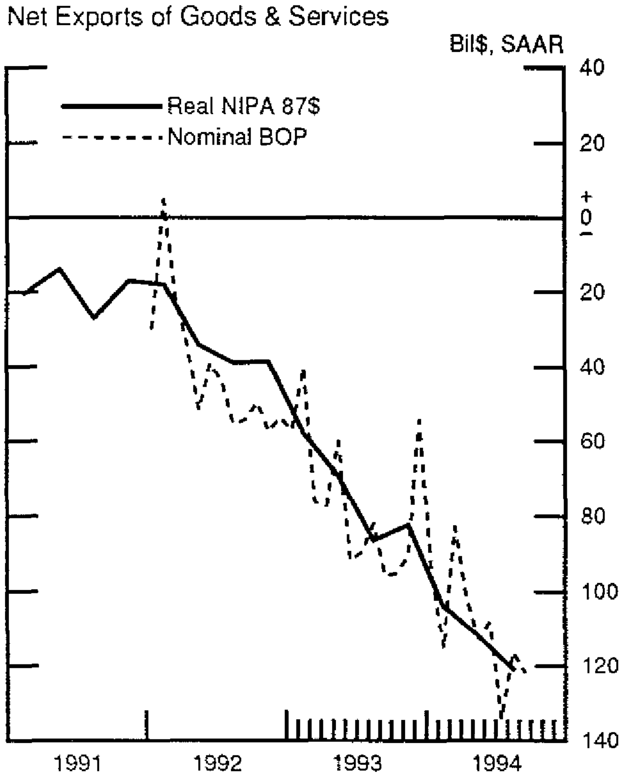
	Year 1993	Quarters 94Q1	94Q2	94Q3	Months Jul	Aug	Sep
		(annual rates)			(monthly rates)		
Real NIPA 1/							
Net Exports of G&S	-73.9	-104.0	-111.8	-120.8	--	--	--
Nominal BOP							
Net Exports of G&S	-75.7	-97.3	-107.5	-124.0	-11.2	-9.7	-10.1
Goods, net	-132.6	-147.8	-166.5	-178.6	-15.9	-14.1	-14.6
Services, net	56.8	50.5	59.0	54.6	4.8	4.4	4.5

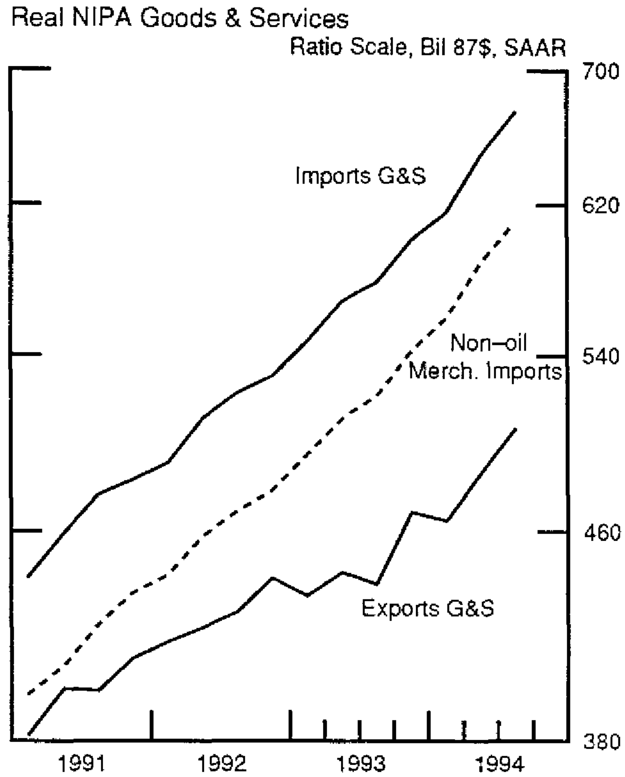
1/ In billions of 1987 dollars, SAAR.
Source: U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

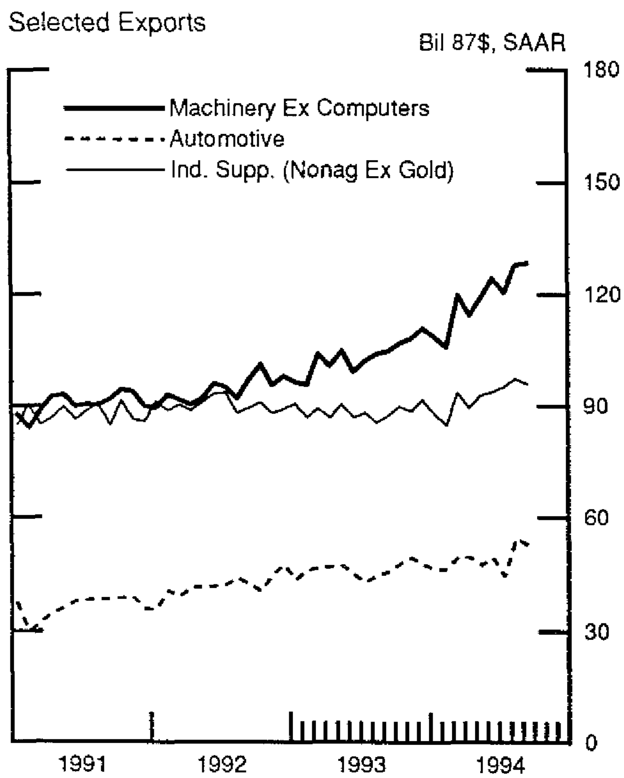
Exports in September were slightly less than in August as rises in exported aircraft, passenger cars shipped to overseas markets, and service receipts from foreigners traveling in the United States were more than offset by declines in most other categories of trade. Nonetheless, third-quarter exports were 3 percent higher than in the second quarter; the largest increases were in machinery, industrial supplies, and consumer goods. Most of the rise was in quantity, with the exception of industrial supplies (where virtually all of the increase was in prices). By area, most of the increase in the third quarter went to developing countries in Asia and Latin America. Over the past year, exports to developing countries, and to Canada and Japan, rose 15-20 percent on average, while exports to countries in Western Europe rose an average of 6 percent.

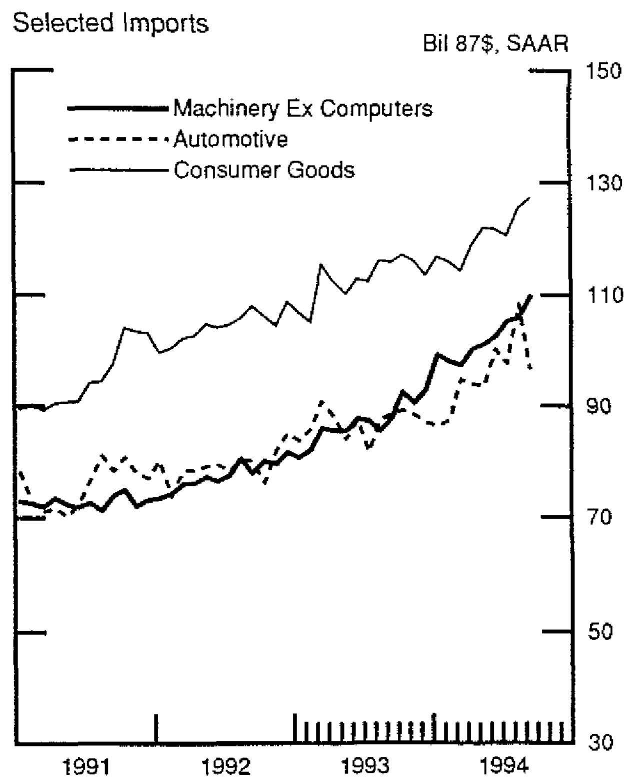
U.S. International Trade in Goods & Services

12/14/94









U.S. EXPORTS AND IMPORTS OF GOODS AND SERVICES
(Billions of dollars, SAAR, BOP basis)

	Quarters				Months		
	Levels		$Change 1/		Levels		$Chg 1/
	94Q2	94Q3	Q2	Q3	Aug	Sep	Sep
Exports of G&S	684.6	703.8	25.1	19.1	719.3	716.1	-3.2
Goods Exports	490.7	511.2	18.6	20.5	529.5	522.5	-7.0
Agricultural	43.8	46.7	0.1	2.9	49.7	47.7	-2.0
Gold	5.7	4.6	-3.6	-1.1	6.4	2.9	-3.5
Computers	31.9	33.8	0.6	1.8	33.8	34.5	0.7
Other Goods	409.2	426.1	21.5	16.9	439.6	437.3	-2.3
Aircraft & Pts	34.1	28.6	-0.2	-5.4	30.3	32.4	2.1
Semiconductors	24.0	25.3	0.6	1.3	25.6	26.6	1.0
Other Cap Gds	114.1	119.5	8.5	5.4	122.2	120.8	-1.4
Automotive	55.9	58.1	1.6	2.1	62.5	60.5	-2.0
to Canada	30.6	31.1	1.7	0.5	35.8	31.0	-4.8
to Mexico	8.4	7.6	0.5	-0.8	7.8	8.2	0.3
to ROW	16.9	19.3	-0.6	2.4	18.8	21.3	2.5
Ind Supplies	102.3	111.7	6.1	9.4	113.0	112.9	-0.1
Consumer Goods	58.3	61.4	2.9	3.1	63.7	62.3	-1.4
All Other	20.5	21.5	2.1	1.0	22.4	21.9	-0.5
Services Exports	193.9	192.6	6.5	-1.3	189.8	193.6	3.8
Imports of G&S	792.1	827.8	35.3	35.6	835.5	837.6	2.1
Goods Imports	657.2	689.8	37.3	32.5	698.6	697.7	-0.9
Petroleum	51.4	60.7	9.8	9.3	62.1	59.1	-3.0
Gold	4.7	2.8	-4.1	-1.8	3.7	2.2	-1.5
Computers	44.3	47.1	2.6	2.8	46.2	50.6	4.4
Other Goods	556.8	579.1	29.1	22.3	586.7	585.9	-0.8
Aircraft & Pts	12.3	9.9	1.0	-2.5	8.2	11.4	3.2
Semiconductors	23.7	27.0	0.6	3.3	27.4	28.4	1.0
Other Cap Gds	98.6	104.0	4.2	5.4	101.9	107.6	5.6
Automotive	116.5	123.4	8.4	6.9	132.7	118.6	-14.1
from Canada	41.2	44.2	4.3	3.0	50.3	45.3	-5.0
from Mexico	14.2	13.9	0.8	-0.3	14.9	15.6	0.7
from ROW	61.1	65.3	3.3	4.2	67.4	57.6	-9.8
Ind Supplies	106.5	111.0	5.2	4.5	112.1	111.1	-0.9
Consumer Goods	144.5	148.6	6.7	4.1	149.8	151.6	1.9
FFB	30.5	32.2	1.1	1.7	32.4	32.6	0.2
All Other	24.2	23.1	1.8	-1.1	22.3	24.5	2.2
Services Imports	134.9	138.0	-2.0	3.1	136.8	139.9	3.1
Memo:							
Oil Qty (mb/d)	9.59	10.24	0.59	0.65	10.18	10.46	0.28

1/ Change from previous quarter or month.
Source: U.S. Dept. of Commerce, Bureau of Economic Analysis and Census

Imports in September were marginally higher than in August. A sharp drop in imported automotive products (from strong levels reported in August) was offset by a large increase in imported capital goods (aircraft, computers, and other machinery). Imported consumer goods moved up slightly from the high levels reported in August. The value of oil imports declined in September; a drop in price was only partly offset by a moderate increase in the quantity imported. The quantity of oil imports remained over 10 mb/d in September (for the fourth consecutive month) as the pace of inventory accumulation quickened.

For the third quarter, imports were 4.5 percent higher than in the second quarter; the increases were spread among all major trade categories and reflected the strength of consumption and investment spending in the United States.

In October and November, preliminary Department of Energy statistics indicate that higher oil consumption was met, in part, by stock draws resulting in an easing of imported oil. Oil imports are expected to be less in the fourth quarter than in the third quarter.

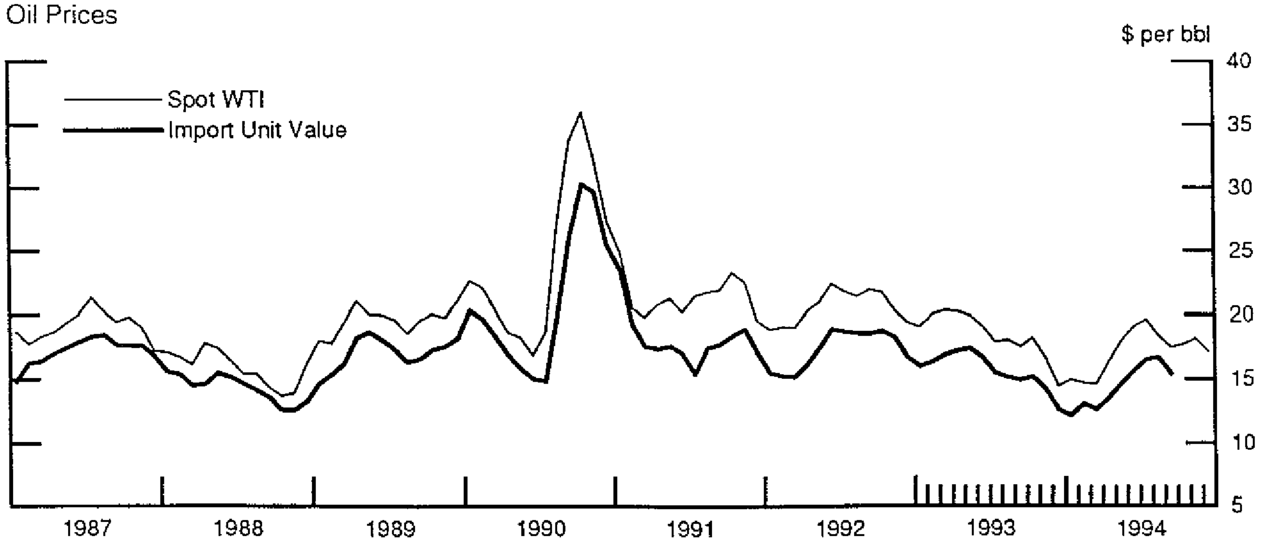
Prices of Merchandise Imports and Exports

After rising since April, the price of imported oil fell $1.25 per barrel in September. Prices fell as world oil production rebounded from low levels associated with effects of summer oilfield maintenance and the strike in Nigeria. In October and November, the price of imported oil appears to have remained near the September average. In early November, spot oil prices (West Texas Intermediate) fell as concerns over new shipping insurance regulations (COFRs) abated. Prices have continued to ease downward on balance in late November and early December. The twelve-month extension of OPEC's quota has not put upward pressure on prices

PRICES OF U.S. IMPORTS AND EXPORTS
(percent change from previous period)

	Quarters			Months		
	94Q1	94Q2	94Q3	Aug	Sep	Oct
	(annual rates)			(monthly rates)		
	BLS Prices					
Merchandise Imports	-2.1	7.4	8.1	0.5	-0.5	0.8
Oil	-30.2	67.5	36.6	-1.2	-7.4	0.9
Non-Oil	1.3	2 8	5.3	0.6	0.3	0.7
Foods, Feeds, Bev.	0.8	16.0	37.8	2.4	0.7	1.4
Ind Supp Ex Oil	5.4	4.4	8.9	1.1	1.1	1.2
Computers	-5.1	-6.7	-8.5	-0.3	0.3	-1.0
Capital Goods Ex Comp	-0.1	2.7	4.2	0.7	-0.1	0.4
Automotive Products	2.0	2.4	2.4	0.5	0.2	1.1
Consumer Goods	-0.1	1.0	1.1	0.1	0.2	0.1
Memo:						
Oil Imports ($/bbl)	12.67	14.67	16.23	16.70	15.46	--
Merchandise Exports	4.1	1.4	2.0	0.2	0.3	0.5
Agricultural	19.9	-7.4	-14.4	-1.2	0.5	-0.2
Nonagricultural	2.2	2.9	4.4	0 3	0.3	0.5
Ind Supp Ex Ag	7.8	9.4	17.1	1.3	0.7	1.7
Computers	-10.0	-6.2	-11.2	-2.6	0.0	-0.5
Capital Goods Ex Comp	0.9	-0.2	0.3	0.0	-0.1	-0.1
Automotive Products	1.5	0.9	1.2	0.0	0.1	0.5
Consumer Goods	0.8	0.4	-0.5	0.2	0.2	0.1
	Prices in the NIPA Accounts					
Fixed-Weight						
Imports of Gds & Serv.	-2 8	7 8	9 1	--	--	--
Non-oil Merch Ex Comp	0.5	3.6	6.2	--	--	--
Exports of Gds & Serv.	4.4	2 2	2.9	--	--	--
Nonag Merch Ex Comp	2.9	3.5	6.1	--	--	--

Oil Prices



because of rising concern over the potential effects of a warm winter on needs for fuel at a time when there are ample product inventories. Overall, the price of imported oil in the fourth quarter should average about $0.85 per barrel less than in the third quarter.

Prices of U.S. non-oil imports rose strongly in October, pushed by a continued advance in the price of imported industrial supplies. Also contributing to the rise was an upswing in the prices of imported passenger vehicles (primarily associated with model changeovers) and foods. In the third quarter, non-oil import prices rose significantly more than in the second quarter, largely because of prices of industrial supplies and foods.

Prices of exported nonagricultural products rose somewhat faster in October than in recent months; in both October and the third quarter increases were led by rising prices of industrial supplies. Prices of U.S. agricultural exports fell slightly in October; declines were recorded in four of the last five months.

U.S. International Financial Transactions

Foreign official assets in the United States rose by more than $10 billion in October. (See line 1 of the Summary of U.S. International Transactions table.) There were large increases in holdings of several developing countries in Asia and Latin America. In addition, holdings by Israel also rose substantially, probably reflecting the proceeds of U.S. aid and bonds issued with U.S. guarantees. Partial information from FRBNY indicates little increase in G-10 reserves in November.

Private foreign net purchases of U.S. Treasury bonds were large in October (line 4a). Entities in the Netherlands Antilles accounted for most of the total. Net purchases of U.S. corporate

SUMMARY OF U S. INTERNATIONAL TRANSACTIONS[1]
(Billions of dollars, not seasonally adjusted except as noted)

	Year		Quarter				Month		
			1993	1994			1994		
	1992	1993	Q4	Q1	Q2	Q3	Aug.	Sept.	Oct.
<u>Official capital</u>									
1. Changes in foreign official reserve assets in U.S. (+ = increase)	**38.3**	**70.2**	**23.3**	**10.3**	**8.7**	**18.4**	**2.3**	**1.5**	**10.4**
a. G-10 countries	4.8	29.9	4.8	10.8	15.7	9 0	3.3	-.5	1.0
b. OPEC countries	4.9	-5.1	-.9	-2.3	-4.7	3.3	1.1	.7	5
c. All other countries	28.6	45 4	19 4	1.9	-2.4	6.0	-2.2	1.3	8.9
2. Changes in U.S. official reserve assets (+ = decrease)	**3.9**	**-.7**	**-.7**	**-.1**	**3.5**	**-.2**	**-.1**	**-.1**	**-.2**
<u>Private capital</u>									
Banks									
3. Change in net foreign positions of banking offices in the U.S.[2]	**35.6**	**8.5**	**4.7**	**38.0**	**38.1**	**10.0**	**-8.1**	**7.7**	**1.3**
Securities[3]									
4. Foreign net purchases of U.S. securities (+)	**68.1**	**105.5**	**45.8**	**31.1**	**6.3**	**19.7**	**18.5**	**5.9**	**8.9**
a. Treasury securities[4]	37.4	24.7	8.1	9.5	-7.3	5 2	9 3	5.3	8.0
b. Corporate and other bonds[5]	34.3	61 2	25.5	13.7	14.8	13.3	6 2	1.7	2.7
c Corporate stocks	-3.7	19.6	12.2	8.0	-1.3	1.1	3.0	-1.2	-1.9
5. U.S. net purchases (-) of foreign securities	**-47.9**	**-132.8**	**-34.6**	**-25.1**	**-18.0**	**-9.2**	**-3.7**	**-.2**	**-7.9**
a. Bonds	-15.6	-69.5	-13.9	-6.6	-5.3	-2 3	- 9	-.9	-3 9
b. Stocks	-32 3	-63 3	-20.7	-18.5	-12.7	-7.0	-4.6	.7	-4 0
Other flows (quarterly data, s a.)									
6. U.S. direct investment (-) abroad	-41.0	-57.9	-22.7	-24.8	-7.8	n.a.	n.a	n.a.	n.a.
7. Foreign direct investment in U.S.	9.9	21.4	8.1	12.0	3.9	n.a.	n.a	n.a.	n.a.
8. Other (+ = inflow)[6]	18 1	68.4	2.7	4.4	6.9	n.a.	n.a.	n.a.	n.a.
<u>U.S. current account balance (s.a.)</u>	-67.9	-103.9	-30.6	-32.3	-37.0	n.a.	n.a.	n a.	n a.
<u>Statistical discrepancy (s.a.)</u>	-17.1	21.1	4 0	-14.5	-3 5	n.a.	n.a.	n.a.	n.a.

1. The sum of official capital, private capital, the current account balance, and the statistical discrepancy is zero. Details may not sum to totals becuse of rounding.
2. Changes in dollar-denominated positions of all depository institutions and bank holding companies plus certain transactions between broker-dealers and unaffiliated foreigners (particularly borrowing and lending under repurchase agreements). Includes changes in custody liabilities other than U S. Treasury bills.
3. Includes commissions on securities transactions and therefore does not match exactly the data on U.S. international transactions published by the Department of Commerce.
4. Includes Treasury bills.
5. Includes U.S. government agency bonds.
6. Transactions by nonbanking concerns and other banking and official transactions not shown elsewhere plus amounts resulting from adjustments made by the Department of Commerce and revisions in lines 1 through 5 since publication of the quarterly data in the <u>Survey of Current Business</u>.
n.a. Not available. * Less than $50 million.

and government agency bonds (line 4b) were also significant, but foreigners continued to sell U.S. corporate stocks (line 4c).

U.S. net purchases of foreign stocks and bonds (lines 5a and 5b) rebounded strongly in October. Bond purchases were almost entirely from Europe and Canada. More than half of stock purchases were also from developed countries. However, there were also net purchases of stocks from Indonesia, China, Hong Kong, and South Korea.

For the first ten months of 1994, U.S. net purchases of foreign bonds were down sharply from the 1993 pace. In fact, U.S. residents were net sellers of bonds in Europe. Bond purchases in Latin America (excluding the Caribbean financial centers) were up in 1994, but only because of more than $5 billion in Brazilian bonds acquired as part of that country's bank debt rescheduling. Rising interest rates on bonds denominated in dollars and many other major currencies produced capital loses for holders of long-term bonds and outflows from U.S. international bond funds.

U.S. net purchases of foreign stocks in the first ten months of 1994 have come closer than bonds to maintaining the record 1993 pace. Net purchases of stocks in Japan were very large, particularly in the first quarter, and accounted for one-third of U.S. net purchases in the first 10 months of 1994. Net purchases in the rest of the world were down from the 1993 pace. In particular, the developing countries that received the largest net equity inflows from the United States in 1993 (Hong Kong, Mexico, Argentina, Brazil, and Singapore) have all received smaller inflows in 1994. U.S. investor interest has picked up, though, in a wide assortment of other developing countries, including South Korea, Chile, Indonesia, China, India, and Peru.

INTERNATIONAL BANKING DATA 1/
(Billions of dollars)

	1991 Dec.	1992 Dec.	1993 Dec.	1994 Mar.	June	Sep.	Oct.	Nov. 2/
1. Net claims of U.S. banking offices (excluding IBFs) on own foreign offices and IBFS	-35.8	-71.6	-122.1	-157.5	-175.4	-200.7	-213.0	-209.6
a. U.S.-chartered banks	12.4	17.0	4.2	-15.1	-29.9	-53.0	-62.7	-63.2
b. Foreign-chartered banks	-48 3	-88.6	-126.3	-142.4	-145.6	-147.7	-150.2	-146.4
2. Credit extended to U.S. nonbank residents								
a. By foreign branches of U.S. banks	23.9	24.8	21.8	21.4	22.2	23.2	22.8	22.9
b. By Caribbean offices of foreign-chartered banks	n.a.	n.a.	90.9	88.6	83.9	n.a.	n.a.	n.a.
3. Eurodollar holdings of U.S. nonbank residents								
a. At all U.S.-chartered banks and foreign-chartered banks in Canada and the United Kingdom	102.9	90.0	77.8	75.1	73.6	80.9	85.0	86.2
b. At the Caribbean offices of foreign-chartered banks	n.a.	n.a.	79.2	84.2	82.1	n.a.	n.a.	n.a.
MEMO: Data as recorded in the U.S. international transactions accounts								
4. Credit extended to U.S. nonbank residents	179	192	202	207	n.a.	n.a.	n.a.	n.a.
5. Eurodeposits of U.S. nonbank residents	239	237	235	234	n.a.	n.a.	n.a.	n.a.

1. Data on lines 1 through 3 are from Federal Reserve sources and sometimes differ in timing from the banking data incorporated in the U.S. international transactions accounts.

Lines 1a, 1b, and 2a are averages of daily data reported on the FR 2950 and FR 2951.

Lines 2b and 3b are end-of-period data reported quarterly on the FFIEC 002s.

Line 3a is an average of daily data (FR 2050) supplemented by the FR 2502 and end of quarter data supplied by the Bank of Canada and the Bank of England. There is a break in the series in April 1994.

Lines 4 and 5 are end-of-period data estimated by BEA on the basis of data provided by the BIS, the Bank of England, and the FR 2502 and FFIEC 002s. It includes some foreign-currency denominated deposits and loans. Source: SCB

2. Data for November is a monthly average through November 28.

Foreign Exchange Markets

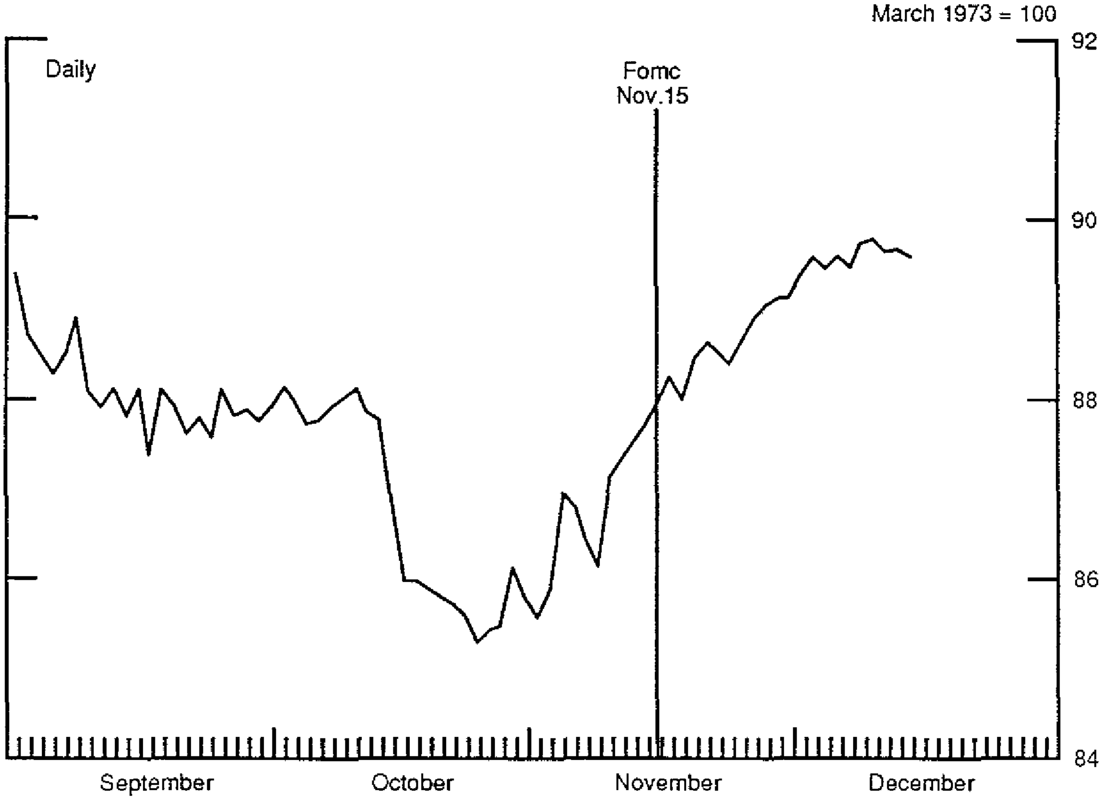
Since the November 15 FOMC meeting, the weighted average value of the dollar, shown in the chart, has risen 2 percent. The dollar rose by similar amounts against the mark and the yen. The larger than expected increase in U.S. short-term rates on November 15 reassured the market of the Federal Reserve's determination to contain inflation and contributed to the dollar's rise early in the period. The dollar continued strengthening for most of the period, buoyed in large part by strong U.S. labor market data and the rising expectation that the Federal Reserve would tighten again before the end of the year. The dollar rose only 1-1/2 percent on balance against British sterling; tightening by the Bank of England helped stem the decline of the U.K. currency.

Three-month interest rates rose about 20 to 40 basis points in most foreign G-10 countries during the intermeeting period, but rose about 170 basis points in Canada, 70 basis points in Italy, and 50 basis points in France. Three-month rates remained about unchanged in Japan.

The large rise in Canadian short-term rates is mainly a response to concerns about large and stubborn fiscal deficits of the provincial and central governments, which weighed on the Canadian dollar over the period. The rise in three-month rates to a lesser extent reflects the Bank of Canada's 50 basis point tightening of overnight rates during the period and anticipated further tightening in response to strong growth of economic activity.

U.K. short-term rates rose 20 basis points during the period after the Bank of England raised its minimum lending rate by 50 basis points on December 7. Most market participants had not expected a rate rise of this magnitude until early next year.

Weighted Average Exchange Value of the Dollar



INTEREST RATES IN MAJOR INDUSTRIAL COUNTRIES

	Three-month Rates			10-year Bond Yields		
	Nov. 15	Dec. 14	Change	Nov. 15	Dec. 14	Change
Germany	5.15	5.45	0.30	7.40	7.49	0.09
Japan	2.33	2.34	0.01	4.64	4.51	-0.13
United Kingdom	6.13	6.31	0.18	8.61	8.53	-0.08
Canada	5.77	7.45	1.68	9.09	9.20	0.11
France	5.50	5.97	0.47	8.12	8.08	-0.04
Italy	8.63	9.31	0.68	11.86	12.30	0.44
Belgium	5.10	5.50	0.40	8.25	8.34	0.09
Netherlands	5.11	5.54	0.43	7.50	7.67	0.17
Switzerland	3.81	4.13	0.32	5.38	5.35	-0.03
Sweden	8.36	8.60	0.24	10.85	10.89	0.04
Weighted-average foreign	5.08	5.46 p	0.38	7.71	7.74 p	0.03
United States	5.74	6.40 p	0.66	7.92	7.82 p	-0.10

In Italy, short-term increases in interest rates reflected ongoing turmoil within the Berlusconi government. In France, short-term rates moved higher after Jacques Delors announced that he does not intend to run for President. Delors was viewed as a strong proponent of EMU, and his withdrawal from the race is viewed as increasing the chances that EMU could emerge as an issue in the Presidential election, or that the next President of France may not be as staunch a supporter of EMU.

Weighted average foreign long-term interest rates were little changed on balance during the intermeeting period. Long-term rates rose about 10 basis points in Germany and Canada and declined by about the same amounts in the United Kingdom and Japan.

Developments in Foreign Industrial Countries

In the third quarter, growth of real GDP appears to have exceeded potential output growth in all of the major foreign industrial countries for the first time in the current recovery. Growth in Japan and Germany accelerated in the third quarter on the strength of private consumption and investment. In France, the

United Kingdom, and Canada, growth slowed in the third quarter but remained at least 3 percent. The slowdowns in France and the United Kingdom were largely accounted for by declines in the contribution of net exports. In contrast, deceleration in Canada was more than accounted for by a decline in domestic demand, particularly in investment. Italian industrial production grew robustly in the third quarter but somewhat slower than in the second quarter. (Third-quarter GDP data are not yet available for Italy.) In the fourth quarter, the pace of activity in the major foreign industrial countries generally appears to have slowed somewhat and may have fallen in Italy due to recent strikes and a major flood.

Consumer-price inflation remains subdued in most major foreign industrial countries. Unemployment rates have stabilized or begun to fall, although they generally remain well above estimates of structural unemployment rates.

Individual country notes. In Japan, real GDP increased 3.7 percent (SAAR) in the third quarter, after increasing a revised 0.7 percent in the second quarter. The third-quarter increase was driven by a strong recovery in private consumption and the first positive growth in private plant and equipment investment since the third quarter of 1991. The latest rise in GDP was the third consecutive quarterly increase, pointing to a firming of the economic recovery.

JAPANESE REAL GDP
(percent change from previous period, SAAR)

	1992	1993	1993		1994		
	Q4/Q4	Q4/Q4	Q3	Q4	Q1	Q2	Q3
GDP	-0.4	-0.5	1.0	-3.2	3.2	0.7	3.7
Total Domestic Demand	-0.9	0.5	2.0	-1.3	2.1	0.7	3.9
Consumption	0.2	1.8	1.5	2.8	5.3	-0.9	4.3
Investment	-2.2	-1.4	2.0	-6.2	-7.0	1.9	3.7
Government Consumption	2.9	0.9	10.6	-0.3	4.4	0.1	6.6
Exports	3.6	-2.3	-1.6	-8.0	15.3	14.2	0.7
Imports	-0.7	5.0	1.6	9.2	7.0	13.6	4.4
Net Exports (contribution)	0.6	-1.0	-0.5	-2.4	1.2	0.1	-0.5

Data for the fourth quarter are mixed, but on balance suggest a continuation of growth, albeit at a slower pace. In October, industrial production edged down somewhat, while housing starts rebounded. There was a large decline in new car registrations. The recent stability in the unemployment rate and in the job offers/applicants ratio suggest that the labor market has hit bottom.

JAPANESE ECONOMIC INDICATORS
(percent change from previous period except where noted, SA)

	1993	1994						
	Q4	Q1	Q2	Q3	Q4	Aug.	Sept.	Oct.
Industrial Production	-3.7	1.9	1.1	1.7	n.a.	3.9	-1.3	-0.3
Housing Starts	-2.0	3.7	1.7	-1.7	n.a.	4.1	-6.9	1.4
Machinery Orders	-0.7	6.9	-16.5	19.3	n.a.	1.8	3.4	n.a
New Car Registrations	-3.3	8.5	-7.5	8.9	n.a.	7.8	1.6	-12.2
Unemployment Rate (%)	2.7	2.8	2.8	3.0	n.a.	3.0	3.0	3.0
Job Offers Ratio*	0.66	0.66	0.64	0.63	n.a.	0.63	0.64	0.64
Business Sentiment**	-56	-56	-50	-39	-29	--	--	--

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

In the Bank of Japan's November economic survey (Tankan), the index of business sentiment of major manufacturing firms registered -29, up from -39 in the previous survey taken in August, the third consecutive increase after more than four years of decline. However, firms predicted a roughly 4 percent decline in investment in the fiscal year that began in April, about the same predicted decline as in August's survey.

Economic recovery is continuing at a brisk pace in western Germany. Real GDP rose 5.3 percent (SAAR) in the third quarter following a 4 percent gain in the second quarter. Since the recession trough in the first quarter of last year, real GDP has risen 4 percent and is now almost 1 percent above its previous peak.

The largest increase in third quarter spending was in consumption, which rose 6.1 percent, more than reversing the second-quarter decline. Investment spending was up moderately, due to a substantial gain in equipment purchases. Construction expenditures, which surged during the mild winter, were unchanged in the third quarter after falling a little in the second quarter. Net exports dropped somewhat.

WEST GERMAN REAL GDP
(percent change from previous period, SAAR)

	1992	1993	1993		1994		
	Q4/Q4	Q4/Q4	Q3	Q4	Q1	Q2	Q3
GDP	0.3	-0.5	4.4	-1.2	2.2	4.0	5.3
Total Domestic Demand	1.7	-2.4	4.6	-5.2	3.4	3.6	6.4
Consumption	3.7	-0.8	8.4	-1.3	1.4	-3.9	6.1
Investment	-2.8	-8.2	1.3	-9.3	18.0	-2.7	5.0
Government Consumption	4.4	-1.8	4.1	2.4	-3.9	-1.7	4.4
Inventories (contribution)	-0.6	0.2	-1.3	-2.8	-0.1	6.4	0.3
Exports	-2.8	0.8	5.2	9.2	3.4	20.3	-0.5
Imports	1.2	-5.1	6.2	-2.9	8.1	23.3	1.7
Net Exports (contribution)	-1.3	1.7	0.1	3.7	-1.0	0.6	-0 7

Recent data suggest that economic growth is continuing at a robust pace in the fourth quarter, and forward-looking indicators are positive as well. Industrial production in October was about 1-1/2 percent above the third-quarter level, while orders for manufactured goods surged in September and remained at a high level in October. Most of the recent strength in orders was due to foreign demand, suggesting renewed strength in exports in the coming months. Other business indicators, including manufacturers' production plans and firms' assessment of their inventory situation, also showed an improvement in October. However, retail sales dropped sharply in October and were about 2 percent lower than the third-quarter average.

The recovery has still had only a minor impact on the labor market, as the unemployment rate edged down to 9.1 percent in

November Meanwhile, inflation continues to decelerate. In November, 12-month consumer price inflation for western Germany was 2.7 percent, the lowest rate since early 1991. Wage growth continues to be relatively moderate, with earnings per hour up only about 1-1/2 percent in the year ending in September.

WEST GERMAN ECONOMIC INDICATORS
(percent change from previous period except where noted, SA)

	1993	1994						
	Q4	Q1	Q2	Q3	Aug.	Sept.	Oct.	Nov.
Industrial Production	-0.3	0.4	2.6	1.0	-2.5	1.1	1.6	n.a.
Manufacturing Orders	-0.7	2.5	4.0	1.9	-2.0	5.4	-0.2	n.a.
Capacity Utilization	78.1	79.5	81.4	82.9	--	--	--	--
Retail Sales Volume	-1.9	1.4	-3.2	1.2	2.4	1.2	-3.7e	n.a.
Unemployment Rate (%)	9.0	9.2	9.3	9.2	9.3	9.2	9.2	9.1
Production Plans*	-8.0	3.3	7.7	8.7	6.0	11.0	13.0	n.a.

e Estimated
* Percent of manufacturing firms planning to increase production in the next three months minus those planning to decrease production.

Production in eastern Germany has continued to expand at a rapid rate, with industrial production in September up 14 percent from its year-earlier level. Orders for manufactured goods were 16 percent above their previous-year level in September. The unemployment rate fell in November to 13 percent, 2 percentage points below its year-earlier level.

In France, real GDP growth slowed to 3 percent (SAAR) in the third quarter from 4.6 percent in the second. The slowdown occurred because the contribution from net exports turned negative as imports continued to grow at a relatively rapid pace and exports were almost flat. Also contributing was a modest slowing in consumption growth. Inventories made a significant positive contribution to growth.

Monthly indicators suggest that, on balance, growth may slow further in the fourth quarter. Consumption of manufactured products (one-third of total consumption) fell very sharply in October, while retail sales (SA) were flat. Preliminary data for large stores

FRENCH REAL GDP
(percent change from previous period, SAAR)

	1992	1993	1993		1994		
	Q4/Q4	Q4/Q4	Q3	Q4	Q1	Q2	Q3
GDP	0.3	-0.5	0.7	0.5	3.4	4.6	3.0
Total Domestic Demand	0	-2.0	-1.8	-0.5	8.1	3.3	4.7
Consumption	1.4	0.4	2.1	-0.1	0.2	4.4	3.5
Investment	-2.9	-4.6	0	-0.2	-0.6	3.5	3.5
Government Consumption	2.3	0.2	1.2	0.7	1.9	1.6	2.6
Inventories (contribution)	-0.6	-1.3	-3.3	-0.5	7.5	-0.4	1.3
Exports	2.0	2.9	14.4	3.8	-3.7	11.0	0.5
Imports	1.0	-2.6	4.3	0.3	13.2	6.6	6.5
Net Exports (contribution)	0.3	1.5	2.5	0.9	-4.5	1.1	-1.6

suggest they were weak in November as well. INSEE's index of consumer sentiment worsened slightly in November for the second month in a row. Output indicators were somewhat more favorable. INSEE's October business survey showed orders were strong in all sectors except automobiles. Foreign orders were especially strong. Also, inventories were considered to be below desired levels. Unemployment edged down in October from its all-time peak of 12.7 percent.

FRENCH ECONOMIC INDICATORS
(percent change from previous period except where noted, SA)

	1993	1994						
	Q4	Q1	Q2	Q3	Aug.	Sep.	Oct.	Nov.
Industrial Production*	-0.7	1.2	2.7	1.6	1.8	-0.3	n.a	n.a
Unemployment Rate (%)	12.3	12.5	12.6	12.6	12.6	12.7	12.6	n.a
Consumption of Manufactured Products	-1.9	0.7	1.5	1.5	1.0	0.1	-2.5	n.a
Consumer Prices (NSA)	0.5	0.4	0.6	0.1	0.0	0.3	0.3	0.0

* French statistical authorities release an average for July and August.

Consumer price inflation edged up in November to 1.6 percent at a 12-month rate. However, underlying inflation, which excludes a large increase in fruit and vegetable prices, declined slightly to 1.5 percent. This good inflation performance has been supported by a slight slowing of wage inflation to 2.3 percent in the third quarter.

In the United Kingdom, the pace of activity slowed in the third quarter from very rapid increases in the second quarter, due primarily to a decline in the contribution of net exports. In addition, domestic demand growth decelerated for the third consecutive quarter as inventory accumulation slowed.

UNITED KINGDOM REAL GDP
(percent change from previous period, SAAR)

	1992	1993	1993		1994		
	Q4/Q4	Q4/Q4	Q3	Q4	Q1	Q2	Q3
GDP	0.3	2.7	3.7	3.5	3.8	5.5	3.8
Total Domestic Demand	0.8	2.9	2.4	4.0	3.1	2.2	1.8
Consumption	1.3	3.1	4.1	3.7	1.4	2.0	2.0
Fixed Investment	0.0	1.7	7.0	9.1	9.4	-4.8	-3.8
Government Consumption	-0.6	1.9	1.4	0.8	1.2	1.6	1.3
Inventories (contribution)	0.0	0.3	-1.7	0.0	0.4	1.6	0.9
Exports	3.9	4.3	12.5	9.2	11.6	8.3	5.5
Imports	6.5	3.9	7.2	12.1	8.7	-4.3	-0.2
Net Exports (contribution)	-0.8	0.0	1.1	-1.0	0.5	3.4	1.5
Non-oil GDP	0.2	2.4	3.3	2.4	3.2	4.9	4.0

In the fourth quarter, growth may slow somewhat further, but it appears to have remained robust. Although essentially flat in October, industrial production and retail sales were 0.9 percent and 0.3 percent above their third-quarter averages, respectively. Producer and consumer confidence edged back slightly in October and November from their strong showing in the third quarter. In November, the unemployment rate fell to 8.8 percent, and job vacancies increased to their highest level in over four years. Underlying wage inflation in October picked up to 4 percent (SAAR) from 3.75 percent recorded most of this year, and underlying inflation increased to 2.3 percent in November on the strength of food price increases.

On November 29, the government released its budget, in which the projected public sector borrowing requirement (PSBR) for the current fiscal year was lowered to \34.5 billion (5 percent of GDP)

UNITED KINGDOM ECONOMIC INDICATORS
(percent change from previous period, SA, except where noted)

	1993	1994						
	Q4	Q1	Q2	Q3	Aug.	Sep.	Oct.	Nov.
Industrial Production	1.3	1.1	2.2	1.2	0.3	1.1	0.1	n.a.
Retail Sales	0.8	1.1	0.9	0.7	-0.2	0.4	0.1	n.a.
Unemployment Rate (%)	10.0	9.8	9.4	9.2	9.2	9.1	8.9	8.8
RPI ex. MIP *	2.7	2.7	2.4	2.2	2.3	2.0	2.0	2.3
Input Prices *	-0.7	-3.0	0.6	4.5	4.1	6.3	6.9	7.9

* NSA, percent change from preceding year. Retail price inflation excludes mortgage interest payments.

from \45.4 billion in FY1993-94. The PSBR for FY1995/96 was lowered to \21.5 billion (3 percent of GDP) from the summer forecast of \28 billion.

On December 7, the government increased the minimum lending rate 50 basis points to 6-1/4 percent. The rate was last changed on September 12 when it was also raised 50 basis points. According to Chancellor Clarke, the increase was taken "in order to sustain economic recovery with low inflation" and followed the surprising defeat of a government budget measure in Parliament the previous night. (The measure would have increased the VAT on home fuel to 17.5 percent from 8 percent.)

Indicators in Italy suggest that the recovery continued to move ahead in the third quarter. Although capacity utilization edged down slightly, industrial production expanded briskly, the unemployment rate fell sharply as employment rose, and business sentiment firmed further. However, activity in the fourth quarter looks weaker. Consumer confidence dipped in October and November due to uncertainty over pension reform, and a forecast released by ISCO, a respected research institute, calls for a 2.4 percent (SAAR) decline in GDP in the fourth quarter after a projected 3.6 percent increase in the third quarter because of widespread strikes by labor unions and last month's devastating flood.

Although consumer price inflation has remained steady near 4 percent, wholesale and producer prices recently have accelerated somewhat.

ITALIAN ECONOMIC INDICATORS
(non-seasonally adjusted except where noted)

	1993	1994						
	Q4	Q1	Q2	Q3	Aug.	Sep.	Oct.	Nov.
Industrial Production*	0.2	0.1	4.6	3.6	4.7	-4.1	n.a.	n.a.
Capacity Utilization (%)	74.4	74.5	76.0	75.8	--	--	--	--
Unemployment Rate (%)	11.3	11.3	11.6	11.0	--	--	--	--
Business Sentiment** (%)	4	19	17	19	21	21	16	n.a.
Consumer Confidence	96.3	100.6	112.8	117.1	117.1	117.4	112.0	112.9

* Percent change from previous period (seasonally adjusted).
** Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook.

On December 1, the Berlusconi government signed an agreement with the labor unions that will postpone most elements of pension reform until June 1995 when legislation will be drafted. In return, the unions agreed to call off a general strike planned for December 2 and to continue to abide by the July 1993 labor agreement that limits wage growth to the government's projected inflation rate.

In Canada, real GDP continued to expand at a vigorous pace in the third quarter. Most of the strength came from merchandise exports; final domestic demand increased only 1.1 percent (SAAR), its slowest advance in a year and a half. After surging in the second quarter, fixed investment fell as a drop in residential construction offset moderate increases in machinery and equipment investment and nonresidential construction.

Early indicators for the fourth quarter suggest that economic activity is continuing at a robust pace. Full-time employment in both goods-producing and service industries grew strongly in November. Slack still remains in labor markets, however, and

CANADIAN REAL GDP
(percent change from previous period, SAAR)

	1992 Q4/Q4	1993 Q4/Q4	1993 Q3	1993 Q4	1994 Q1	1994 Q2	1994 Q3
GDP	0.5	3.2	1.3	3.6	4.3	6.7	4.7
Total Domestic Demand	-1.2	3.4	0.7	4.9	2.3	4.7	-0.1
Consumption	0.6	2.2	1.7	2.4	5.0	3.0	2.6
Fixed Investment	-5.8	4.5	3.6	11.3	0.8	12.9	-0.6
Government Consumption	0.8	-0.1	-0.8	0.2	-3.3	-3.9	-1.5
Inventories (contribution)	-0.5	1.3	-0.9	1.1	-0.1	1.1	-1.3
Exports	9.4	10.9	6.8	14.3	4.1	22.2	21.4
Imports	3.3	11.1	4.4	15.6	1.7	14.5	8.3
Net Exports (contribution)	1.7	-0.3	0.7	-0.7	0.8	2.2	4.3

productivity gains and low wage increases have led to continued declines in unit labor costs. Consumer price inflation remains subdued. Excluding the effects of recent excise tax cuts, 12-month inflation was 1.3 percent in October.

CANADIAN ECONOMIC INDICATORS
(percent change from previous period except where noted, SA)

	1993 Q4	1994 Q1	1994 Q2	1994 Q3	1994 Aug.	1994 Sept.	1994 Oct.	1994 Nov.
Industrial Production	1.0	0.8	3.2	2.2	1.2	-0.4	n.a.	n.a.
Employment	0.3	0.4	0.8	1.0	0.2	0.5	-0.2	0.7
Unemployment Rate (%)	11.1	11.0	10.7	10.2	10.3	10.1	10.0	9.6
Unit Labor Costs**	-0.8	-1.2	-0.6	-1.3	--	--	--	--
Consumer Prices**	1.8	0.6	0.0	0.2	0.2	0.2	-0.2	n.a.

* NSA.
** Percent change from year earlier.

The Bank of Canada raised its target for the overnight (call) rate by 25 basis points on November 28 and an additional 25 basis points on December 8 to a range of 5-1/4 - 5-3/4 percent. These moves came after three consecutive 25 basis point reductions in the call rate target since July.

EXTERNAL BALANCES
(Billions of U.S. dollars, seasonally adjusted)

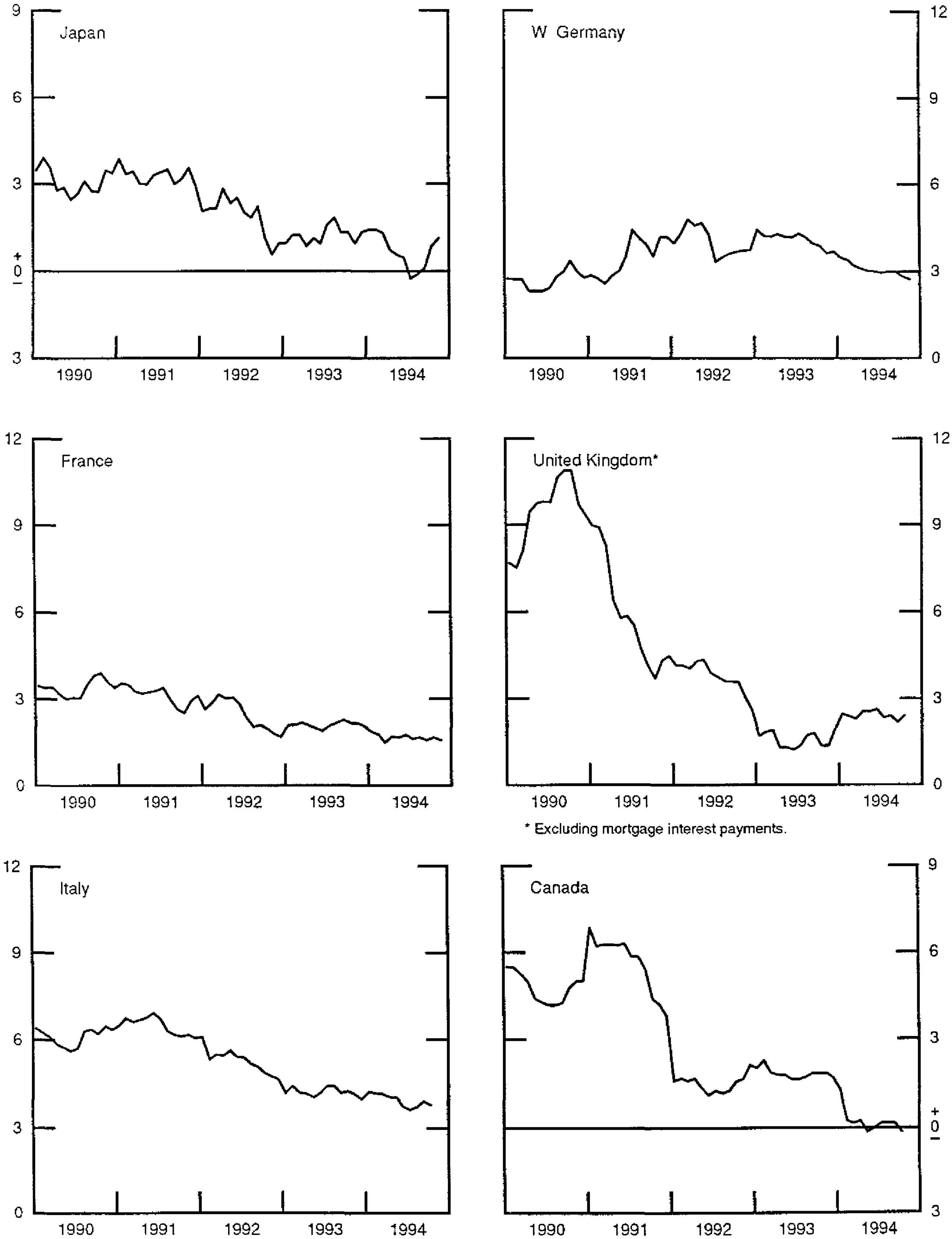
	1994					
	Q1	Q2	Q3	Aug.	Sep.	Oct.
Japan: trade	31.3	30.9	28.4	8.3	8.5	8.7
current account	33.8	34.2	32.0	9.5	10.5	8.0
Germany: trade	8.6	12.8	10.5	4.6	3.7	n.a.
current account*	-6.6	-3.1	-16.2	-4.2	-3.4	n.a.
France: trade	3.6	4.1	4.3	1.6	1.7	n.a.
current account	3.5	n.a.	n.a.	--	--	--
U.K.: trade	-4.4	-3.7	-2.5	-0.8	-0.8	n.a.
current account	-1.9	-1.1	n.a.	--	--	--
Italy: trade	6.9	6.1	n.a.	n.a.	n.a.	n.a.
current account*	1.3	3.3	n.a.	2.1	n.a.	n.a.
Canada: trade	1.5	2.0	3.7	1.0	1.2	n.a.
current account	-5.5	-5.5	-3.7	--	--	--

* Not seasonally adjusted.
-- Data not available on a monthly basis.

12-14-94

Consumer Price Inflation for Major Foreign Countries

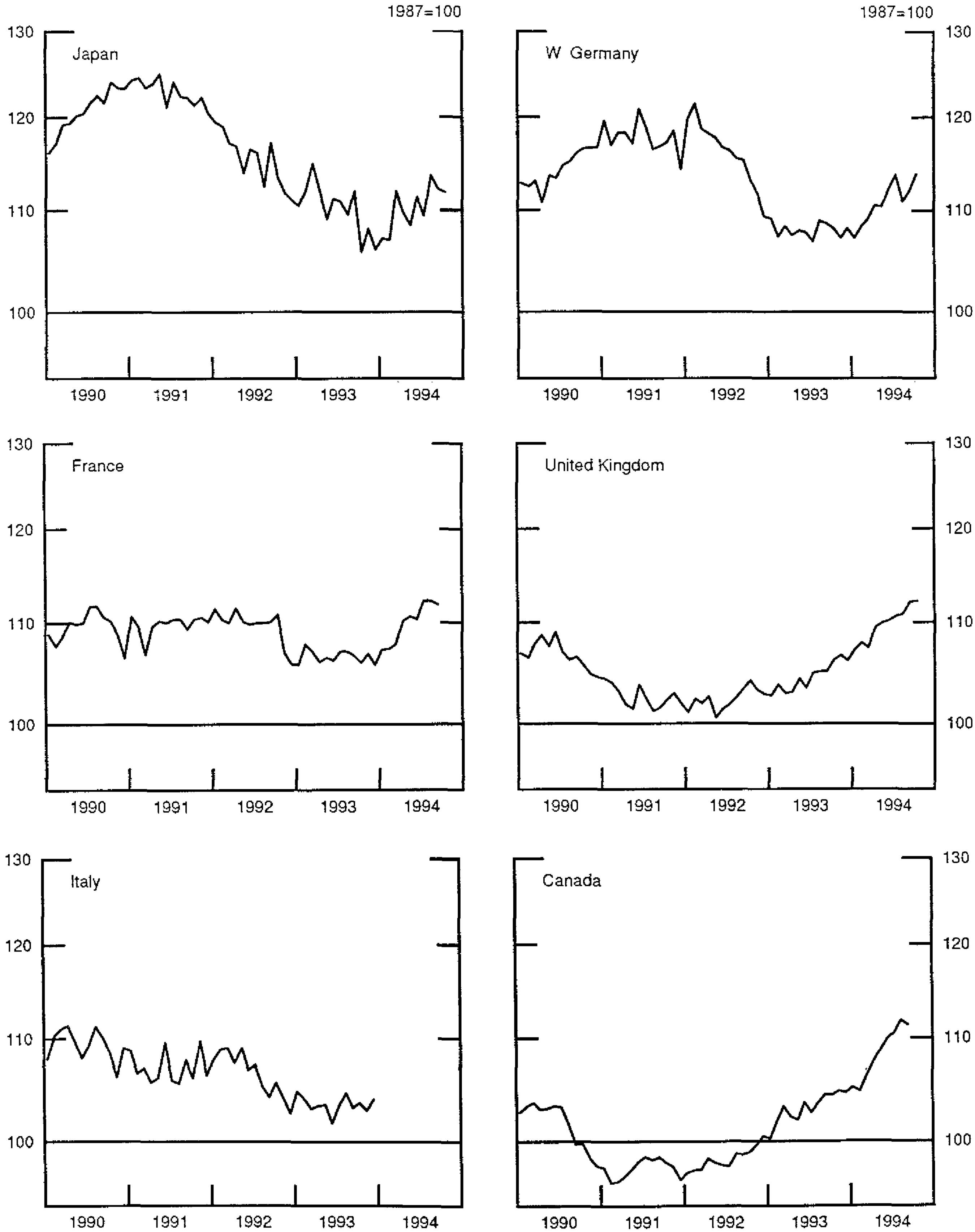
(12-month percent change)



* Excluding mortgage interest payments.

Industrial Production for Major Foreign Countries

(Ratio scale; seasonally adjusted; monthly)



Economic Situation in Other Countries

Economic activity appears strong in major developing countries and economies in transition with the exceptions of Venezuela and Russia. Inflation performance has been mixed.

In Mexico, real GDP has grown strongly in recent quarters while inflation has remained restrained; newly inaugurated President Ernesto Zedillo has chosen a cabinet that promises continued free-market policies. In Brazil, growth has picked up while inflation remains low following the stabilization of the exchange rate last July; President-elect Henrique Cardoso's prospective choices for Central Bank head and Economy Minister have been closely associated with the disinflation program. Argentina and Taiwan continue to combine steady growth with low inflation. In Korea, very robust economic activity has taken place alongside stable inflation, but in China, rapid growth has fueled strong inflationary pressures. Both Russia and Venezuela have experienced contractions of economic activity combined with rising inflation. However, there are signs that Russian output may be stabilizing.

Individual country notes. In Mexico, real GDP was 2.9 percent above its year-earlier level in the January-September period, with year-over-year growth in the third quarter alone coming in at 4.5 percent. Industrial production has been particularly buoyant, registering 6.1 percent above its year-earlier level in September. While these high rates of growth in part reflect the depressed level of the economy in the third quarter of 1993, they also signal that the economic recovery is becoming firmly established. Increases in public spending are believed to be contributing to the recovery, but Mexico's general government budget continued to show a small surplus for the January-September period, although it was much reduced from its year-earlier level.

Notwithstanding the stronger pace of activity, consumer price inflation has remained quiescent. It registered 6.9 percent on a year-over-year basis in November, slightly above the third quarter's 6.7 percent rate, but equal to the rate averaged in the January-October period. However, the trade deficit has grown to $13.7 billion in the January-September period, up from $10.4 billion in the same period last year.

President Ernesto Zedillo, inaugurated on December 1, chose former Commerce Department head Jaime Serra Puche as Secretary of Finance. While previous Finance Secretary Pedro Aspe, a key figure in Mexico's stabilization program, was not included in Zedillo's cabinet, it is expected that the new economic team will continue the free-market policies of the Salinas Administration. In the 1995 budget proposal sent to Congress on December 9, President Zedillo affirmed the goals of higher growth, lower inflation, and a balanced budget that were contained in the annual social pact signed by the Salinas Administration last September.

In spite of this continuity in economic policymaking, financial markets have remained unsettled due to continued political uncertainty, increased foreign interest rates, and the growing trade deficit. The peso/dollar exchange rate has remained within one percent of the "lower" limit of its fluctuation band. The spread between the rate on three-month peso-denominated Treasury bills and comparable Eurodollar rates registered 858 basis points at the December 14 auction compared with a recent low of 791 basis points at the September 28 auction. The Mexico City stock market is well below its September peak.

In Brazil, growth has been robust while inflation appears to be relatively low. Real GDP in the third quarter was up 6 percent over the third quarter of 1993, compared with growth of 4 percent in

1993. Anecdotal accounts suggest that the credit controls imposed in late October have dampened demand for durable goods, while growth in sales of non-durable goods remains strong. Analysts expect that consumer prices in December will rise by 2.5 percent, compared with an increase of 3 percent in November. Monthly inflation is far below the nearly 50 percent level reached before the new currency, the *real*, was adopted last July.

The trade surplus was $11.9 billion in the January-October period, up from a surplus of $11.4 billion over the same period in 1993, reflecting import growth of 17 percent and export growth of 13 percent. The *real*/dollar exchange rate has remained stable at about 0.85 since September. Under Brazil's current anti-inflation plan, the central bank is committed to maintaining the value of the currency at no lower than one *real* per dollar.

It is widely expected that Central Bank President Pedro Malan will be President-elect Henrique Cardoso's Economy Minister, and Persio Arida, currently head of Brazil's main development bank, will be the new central bank president. Cardoso, who has not confirmed the appointments, takes office January 1. Malan and Arida have been closely associated with Brazil's anti-inflation plan, and their appointments have been regarded as a reaffirmation of Cardoso's commitment to economic reform.

In Argentina, growth is steady while inflation remains low. Industrial production during the first nine months of 1994 was up 5.1 percent from a year earlier. Consumer prices were 3.7 percent higher in November than a year earlier. The cumulative trade deficit for the year through October widened to $4.9 billion compared with its year-earlier level of $2.4 billion. However, in the third quarter, year-over-year export growth registered 22.1

percent, exceeding import growth of 20.7 percent for the first time since the start of the Convertibility Plan in April 1991.

After ceasing auctions in October because it considered the interest rates that were bid to be too high, Argentina resumed its local auctions of 91- and 182-day Treasury bills, which are offered both on a peso- and dollar-denominated basis, on November 22. For 91-day bills, the only offering for which data are available, the government accepted bids for 200 million pesos and $200 million at rates of 9.5 percent and 7.58 percent respectively. These rates represent an increase from the last tender on September 26, when peso-denominated bills were auctioned at 7.5 percent and dollar-denominated bills at 6.2 percent. The increase in the spread reflects growing fears that Argentina's budget may have moved into deficit, raising concerns about the sustainability of the Convertibility Plan.

In Venezuela, the highly expansionary monetary policy implemented by the central bank in recent months has not stopped the decline in economic activity. Consumer price inflation was 4.3 percent in November, down from 5 percent in October but up from monthly rates of about 3 percent last year, despite the imposition of price controls in late June.

The cumulative trade deficit for the year through October was $3.3 billion, down from the deficit of $6.8 billion recorded over the same period in 1993, reflecting a 32 percent decline in imports and a 16 percent increase in exports. The fall in imports reflects continued weak aggregate demand and strict foreign exchange controls imposed in June 1994. The central bank's official reserves, excluding gold, stood at an estimated $8 billion at the end of October.

In <u>China</u>, economic activity and inflationary pressures continue to be strong. Industrial value added rose 24 percent above its year-earlier level in both October and November. Consumer prices in October were 28 percent above their year-earlier level; for the three months ending in October, consumer prices rose at an annual rate of 42 percent.

In the first ten months of 1994, China ran a trade surplus of $2.4 billion, reflecting export growth of 30 percent and import growth of 15 percent over the year-earlier period. In the first ten months of 1994, foreign direct investment was $25 billion. Some financial market participants appear to be reassessing the creditworthiness of Chinese companies, however, in the wake of a recent lawsuit filed by Lehman Brothers against two Chinese companies for nonpayment of debts, as well as other reports of nonpayment by Chinese firms.

In <u>Taiwan</u>, growth continues to be relatively steady, while inflation has been moderate. Real GDP rose 6.1 percent in the third quarter of 1994 from a year earlier, after rising 6.4 percent in the second quarter. Industrial production in October was 9.4 percent higher than a year earlier. Consumer prices in November were 3.9 percent higher than a year earlier. The trade surplus for the January-November period was $7 billion, down slightly from its year-earlier level, reflecting a 9 percent growth in exports and 11 percent growth in imports

Real GDP in <u>Korea</u> increased by 7.7 in the third quarter from the same period a year earlier. Fixed investment continued to expand rapidly, increasing by 11.2 percent during the third quarter. Despite strong growth in economic activity, inflation has remained stable at roughly a 6 percent annual rate since the beginning of this year. Consumer prices rose by 6.1 percent in November from a year earlier.

Merchandise exports increased by 13 percent in the first 10 months of 1994, in part because a substantial real depreciation of the Korean won against the yen has enhanced Korean competitiveness. However, imports rose 19 percent over the same period. This contributed to a widening of the current account deficit for the first ten months of this year to $4.6 billion, from $170 million during the same period a year earlier.

Russian inflation has surged in recent months. Consumer prices, after rising only 5 percent during August 1994--a 30-month low--increased 15 percent in October and 14 percent in November. The government has attributed the jump in inflation to seasonal increases in food prices and to rising import prices triggered by the ruble's sharp depreciation during September and October. It seems unlikely that inflation will fall to 7 percent in December, the target specified in Russia's IMF Systemic Transformation Facility.

The ruble was relatively stable during November and early December, depreciating against the dollar at a steady rate of about 1-1/2 percent a week. On December 14, the MICEX ruble-dollar exchange rate closed at 3368.

According to Russian official statistics, real GDP during the first ten months of 1994 contracted by 15 percent, compared with the same period last year, and industrial production was 22 percent below its year-earlier level. During the fourth quarter, however, economic activity may have begun to stabilize. In October, for example, real GDP grew by 4 percent (year/year). The government recently estimated that the "shadow" economy, which is not included in official statistics, accounts for at least 20 percent of economic activity and is still growing.

Discussions between the Russian government and the IMF on a stand-by arrangement reportedly are making progress, but the Fund has rejected the government's proposed 1995 budget. The IMF estimates that the budget, as written, would generate a deficit equal to 10 percent of GDP, and has urged the government to take steps to increase budget revenues by 3-4 percent of GDP.