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

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Part 2

November 8, 1995

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

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

DOMESTIC NONFINANCIAL DEVELOPMENTS

Recent news on the pace of economic activity has been unusually conflictive. The surprisingly strong advance estimate of third-quarter GDP growth was followed by a further decline in the unemployment rate and a jump in hours worked in October. However, the tone of much of the anecdotal evidence is less robust, and manufacturing activity appears to have contracted last month after expanding only moderately in the third quarter. The rate of inflation has remained relatively low and stable, with firms benefiting from decelerating labor costs.

Third-Quarter GDP

According to the advance estimate from the Bureau of Economic Analysis, the growth in real GDP last quarter was $57 billion (1987 dollars), or 4.2 percent at an annual rate. BEA had to make a number of assumptions about missing data, and the incoming figures have deviated considerably from these assumptions. Manufacturing inventory investment and outlays for construction were larger than BEA wrote in, but wholesale inventory investment declined unexpectedly. On net, as best we can estimate, these numbers appear to point to a very slight downward revision.

INCOMING DATA LESS ADVANCE ESTIMATE FOR Q3
(Billions of 1987 dollars)

Source	Revision[1]
Construction put in place	
State and local government	1.4
Residential construction	.1
Nonresidential construction	1.4
Manufacturers' shipments and inventories	
Producers' durable equipment	.5
Inventory investment	5.2
Wholesale inventory investment	-11.7
Total	-3.1

1 FR staff estimate.

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

	1993	1994	1995 Q1	1995 Q2	1995 Q3	1995 Aug.	1995 Sept.	1995 Oct.
	----------Average monthly changes---------							
Nonfarm payroll employment[2]	235	294	226	82	114	263	50	116
(Previous)						(262)	(121)	
Private	215	273	216	70	107	199	93	121
Manufacturing	4	30	18	-32	-36	4	-38	-21
Durable	3	25	20	-12	-8	18	-14	-15
Nondurable	0	5	-2	-20	-28	-14	-24	-6
Construction	24	30	30	-9	9	7	25	28
Trade	57	75	20	24	36	-7	49	20
Finance, insurance, real estate	19	4	2	-3	9	9	9	18
Services	100	117	130	87	90	166	67	57
Business services	36	46	28	6	53	81	68	-1
Total government	20	21	10	12	7	64	-43	-5
Private nonfarm production workers	194	242	194	54	94	163	93	151
Manufacturing production workers	10	31	16	-31	-28	12	-29	-7
Total employment[3]	209	326	235	-263	218	-180	361	259
Nonagricultural	219	289	179	-181	278	-133	450	77
Memo:								
Aggregate hours of private production workers (percent change)	.3	.4	.1	.0	.2	-.4	.5	.8
Average workweek (hours)	34.5	34.7	34.7	34.4	34.5	34.4	34.5	34.7
Manufacturing (hours)	41.5	42.0	42.1	41.5	41.5	41.5	41.7	41.5

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)

	1993	1994	1995 Q1	1995 Q2	1995 Q3	1995 Aug.	1995 Sept.	1995 Oct.
Civilian unemployment rate (16 years and older)	6.8	6.1	5.5	5.7	5.6	5.6	5.6	5.5
Teenagers	19.0	17.6	16.8	17.2	17.8	17.7	17.5	17.1
20-24 years old	10.5	9.7	8.7	8.8	9.8	9.9	10.1	9.5
Men, 25 years and older	5.8	4.8	4.2	4.4	4.2	4.2	4.3	3.9
Women, 25 years and older	5.4	4.9	4.4	4.5	4.4	4.4	4.2	4.5
Full-time workers	6.8	6.1	5.4	5.6	5.6	5.6	5.6	5.4
Labor force participation rate	66.2	66.6	66.9	66.6	66.6	66.5	66.6	66.6
Teenagers	51.5	52.7	53.9	54.0	53.6	53.4	53.6	53.0
20-24 years old	77.1	77.0	77.3	76.7	76.3	76.2	76.1	75.8
Men, 25 years and older	76.2	76.0	76.4	76.0	75.8	75.7	75.9	75.8
Women, 25 years and older	57.1	58.1	58.2	58.1	58.5	58.4	58.4	58.6

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

We share the widespread uneasiness about the high third-quarter number, and upcoming data--such as those on retail trade and international trade due out next week--could significantly alter the picture. Nonetheless, we have no compelling reason to anticipate that GDP will be appreciably different from the advance estimate. One consideration in this regard is that the available evidence on the income side of the accounts does not call the published nominal GDP figure into question, and profit reports that have been published to date seem to support a robust estimate.[1]

Employment and Unemployment

Moving into the fourth quarter, labor demand continued to expand at a solid pace. Nonfarm payroll employment increased a comparatively mild 116,000 in October, held down, in part, by the net loss of about 23,000 strikers from the job count.[2] However, average weekly hours of production or nonsupervisory workers jumped 0.2 hour, to 34.7 hours, pushing aggregate hours up 0.8 percent in October. And the unemployment rate fell 0.1 percentage point last month, to 5.5 percent--the lowest level since last March.

In manufacturing, the strike at Boeing by 33,000 members of the International Association of Machinists, which began on October 6, contributed to a decline of 21,000 jobs; adjusted for changes in strike activity, however, the net gain was still only 5,000.[3] Employment rose in lumber, fabricated metals, industrial machinery, food, chemicals, and electronic equipment but fell in furniture,

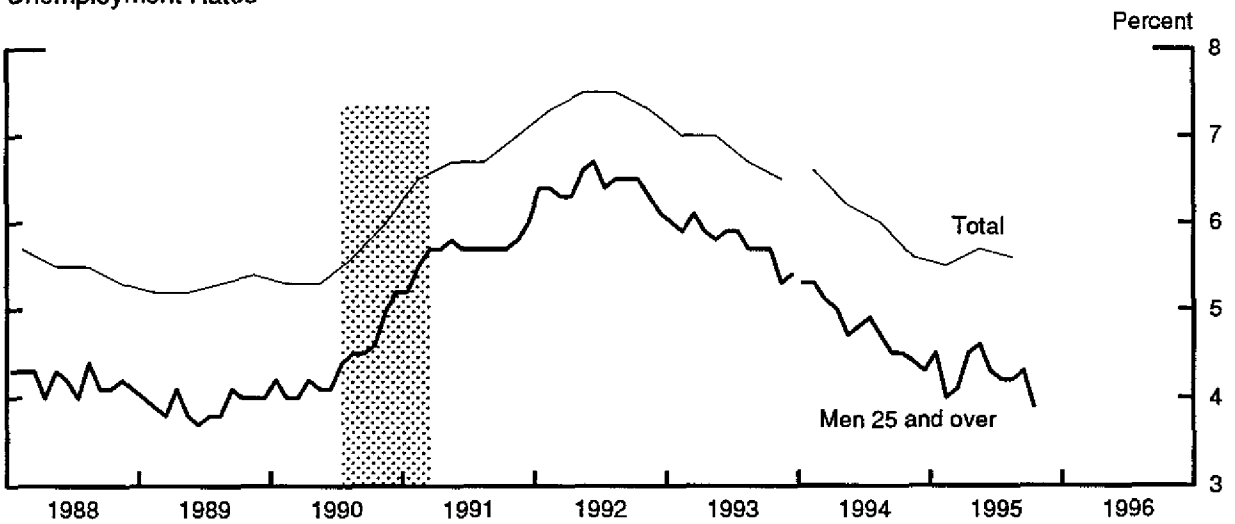
1. Furthermore, the growth of real output when measured on a chain-index basis is considerably lower than the 1987-based figure and less difficult to reconcile with the data on labor inputs.

2. In addition, September's growth in employment was revised down 70,000, to 50,000, with transportation and services undergoing the largest revisions.

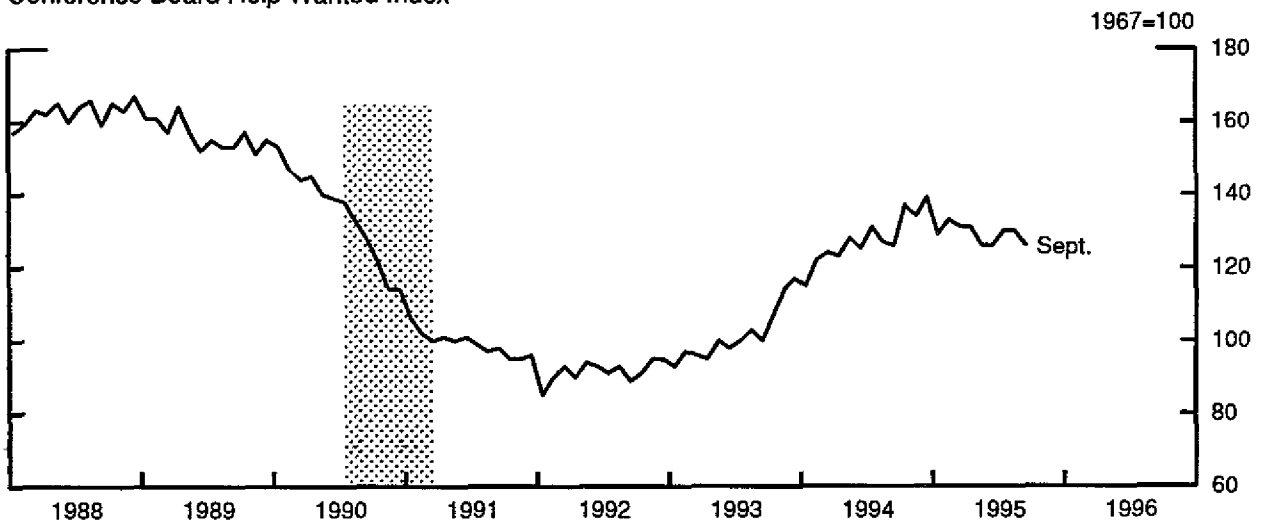
3. About 7,000 Boeing workers began the strike one day into the pay period and so were recorded as employed.

Labor Market Indicators

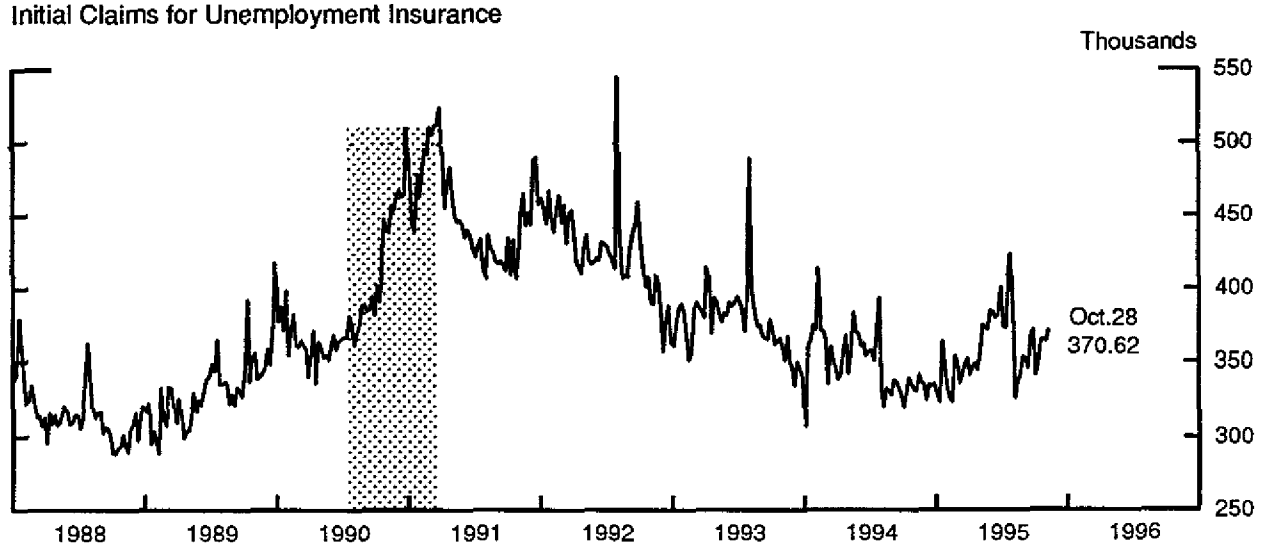
Unemployment Rates



Conference Board Help Wanted Index



Initial Claims for Unemployment Insurance



Note. Includes adjustment for EUC.

transportation equipment, instruments, apparel, paper, printing, and rubber and plastics.

In other sectors, job gains were widespread.[4] The construction industry added 28,000 jobs in October after an upward revised increase of 25,000 in September. Most of the recent gains in construction have been in residential construction and in special trades (electricians, carpenters, etc.).

Transportation and public utilities added 22,000 jobs, led by trucking and warehousing (helped by the return of 5,000 striking workers). Employment was also up in wholesale trade (12,000), with most of the increase related to computers, peripherals, and software. A small gain was recorded in retail trade (8,000), where increases at general merchandisers (mostly department stores) and at automotive dealers and service stations were partially offset by a drop at eating and drinking establishments. Real estate posted another increase (7,000), and finance employment rose 9,000 partly because of job growth at nondepository institutions (including mortgage bankers).

Services added 57,000 jobs last month. Computer, health, engineering and management, auto repair, and educational services all posted noticeable gains. However, personnel supply services dropped back 16,000 after two months of strong increases. Employment in hotels and in amusement and recreation services also declined.

The October jump in average weekly hours is not unusual for this volatile series, and such a change is often reversed the

4. The one-month diffusion index of employment change in 356 industries moved up 4 points to 54.8 in October after dropping a similar amount in September.

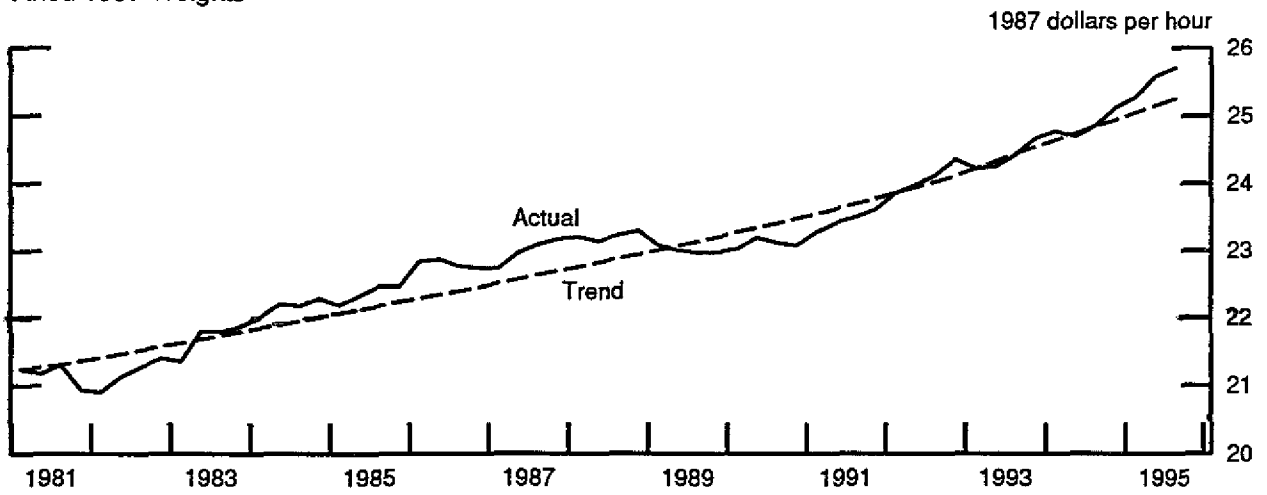
LABOR PRODUCTIVITY
(Percent change from preceding period at compound annual rate; based on seasonally adjusted data)

	1993[1]	1994[1]	1994 Q4	1995 Q1	1995 Q2	1995 Q3	1994:Q3 to 1995:Q3
Output per hour							
Total business	1.4	2.0	4.3	2.1	4.6	2.1	3.3
Nonfarm business	1.3	1.8	4.3	2.5	4.9	2.0	3.4
Manufacturing	3.5	4.2	3.7	3.5	2.7	6.2	4.0
Nonfinancial corporations[2]	2.3	1.6	3.4	1.7	5.2	ND	ND
Fisher nonfarm business	-.3	.9	1.2	.3	3.5	.7	1.4

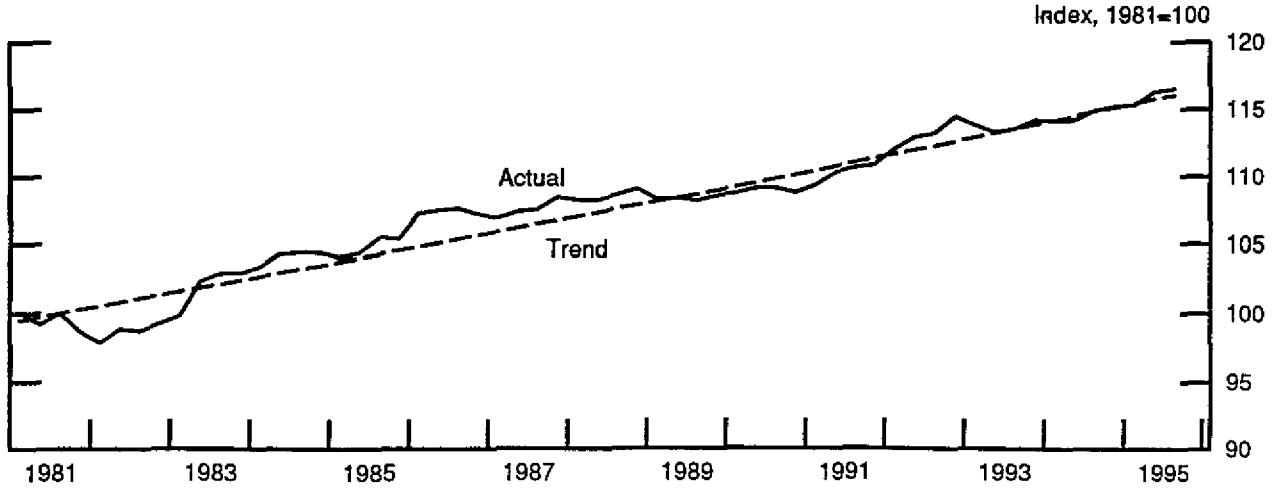
1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.
2. The nonfinancial corporate sector includes all corporations doing business in the United States with the exception of banks, stock and commodity brokers, finance and insurance companies; the sector accounts for about two-thirds of business employment.

Output per Hour
Nonfarm Business Sector

Fixed 1987 Weights



Chain



following month.[5] Even if all of October's increase in the workweek is given back in November, however, aggregate hours are off to a fast enough start to grow at a 3 percent annual rate in the fourth quarter with only moderate increases in employment. In manufacturing, the workweek fell 0.2 hour to 41.5 hours in October; overtime was down as well. The decline was spread among a number of durable and nondurable manufacturing industries.[6]

Employment, as measured by the household survey, rose 259,000 in October, and the employment-to-population ratio edged back up to 63 percent--this ratio has changed little over the past year. The labor force participation rate was unchanged at 66.6 percent in October. Most of the decline in the overall unemployment rate last month can be traced to a 0.4 percentage point decline, to 3.9 percent, in the rate for men aged 25 and over. The unemployment rate for this group is now at its lowest level since the redesign of the Current Population Survey in January 1994.

The Conference Board's help-wanted index fell 0.4 percentage point in September after holding steady for the previous two months. The index has moved within a relatively narrow range since early 1994. Initial claims for unemployment insurance moved back above 370,000, at the end of October. Initial claims in this range are consistent with further moderate employment gains in the months ahead.

Labor productivity, measured with output aggregated using fixed 1987 weights, rose at an annual rate of 2.0 percent in the third quarter and was up 3.4 percent over the past four quarters. This pace is well above its estimated trend rate of growth of

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5. In October 1994, for example, the workweek also rose 0.2 hour. Then, as now, the increase appeared to be concentrated in finance, insurance, and real estate and in services. But the workweek dropped back to its earlier level the following month.

6. The BLS reported that the strike at Boeing had no noticeable effect on the factory workweek.

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

	Proportion in total IP 1994:Q4	1994[1]	1995 Q1	1995 Q2	1995 Q3	1995 July	1995 Aug.	1995 Sept.
			----Annual rate-----			----Monthly rate----		
Total index	100.0	6.0	5.2	-2.3	3.5	.2	1.1	-.2
Previous		6.0	5.2	-2.4		.3	1.1	
Manufacturing	86.8	6.9	5.1	-3.3	2.5	.0	.9	.2
Motor veh. & parts	5.7	7.9	13.0	-24.4	.0	-1.7	3.9	.3
Mining	6.1	.8	4.4	1.0	1.9	1.2	-1.2	.6
Utilities	7.2	.2	6.8	8.7	15.7	1.5	4.3	-5.4
Manufacturing ex. motor veh. & parts	81.1	6.8	4.5	-1.7	2.7	.1	.7	.2
Consumer goods	23.4	3.9	3.1	-1.5	-.1	-.6	.5	.1
Durables	3.6	4.8	1.5	-9.1	2.1	-.1	.8	1.0
Nondurables	19.8	3.7	3.5	-.1	-.5	-.7	.4	.0
Business equipment	13.8	10.1	7.8	4.6	9.2	.9	1.3	.4
Office and computing	2.3	20.2	27.3	28.1	26.9	2.7	1.9	2.0
Industrial	4.2	8.7	6.3	-2.1	9.9	1.0	1.3	.4
Other	7.3	8.0	3.0	1.3	3.1	.1	1.1	-.2
Defense & space equip.	2.4	-9.4	-5.0	-6.4	-4.3	-.6	-.5	-.9
Construction supplies	5.5	8.4	3.2	-12.3	2.6	.4	.6	.6
Materials	28.9	9.3	6.4	-2.1	3.4	.4	.8	.4
Durables	20.0	10.9	8.9	-.8	7.8	.8	1.2	.8
Nondurables	8.6	5.5	1.2	-4.9	-6.1	-.5	.2	-1.0
Energy	0.2	16.3	-10.1	-9.5	-14.5	2.6	-11.2	11.5

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

CAPACITY UTILIZATION
(Percent of capacity; seasonally adjusted)

	1988-89 High	1967-94 Avg.	1995 Q2	1995 Q3	1995 June	1995 July	1995 Aug.	1995 Sept.
Total industry	84.9	82.0	84.0	83.9	83.7	83.6	84.2	83.8
Manufacturing	85.2	81.3	83.2	82.8	82.8	82.5	83.0	82.9
Primary processing	89.0	82.5	87.4	86.3	86.6	86.4	86.3	86.3
Advanced processing	83.5	80.7	81.5	81.4	81.3	81.0	81.7	81.6

1-1/2 percent annually, and the recent strong performance of output per hour has pushed the level of productivity further above its trend level (chart). In contrast, productivity growth using output measured on a chain-weighted basis increased 0.7 percent at an annual rate in the third quarter.[7] Although the level of this measure of productivity also was above trend in the third quarter, the gap was much smaller than that using the official series (1987 prices).

Industrial Production

Industrial production slowed in September as a sharp weather-related drop in electricity generation more than offset a modest gain in manufacturing output. For the third quarter as a whole, the rise in total industrial output more than reversed its second-quarter decline. However, the rebound in manufacturing output was more subdued--at just a 2-1/2 percent annual rate of increase--and this left the factory utilization rate slightly below 83 percent.

Available indicators point to a further retreat in industrial production in October; both the production worker hours and physical product available for the initial estimate of October IP decreased last month. Unlike September, the expected decline in October is likely to reflect a drop in manufacturing output.

The strike at Boeing is estimated to have lowered growth in manufacturing IP in October roughly 0.2 percentage point. Virtually all of Boeing's commercial aircraft and parts facilities are affected by the strike. To date, however, the strike has not adversely affected production of parts by suppliers.

Another drag on factory output last month was the drop in the production of motor vehicles. Weekly data indicate that

7. The chain-weighted measure avoids the distortion in output growth from using 1987 prices and measures output from the product side, whereas the current 1987-dollar series measures output from the income side.

manufacturers assembled motor vehicles at an 11.6 million unit rate last month--down from the 12.0 million unit assembly rate in September. Although production is scheduled to pick up from the October pace over the remainder of the year, those schedules appear slightly optimistic in light of the fact that, over the past two months, the days' supply for automobiles and for light trucks have each moved further above the ranges that the industry considers "comfortable."

PRODUCTION OF DOMESTIC AUTOS AND TRUCKS, 1995
(Millions of units, annual rate; FRB seasonal basis)

	Aug.	Sept.	Oct.	Nov.	Dec.
				---scheduled---	
U.S. production	11.9	12.0	11.6	12.1	11.9
Autos	6.1	6.2	6.0	6.4	6.2
Trucks	5.8	5.8	5.6	5.7	5.7
Days' supply					
Autos	64.6	70.2	73.0	n.a.	n.a.
Light trucks	66.1	72.0	75.3	n.a.	n.a.

Outside of motor vehicles and aircraft, manufacturing activity also apparently fell in October. Production-worker hours in manufacturing (FRB seasonal basis) excluding transportation equipment (most of which is motor vehicles and aircraft) declined 0.2 percent last month; the slowdown was spread widely across industries. Producers of computing and high-technology electrical equipment were noteworthy exceptions, continuing to post gains in hours worked. Weekly information on physical output points to declines in some industries, particularly appliances, lumber, steel, meat products, and refined petroleum products.

Other recent indicators of manufacturing activity are mixed. Real new orders for goods in the adjusted durable goods category rose 1-3/4 percent in August and 2-1/2 percent in September, resulting in a growth rate of 2.9 percent (annual rate) in the third

quarter. The national purchasing managers' indexes of new orders and production, however, turned back down in October and are below 50. Nonetheless, reports from some regions, notably Philadelphia and Chicago, suggest continued improvement in manufacturing activity in these areas. Our most recent conversations with industry sources provided diverse reports: Orders for high-grade paper and motor-vehicle-related products were said to be soft, while demand for high-technology goods and building products has been strong.

With the rate of capacity expansion running faster than manufacturing output growth for much of this year, the factory operating rate has dropped roughly 2-1/2 percentage points since January, to 82.9 percent in September. Notwithstanding the further slowdown in the manufacturing sector last month, utilization rates in most manufacturing industries should remain above their respective long-run averages.

After increasing at a relatively sluggish rate of 2.4 percent, on average, over the six years ended in 1994, growth in manufacturing capacity is currently estimated to be expanding 4.2 percent this year.[8] The Investment Plans Survey (IPS), which was updated in late September, indicated that manufacturers plan to boost investment 24 percent in 1995 after increases that averaged 5 percent over the previous six years; the level of spending is now well above that needed for replacement investment.

The sharp increase in aggregate manufacturing investment this year reflects widespread gains across industries. The following table shows capacity utilization, investment spending growth, and manufacturing capacity growth for selected manufacturing industries. Manufacturing industries with the fastest growth in investment

8. The annual revisions to industrial production and capacity utilization, scheduled to be released on November 30, will incorporate more comprehensive information on annual output and survey results on year-end utilization rates for 1993 and 1994.

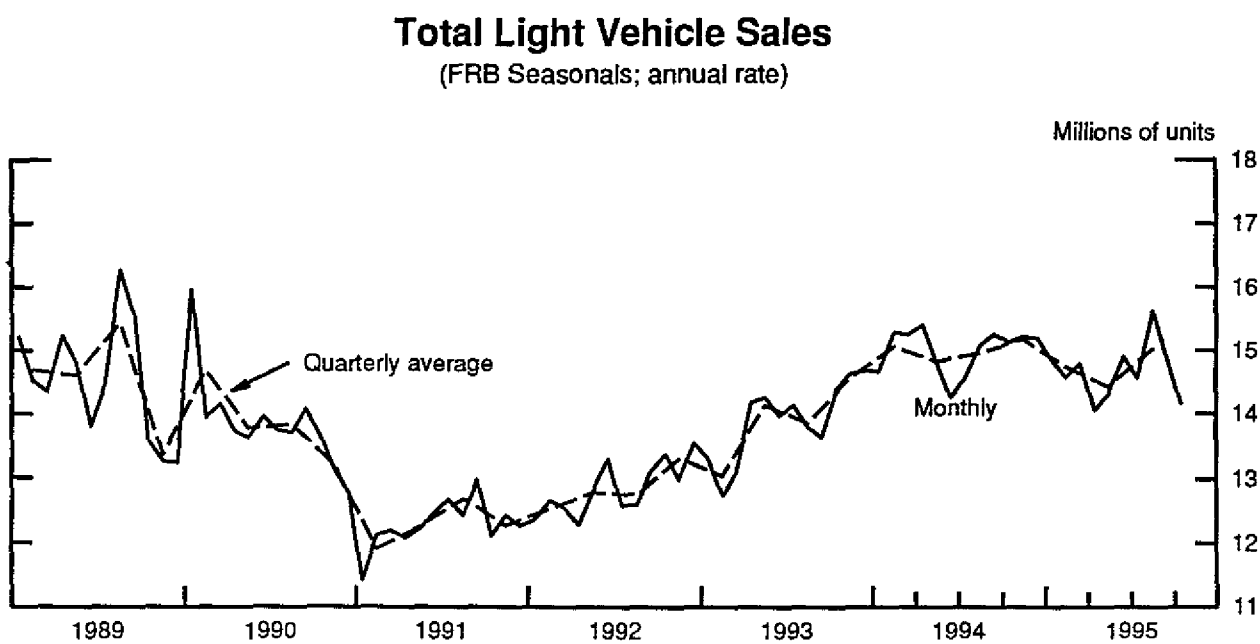
SALES OF AUTOMOBILES AND LIGHT TRUCKS[1]
(Millions of units at an annual rate; FRB seasonals)

			1995			1995		
	1993	1994	Q1	Q2	Q3	Aug.	Sept.	Oct.
Total	13.9	15.0	14.7	14.4	15.0	15.6	14.9	14.2
(BEA seasonals)	13.9	15.0	14.9	14.4	14.7	15.7	14.8	14.4
Autos	8.7	9.2	8.9	8.7	9.2	9.6	9.1	8.6
Light trucks	5.2	5.8	5.9	5.7	5.9	6.0	5.8	5.6
North American[2]	11.7	12.9	12.7	12.5	13.2	13.7	13.0	12.4
Autos	6.7	7.3	7.1	6.9	7.5	7.9	7.4	7.0
Big Three	5.5	5.7	5.5	5.3	5.6	5.7	5.6	5.5
Transplants	1.3	1.5	1.5	1.6	1.9	2.1	1.8	1.5
Light trucks	5.0	5.7	5.7	5.5	5.7	5.9	5.6	5.5
Foreign produced	2.1	2.1	2.0	2.0	1.9	1.9	1.9	1.7
Autos	2.0	2.0	1.8	1.8	1.7	1.7	1.7	1.6
Light trucks	.2	.2	.2	.2	.1	.1	.2	.2

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.



spending include industrial machinery and equipment, electrical machinery, and rubber and plastics products. For many producers, the pickup in investment may reflect efforts to alleviate capacity constraints; the table shows that industries with the greatest increase in investment spending have experienced high operating rates this year relative to their 1988-89 cyclical peaks. However, some manufacturers, especially in the paper and chemical industries, direct a notable amount of their capital expenditures toward environmental protection.

SELECTED COMPONENTS OF MANUFACTURING INVESTMENT AND CAPACITY
(Percent)

	Capacity utilization[1]		Change in investment[2]		Change in capacity[3]	
	1988-89 high	1995 high	1989-94	1995	1989-94	1995
Manufacturing	85.2	85.2	5.0	24.4	2.4	4.2
Durable manufacturing	84.0	85.3	4.0	29.0	2.6	5.6
Indust. mach. & eq.	84.0	92.0	7.1	29.5	4.4	10.3
Comput. & office eq.	84.4	93.8	9.2	27.6	13.9	21.9
Electrical machinery	84.9	90.1	5.4	54.2	6.1	12.6
Semiconductors	83.8	93.0	8.6	64.7	12.0	20.6
Motor veh. & parts	85.1	89.4	11.3	30.1	2.9	5.6
Nondurable manufacturing	86.7	85.1	6.3	19.7	2.1	2.6
Paper & products	94.8	93.8	8.2	14.2	2.3	2.6
Chemicals & products	85.9	83.8	9.4	21.2	3.2	3.7
Rubber & plastics	90.5	92.4	3.5	52.5	4.1	5.8

1. Seasonally adjusted.
2. Annual rate, calculated from annual totals; 1995 values are based on plans reported in the IPS.
3. Annual rate, fourth quarter to fourth quarter; 1995 values are staff estimates.

Motor Vehicles

Sales of light vehicles in October--at a 14.2 million unit annual rate (FRB seasonals)--were down sharply from the September rate of 14.9 million units and well below the average pace over the first half of the year. Two special factors account for the bulk of

the decline: a reporting problem at a Japanese firm that misallocated some October sales to September and the limited supplies of some General Motors vehicles stemming from the car-hauler strike that ended in early October.

Cutting through the recent gyrations in the data, sales of new light vehicles averaged 14.6 million units in September and October, about even with the pace set in the first half of the year. The relative stability in sales trends this year--at a level about 1/2 million units below the 1994 pace--is also reflected in the Michigan index for consumers' assessments of buying conditions for cars--an indicator of underlying consumer demand. Except for an uptick in July, that index has fluctuated in a narrow range for much of the year, well below last year's optimistic readings.

The pace of sales this year has been relatively subdued despite generous incentive programs that have slowed the rise in the effective prices of motor vehicles. In the first three quarters of 1995, the average value of incentives per vehicle at Ford and Chrysler was substantially above year-ago levels; anecdotal evidence suggests that the same was true for Japanese makes. Incentives at General Motors, however, trailed year-ago levels.

AVERAGE RETAIL INCENTIVES PER VEHICLE, 1995
(Current dollars; year-ago levels in parentheses)

	Q1	Q2	Q3
General Motors	693 (793)	714 (756)	671 (935)
Ford	705 (695)	760 (550)	850 (725)
Chrysler	590 (708)	1035 (613)	870 (515)

Source: Firms' 10K reports.

Prices for autos and light trucks--as measured by the CPI--rose 1.6 percent and 2.7 percent respectively over the year ended in September, down from 3.9 and 4.6 percent over the previous twelve-month period. Looking ahead, announced increases in sticker prices for 1996 models appear modest--ranging from 1.4 to 2.7 percent on a comparably equipped basis--but it remains to be seen whether the third-quarter level of incentives will be maintained.

Consumption and Personal Income

Real consumer spending grew at a 2.9 percent annual rate in the third quarter, a bit above the average pace during the first half of 1995. Gains were concentrated in consumer durables; growth in spending on nondurable goods was particularly weak. The auto sales figures and various chain store reports suggest tepid spending in October, although anecdotal evidence points to strong demand for home electronics. Income continued its solid uptrend through October and presumably could support substantial spending growth in the near term.

A jump in purchases of durable goods accounted for more than half of the growth in total real PCE in the third quarter. Spending in this category was boosted by a healthy gain in expenditures on used cars. In addition, spending on electronic goods posted another sizable increase, in part because of continued strength in purchases of computers. Outlays for electronic goods have climbed at double-digit rates (in 1987 dollar terms) in every quarter since the middle of 1992.

Spending on nondurable goods was flat in the third quarter. Real apparel outlays were unchanged, and a modest increase in food expenditures was offset by declines in other categories.

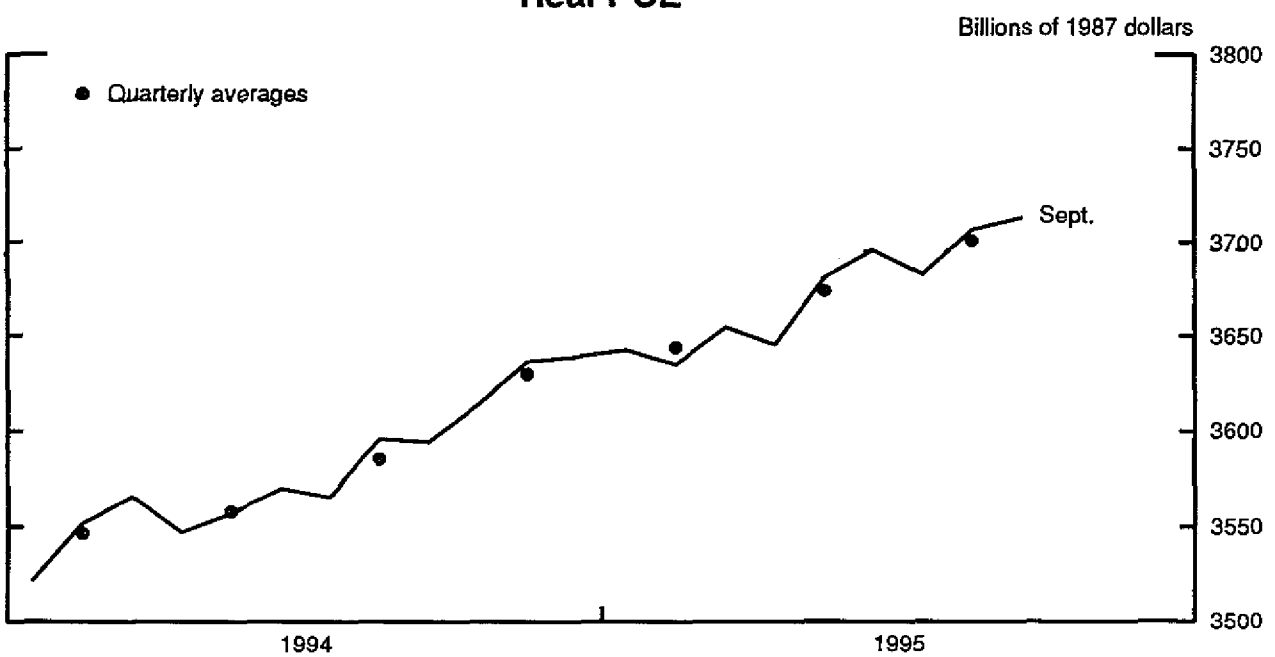
Growth in services expenditures slowed to a 2.2 percent annual rate in the third quarter after being boosted in the previous

Personal Consumption Expenditures
(Percent change from preceding period)

	Share of total PCE 1994	1994 [1]	1995 Q1	1995 Q2	1995 Q3	1995 Aug.	1995 Sept.
			-- Annual rate --			--Monthly rate--	
PCE	**1.00**	**3.5**	**1.6**	**3.4**	**2.9**	**.6**	**.2**
Durables	.15	8.6	–3.4	3.5	11.7	4.3	–.9
Motor vehicles	.06	3.5	–15.4	–1.0	10.7	8.9	–4.2
Electronics	.03	23.0	11.1	13.5	33.4	5.6	2.2
Other	.06	7.4	1.6	2.8	2.7	–.3	.5
Nondurables	.31	3.1	2.3	1.9	.1	–.2	.6
Food	.15	2.0	1.9	–.2	1.0	.1	.1
Apparel	.06	6.9	.4	5.1	.0	–1.5	1.5
Other	.10	2.7	3.9	3.2	–1.2	.0	.8
Services	.54	2.4	2.6	4.2	2.2	.1	.3
Energy	.03	–5.1	9.2	30.1	3.1	1.8	–1.4
Other	.51	2.8	2.3	3.0	2.2	.0	.3

1. Changes are from 1993:Q4 to 1994:Q4.

Real PCE

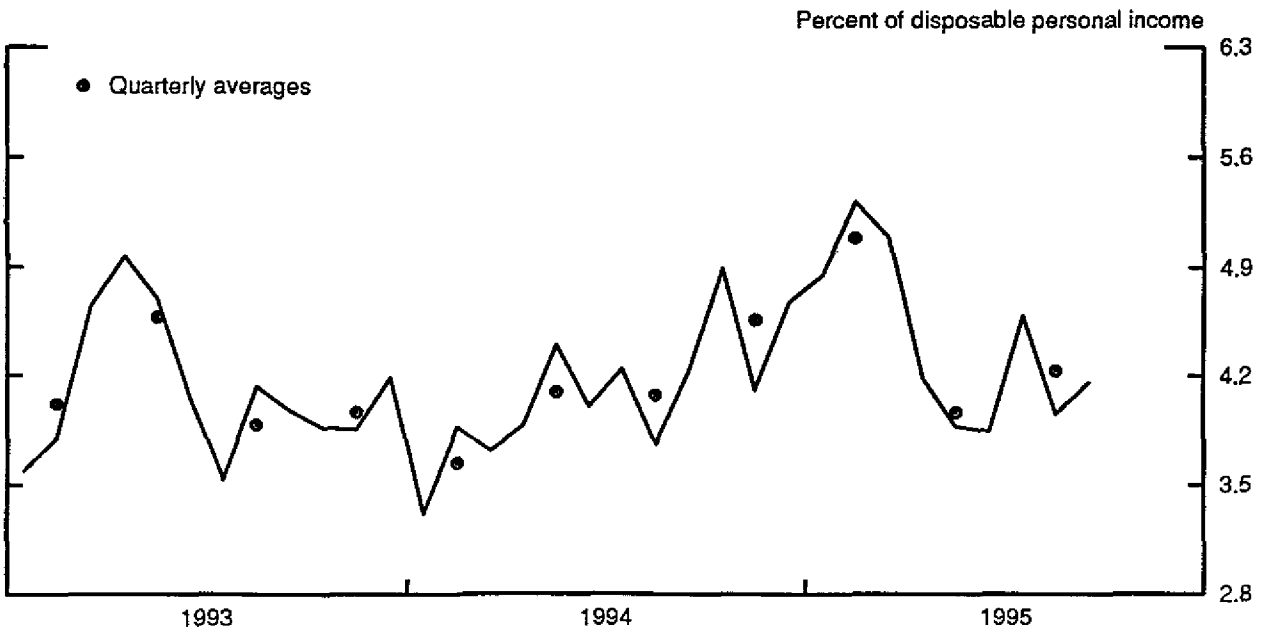


CHANGES IN PERSONAL INCOME
(Billions of dollars)

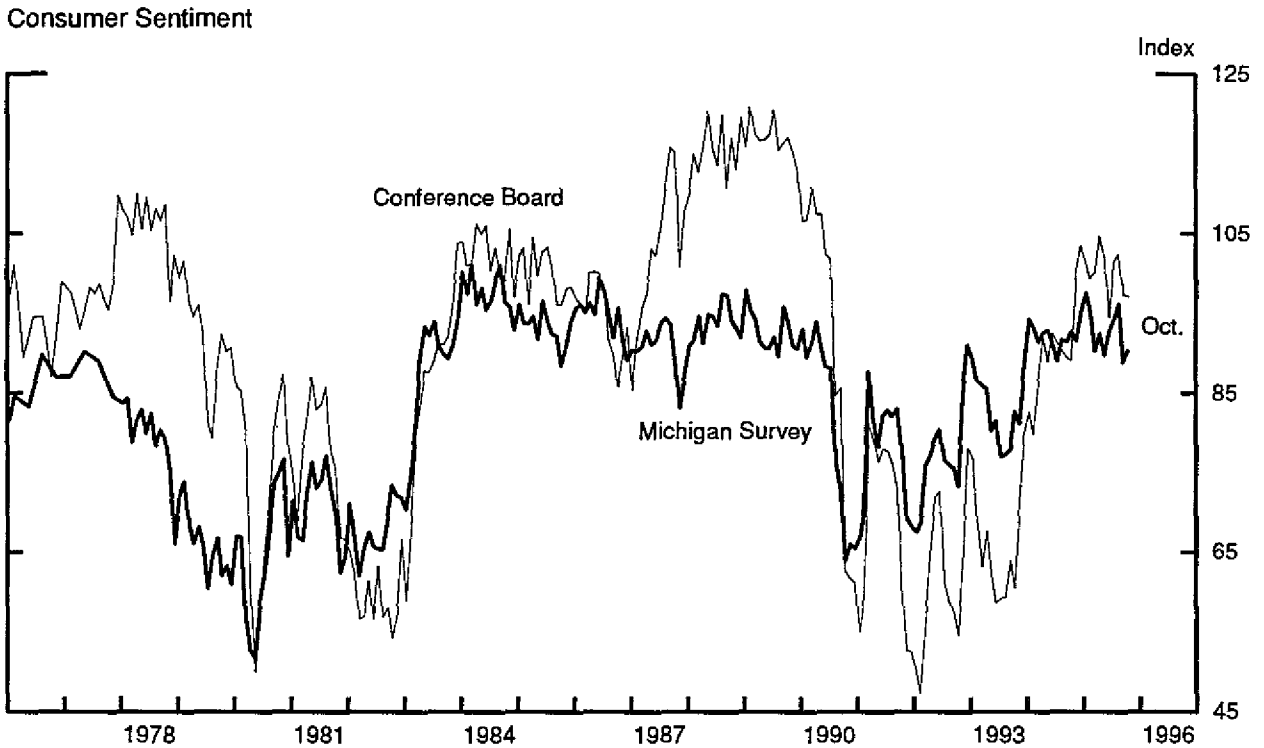
	1994	1995 Q1	1995 Q2	1995 Q3	1995 Aug.	1995 Sept.
Total personal income	326.6	105.3	46.1	67.7	6.9	26.7
Wages and salaries	198.2	47.0	18.9	40.4	-4.9	16.5
Private	179.2	38.8	15.7	36.3	-6.2	14.8
Other labor income	25.7	10.9	4.3	3.9	1.2	1.4
Proprietors' income	32.1	7.9	-6.5	5.1	6.5	4.6
Farm	2.2	2.7	-9.4	-1.0	3.8	1.7
Rent	3.6	-3.6	-1.2	-3.7	-3.2	-2.4
Dividend	12.9	2.9	2.6	3.5	1.3	1.7
Interest	26.1	22.5	15.7	9.0	2.3	2.0
Transfer payments	48.0	25.1	13.8	12.5	3.7	3.8
Less: Personal contributions for social insurance	20.1	7.2	1.6	3.0	-0.2	1.2
Less: Personal tax and nontax payments	55.7	22.8	29.4	0.0	1.8	6.1
Equals: Disposable personal income	270.9	82.5	16.6	67.7	5.1	20.6
Memo: Real disposable income	131.6	39.5	-11.0	41.7	-0.6	15.8

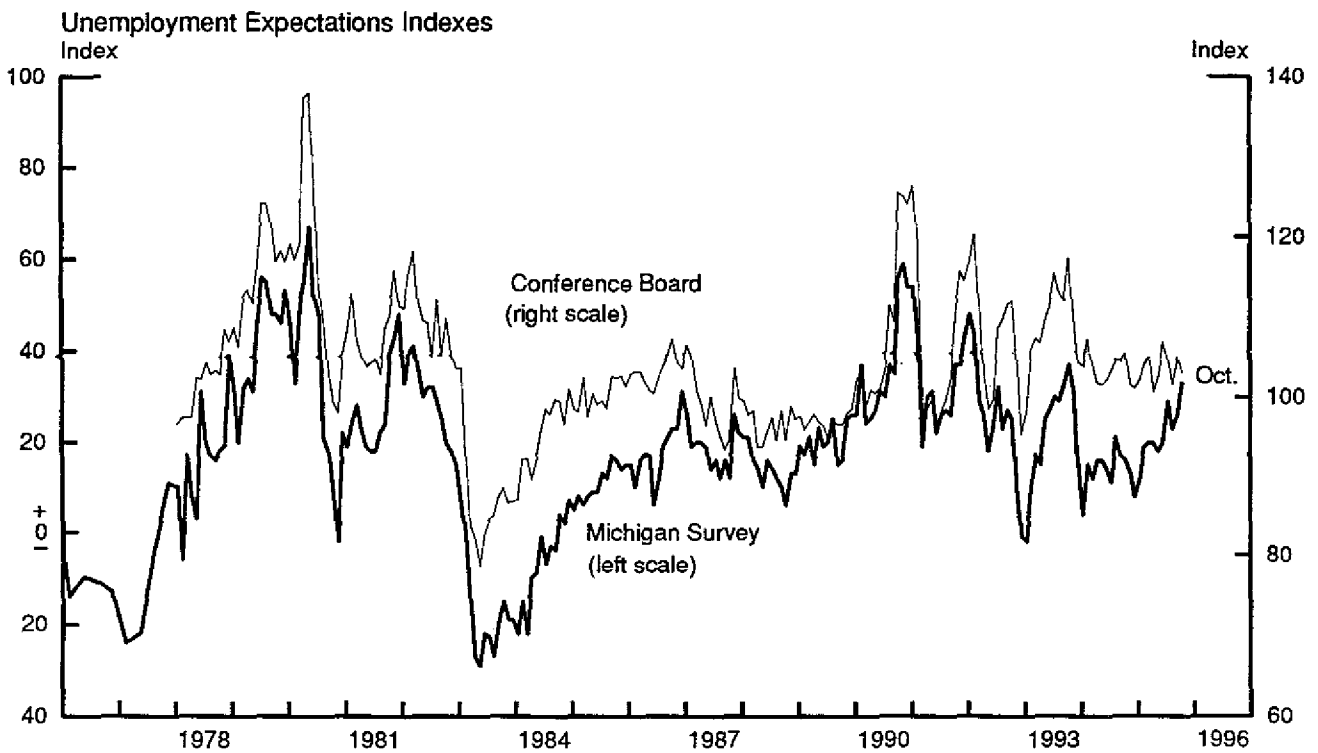
1. Quarterly changes are the difference between the average level in a given quarter and the average level in the previous quarter.
2. Annual changes are the difference between the average level in a given year and the average level in the previous year.

Personal Saving Rate



Consumer Surveys





quarter by a surge in energy spending. Unusually hot weather in the third quarter caused spending on energy services to rise above its already elevated second-quarter level. For the fourth quarter, the available weather data indicate somewhat milder temperatures thus far; if weather during the remainder of the quarter is about average, the return of energy spending to more normal levels could depress total PCE growth as much as 0.5 percentage point. Spending on non-energy services rose 2.2 percent at an annual rate in the third quarter, with a decline in transportation services and moderate gains in most other categories.

Consumer spending was buttressed last quarter by fairly robust growth in income. Real disposable income rose 4.3 percent at an annual rate in the third quarter, pushing the saving rate up 0.2 percentage point, to 4.2 percent. The sizable gain in disposable income was partly attributable to the timing of personal tax payments: Payments jumped in the second quarter as some high-income taxpayers paid some of the additional taxes associated with the Omnibus Budget Reconciliation Act of 1993, and then payments were flat in the third quarter. In addition, pretax wages and salaries posted a healthy advance in the third quarter. For the current quarter, wage and salary income likely advanced substantially in October, as indicated by the 0.8 percent increase in aggregate private hours and 0.5 percent increase in average hourly earnings.

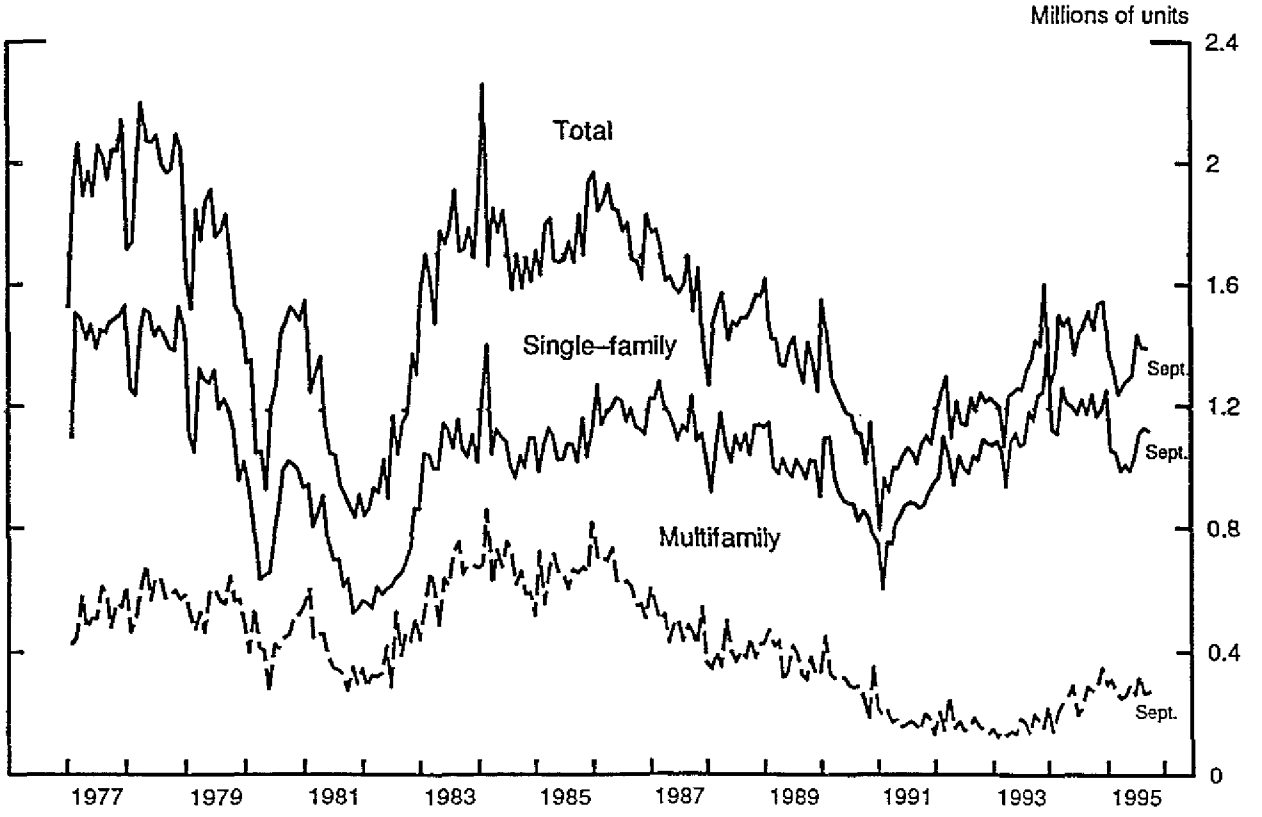
Meanwhile, indicators of consumer sentiment remain in a generally optimistic range, although recent data point to some deterioration since the summer. The Michigan index of consumer sentiment rose 1.3 points in October, reversing only a small portion of its appreciable September decline. The October level of the Conference Board index of consumer sentiment was more than 3 points

Private Housing Activity
(Millions of units; seasonally adjusted annual rate)

	1994	1995					
	Annual	Q1	Q2[r]	Q3[p]	July[r]	Aug.[r]	Sept.[p]
All units							
Starts	1.46	1.31	1.28	1.41	1.43	1.39	1.39
Permit	1.37	1.27	1.25	1.37	1.36	1.37	1.39
Single-family units							
Starts	1.20	1.03	1.01	1.12	1.11	1.13	1.12
Permits	1.07	.94	.93	1.04	1.01	1.04	1.05
New-home sales	.67	.61	.67	.74	.79	.70	.73
Existing-home sales	3.95	3.55	3.58	4.09	3.99	4.12	4.15
Multifamily units							
Starts	.26	.28	.27	.29	.33	.27	.27
Permits	.31	.33	.32	.34	.34	.32	.34

Note. p Preliminary. r Revised.

Private Housing Starts
(Seasonally adjusted annual rate)



below its third-quarter average. In addition, the Michigan index of unemployment expectations continued to climb in October; it now stands at its highest level in two years.[9]

Housing Markets

Housing demand and production firmed considerably in the third quarter, reaching their highest levels since late last year. The single-family segment of the market accounted for almost all of the gain as multifamily construction continued flat. Of the four regions, only the Northeast failed to post stronger housing numbers in the third quarter than earlier in the year.

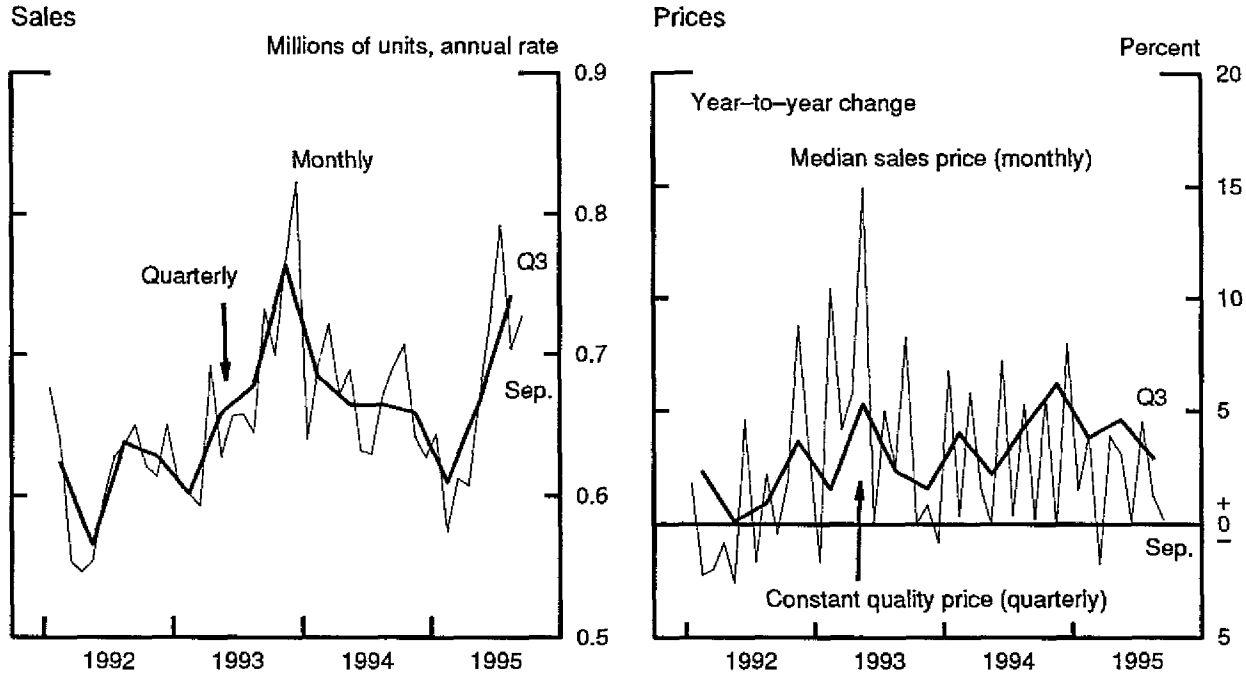
In the single-family sector, both starts and permit issuance rose 11 percent in the third quarter. Most of the improvement came in July, after which these indicators were essentially flat. The higher level of construction is broadly consistent with the gains in demand reflected in sales of new and existing homes. For the quarter, sales in these markets rose 11 percent and 14 percent, respectively. House prices, however, paint a more mixed picture. In the resale market, both transactions prices and the "repeat transactions" price index accelerated in the third quarter, but no such pickup was apparent in new home prices.

Most early indications of housing activity in October suggest continued strength in single-family demand. Home builders' assessments of their current sales improved for the fourth consecutive month, and applications for home purchase loans have averaged higher in recent weeks. In contrast, consumers' attitudes toward homebuying, as reported in the October Michigan survey, were slightly less bullish than in September. Consumers viewed mortgage

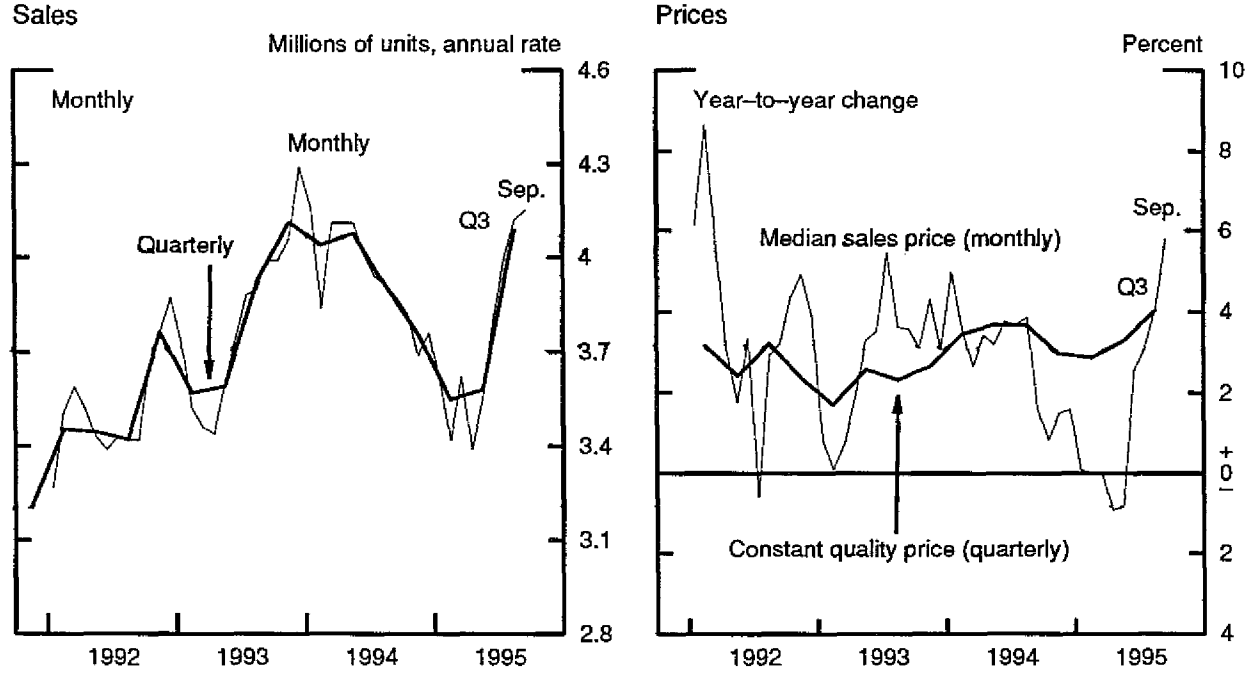
9. The Conference Board index of unemployment expectations has shown virtually no deterioration in recent months, but this index historically has been less highly correlated with patterns of consumer spending.

Single–Family Homes

New Homes

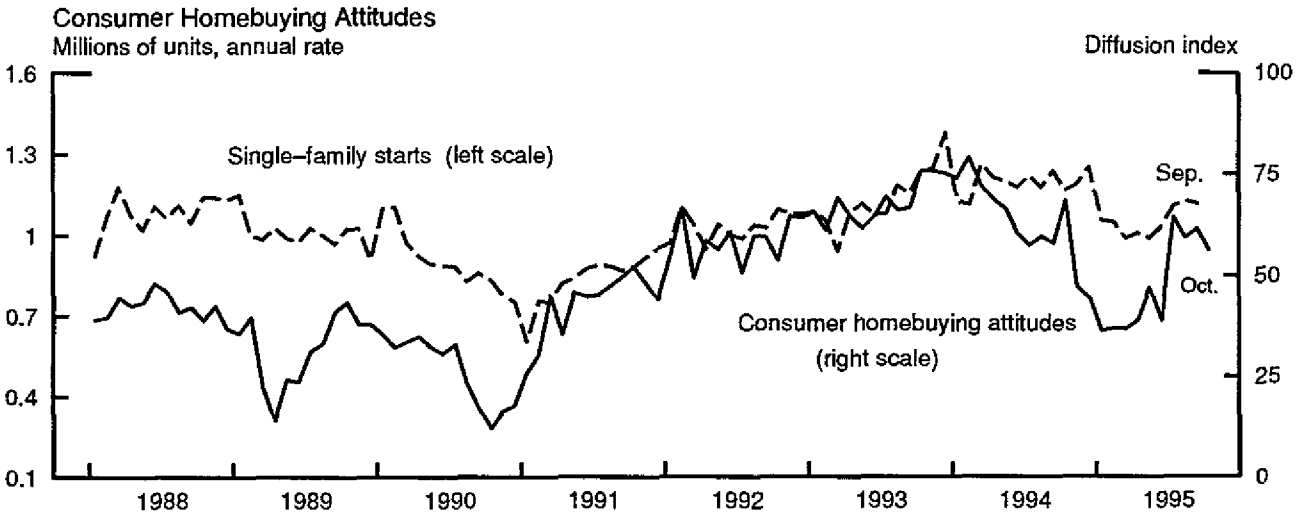


Existing Homes

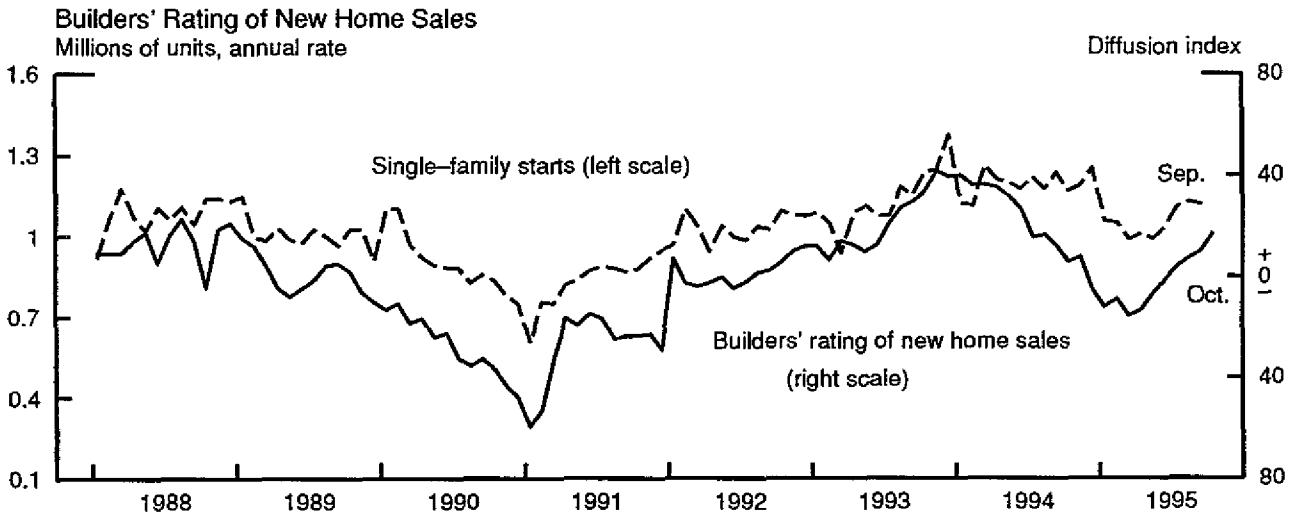


Indicators of Housing Demand

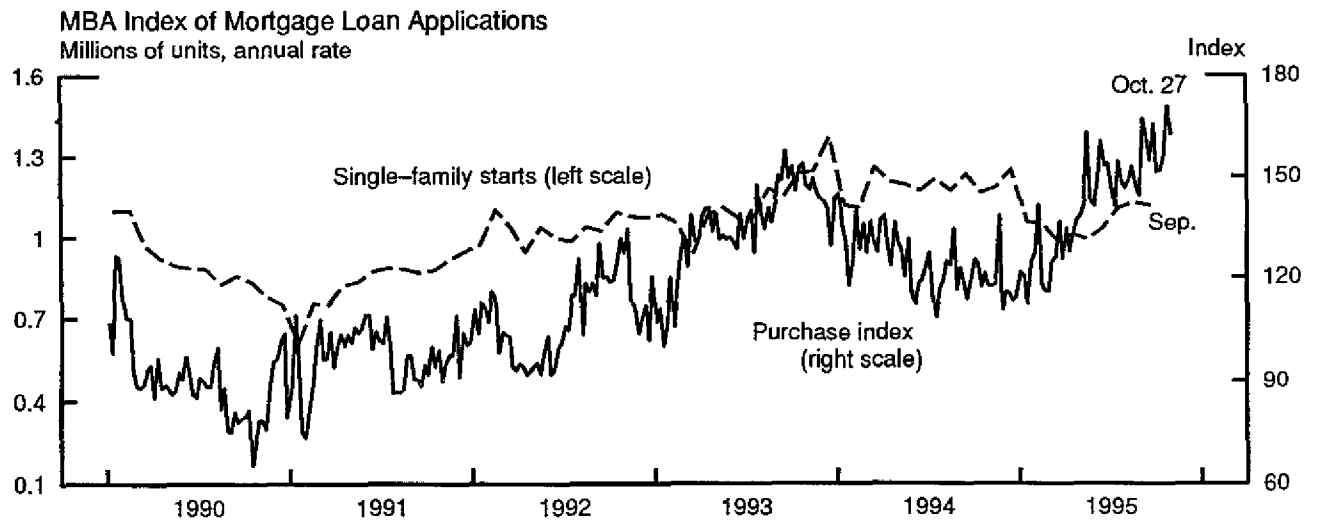
(Seasonally adjusted; FRB seasonals except starts)



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.



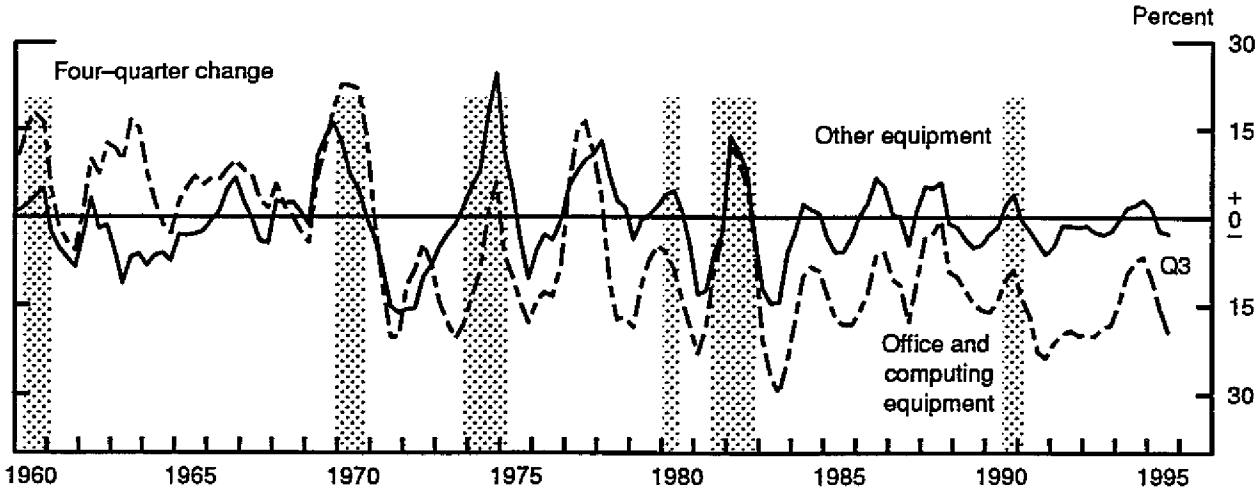
Note. The index is calculated from National Association of Homebuilders data as the proportion of respondents rating current sales as good to excellent minus the proportion rating them as poor.



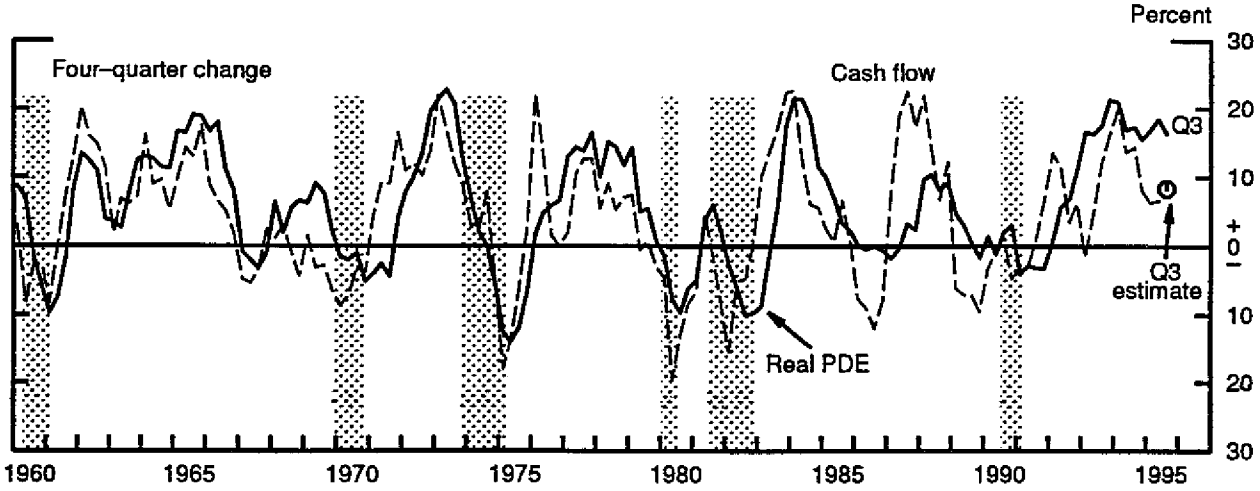
Note. MBA purchase index equals 100 on March 16, 1990 for NSA series.

Fundamental Determinants of Equipment Spending

User Cost of Capital

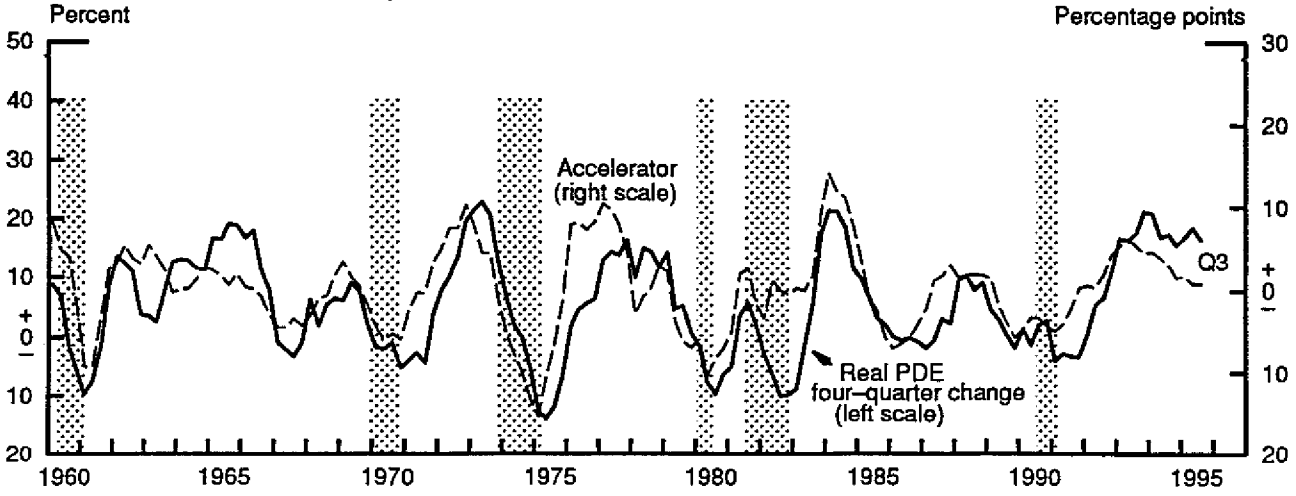


Real Domestic Corporate Cash Flow



Note. Data on cash flow are historical only through the second quarter.

Acceleration of Business Output



Note. The accelerator is the eight–quarter percent change in business output less the year–earlier eight–quarter percent change.

interest rates less favorably in October than September, even though rates actually declined a bit during the month.

The generally favorable conditions for home purchase over the past year have contributed to a rise in the home ownership rate. In the third quarter, 65.0 percent of all households were homeowners, up more than 1 percentage point from early 1994 and the highest level since the early 1980s. Ownership has increased among both young adults and the elderly.

Multifamily construction has not contributed much to the recent strengthening in housing activity. Starts of these units, about 80 percent of which are rental apartments, increased in the third quarter but did not reverse the declines recorded earlier in the year. No market tightening was evident in vacancy rates and rents in the third quarter, despite the continuing low level of production. Mobile home shipments this year, meanwhile, have been the highest since 1974, surpassing multifamily starts by 20 percent. Improved product design and robust growth in some key southern markets appear to have contributed to the doubling of shipments since 1991.

Business Fixed Investment

Real business fixed investment in both equipment and structures decelerated in the third quarter. The moderation of growth in these categories is not surprising, given the movements of the fundamental determinants of BFI over the past few quarters. The cost of capital--which has benefited from lower interest rates and declining capital goods prices--has continued to decline, but accelerator and cash flow effects have worked to slow investment growth in recent quarters. Nevertheless, fundamentals still appear supportive of strong investment; indeed the most recent reading on profits

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

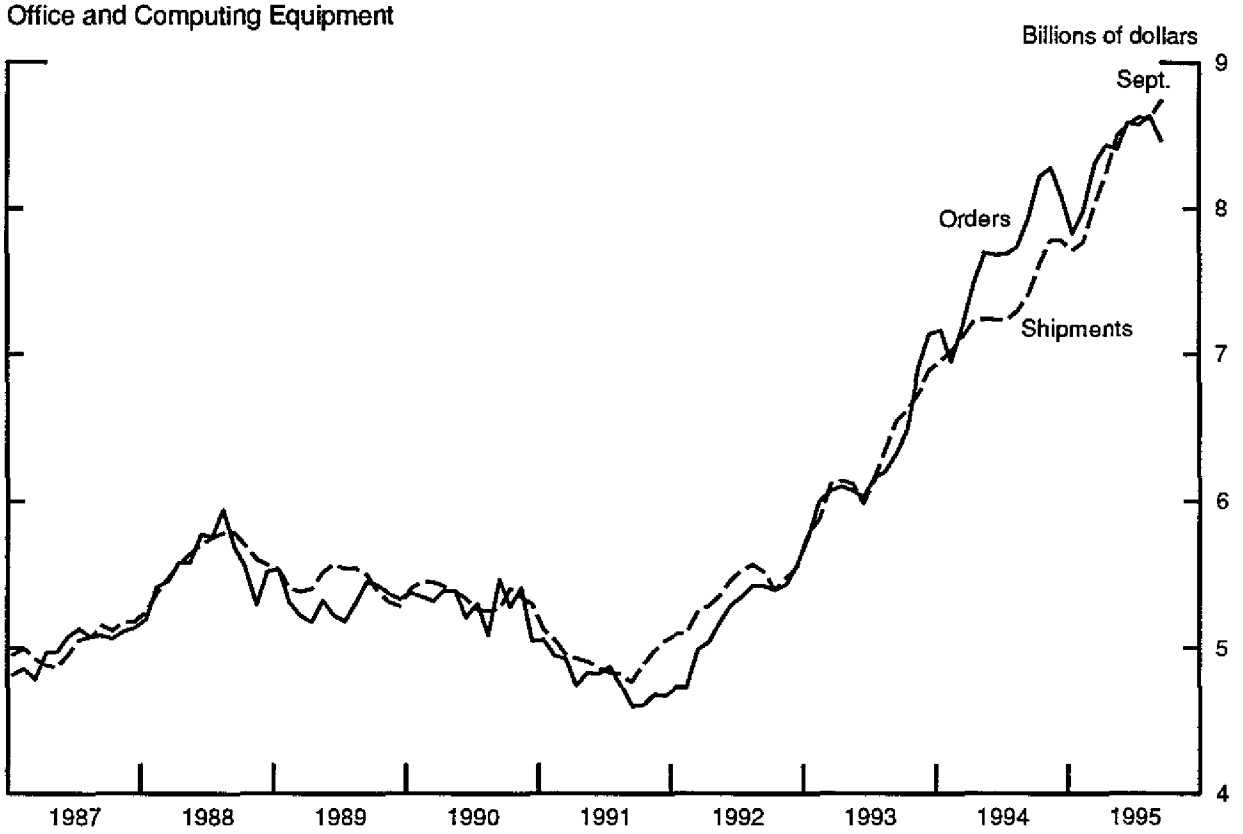
	1995			1995		
	Q1	Q2	Q3	July	Aug.	Sept.
Producers' durable equipment						
Shipments of nondefense capital goods	5.3	3.3	.5	-4.7	3.6	2.0
Excluding aircraft and parts	4.8	3.8	1.1	-4.5	3.8	2.2
Office and computing	3.1	6.8	1.9	-4.0	4.5	4.0
All other categories	5.2	2.9	.9	-4.7	3.6	1.6
Shipments of complete aircraft[1]	12.5	-5.0	-9.5	-25.4	8.5	6.9
Sales of heavy trucks	8.8	-3.6	-9.5	-17.0	10.9	-2.8
Orders of nondefense capital goods	8.3	-.3	1.9	-6.4	3.6	11.9
Excluding aircraft and parts	6.4	.3	-.5	-8.1	3.0	7.0
Office and computing	2.8	3.3	-1.3	-11.9	4.5	2.8
All other categories	7.4	-.5	-.3	-6.9	2.6	8.2
Nonresidential structures						
Construction put-in-place	.5	2.4	3.0	2.5	-1.0	-.2
Office	.1	3.9	5.7	11.1	-7.7	-4.2
Other commercial	5.7	-2.3	2.2	-2.0	1.1	1.7
Institutional	-.1	.3	1.6	6.0	-3.7	.9
Industrial	.4	5.6	-1.5	.0	-.8	-.5
Public utilities	-14.2	15.0	3.8	2.2	-.2	-.4
Lodging and miscellaneous	9.1	1.5	15.0	4.4	8.9	.7
Rotary drilling rigs in use	-1.7	1.3	.8	3.9	2.5	-1.6
Memo:						
Business fixed investment[2]	21.5	11.3	8.3	n.a.	n.a.	n.a.
Producers' durable equipment[2]	24.5	11.9	9.7	n.a.	n.a.	n.a.
Nonresidential structures[2]	11.5	9.0	3.5	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.

Recent Data on Orders and Shipments

(three-month moving average)

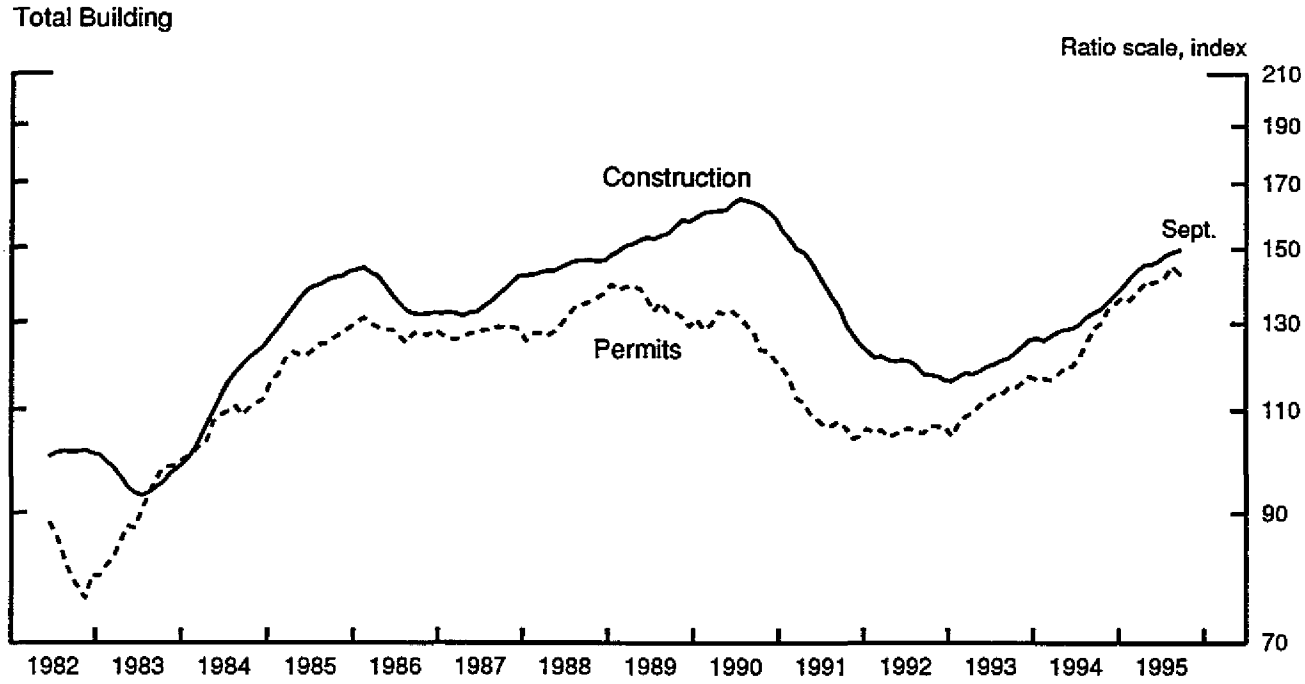
Office and Computing Equipment

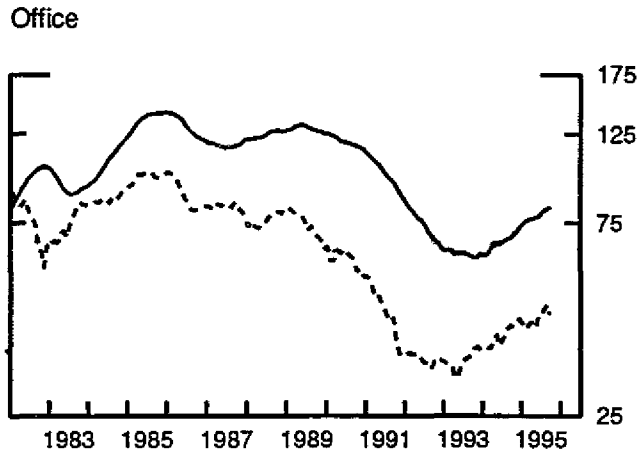


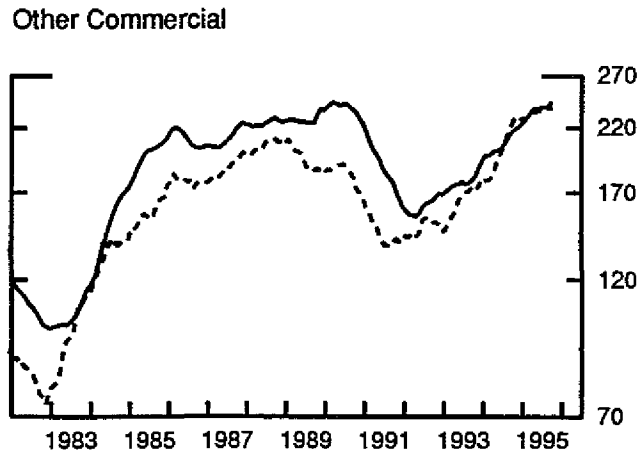
Other Equipment (excluding aircraft and computers)

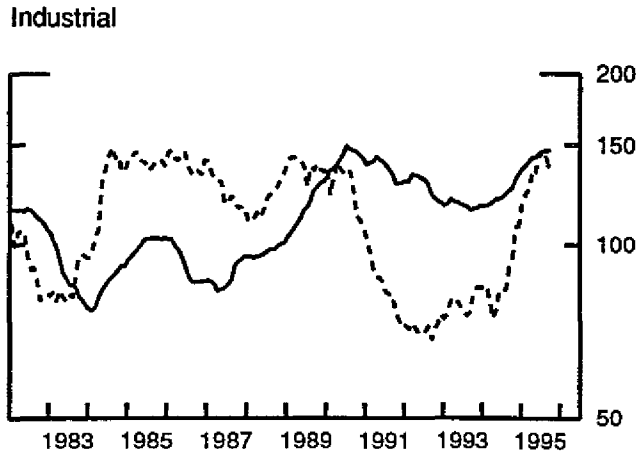
Nonresidential Construction and Permits

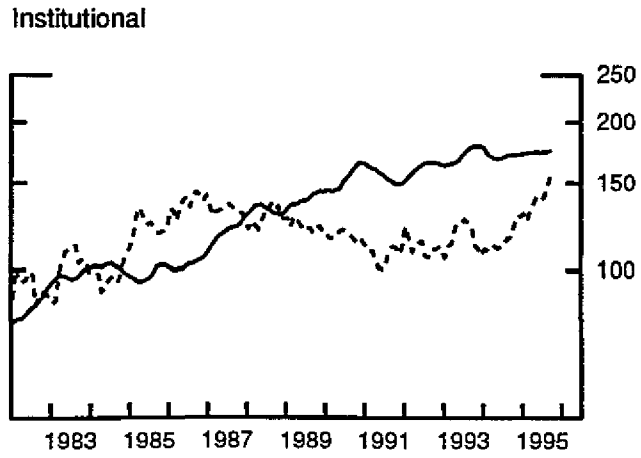
(Six-month moving average)











Note. The underlying monthly data were indexed to Dec. 1982 = 100; a six-month moving average was applied to the indexed data.

indicates that the downward pressure from slackened growth in cash flow may have eased in the third quarter.[10]

After dropping sharply in July, orders and shipments of nondefense capital goods posted solid gains in August and September. Shipments of nondefense capital goods excluding aircraft advanced 2.2 percent in September, with both office and computing and other equipment moving up. However, for the third quarter as a whole, shipments of nondefense capital goods excluding aircraft and parts increased 1.1 percent, a slower pace than that of the previous two quarters.

Despite rising 7.0 percent in September, orders for nondefense capital goods excluding aircraft and parts were down slightly in the third quarter and failed to keep pace with shipments.[11] As a result, the rapid accumulation of backlogs during the past few years appears to have subsided.

The strike at Boeing is likely to lower aircraft deliveries in the fourth quarter, although our industry contacts suggest some shipments (including exports) will proceed. Elsewhere, McDonnell Douglas reported large commercial orders from Saudi Arabia and from Valujet. Although these orders will not affect output significantly in the near term, they are important milestones because many analysts have been predicting that McDonnell would be forced by weak orders to abandon commercial aircraft construction.

Outlays for motor vehicles were fairly strong in the third quarter, mostly because of a temporary surge in business purchases of light motor vehicles as automakers unloaded model-year-end

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10. Assuming that the statistical discrepancy remained constant, real corporate cash flow advanced at an annual rate of more than 20 percent in the third quarter. Because the influence of cash flow is subject to lags, this would tend to boost investment in the following few quarters.

11. A good part of the September increase was attributable to sharp rebounds in two volatile categories: communications equipment and railroad equipment.

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

	1995			1995		
	Q1	Q2	Q3	July	Aug.	Sept.
Total	104.8	69.7	n.a.	56.8	45.4	n.a.
Excluding wholesale and retail motor vehicles	75.2	61.7	n.a.	68.6	46.8	n.a.
Manufacturing	41.1	31.7	22.2	28.9	8.7	29.0
Wholesale	35.0	25.4	10.6	39.0	-.5	-6.5
Excluding motor vehicles	28.9	19.1	13.2	40.2	1.8	-2.3
Retail	28.7	12.5	n.a.	-11.1	37.2	n.a.
Automotive	23.4	1.7	n.a.	-10.5	.9	n.a.
Excluding auto dealers	5.3	10.8	n.a.	-.5	36.3	n.a.
Constant-dollar basis						
Total	43.2	29.6	n.a.	61.5	5.4	n.a.
Excluding motor vehicles	29.0	28.1	n.a.	49.6	34.7	n.a.
Manufacturing	12.0	15.2	n.a.	24.9	1.3	n.a.
Wholesale	21.5	13.1	n.a.	27.0	6.6	n.a.
Excluding motor vehicles	16.4	8.4	n.a.	28.5	6.7	n.a.
Retail	9.7	1.3	n.a.	9.7	-2.5	n.a.
Automotive	8.9	-2.4	n.a.	13.0	-29.1	n.a.
Excluding auto dealers	.8	3.7	n.a.	-3.3	26.7	n.a.

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

	1995			1995		
	Q1	Q2	Q3	July	Aug.	Sept.
Total	1.40	1.42	n.a.	1.43	1.41	n.a.
Excluding wholesale and retail motor vehicles	1.36	1.38	n.a.	1.40	1.38	n.a.
Manufacturing	1.35	1.38	1.38	1.41	1.36	1.37
Wholesale	1.33	1.34	1.35	1.36	1.35	1.34
Excluding motor vehicles	1.30	1.32	1.32	1.33	1.33	1.32
Retail	1.54	1.54	n.a.	1.53	1.54	n.a.
Automotive	1.81	1.79	n.a.	1.75	1.70	n.a.
Excluding auto dealers	1.46	1.46	n.a.	1.46	1.48	n.a.
Constant-dollar basis						
Total	1.44	1.46	n.a.	1.48	1.45	n.a.
Excluding motor vehicles	1.42	1.44	n.a.	1.45	1.43	n.a.
Manufacturing	1.38	1.41	n.a.	1.44	1.39	n.a.
Wholesale	1.42	1.44	n.a.	1.46	1.46	n.a.
Excluding motor vehicles	1.40	1.42	n.a.	1.43	1.44	n.a.
Retail	1.57	1.56	n.a.	1.56	1.55	n.a.
Automotive	1.72	1.69	n.a.	1.70	1.59	n.a.
Excluding auto dealers	1.53	1.52	n.a.	1.51	1.53	n.a.

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

inventories onto their fleet customers. Sales of heavy trucks declined 2.8 percent in September and dropped 9.5 percent for the third quarter as a whole. Manufacturers have reported many cancellations of existing orders, and heavy truck purchases have clearly entered a downswing.

Outlays for nonresidential structures were estimated by the BEA to have advanced only 3 percent in the third quarter.[12] However, construction data received since the advance GDP release imply that real NRS growth will be revised upward to an annual rate of 7 percent.[13] Nonetheless, the movements of permits for new nonresidential buildings appear to point to growth in construction in the coming months that will be slower than we have seen over the past few years. Permit issuance varied greatly from the second quarter to the third quarter in the various categories, but--smoothing through the ups and downs--the strong recent uptrend in permits for new construction appears to have leveled off.

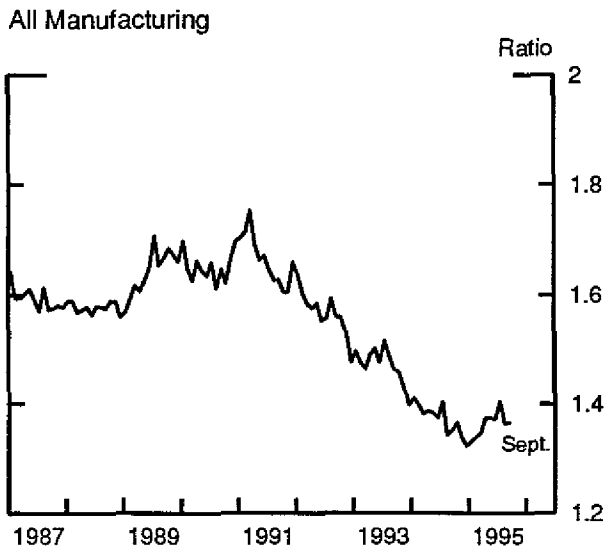
Business Inventories

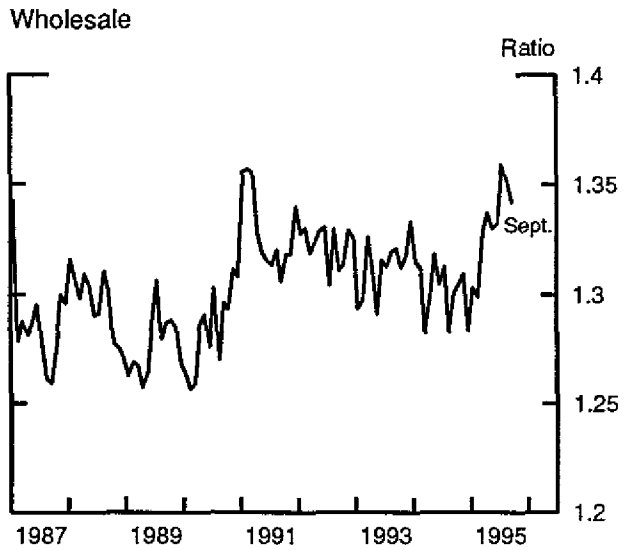
In the advance GDP estimate for the third quarter, BEA assumed real nonfarm inventory investment of $36.8 billion at an annual rate. Census book-value data released so far suggest a lower rate of accumulation. Based on the book-value data, we expect a modest downward revision of $6.5 billion to real nonfarm inventory investment in the third quarter. However, the retail

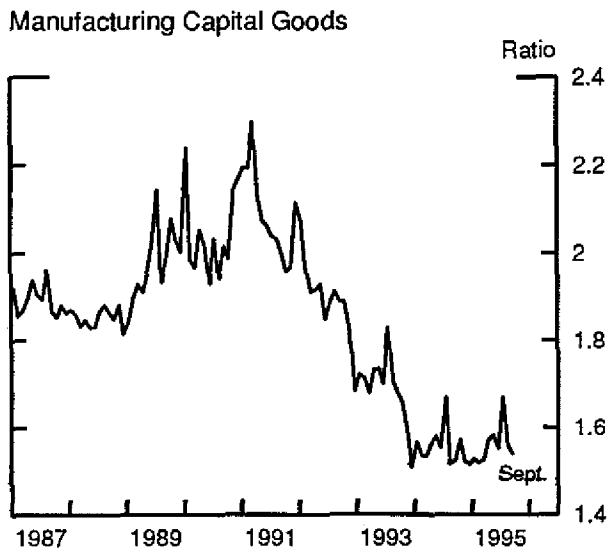
12. Construction of office buildings and lodging and miscellaneous structures surged, but industrial construction dropped back a bit, while other commercial construction recovered most of the ground lost in the second quarter.

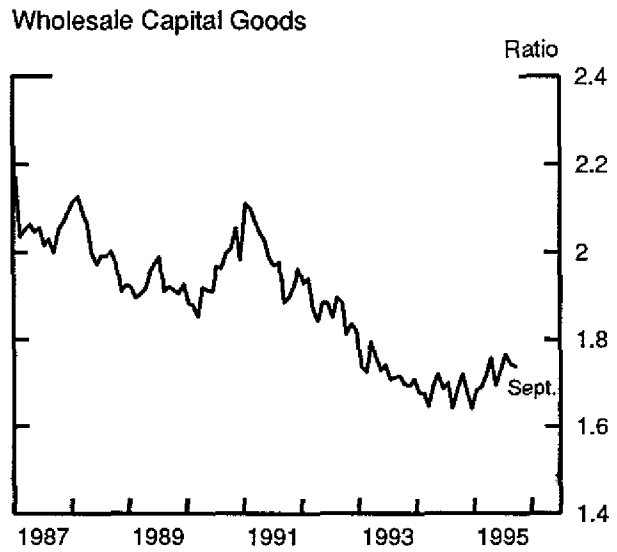
13. Real spending for commercial structures appears to have risen more rapidly than previously estimated, and the estimated decline in industrial building has been largely erased.

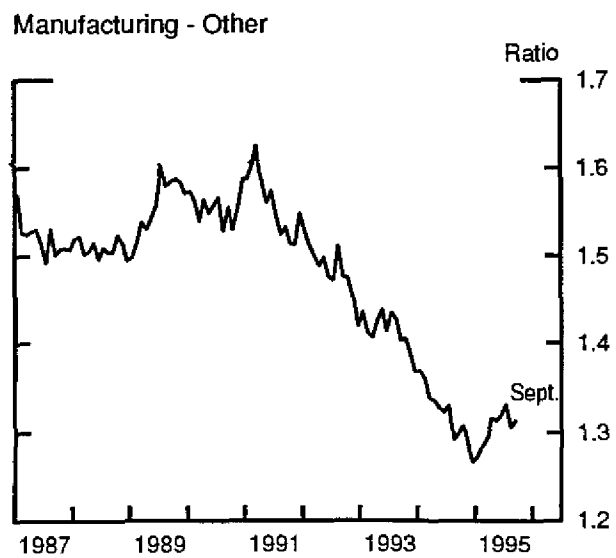
Inventory-Sales Ratios
Manufacturing and Wholesale Trade

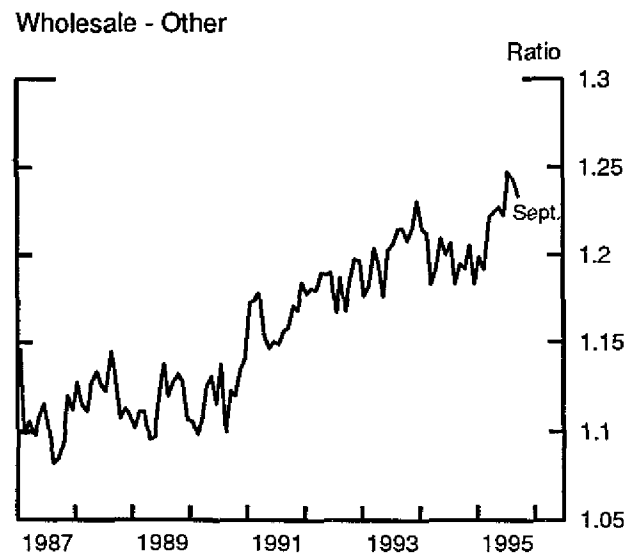












inventory data for September, to be released on November 15, might well alter this estimate.[14]

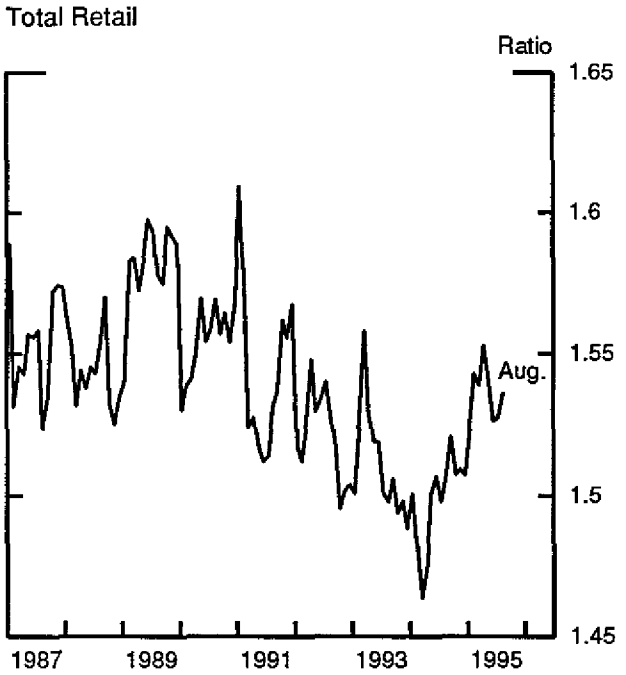
Manufacturers' inventories rose $29 billion at an annual rate in September after a modest increase in August. Stocks of capital goods--in particular telecommunications equipment and electronic components--continued to expand rapidly, apparently reflecting the robust equipment orders and shipments in recent months. Outside of capital goods, however, the accumulation of factory stocks in August and September was well below the pace observed during the second quarter. Inventories at many material-producing industries, including primary metals, chemicals, and rubber and plastics, have posted relatively small net changes since July; inventories held by producers of home goods and apparel also showed only modest increases.

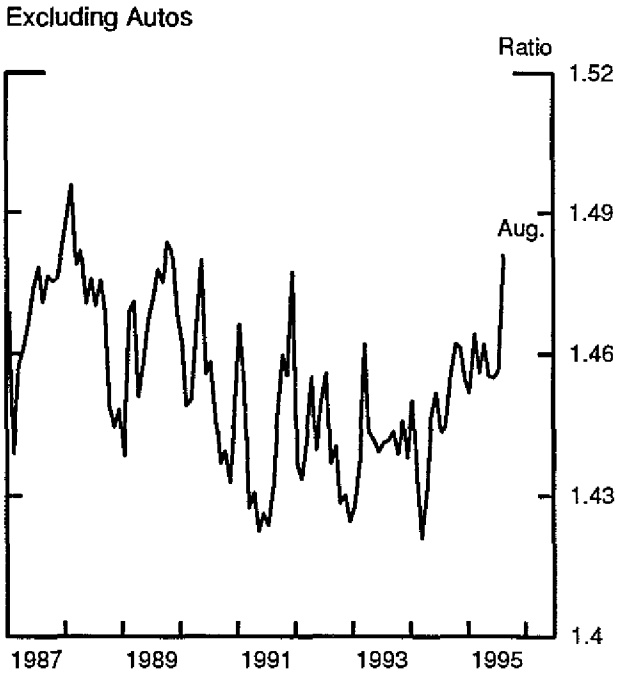
In the trade sector, wholesale inventories were reduced in both August and September following substantial buildups in the preceding months. Stocks of motor vehicles and auto accessories fell further in September; nonauto inventories also posted widespread declines. In contrast to developments in manufacturing, stocks of machinery and equipment held by wholesalers were drawn down in September, although for the quarter as a whole they showed a net accumulation.

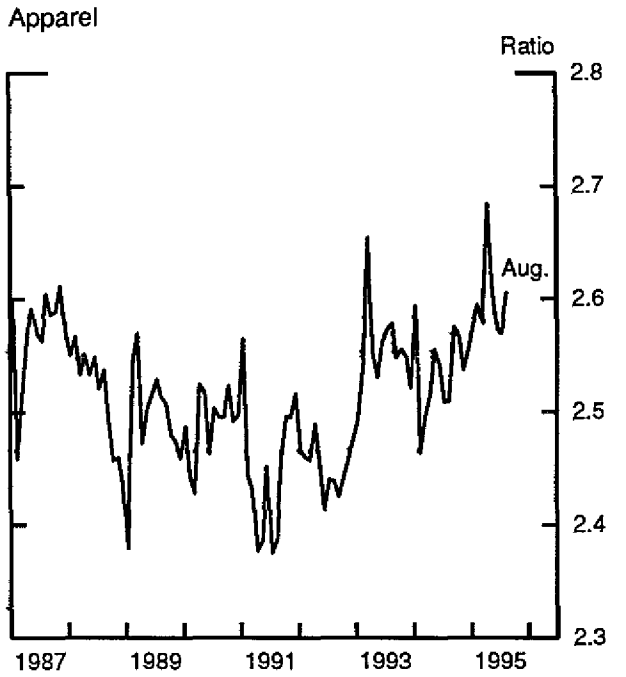
In the retail sector, inventories at most types of stores expanded significantly in August following drawdowns in July. A sharp runup in stocks at general merchandise, apparel, and furniture and appliance outlets (GAF) lifted the inventory-sales ratio for this wide range of stores to a relatively high 2.38 months. However, given the gain in GAF sales shown in the September advance

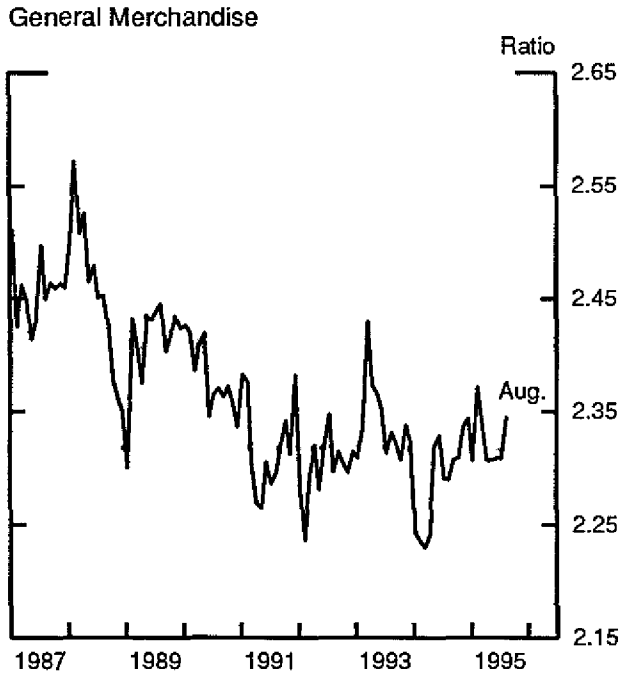
14. The staff's estimated revision to 1987-dollar manufacturing and wholesale trade inventory investment (excluding motor vehicles) is larger than the revisions to the book-value inventory figures underlying BEA's advance estimate. The difference reflects a tilt in the composition of recent inventory investment toward items with relatively large price increases.

Inventory-Sales Ratios
Retail Trade









report, the inventory position for stores in this broad category may have improved since August.

By and large, the pace of inventory investment in the latter part of the third quarter was in line with growth in shipments and sales, and inventory-sales ratios for most types of businesses in manufacturing and trade remained within the ranges that prevailed over the past year.

Federal Sector

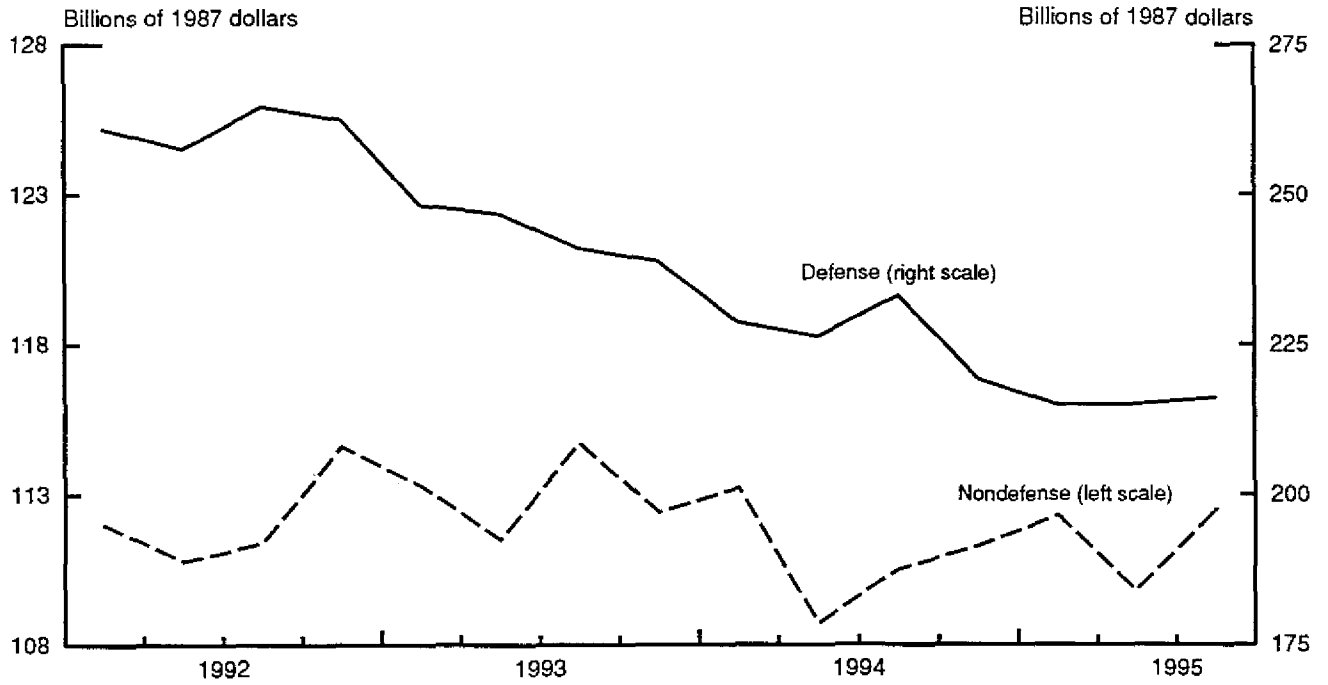
Real federal purchases increased 4.9 percent at an annual rate in the third quarter, according to BEA's advance estimate. Real defense purchases rose at a 2.1 percent annual rate, despite a small decline in nominal spending. In large part, the rise in real spending reflects a marked shift in the composition of nominal purchases toward computers, whose deflator is lower than average.[15] The third-quarter surge notwithstanding, real defense purchases fell 6.6 percent for fiscal 1995, only slightly less than the 7.2 percent decline posted in fiscal 1994 (chart).

Real federal purchases were also boosted in the third quarter by a 10.2 percent (annual rate) increase in real nondefense purchases. This growth was primarily a result of a jump in spending for noncompensation services. However, real nondefense purchases are quite volatile, and this third-quarter increase merely raised real nondefense purchases to slightly above their recent average level after a drop in the second quarter. Indeed, real nondefense purchases have been approximately flat over the past four years.

The unified budget deficit for fiscal 1995 was $164 billion, a $39 billion decline from the $203 billion deficit posted in fiscal 1994. Fiscal 1995 receipts from spectrum auctions accounted for

15. A significantly smaller factor contributing to the decline in the deflator for defense purchases was the delivery of two satellites in the second quarter and none in the third quarter; satellites have a higher-than-average deflator.

Real Federal Government Purchases



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

	Aug. & Sept.		Fiscal years totals			
	1994	1995	1994	1995	Dollar change	Percent change
Outlays	253.2	266.3	1460.6	1514.4	53.8	3.7
Deposit insurance (DI)	-2.9	-1.0	-7.3	-17.6	-10.3	141.7
Spectrum auction (SA)	.0	.0	.0	-7.6	-7.6	n.a.
Other	254.2	267.3	1467.8	1539.6	70.6	4.8
Receipts	233.2	239.8	1257.5	1350.6	93.1	7.4
Deficit(+)	20.0	26.6	203.1	163.8	-39.3	-19.3
	Adjusted for payment timing shifts[1] and excluding DI and SA					
Outlays	256.1	267.3	1462.2	1539.6	77.4	5.3
National defense	51.5	49.9	279.0	272.2	-6.8	-2.4
Net interest	35.3	39.5	203.0	232.2	29.2	14.4
Social security	53.6	56.1	319.6	335.8	16.3	5.1
Medicare and Medicaid	39.9	44.8	226.8	248.9	22.1	9.7
Other health spending	4.2	4.3	24.8	25.7	0.9	3.6
Income security	34.0	36.5	212.3	220.2	7.9	3.7
Other	37.5	36.1	192.5	204.6	10.9	5.7
Receipts	233.2	239.8	1257.5	1350.6	93.1	7.4
Personal income and social insurance taxes	180.8	184.7	1004.5	1074.8	70.3	7.0
Corporate	30.4	35.5	140.4	157.5	17.1	12.2
Other	22.1	19.5	112.6	118.7	6.2	5.5
Deficit(+)	22.8	27.6	204.7	189.0	-15.7	-7.7

n.a. Not applicable.
1. A shift in payment timing occurs when the first of the month falls on a weekend or holiday. The monthly and fiscal year to date outlays for defense, income security, and "other" have been adjusted to account for this shift.
Components may not sum to totals because of rounding.

almost $8 billion of the decline. Another $10 billion results from lower net deposit insurance outlays. Excluding these factors and adjusting for shifts in the timing of payments between fiscal years, the deficit fell $16 billion.[16]

Compared with fiscal 1994, receipts rose 7 percent last year and timing-adjusted outlays (outlays excluding deposit insurance and spectrum auction proceeds) increased 5 percent. Most receipt categories showed strong growth; individual income taxes were up 9 percent, and corporate tax receipts were up 12 percent. On the outlay side, growth was led by net interest payments, which rose 14 percent. Health-related spending for Medicare and Medicaid was up almost 10 percent. Income security outlays increased only 3 percent, reflecting favorable economic developments. Spending restraint was provided by defense, which fell 2 percent.

The fiscal 1995 deficit was $4 billion higher than the Administration's mid-session review had anticipated in July but $29 billion below the deficit projection in the President's February budget. Similarly, the fiscal 1995 deficit was $3 billion higher than CBO's midyear deficit estimate released in August but $12 billion below CBO's January estimate.

September contains one of the four "due dates" for estimated individual and corporate tax payments, and these payments normally are a useful indicator of total tax liabilities for the year. Individual nonwithheld tax payments for September were more than 9 percent higher than a year earlier. Moreover, gross corporate payments were almost 17 percent above September of last year.

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16. Military pay, Supplemental Security Income benefits, and veterans benefits scheduled to be paid on the first of the month are shifted into the previous month if the first falls on a weekend. For both fiscal 1995 and fiscal 1996, the first day of the fiscal year--October 1--fell on a weekend, so these payments were shifted into the previous fiscal year.

Even though the new fiscal year began on October 1, a substantial amount of work on the fiscal 1996 budget remains to be done. A continuing resolution signed by the President on September 30 avoided a government shutdown when none of the thirteen appropriations bills, which provide annual funding for most discretionary spending programs, had been signed into law by the beginning of fiscal 1996. The resolution funds currently ongoing discretionary government programs between October 1 and November 13 if the pertinent appropriation bill has not been enacted.[17] As of November 7 the President had signed only two appropriations bills (Agriculture and Military Construction) and vetoed one (Legislative Branch). A complete set of the appropriations bills will not be signed into law by November 13. A second continuing resolution extending funding through December 1 for programs covered by the eleven unsigned appropriations bills is being considered by Congress.[18]

Both the House and Senate have passed their respective versions of a budget reconciliation bill, which proposes the legislative changes to mandatory spending programs and tax laws designed to meet the guidelines of the budget resolution. A House-Senate conference is working currently to resolve the differences between the bills.

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17. In general, the resolution funds programs at a provisional level equal to 95 percent of the average annual funding in the Senate and House versions of the appropriations bills. However, most programs that would have their funding "significantly reduced" under this funding formula can have their funding rate increased to 90 percent of the fiscal 1995 level, and adequate funding is assured to avoid worker layoffs. The staff estimates that the current resolution, if extended at similar terms, would reduce nominal discretionary spending by approximately $15 billion (annual rate) in 1995:Q4 relative to the level set by the discretionary spending caps enacted in the Omnibus Budget Reconciliation Act of 1993.

18. This pending resolution would set spending at the House or Senate versions of the spending bills or at last year's level, whichever is lowest. However, no program would be funded below 60 percent of its current level, and sufficient funding is allowed to avoid layoffs.

Republicans in the Congress appear to remain committed to keeping debt-limit legislation tied to the budget reconciliation bill. The Congress is considering a bill to temporarily raise federal borrowing authority by $67 billion through December 12 to allow time for the Congress and the President to continue work on budget legislation without forcing Treasury to default when the debt limit is hit and its cash balances are depleted. The bill also contains restrictions on Treasury's authority to disinvest or underinvest government trust funds and provides authority for the continuation of certain benefit payments in the event of a Treasury default.

State and Local Government Sector

Real purchases of goods and services by state and local governments were estimated by BEA to have risen at a 2.1 percent annual rate in the third quarter, about the same as in the second quarter. Within that total, real construction spending was initially estimated to have risen at a 3.5 percent pace in the third quarter, but will likely be revised upward when BEA incorporates the monthly data on construction put in place in September. The revision may bring growth in total state and local purchases in the third quarter to 3 percent, making this the strongest gain in a year. State and local government employment increased 55,000 in the third quarter, the largest advance since the fourth quarter of last year. In October, employment rose just 6,000; sizable declines were reported among education workers at both the state and the local levels for the second consecutive month.

Heightened concern about both revenue growth and future cuts in federal aid has raised questions about the budget assumptions of many state and local governments. Most states based their fiscal 1996 budget on the assumption that federal aid would not be altered, but they now face likely cuts in aid and a consolidation of programs

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

	Relative importance, Dec. 1994	1993	1994	1995 Q1	1995 Q2	1995 Q3	1995 Aug.	1995 Sept.
				-----Annual rate------			-Monthly rate-	
All items[2]	100.0	2.7	2.7	3.2	3.2	1.8	.1	.1
Food	15.8	2.9	2.9	.0	3.6	3.6	.2	.5
Energy	7.0	-1.4	2.2	-1.1	5.4	-11.5	-.8	-1.4
All items less food and energy	77.2	3.2	2.6	4.1	3.0	2.8	.2	.2
Commodities	24.1	1.6	1.4	2.6	.6	2.3	.4	.1
Services	53.1	3.9	3.2	4.8	4.3	3.0	.1	.3
Memo:								
CPI-W[3]	100.0	2.5	2.7	3.6	2.7	1.6	.1	.2

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

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

	Relative importance, Dec. 1994	1993	1994	1995 Q1	1995 Q2	1995 Q3	1995 Aug.	1995 Sept.
				-----Annual rate------			-Monthly rate-	
Finished goods	100.0	.2	1.7	3.2	.9	.9	-.1	.3
Consumer foods	22.8	2.4	1.1	-1.2	-4.9	9.1	.0	1.0
Consumer energy	13.6	-4.1	3.5	11.3	2.0	-14.7	-.9	-.5
Other finished goods	63.7	.4	1.6	2.9	2.9	2.0	.1	.2
Consumer goods	40.2	-.4	1.4	2.9	3.2	2.3	.1	.3
Capital equipment	23.5	1.8	2.0	3.0	2.4	1.5	.1	.1
Intermediate materials[2]	95.6	.8	4.8	10.6	3.9	-.6	-.1	-.1
Excluding food and energy	82.9	1.6	5.2	10.5	4.2	1.8	.1	.1
Crude food materials	40.4	7.2	-9.4	-4.6	-.4	41.7	.7	4.2
Crude energy	34.5	-12.3	-.1	-4.5	15.3	-22.4	-3.8	3.2
Other crude materials	25.1	10.7	17.3	21.9	4.1	-17.8	-.9	-2.1

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

into block grants. Regarding revenue, the growth in tax bases appears to be slowing. Notably, consumption and taxable income--considered indicators of state and local tax bases--rose at an annual rate of about 4.5 percent over the first three quarters of this year, compared with gains of 6 to 7 percent during the preceding year. Among the largest states, California, Illinois, New Jersey, and New York incorporated particularly optimistic assumptions about revenue. Meanwhile, budget difficulties continue to be foreshadowed by structural imbalances, especially in states like Florida and Texas, where both the population and public-school enrollment have risen.

Prices

Inflation remained modest in September. The overall CPI increased 0.1 percent, the same as in August, and the September increase in the CPI excluding food and energy was 0.2 percent, the fifth consecutive increase of this size. Over the twelve months ended in September, the overall CPI rose 2.5 percent, down from a 3.0 percent increase over the preceding twelve months, while the CPI excluding food and energy increased 2.9 percent in the latest twelve-month period, little changed from the 3.0 percent increase in the preceding twelve months.

The CPI for energy fell 1.4 percent in September, its third consecutive decline. A large drop in gasoline prices over the past three months--reflecting the reversal of a bulge in crude oil prices in the spring--accounted for most of the decline in energy prices in the third quarter. But utility rates also fell as natural gas prices continued the downtrend that began in 1994. Food prices increased 0.5 percent in September, the largest increase since April. The increase was concentrated in prices of fresh vegetables,

INFLATION RATES EXCLUDING FOOD AND ENERGY
(Percentage change from twelve months earlier)

	Sept. 1993	Sept. 1994	Sept. 1995
CPI	3.2	3.0	2.9
Goods	1.5	1.9	1.5
Alcoholic beverages (2.0)[1]	1.3	1.0	2.0
New vehicles (6.6)	3.0	4.1	1.8
Apparel (6.6)	0.9	-0.6	-1.3
House furnishings (4.5)	0.8	1.4	0.4
Housekeeping supplies (1.4)	0.7	1.5	4.3
Medical commodities (1.7)	3.5	2.8	1.5
Entertainment (2.5)	1.8	2.5	1.7
Tobacco (2.1)	-4.0	2.6	3.4
Used cars (1.7)	8.6	4.8	7.6
Services	4.0	3.5	3.6
Owners' equivalent rent (26.3)	3.4	3.5	3.2
Tenants' rent (7.5)	2.6	2.6	2.3
Other renters' costs (2.8)	1.2	2.3	6.0
Airline fares (1.3)	23.8	2.4	2.4
Medical care (7.7)	6.3	5.1	5.0
Entertainment (3.1)	2.8	3.1	3.8
Auto financing (0.8)	-7.8	13.9	11.4
Tuition (3.4)	7.6	6.1	5.7
PPI finished goods	0.4	2.0	2.1
Consumer goods	-0.5	1.8	2.2
Capital goods, excluding computers	2.3	2.7	1.9
Computers	-12.5	-5.4	-13.9
PPI intermediate materials	1.2	3.6	6.2
PPI crude materials	7.2	13.9	7.5
Factors affecting price inflation			
ECI hourly compensation[2]	3.7	3.3	2.6
Goods-producing	4.0	3.3	2.1
Service-producing	3.6	3.2	2.9
Civilian unemployment rate[3,4,5]	6.7	5.7	5.5
Capacity utilization[3] (manufacturing)	80.8	83.6	82.9
Inflation expectations[4,6]			
Michigan Survey	4.0	3.9	3.6
Conference Board	4.8	4.3	3.6
Non-oil import price[7]	0.3	3.2	3.5
Consumer goods, excluding autos, food, and beverages	0.6	0.7	1.7
Autos	1.6	3.5	3.4

1. Relative-importance weight in CPI excluding food and energy.
2. Private industry workers, periods ended in September.
3. End-of-period value.
4. Latest reported value: October.
5. Data after 1993 are not directly comparable with earlier values because of a redesign of the CPS in January 1994.
6. One-year-ahead expectations.
7. BLS import price index (not seasonally adjusted).

which are very erratic. Increases in other food prices, at just 0.2 percent, were in line with increases over the past year.

The CPI for commodities other than food and energy increased 0.1 percent in September after a 0.4 percent increase in August. Over the twelve months ended in September, the index for nonfood, non-energy goods has increased 1.5 percent, less than the rise over the preceding year. Over the past twelve months, prices of new motor vehicles have increased less rapidly than in the preceding twelve-month period. Apparel prices have continued to decelerate; soft demand has also likely been a factor here. Prices of housekeeping supplies have increased more rapidly over the past year, reflecting the pass-through to the consumer level of large increases early this year in paper and chemical prices at early stages of processing.

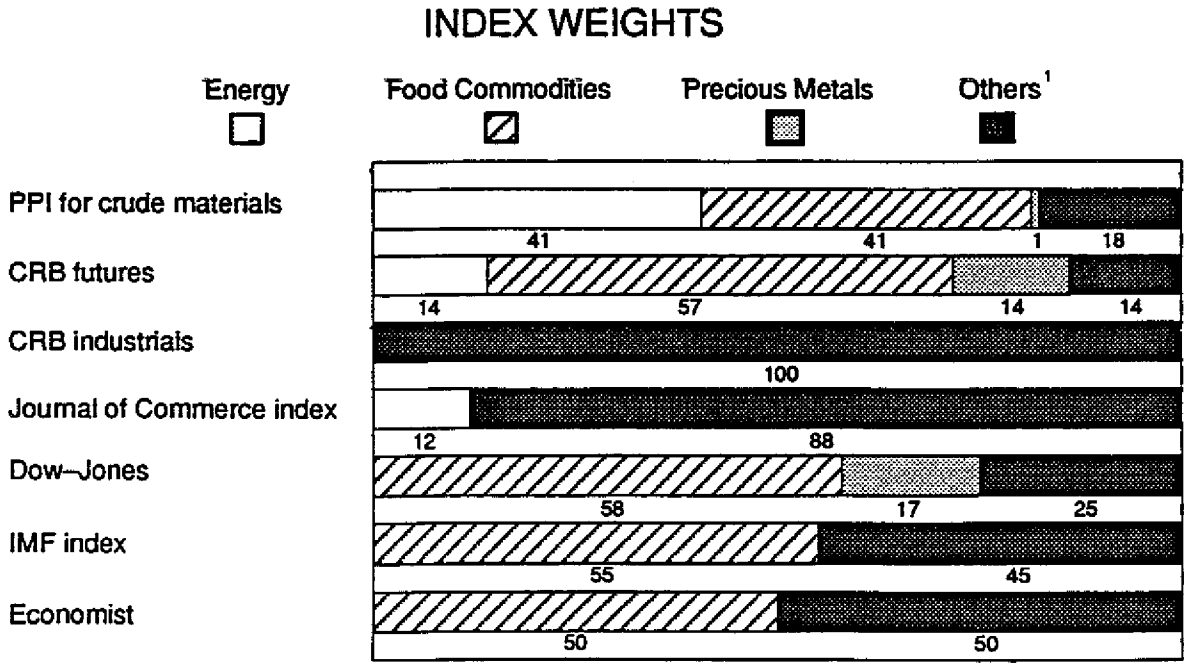
The rise in the CPI for services other than energy, 0.3 percent in September, was in line with the average pace over the past two years. Medical care prices, which decelerated sharply from 1990 to 1994, have increased at about a 5 percent pace in each of the past two years. The latest twelve-month change in airfares (2.4 percent) masks considerable gyration over the year; fares have fallen about 5 percent over the past three months after increasing more than 20 percent in the first six months of the year.

Over the past twelve months, the PPI for personal computers has fallen rapidly--down 25 percent. These price declines are in line with anecdotal evidence on changes in "street prices." In contrast, the PPI for personal computers fell at only a 4-1/2 percent annual rate in the first half of 1994 even though advertised mail-order prices of personal computers were falling at a rate of at least 15 percent. At the time, we noted that the discrepancy was probably the result of an out-of-date sample of

COMMODITY PRICE INDEXES

	Last observation	Percent change[1] 1993	1994	Dec. 94 to Sept. 19[2]	Sept. 19[2] to date	Memo: Year earlier to date
PPI for crude materials[3]	Sep.	0.1	-0.5	1.9	n.a.	2.7
Foods and feeds	Sep.	7.2	-9.4	7.0	n.a.	7.3
Energy	Sep.	-12.3	-0.1	-3.9	n.a.	-5.8
Excluding food and energy	Sep.	10.7	17.3	1.6	n.a.	7.5
Excluding food and energy, seasonally adjusted	Sep.	10.5	17.6	1.1	n.a.	7.5
Commodity Research Bureau						
Futures prices	Nov. 07	11.6	4.8	3.1	0.4	4.4
Industrial spot prices	Nov. 07	-0.0	29.1	-3.1	2.1	4.1
Journal of Commerce industrials	Nov. 07	-2.9	22.1	-0.2	-1.1	0.3
Metals	Nov. 07	-1.8	31.9	-1.5	1.1	1.7
Dow-Jones spot	Nov. 07	5.1	14.8	2.0	-1.3	1.4
IMF commodity index[3]	Sep.	2.4	15.2	17.9	n.a.	20.9
Metals	Sep.	-14.4	39.1	-6.4	n.a.	7.4
Nonfood agricultural	Sep.	0.2	14.8	3.5	n.a.	6.8
Economist (U.S. dollar index)	Oct. 31	9.1	31.0	-6.9	1.1	-5.0
Industrials	Oct. 31	4.4	38.6	-5.1	-2.3	-2.2

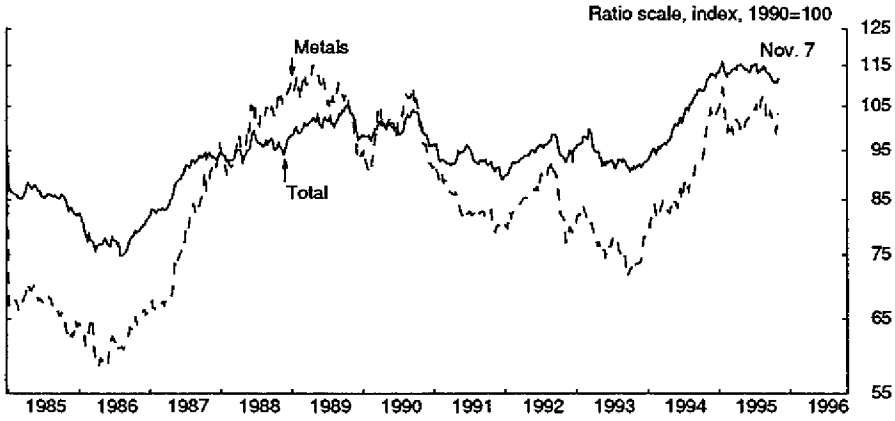
Note. Not seasonally adjusted. Copyright for Journal of Commerce data is held by CIBCR, 1994.
1. Change is measured to end of period, from last observation of previous period.
2. Week of the September Greenbook.
3. Monthly observations. IMF index includes items not shown separately.
n.a. Not available.

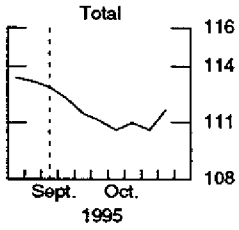


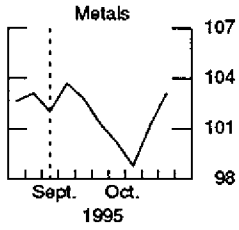
1. Forest products, industrial metals, and other industrial materials.

Commodity Price Measures

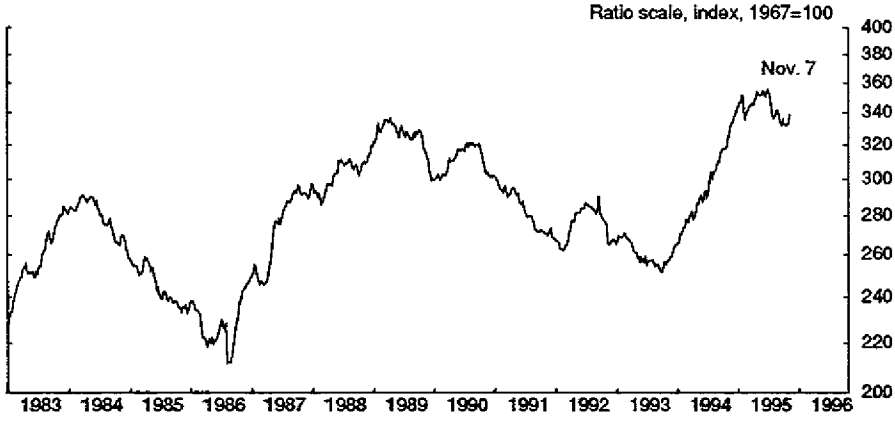
Journal of Commerce Index

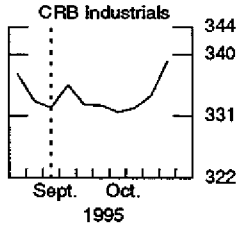




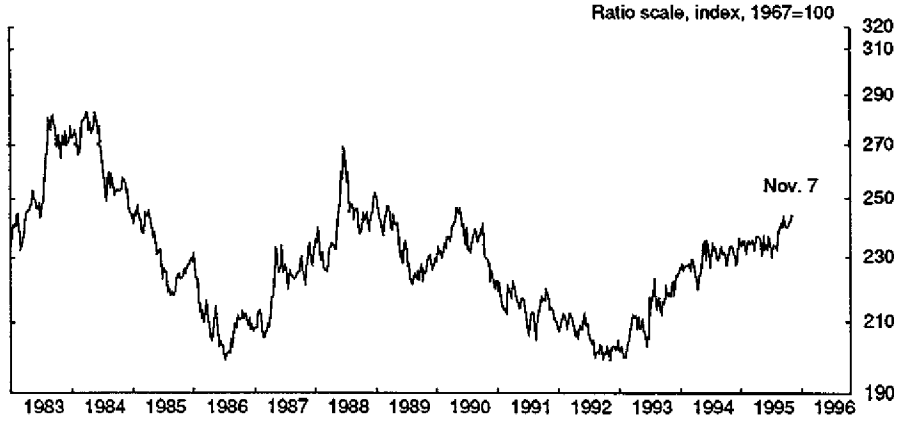


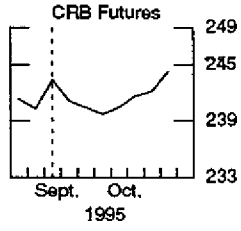
CRB Spot Industrials





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.

SPOT PRICES OF SELECTED COMMODITIES

	Current price ($)	Percent change[1] 1993	1994	To Sept. 19[2]	Sept. 19[2] to Nov. 07	Memo: Year earlier to date
	INDUSTRIAL COMMODITIES					
Metals						
Copper (lb.)	1.400	-19.0	64.9	-4.3	3.7	8.5
Steel scrap (ton)	134.500	46.8	2.9	.0	-6.3	.7
Aluminum, London (lb.)	.757	-10.7	73.5	-8.4	-4.8	-9.2
Lead (lb.)	.436	3.0	20.7	.4	4.3	6.7
Zinc (lb.)	.528	-7.5	23.6	-14.4	6.8	-10.6
Tin (lb.)	4.224	-14.1	21.4	5.9	.5	2.8
Textiles and fibers						
Cotton (lb.)	.848	19.6	38.5	5.7	-6.7	19.3
Burlap (yd.)	.365	8.2	10.2	8.7	15.0	26.1
Miscellaneous materials						
Hides (lb.)	.800	1.3	14.2	-8.9	-2.7	-14.0
Rubber (lb.)	.810	-7.3	75.4	-9.6	14.1	14.1
	OTHER COMMODITIES					
Precious metals						
Gold (oz.)	384.800	16.6	-1.7	1.0	.0	.0
Silver (oz.)	5.325	38.8	-5.0	13.6	-2.1	1.3
Platinum (oz.)	408.250	8.0	7.5	6.1	-7.1	-.4
Forest products						
Lumber (m. bdft.)	252.000	75.8	-37.1	-1.4	-12.5	-20.0
Plywood (m. sqft.)	318.000	-6.3	1.5	11.2	-13.4	-18.5
Petroleum						
Crude oil (barrel)	16.820	-25.0	15.6	10.3	-2.2	-3.1
Gasoline (gal.)	.495	-31.0	32.4	20.8	-16.4	-10.3
Fuel oil (gal.)	.507	-22.4	12.7	3.5	-.5	-.3
Livestock						
Steers (cwt.)	67.000	-7.3	-3.4	-8.6	4.7	-4.3
Hogs (cwt.)	41.000	.6	-12.9	39.4	-17.2	46.4
Broilers (lb.)	.581	6.1	-4.9	25.2	-5.3	20.0
U.S. farm crops						
Corn (bu.)	3.255	41.7	-23.2	30.8	12.8	61.5
Wheat (bu.)	5.260	5.8	11.4	13.7	6.1	21.8
Soybeans (bu.)	6.765	24.5	-19.6	13.4	7.0	23.2
Other foodstuffs						
Coffee (lb.)	1.240	-2.3	153.1	-27.4	4.6	-32.1
Memo:						
Exchange value of the dollar (March 1973=100)	84.245	3.4	-5.5	-3.4	-3.1	-2.2
Yield on Treasury bill, 3-month[3]	5.370	-14	247	-33	17	14

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 September Greenbook.
3. Changes are in basis points.

computers. Conversations with BLS analysts suggest that the agency has recently done a better job of keeping its sample of computers up to date with the mix of products in the marketplace.

Pressures on materials prices have eased considerably since the spring. Over the past five months, the PPI for intermediate materials other than food and energy has increased at a 2.1 percent annual rate, down from a 7.8 percent increase over the preceding twelve-month period. The easing in intermediate materials prices likely reflects the drop-off in capacity utilization rates since the beginning of the year.

Prices of industrial commodities were slightly lower during most of the period since the last Greenbook; in recent weeks, some commodities have regained much of their price declines. The *Journal of Commerce* index is little changed from its level in late September. Copper cathode prices have been quite volatile this year, and, while having dropped in the past few weeks, were still at about their level at the beginning of the year. The price of aluminum now stands about 13 percent below its level at the beginning of the year. Steel scrap prices have retreated since mid-September and are currently near year-ago levels; the recent declines are consistent with other indicators of sluggishness in manufacturing. In addition, news in the trade press indicates that exports--especially to Asia--have weakened recently, after surging earlier this year.

In the farm sector, prices of crop commodities have moved still higher since mid-September, boosted by further markdowns in estimates of this year's harvest. Corn prices in recent days have been at levels about 70 percent above those of a year earlier, and prices of wheat and soybeans have also increased substantially. Livestock prices have been mixed of late, with cattle prices

FARM PRICES AND FOOD PRICES
BEFORE, DURING, AND AFTER YEARS OF POOR HARVESTS
(Percentage change, Q4 to Q4)

1983 drought	1982	1983	1984
CPI for food	3.2	2.2	3.8
PPI for finished foods	1.8	2.1	3.3
PPI for crude foods	-1.1	7.4	-1.8
Prices received by farmers	-3.6	15.4	-6.7
Crops	-7.6	27.6	-12.4
Livestock	2.3	-.8	2.7
MEMO:			
CPI excluding food and energy	5.2	4.2	5.0

1988 drought	1987	1988	1989
CPI for food	3.5	5.1	5.6
PPI for finished foods	.1	5.1	4.8
PPI for crude foods	1.4	15.2	.5
Prices received by farmers	5.1	16.4	-1.9
Crops	11.5	22.9	-8.4
Livestock	-2.2	7.5	8.0
MEMO:			
CPI excluding food and energy	4.3	4.5	4.4

1993 flood and drought	1992	1993	1994
CPI for food	1.6	2.6	2.6
PPI for finished foods	.9	2.1	.6
PPI for crude foods	1.9	5.6	-8.5
Prices received by farmers	-1.4	5.9	-5.9
Crops	-2.0	9.3	-3.8
Livestock	1.0	1.0	-8.5
MEMO:			
CPI excluding food and energy	3.4	3.1	2.8

1995 flood, drought, and freeze[1]	1994	1995	1996
CPI for food	2.6	2.7	--
PPI for finished foods	.6	2.9	--
PPI for crude foods	-8.5	7.3	--
Prices received by farmers	-5.9	10.5	--
Crops	-3.8	15.2	--
Livestock	-8.5	3.4	--
MEMO:			
CPI excluding food and energy	2.8	2.9	--

1. Data shown for 1995 are twelve-month changes, measured to the last month for which data are available--September 1995 in the case of the CPI and PPI and October 1995 in the case of farm prices.

rebounding from summer lows and hog prices moving down more rapidly than is implied by normal seasonal patterns.

History offers mixed signals as to how much of an effect this year's sharp run-up in crop prices might ultimately have on farm and food prices further down the line (see table). For example, in each of three other recent episodes in which prices of feed grains and oilseeds were pushed up by poor harvests--those of 1983, 1988, and 1993--responses in livestock prices displayed considerable variation, rising modestly in the first episode, soaring in the second, and declining sharply in the third.

Consumer food prices eventually accelerated in all three episodes--at least if measured from the year preceding the poor crop to the year after the poor crop--but the timing varied, and in two of the three episodes the degree of acceleration left food prices still rising at a rate less than the rate of core inflation. The minimal acceleration in retail food prices in all three cases, measured relative to the surge in crop prices, is probably in large part a reflection of the dominance of nonfarm inputs in value added in the food sector.

The duration of the surge in crop prices in all three cases was limited by a rebound in production in the following year. As for the current episode, recent configurations of futures prices suggest that traders anticipate higher crop production and a downturn in crop prices in 1996. At this point, however, with the usual production rebound still uncertain--and with traders fairly bullish about the prospects for farm exports--the markets also appear to be betting on only a partial reversal of the large price advances of the past year.

EMPLOYMENT COST INDEX OF HOURLY COMPENSATION
FOR PRIVATE INDUSTRY WORKERS

	1994		1995		
	Sept.	Dec.	Mar.	June	Sept.
	-----Quarterly percent change------- (compound annual rate)				
Total hourly compensation:[1]	3.3	2.6	2.3	2.9	2.3
Wages and salaries	2.7	2.4	2.7	3.0	2.7
Benefit costs	4.0	3.0	0.6	2.1	2.1
By industry:					
Construction	4.1	-0.3	0.3	2.0	3.3
Manufacturing	3.6	2.9	1.9	2.9	1.6
Transportation and public utilities	5.5	3.7	4.7	2.9	3.9
Wholesale trade	4.8	2.0	6.8	3.6	5.9
Retail trade	4.4	0.3	3.0	1.0	3.0
FIRE	2.7	1.4	4.4	5.4	3.0
Services	2.3	2.9	1.9	3.5	1.3
By occupation:					
White-collar	3.0	2.9	2.9	3.2	2.2
Blue-collar	3.7	2.3	1.6	2.9	2.3
Service occupations	2.7	3.7	1.0	2.6	1.9
Memo:					
State and local governments	2.6	2.6	2.9	3.9	1.9
	-----Twelve-month percent change----				
Total hourly compensation:	3.3	3.1	2.9	2.8	2.6
Excluding sales workers	3.3	3.1	3.0	2.8	2.5
Wages and salaries	2.9	2.8	2.9	2.9	2.8
Benefit costs	4.0	3.7	2.9	2.6	2.1
By industry:					
Construction	3.9	3.7	2.1	1.5	1.4
Manufacturing	3.2	3.1	3.0	2.8	2.3
Transportation and public utilities	3.9	3.9	4.0	4.1	3.8
Wholesale trade	3.4	3.1	4.5	4.3	4.6
Retail trade	3.6	2.8	2.9	2.2	1.8
FIRE	2.4	2.1	2.1	3.5	3.5
Services	2.9	2.8	2.5	2.6	2.4
By occupation:					
White-collar	3.4	3.2	3.1	3.0	2.8
Blue-collar	3.0	2.8	2.7	2.6	2.3
Service occupations	2.4	2.8	2.3	2.5	2.4
Memo:					
State and local governments	3.0	3.0	3.1	3.1	3.0

1. Seasonally adjusted by the BLS.

Labor Costs

The employment cost index (ECI) measure of hourly compensation for private industry workers rose 2.3 percent at an annual rate in the third quarter, bringing the gain over the past twelve months to 2.6 percent. The rise during the same period of a year ago was 3.3 percent. In the past year, growth in hourly compensation has slowed or been little changed in almost all major occupations and industries. The few exceptions include service occupations (security guards, food service workers, barbers, etc.) and the wholesale trade, real estate, and securities/nonbanking financial industries.

Most of the deceleration in growth of ECI hourly compensation over the past year continues to reflect the dramatic slowing in the benefits component. While growth in hourly wages and salaries has held relatively steady at a bit under 3 percent, hourly benefit costs have decelerated from a 4 percent pace over the twelve months ended in September 1994 to a 2.1 percent pace over the most recent twelve-month period. Health insurance costs, which were essentially unchanged over the past twelve months, can account for about one-half of the slowing in benefits growth. The deceleration in the costs of health care has also contributed to the decline in employers' costs for workers' compensation--a legally required benefit--which fell 2.3 percent over the twelve months ended in September. In addition, employer costs for state unemployment insurance declined 2.9 percent over the same period, reflecting the effect of fewer layoffs on firms' experience ratings.

Another measure of hourly compensation growth is available in the productivity and cost data--nonfarm hourly compensation. Unlike ECI hourly compensation, nonfarm hourly compensation does not have fixed weights. Which weighting scheme is desirable depends upon the

EMPLOYMENT COST INDEX OF HOURLY WAGES AND SALARIES
FOR PRIVATE INDUSTRY WORKERS
(Twelve-month percent changes)

	1994		1995		
	Sept.	Dec.	Mar.	June	Sept.
Hourly wages and salaries	2.9	2.8	2.9	2.9	2.8
By industry:					
Construction	3.0	3.2	2.3	1.8	1.9
Manufacturing	3.2	3.0	3.3	3.3	2.9
Transportation and public utilities	3.7	3.6	4.1	4.1	3.4
Wholesale trade	3.3	3.0	4.0	3.7	4.2
Retail trade	3.1	2.4	3.0	2.2	2.1
FIRE	1.3	1.2	1.1	3.4	3.7
Services	2.8	2.8	2.6	2.6	2.5
By occupation:					
White-collar	3.0	2.8	2.9	2.8	2.8
Blue-collar	3.0	2.8	2.9	3.1	2.8
Service occupations	2.3	3.0	2.7	2.7	2.7
Memo:					
State and local governments	2.9	3.1	3.2	3.2	3.1

EMPLOYMENT COST INDEX OF HOURLY BENEFIT COSTS
FOR PRIVATE INDUSTRY WORKERS
(Twelve-month percent changes)

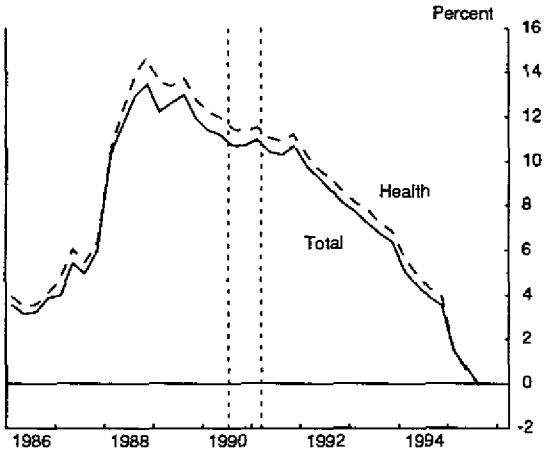
	1994		1995		
	Sept.	Dec.	Mar.	June	Sept.
Hourly benefit costs[1]	4.0	3.7	2.9	2.6	2.1
Insurance costs	3.9	3.6	1.5	0.7	0.0
Health care	4.3	3.9	1.6	0.6	-0.1
Supplemental pay	6.2	4.5	6.2	3.0	1.4
Retirement and savings	10.2	11.1	6.1	8.4	7.8
Paid leave	3.2	3.1	3.7	3.6	3.3
Legally required	2.9	2.3	1.2	0.9	0.9
By industry:					
Goods-producing	3.7	3.5	2.4	1.5	1.0
Service-producing	4.4	3.8	3.3	3.4	2.7
By occupation:					
White-collar occupations	4.7	4.5	3.6	3.3	2.9
Blue-collar occupations	3.3	2.8	2.1	1.6	1.1
Service occupations	2.8	2.4	1.6	1.9	1.1
Memo:					
State and local governments	3.2	2.8	2.5	2.9	2.5

1. The detail on benefit costs is from unpublished data from the BLS.

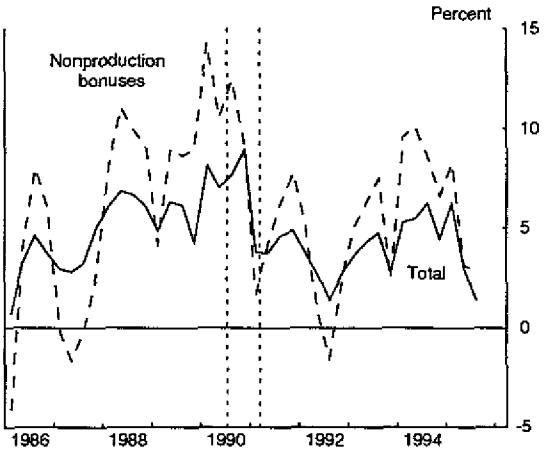
10/31/95

Components of ECI Benefits Costs
(Private industry workers; twelve-month percent change)

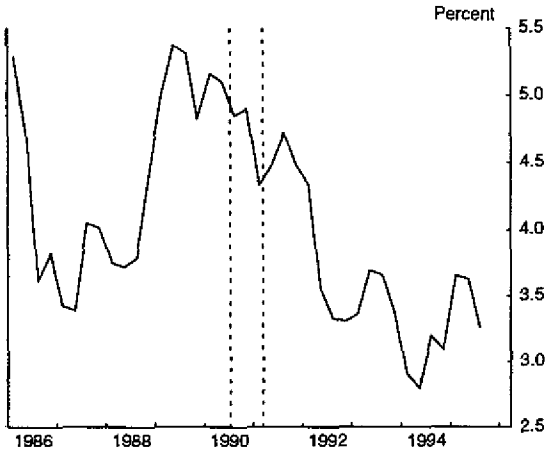
Insurance Costs



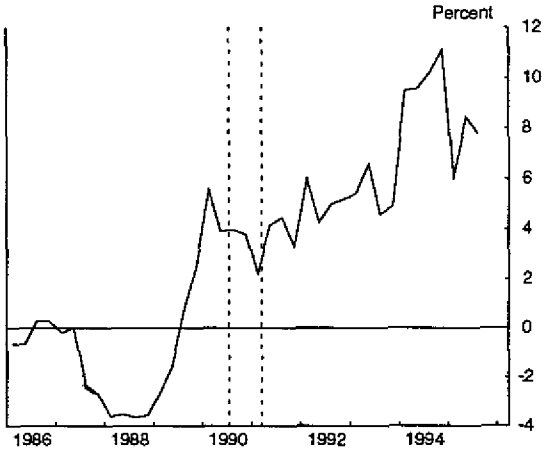
Supplemental Pay



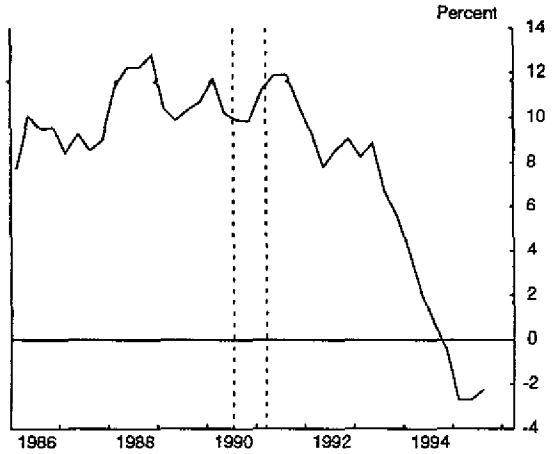
Paid Leave



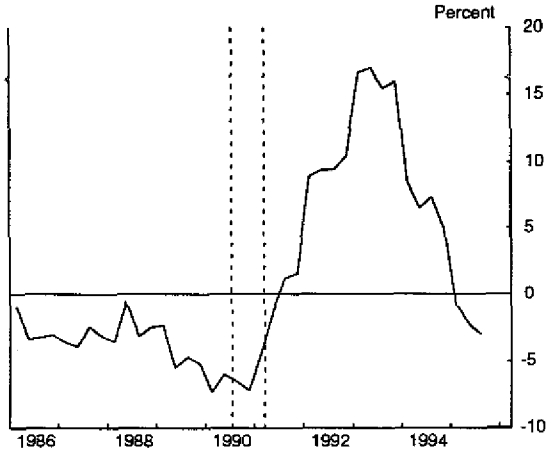
Retirement and Savings



Workers' Compensation Insurance



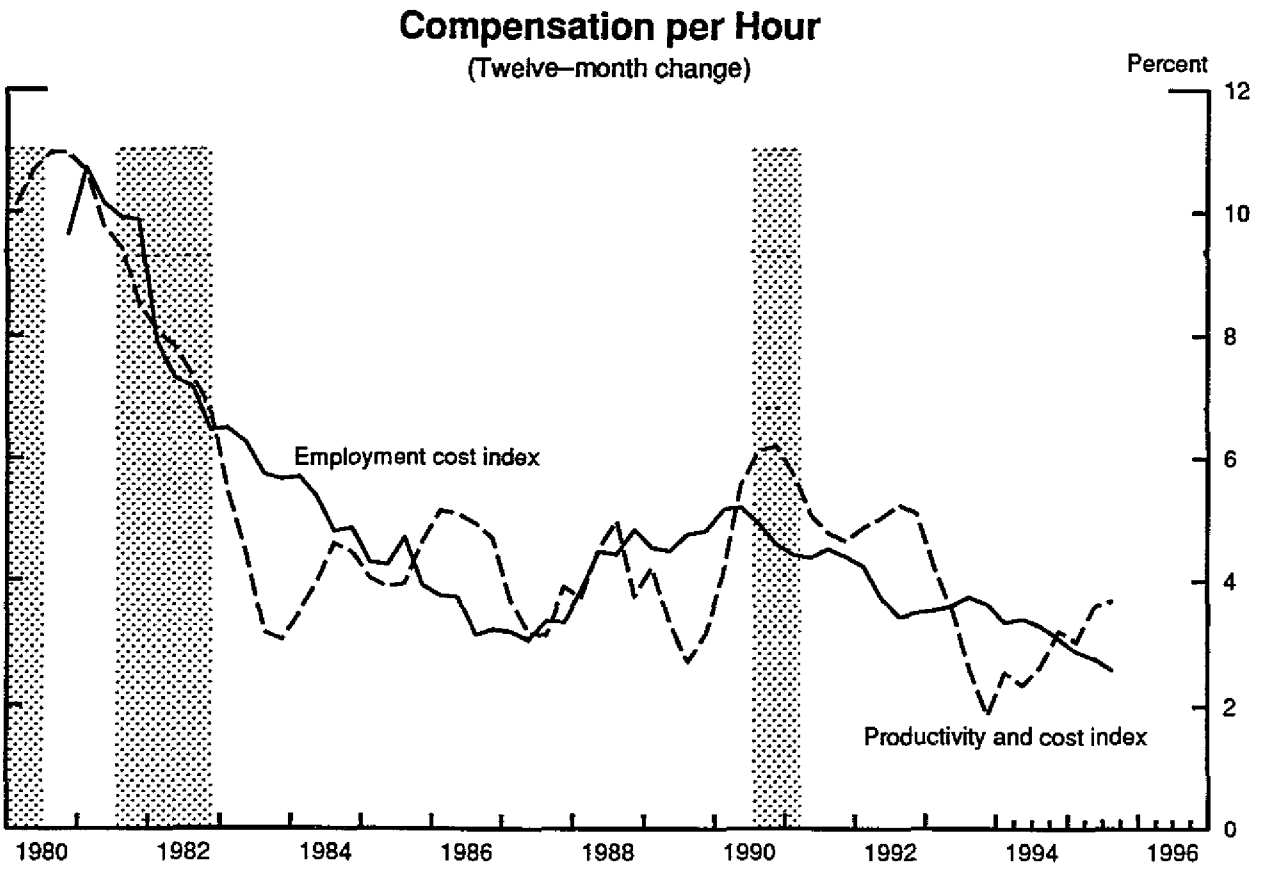
State Unemployment Insurance



HOURLY COMPENSATION
(Percent change from preceding period at compound annual rate; based on seasonally adjusted data)

	1993[1]	1994[1]	1994 Q4	1995 Q1	1995 Q2	1995 Q3	1994:Q3 to 1995:Q3
Compensation per hour							
Total business	2.3	3.2	3.6	3.8	3.8	3.2	3.6
Nonfarm business	1.9	3.2	3.8	4.1	3.7	3.1	3.7
Manufacturing	1.7	1.7	3.8	4.7	.5	3.7	3.2
Nonfinancial corporations[2]	1.3	2.6	3.2	3.4	3.5	ND	ND
Unit labor costs							
Total business	.8	1.2	-.7	1.7	-.8	1.1	.3
Nonfarm business	.5	1.4	-.4	1.6	-1.2	1.1	.3
Manufacturing	-1.7	-2.4	.1	1.1	-2.2	-2.3	-.8
Nonfinancial corporations[2]	-1.0	1.0	-.3	1.8	-1.6	ND	ND

1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.
2. The nonfinancial corporate sector includes all corporations doing business in the United States with the exception of banks, stock and commodity brokers, finance and insurance companies; the sector accounts for about two-thirds of business employment.



use of the data. But one clear disadvantage of the nonfarm compensation measure is that recent estimates of benefits costs are essentially extrapolations. The wages and salaries component is also subject to substantial revision as more complete information comes in over several years. That said, nonfarm hourly compensation rose at an annual rate of 3.1 percent in the third quarter--down from 3.7 percent in the second quarter. Over the four quarters ended in 1995:Q3, nonfarm hourly compensation rose 3.7 percent. In contrast to the ECI measure, this is up from 2.6 percent over the preceding four quarters. The difference in the patterns of hourly compensation growth between the two series may result in part from the fact that recent information on benefit costs in nonfarm compensation may not capture the dramatic slowing in health care costs or legally required benefits that has occurred over the past year.

The only major piece of wage data for the fourth quarter is one month's reading on average hourly earnings of production or nonsupervisory workers. Average hourly earnings rose 0.5 percent in October. Perhaps more telling, however, is that average hourly earnings rose 3.0 percent over the twelve months ended in October--about the same as the 3.1 percent increase over the previous twelve months. After having run somewhat lower than the ECI (for a comparable subset of workers) for much of 1993 and 1994, average hourly earnings have risen faster than ECI in recent quarters.

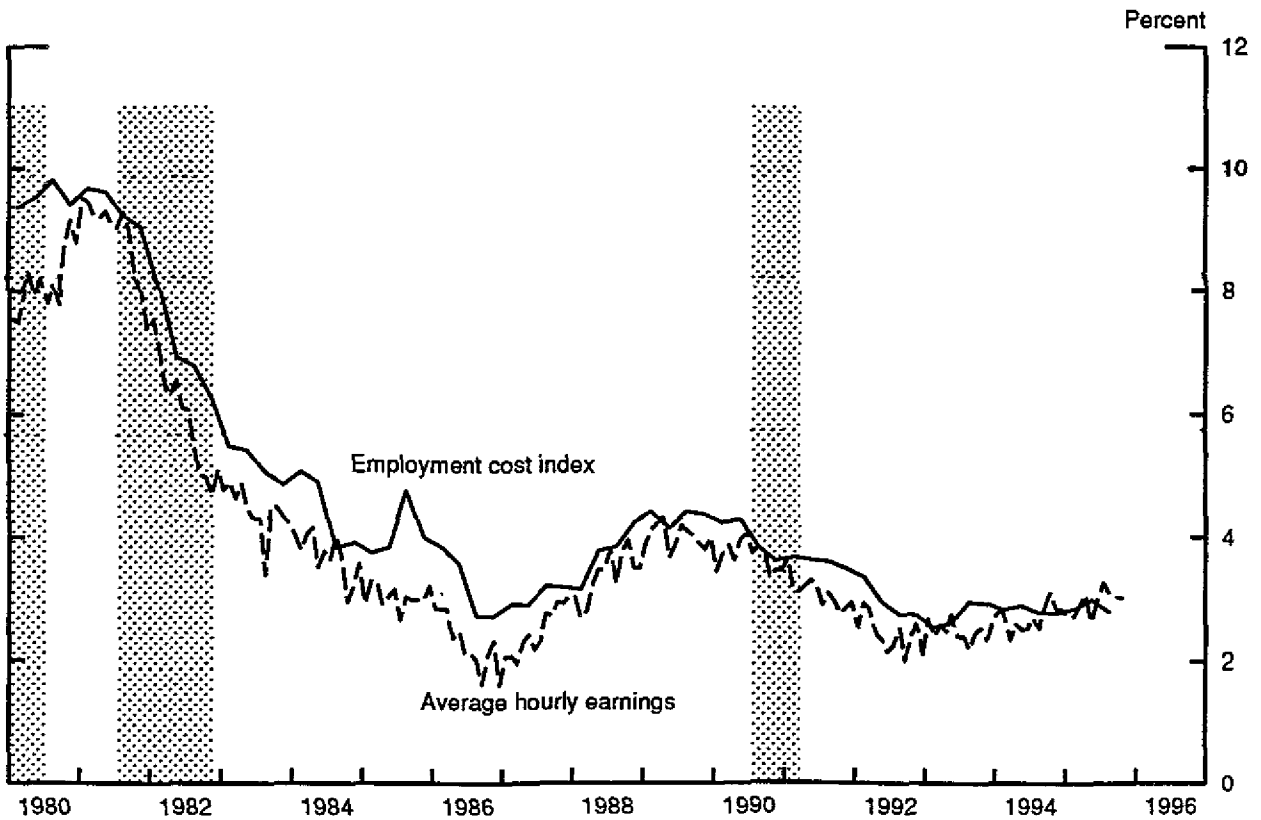
AVERAGE HOURLY EARNINGS
(Percentage change; based on seasonally adjusted data)[1]

	1993	1994	1995 Q1	1995 Q2	1995 Q3	1995 Aug.	1995 Sept.	1995 Oct.
			-Annual rate-			-Monthly rate-		
Total private nonfarm	2.6	2.8	2.5	3.2	3.5	-.2	.4	.5
Manufacturing	3.2	2.2	2.3	2.3	3.6	.1	.2	.2
Durable	3.4	2.0	1.9	.3	4.1	.2	.1	.0
Nondurable	2.5	2.3	2.8	3.9	3.5	.0	.1	.7
Contract construction	1.3	2.4	2.5	5.5	1.1	.0	.3	-.1
Transportation and public utilities	1.3	2.3	1.1	4.6	2.8	.0	.3	1.1
Finance, insurance, and real estate	5.5	3.4	5.1	4.7	4.3	-.5	.5	.7
Total trade	2.4	3.0	1.8	3.2	4.5	.1	.3	.4
Services	2.1	2.9	3.3	2.9	3.2	-.3	.6	.7

1. Annual and quarterly changes are measured from the final month of the preceding period to the final month of the period indicated.

Wages of Production or Nonsupervisory Workers

(Twelve-month change)



DOMESTIC FINANCIAL DEVELOPMENTS

Selected Financial Market Quotations[1]

(Percent except as noted)

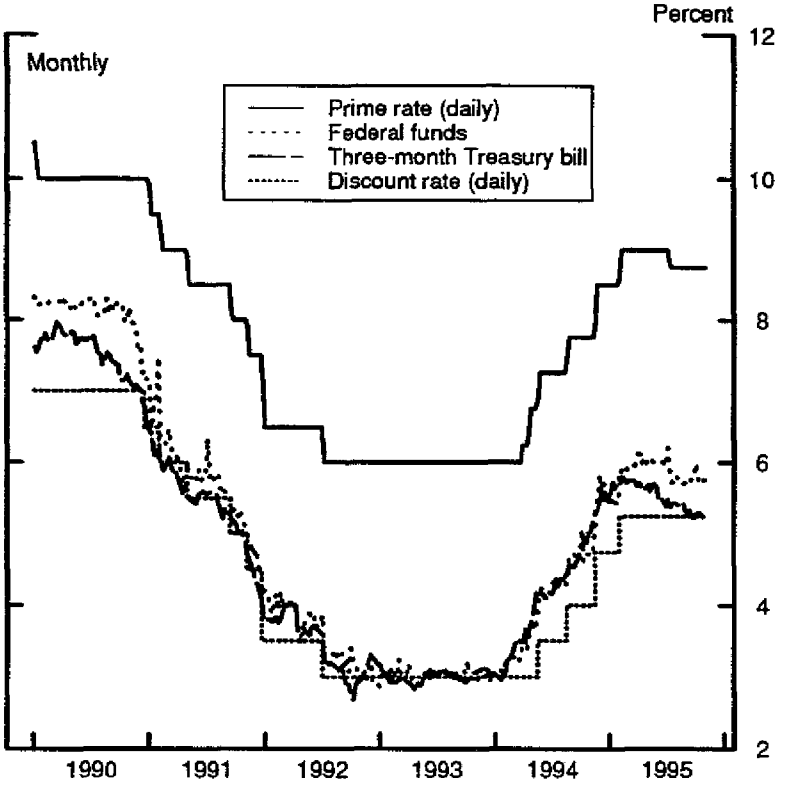
Instrument	1994 Feb. 3	1994 High	1995 FOMC, Sep.26	1995 Nov. 7	Change to Nov. 7,1995 from: 1994 Feb. 3	1994 high	FOMC, Sep. 26
Short-term Rates							
Federal Funds[2]	3.07	5.66	5.80	5.75	2.68	.09	-.05
Treasury Bills[3]							
3-month	3.13	5.78	5.29	5.37	2.24	-.41	.08
6-month	3.27	6.38	5.38	5.30	2.03	-1.08	-.08
1-year	3.52	6.84	5.39	5.19	1.67	-1.65	-.20
Commercial paper							
1-month	3.16	6.13	5.81	5.81	2.65	-.32	.00
3-month	3.25	6.32	5.73	5.75	2.50	-.57	.02
Large negotiable CDs[3]							
1-month	3.11	6.10	5.75	5.74	2.63	-.36	-.01
3-month	3.25	6.39	5.74	5.74	2.49	-.65	.00
6-month	3.41	6.89	5.74	5.66	2.25	-1.23	-.08
Eurodollar deposits[4]							
1-month	3.06	6.06	5.72	5.72	2.66	-.34	.00
3-month	3.25	6.38	5.72	5.75	2.50	-.63	.03
Bank Prime Rate	6.00	8.50	8.75	8.75	2.75	.25	.00
Intermediate- and Long-term Rates							
U.S. Treasury (constant maturity)							
3-year	4.60	7.82	5.98	5.65	1.05	-2.17	-.33
10-year	5.81	8.04	6.28	5.99	.18	-2.05	-.29
30-year	6.31	8.16	6.58	6.31	.00	-1.85	-.27
Municipal revenue (Bond Buyer)[5]	5.49	7.37	6.18	5.93	.44	-1.44	-.25
Corporate-A Utility, recently offered	7.35	9.05	7.57	7.33	-.02	-1.72	-.24
Home mortgages[6]							
FHLMC 30-yr fixed rate	6.97	9.25	7.57	7.44	.47	-1.81	-.13
FHLMC 1-yr adjustable rate	4.12	6.79	5.77	5.67	1.55	-1.12	-.10

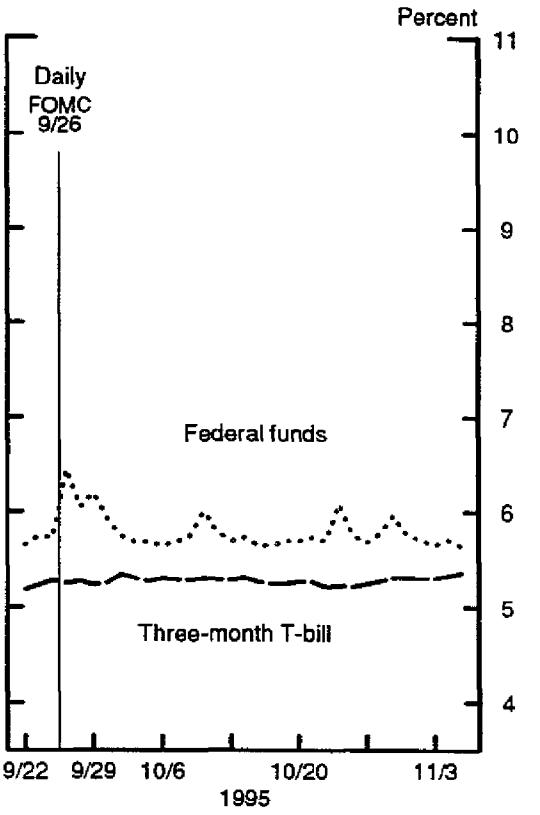
Stock Exchange Index	Record high Level	Record high Date	1989 Low, Jan. 3	1995 FOMC, Sep.26	1995 Nov. 7	Percentage change to Nov. 7 from: Record high	1989 low	FOMC, Sep. 26
Dow-Jones Industrial	4825.57	11/03/95	2144.64	4765.60	4797.03	-.59	123.68	.66
NYSE Composite	315.39	10/25/95	154.00	311.82	312.99	-.76	103.24	.38
NASDAQ (OTC)	1067.40	9/13/95	378.56	1038.05	1043.90	-2.20	175.76	.56
Wilshire	5843.27	9/21/95	2718.59	5774.95	5800.11	-.74	113.35	.44

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 November 8, 1995.
3. Secondary market.
4. Bid rates for Eurodollar deposits at 11 a.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.

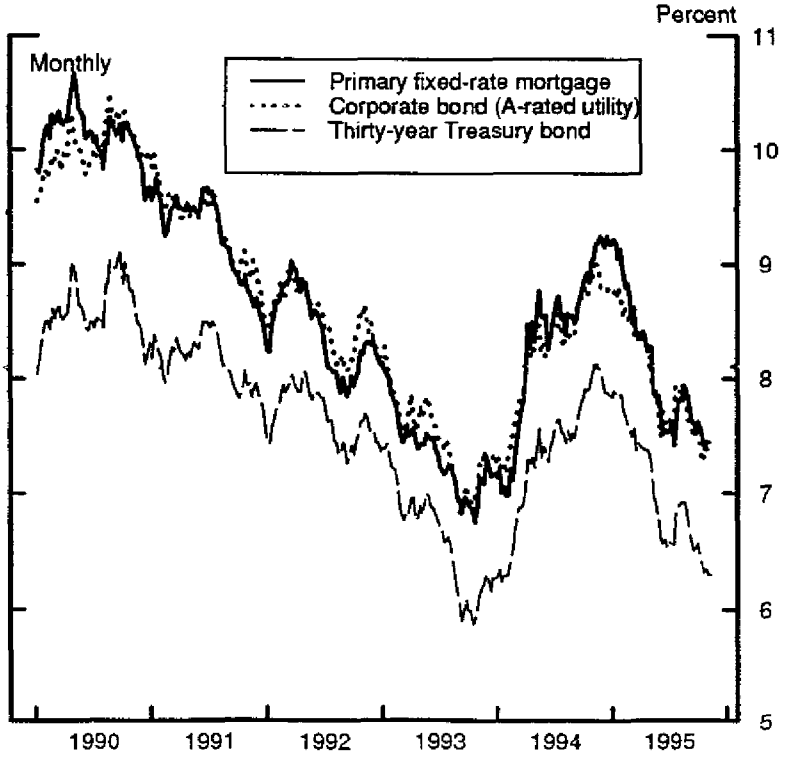
Selected Interest Rates

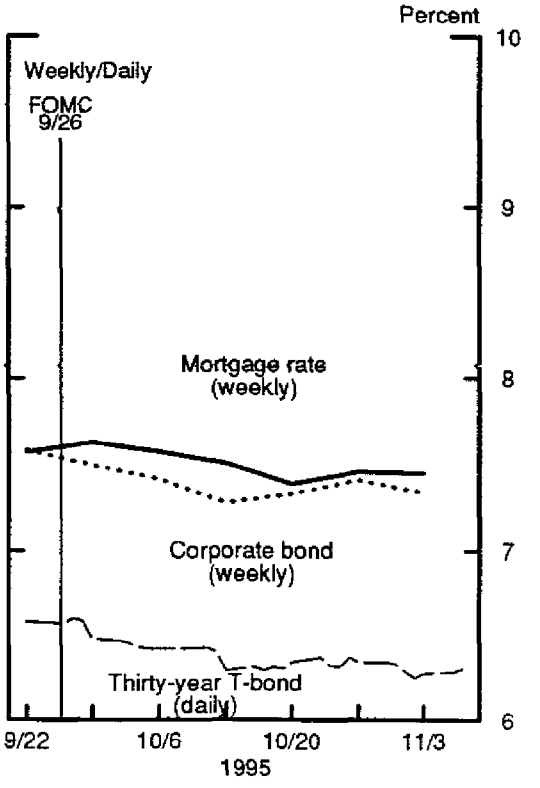
Short-Term





Long-Term





DOMESTIC FINANCIAL DEVELOPMENTS

The Treasury yield curve flattened over the intermeeting period as market participants drew encouragement from signs of subdued inflation and indications that, despite harsh words from both sides and threats of debt default, substantial deficit reduction still lies ahead. Even publication of a surprisingly high third-quarter GDP estimate and a firm October employment report failed to shake the general view that the economy is currently on a moderate growth path that would leave room for further Fed easing. That view has been strongly reinforced by comments of System officials.

Short-term rates are about unchanged to down slightly after accounting for year-end effects, while longer-term rates are down 25 to 35 basis points. The thirty-year Treasury yield touched 6-1/4 percent, a level last seen in January 1994, just prior to the onset of System tightening.

The decision to leave short-term rates unchanged at the September FOMC meeting was widely anticipated, and had little market impact. Quotes on federal funds futures and Eurodollar futures are consistent with an expectation of a 1/4 point easing in the coming months, with another quarter point indicated by next spring. Money market yields imply financing rates for the long weekend at year-end of about 6-1/4 to 7-1/2 percent, suggesting somewhat smaller premiums than in recent years, although year-end premiums are much larger for the troubled Japanese banking sector.

Private rates generally declined less than Treasury yields, resulting in a widening of some spreads, most notably on lower-rated instruments. Stock prices were quite volatile over the last six weeks, as investors nervously scanned third-quarter earnings reports for signs of a downturn in corporate profitability. In the event, third-quarter earnings reports more often than not came in on the

MONETARY AGGREGATES
(Based on seasonally adjusted data)

Aggregate or component	1994	1995 Q2	1995 Q3	1995 Aug.	1995 Sept	1995 Oct. (pe)	1994:Q4 to Oct. 95 (pe)	Level (bil. $) Sept 95
Aggregate	Percentage change (annual rate)[1]							
1. M1	2.4	-0.9	-0.9	-1.5	-3.7	-11	-1¾	1140.2
2. M2	1.1	4.4	7.7	8.3	4.7	0	4¼	3758.0
3. M3	1.4	7.1	8.8	7.6	4.4	4	6½	4535.6
Selected components								
4. Currency	10.2	8.2	1.2	3.6	2.6	5	5½	369.1
5. Demand deposits	0.5	-0.8	7.2	1.8	-0.9	-8	1¼	389.8
6. Other checkable deposits	-2.1	-9.9	-10.7	-9.8	-12.8	-28	-11	372.4
7. M2 minus M1	0.5	6.9	11.6	12.6	8.4	4	7¼	2617.7
8. Savings deposits	-4.5	-9.8	4.9	7.5	7.8	8	-4¼	1105.3
9. Small time deposits	2.5	24.6	7.2	3.4	2.8	3	16¼	929.0
10. Retail money market funds	7.3	18.1	43.3	37.7	17.6	10	23½	462.6
11. Overnight RPs, n.s.a.	14.5	-2.3	0.9	28.2	24.8	-15	5	88.8
12. Overnight Eurodollars, n.s.a.	42.2	-36.5	17.4	81.6	49.7	-11	5	32.7
13. M3 minus M2	3.5	20.7	13.8	4.7	2.5	24	18	777.6
14. Large time deposits, net[2]	7.0	15.5	14.1	6.4	8.1	41	17½	401.1
15. Institution-only money market mutual funds	-8.2	27.2	29.1	-9.0	15.4	13	21¼	213.5
16. Term RPs, n.s.a.	7.0	25.7	-10.7	23.9	-22.4	-2	12¼	115.4
17. Term Eurodollars, n.s.a.	14.4	37.2	8.5	-13.3	-23.0	-18	15	61.4
Memo								
18. Monetary base	8.4	6.2	1.0	3.4	0.8	4	4¼	431.2
19. Household M2[3]	0.5	5.3	8.1	8.0	4.7	2	4¾	3237.9
	Average monthly change (billions of dollars)[4]							
Memo								
Selected managed liabilities at commercial banks:								
20. Large time deposits, gross	2.1	5.3	6.4	8.9	5.7	10	. . .	425.2
21. Net due to related foreign institutions	7.5	-2.2	2.1	11.6	5.9	-2	. . .	253.9
22. U.S. government deposits at commercial banks	0.0	0.8	1.5	-15.4	0.9	-3	. . .	20.1

1. For the years shown, fourth quarter-to-fourth quarter percent change. For the quarters shown, based on quarterly averages.
2. Net of holdings of depository institutions, money market mutual funds, U.S. government, and foreign banks and official institutions.
3. Sum of seasonally adjusted currency, retail money funds, and other checkable, savings, and small time deposits.
4. For the years shown, "average monthly change" is the fourth quarter-to-fourth quarter dollar change, divided by 12. For the quarters shown, it is the quarter-to-quarter dollar change, divided by 3.
pe Preliminary estimate. n.s.a. Not seasonally adjusted.

high side of analysts' expectations. These reports, along with the declines in long-term interest rates, pushed several major stock indexes to new all-time highs during October, though, on net, most major indexes are up less than 1 percent over the intermeeting period.

M2 was about flat in October and M3 growth moderated some, while inflows to long-term mutual funds continued at their brisk third-quarter pace. Meanwhile, the downtrend in private sector debt growth appeared to continue. Household borrowing has slowed, with consumer installment credit growth coming in at 6-1/2 percent for September, and bank consumer lending figures hinting that the pace in October may have remained below that observed earlier in the year. Business credit appears to have expanded at about the same pace or perhaps a bit slower than in September, as reduced borrowing from banks and in the commercial paper market was offset at least in part by a rate-induced pickup in bond issuance. State and local government debt continued to contract, owing to heavy retirements alongside moderate gross issuance.

Absent an increase in the debt ceiling, the Treasury is projected to exhaust its borrowing authority and deplete its cash balances by November 15. Given the uncertainty, the Treasury has had to postpone its midquarter refunding auction. Even if a temporary increase in the ceiling were enacted, it may not come soon enough for the Treasury to be able to sell its midquarter refunding notes on schedule. In that event, the Treasury would have to make do with stop-gap sales of cash management bills.

Money and Bank Credit

M1 declined at an 11 percent annual rate in October (table), as programs that sweep funds out of other checkable deposits and into MMDAs spread to four additional bank holding companies. These sweep

programs, now used by fifteen bank holding companies, pulled down M1 growth by about 7 percentage points in October, and have shaved about 3 percentage points from its growth, on average, since the fourth quarter of 1994. M2, which is unaffected by OCD sweeps, was flat in October, as the growth of M2 components outside of M1 also slowed significantly after their third-quarter burst. Notably, growth in retail money market mutual funds fell to a 10 percent rate from a 17-1/2 percent pace in September and a torrid 23-1/2 percent average rate of increase over the year to date.

M3 growth eased to about a 4 percent annual rate, leaving that aggregate just above its growth cone. The slowing in its M2 component was offset partly by continued rapid growth of institution-only money funds. In addition, large time deposits surged as domestic and foreign banks apparently shifted to domestic funding sources, while net balances due to foreign offices declined.

Growth of M3 was likely held down by a sharp deceleration in bank credit in October (table). The slowdown was broad-based, reflecting sluggish growth in loans and a decline in security holdings. Business loans outstanding were flat in October. While the slackening in overall business lending may be signaling a less rapid pace of inventory accumulation, it was presumably in part a reflection of competition from the capital markets. Issuance of bonds and stocks was brisk last month; moreover, the slowdown in loans was concentrated at large banks as well as at branches and agencies of foreign banks, the lenders that compete most directly with capital markets. In support of this view, respondents to the Senior Loan Officer Opinion Survey in November reported an easing of their business loan terms, on balance, as well as a slight increase in their willingness to lend. The data do not point to significant relative weakness of business loans at Japanese branches, though

Commecial Bank Credit

(Percentage change; seasonally adjusted annual rate)[1]

Type of credit	1994	1995 Q2	1995 Q3	1995 Aug	1995 Sep	1995 Oct p	Level, Oct 1995 p (billions of $)
	Commercial bank credit						
1. Total loans and securities	6.8	13.3	6.2	5.2	7.1	.3	3,552.7
2. Securities	5.2	15.4	-2.5	8.8	6.9	-.5	976.4
3. U.S. government	1.2	-5.7	-2.5	7.5	-4.6	8.5	712.1
4. Other[2]	21.0	85.1	-2.7	12.5	38.1	-24.0	264.3
5. Loans[3]	7.5	12.4	9.5	3.8	7.2	.6	2,576.3
6. Business	8.9	12.5	7.0	2.2	6.7	.2	702.3
7. Real Estate	6.5	8.4	9.0	6.0	4.3	2.9	1,074.3
8. *Home equity*	2.2	6.3	6.7	6.2	6.1	1.5	78.9
9. Other	6.8	8.5	9.2	5.9	4.2	2.9	995.3
10. Consumer	15.1	11.7	9.7	13.0	7.2	-.2	489.2
11. Adjusted[4]	15.3	14.9	14.4	12.8	12.1	8.5	596.5
12. Security	-12.6	69.8	3.7	-63.2	35.5	-51.0	83.4
13. Other[5]	2.4	13.9	22.2	4.9	12.4	13.4	227.2

1. Monthly levels are *pro rata* averages of Wednesday data. Quarterly and annual levels (not shown) are simple averages of monthly levels and levels for the fourth quarter, respectively. Growth rates shown are percentage changes in consecutive levels, annualized but not compounded.
2. Includes municipal securities, foreign government securities, corporate bonds, equities, and trading account assets.
3. Excludes interbank loans.
4. Includes estimates of consumer loans that have been securitized by banks and are still outstanding.
5. Includes loans to nonbank financial institutions, farmers, state and local governments, banks abroad, foreign governments, and all others not elsewhere classified. Also includes lease financing receivables.

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

Type of security	1993	1994	Q2	Q3[p]	Aug.[p]	Sept.[p]	Oct.[p]
All U.S. corporations	52.90	40.57	47.64	45.84	47.42	56.44	49.99
Stocks[2]	9.12	5.46	6.28	6.13	6.35	7.44	8.49
Bonds	43.78	35.11	41.36	39.71	41.07	49.00	41.50
Nonfinancial corporations							
Stocks[2]	5.04	3.12	4.41	4.36	4.07	5.54	6.70
Sold in U.S.	4.64	2.90	4.05	4.09	3.82	5.06	5.93
Utility	1.05	.37	.23	.23	.17	.32	.10
Industrial	3.82	2.55	3.82	3.86	3.65	4.74	5.83
Sold abroad	.40	.22	.37	.27	.25	.47	.78
Bonds	16.19	7.35	11.85	8.79	8.31	10.49	11.70
Sold in U.S.	15.55	6.44	10.76	7.31	6.11	9.20	10.20
Utility	7.34	2.19	3.74	2.93	1.77	5.00	4.70
Industrial	8.21	4.26	7.02	4.38	4.34	4.20	5.50
Sold abroad	.64	.90	1.10	1.48	2.19	1.29	1.50
By quality[3]							
Aaa and Aa	2.56	.58	1.55	.70	.79	1.25	1.84
A and Baa	8.70	3.82	6.94	4.39	3.12	4.47	5.84
Less than Baa	4.17	2.01	2.27	2.12	2.18	3.34	2.43
Unrated or rating unknown	.09	.01	.00	.10	.02	.15	.09
Financial corporations							
Stocks[2]	4.08	2.36	1.87	1.76	2.28	1.90	1.79
Sold in U.S.	3.83	2.11	1.87	1.73	2.28	1.80	1.71
Sold abroad	.25	.25	.00	.03	.00	.10	.08
Bonds	27.60	27.77	29.51	30.93	32.76	38.51	29.80
Sold in U.S.	25.04	23.98	24.31	25.52	26.24	33.80	24.80
Sold abroad	2.56	3.78	5.19	5.41	6.53	4.71	5.00
By quality[3]							
Aaa and Aa	1.78	3.72	3.91	4.37	4.66	6.00	2.28
A and Baa	9.02	9.02	10.45	8.55	9.92	10.10	11.28
Less than Baa	.49	.31	.17	.12	.09	.15	.10
Unrated or rating unknown	.08	.10	.30	.18	.17	.25	.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.

reports suggest that the rising cost of funds for these institutions is discouraging some lending by them.

Consumer loans outstanding on bank balance sheets fell slightly in October. Even after adjusting for securitizations, consumer loans grew at "only" a 8-1/2 percent pace, less than two-thirds the pace posted in the last few quarters. The Senior Loan Officer Opinion Survey suggests that, on balance, banks have not reduced their willingness to lend to consumers in recent months, and that demand by households has not slackened.

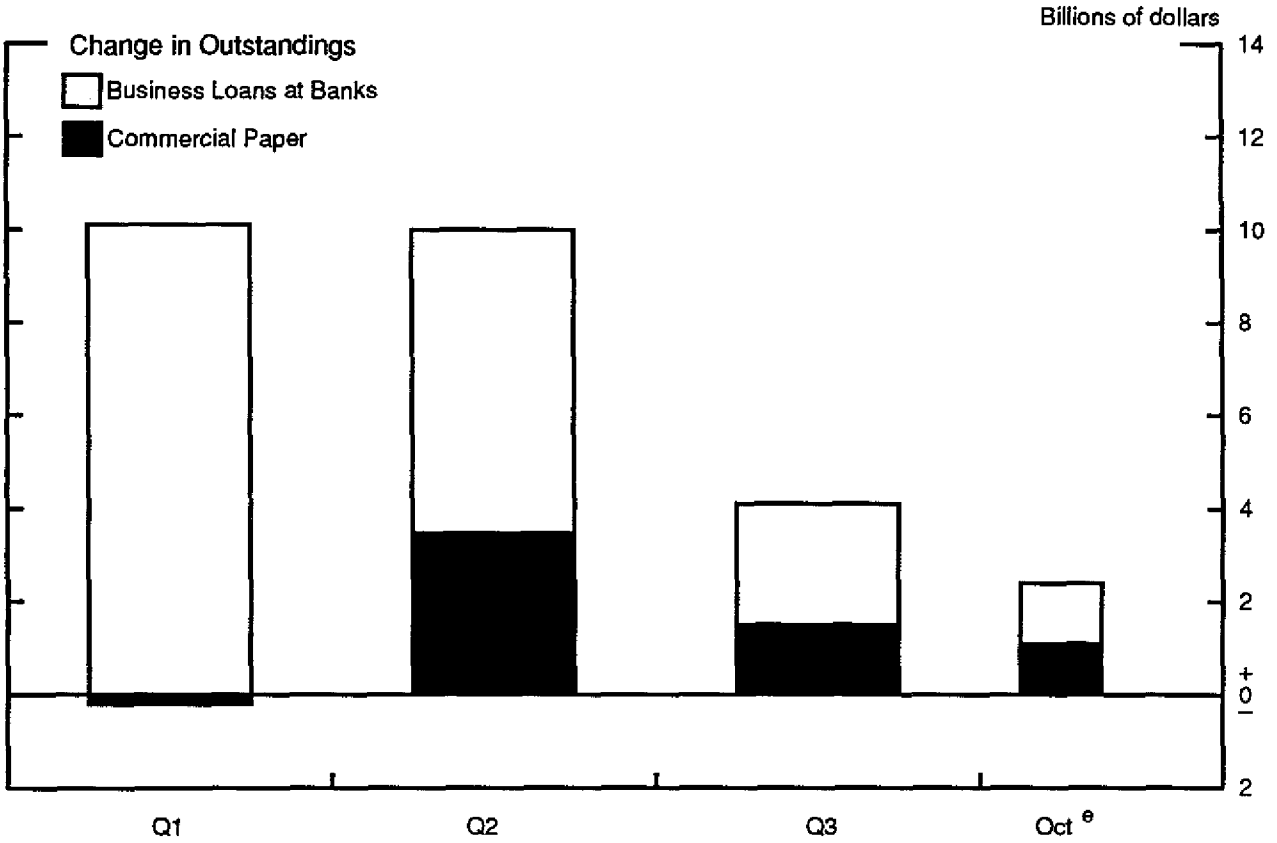
Preliminary data indicate that banks remained highly profitable in the third quarter. Profits were boosted by a $1-1/2 billion refund of deposit insurance premiums resulting from the reduction in deposit premium rates put in place in August, but effective retroactively to June. Respondents to the August Senior Loan Officer Opinion Survey indicated that most of the premium reduction would likely flow through to the bottom line rather than being passed through as higher deposit rates or lower loan rates. In addition to the refund, third-quarter earnings benefited from continued rapid growth in loans, which allowed banks to preserve their net interest margins by increasing the loan share of assets.

Bank stock prices outperformed the market by a significant margin over the third quarter, perhaps sparked by the rapid pace of merger activity in the industry. In mid-October, however, bank stock prices--and those of other lending institutions--retraced some of those gains, as investors reportedly began to focus on incipient signs of deterioration in the quality of consumer loan portfolios cropping up in some lenders' financial reports.

Business Finance

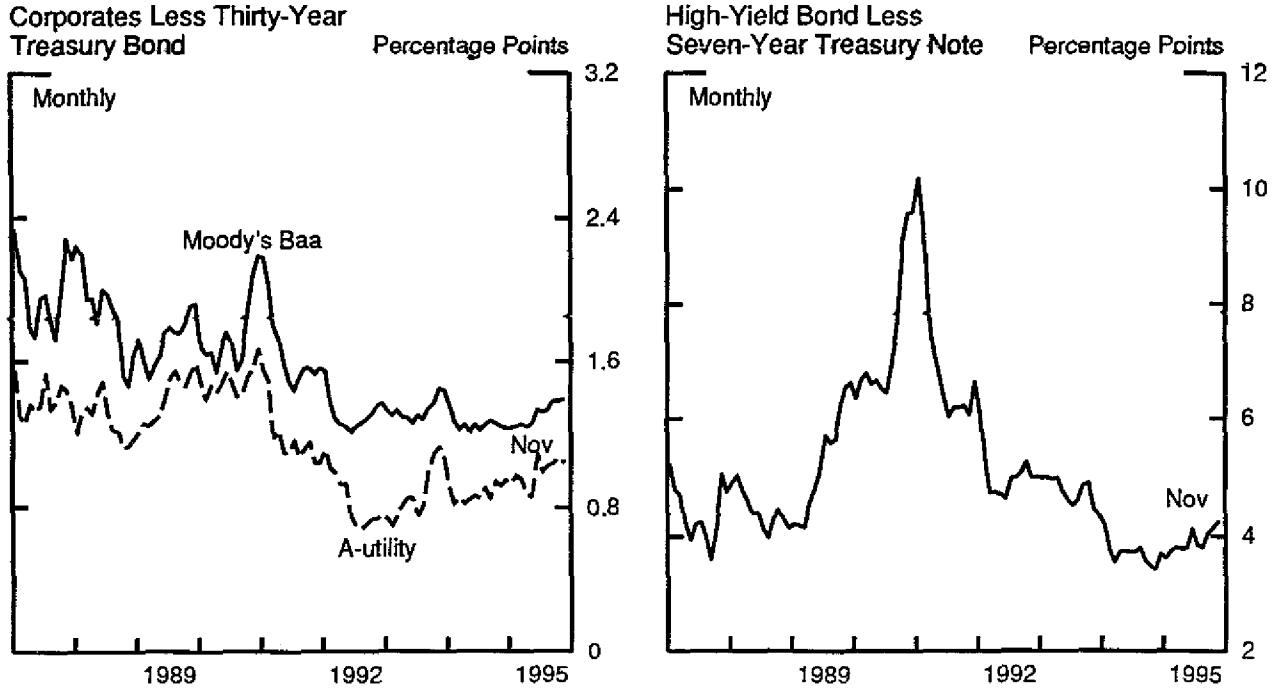
Gross public bond offerings by nonfinancial corporations were more than $10 billion in September, the highest volume since June

Business Loans at Banks and Commercial Paper of Nonfinancial Firms



Note: Monthly data are month-end to month-end changes in outstandings. Quarterly data are quarter-end to quarter-end changes at monthly rates.
e - estimate

Yield Spreads

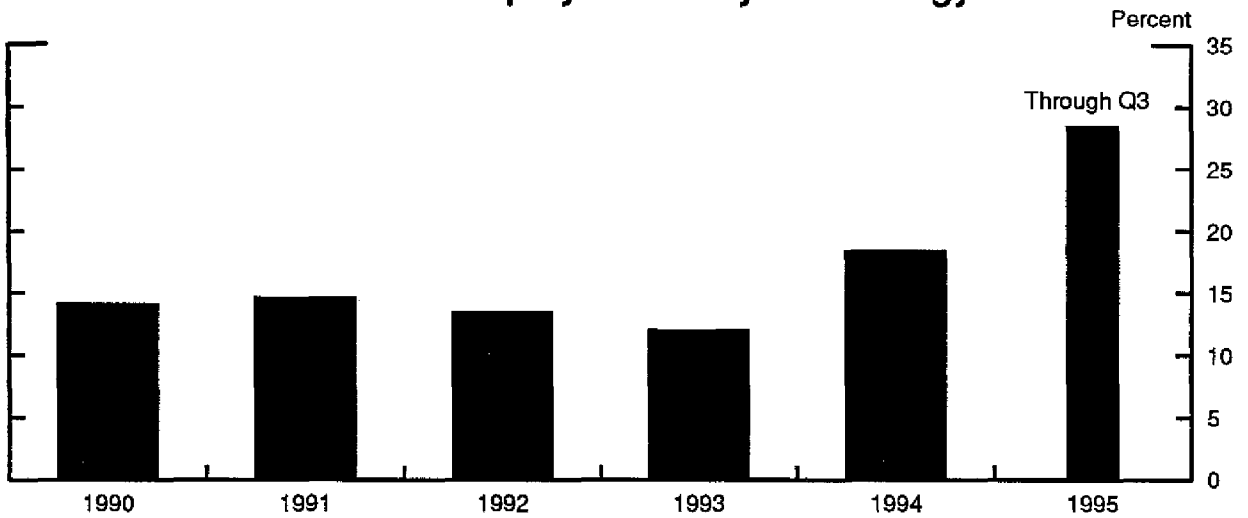


(table), and October issuance strengthened further with the decline in long-term rates. Public offerings of junk bonds jumped to $3.4 billion in September, the highest monthly total this year, and remained strong in October. The weak growth of bank loans and commercial paper (chart)--as well as comments from market participants--suggests that some corporations have used bond proceeds to pay down commercial paper and bank loans. On balance, it appears that business borrowing has remained moderate.

Spreads on investment-grade bonds have widened several basis points of late, reflecting a more cautious tone in the market (chart, lower panel). Junk bond spreads have widened substantially more, about 15 to 35 basis points over the intermeeting period, resulting in year-to-date increases of as much as 100 basis points, perhaps in part the result of supply pressures. The pace of junk bond defaults this year, at 2.4 percent of outstanding debt, represents an increase over the experience of the last couple of years, though it remains below its average in the late 1980s. In the past few months, defaults appear to have been disproportionately concentrated in the retail sector, which has experienced a spate of bankruptcies this year. Retailers--specialty and discount stores in particular--have suffered from stiff price competition and relatively mild growth in retail sales.

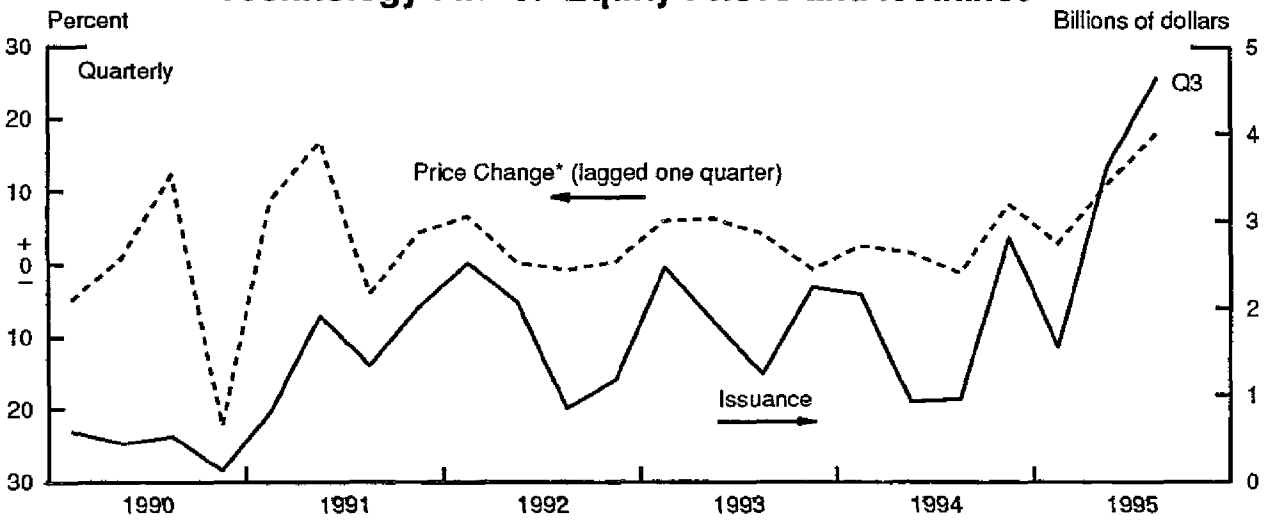
The volume of nonfinancial commercial paper outstanding increased moderately in September and October. As in earlier months, considerable gross issuance was partially offset by paydowns of merger-related paper. AT&T was a heavy issuer in September, to finance its acquisition of LIN Broadcasting and, reportedly, to boost the interest-sensitivity of its debt used to finance its variable-rate credit card receivables. Reflecting funding pressures faced by lower-quality borrowers at the end of the quarter, the

Share of Nonfinancial Equity Issued by Technology Firms*



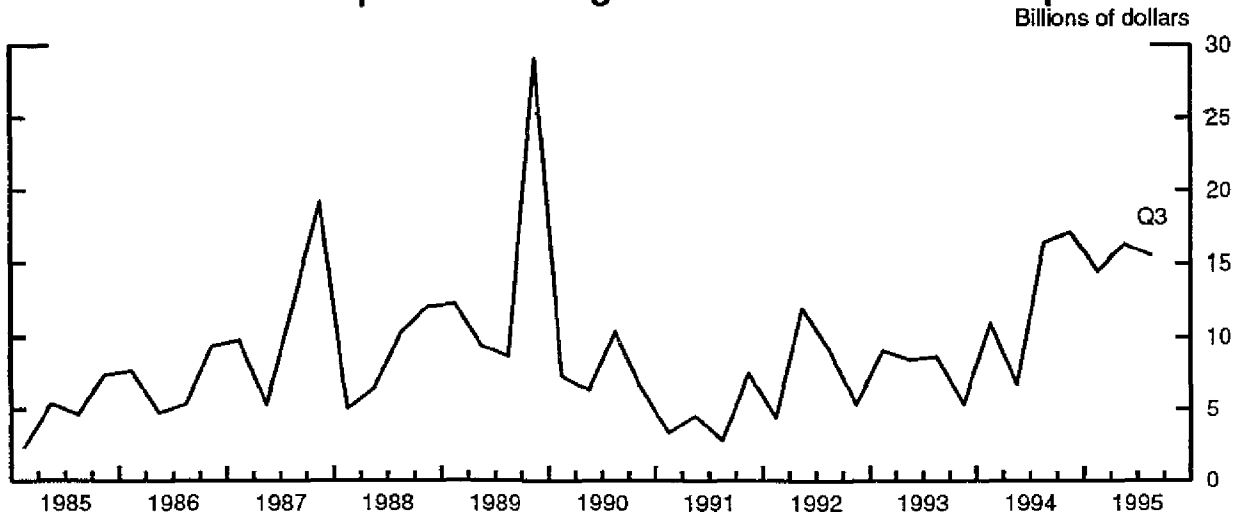
* Technology firms include producers of computer equipment, computer software, communications equipment, electronic components, drugs, and medical equipment.

Technology Firms: Equity Prices and Issuance



* Price changes are measured by end-of-quarter changes in the Dow Jones technology index.

Announced Stock Repurchase Programs at Nonfinancial Corporations



Source: Securities Data Company.

thirty-day A2/P2 quality spread rose sharply in late September and then fell in October.

Gross public equity issuance by nonfinancial corporations in September and October reached the highest level in nearly two years. In addition, there remain a large number of issues in registration. As has been the case all year, technology issues have accounted for an unusually large share of total issuance (chart, top panel), fueled by the strong first-half performance of technology stocks (middle panel). Issuance tends to lag share price increases by about a quarter as a result of delays between the filing of the registration statement and the completion of the offering. In addition to computer-related stocks, new issues of medical-related companies were well-received in the third quarter after encountering several years of lackluster investor demand.

Nonfinancial firms issuing stock this year have been mostly companies that have no public debt outstanding or that are rated as speculative grade. Through October, outside of utilities, only seven investment-grade nonfinancial companies tapped the stock market for capital this year, accounting for just $2.3 billion, or 6 percent, of gross equity issuance. In the current environment, with strong earnings and ample liquidity, investment-grade firms are more likely to repurchase stock than to issue new shares. Announced repurchase programs in the third quarter exceeded $15 billion for the fifth consecutive quarter (chart, lower panel).

The strong pace of merger and acquisition activity by nonfinancial corporations has also resulted in significant share retirements, despite a heavy reliance on stock swaps. Megamergers--those mergers in which the target company is valued at more than $1 billion--resulted in $15 billion of equity retirements in the third quarter, up from a $9 billion pace in the first two quarters.

Smaller mergers resulted in additional retirements of $10.5 billion in the third quarter. In the current quarter to date, retirements from completed megamergers have already reached $12 billion, and a large volume of projected retirements from announced but-not-yet-completed deals remains. With some of these deals expected to close by year-end, and with the high level of share repurchases expected to continue, net equity issuance should remain decidedly negative in the current quarter.

The credit quality of nonfinancial companies, as measured by Moody's, improved in the third quarter, with the value of debt upgraded exceeding the value of debt downgraded by $18 billion. Much of the increase was due to the upgrading of $14 billion of IBM debt, reflecting the success of the company's cost-cutting efforts. Among financial companies, the most notable rating change involved the upgrade on $30 billion of Citicorp debt.

To date, third-quarter earnings have exceeded analysts' expectations by about 3 percent on a weighted-average basis. Positive surprises have outnumbered negative surprises by nearly two to one, with financial companies and utilities having an especially strong quarter relative to analyst predictions. Earnings at utilities were fueled by the hot summer weather, and at commercial banks, as noted, by the decline in deposit insurance premiums. Excluding financial companies and utilities, positive surprises also outnumbered negative surprises, though by a smaller margin. Early in October, disappointing third-quarter earnings announcements by Motorola, Novell, and some other technology companies triggered declines in technology share prices and led analysts to lower fourth-quarter earnings estimates. In retrospect, it appears that companies with the weakest third-quarter earnings released their

earnings early or gave advance warning in an effort to soften the market's reaction.

Though quite volatile over the period, most major market indexes are now only slightly above their level at the last FOMC, and share prices of computer and software firms are up 3 to 5 percent. Also leading the market have been housing-related shares; in contrast, stocks in most other cyclically sensitive sectors have suffered declines.

Municipal Securities

Gross offerings of long-term municipal securities were sluggish in September but bounced up in October, owing primarily to a handful of large issues and a notable increase in refunding bonds (table). Through the end of October, gross offerings have run about 16 percent below the rate for the same period last year. The decline mainly reflects a drop in refunding activity, although issuance to fund new capital projects also was somewhat below last year's pace. Retirements of refunded and maturing bonds have

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

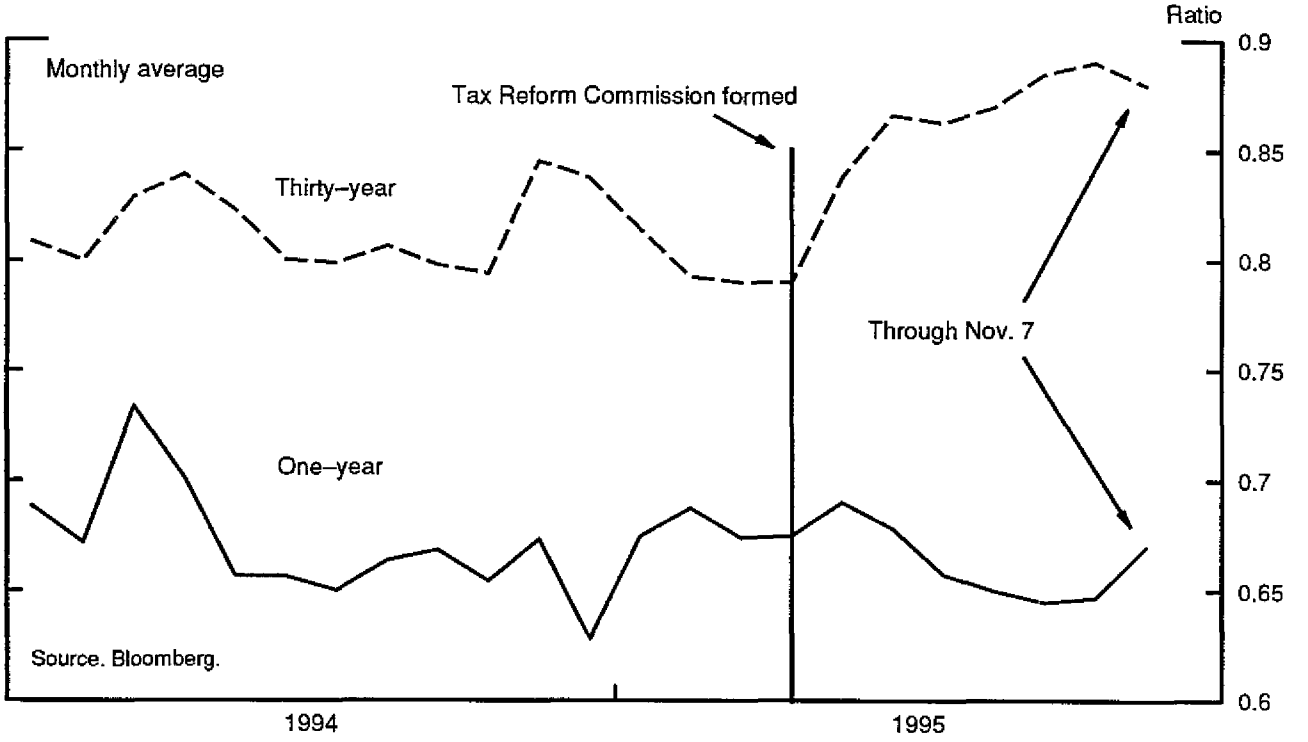
			1995				
	1993	1994	Q1	Q2	Q3	Sept.	Oct.[p]
Total tax-exempt	27.2	16.1	10.9	16.4	14.5	12.7	15.0
Long-term	23.3	12.8	9.0	12.8	10.7	9.7	13.0
Refundings[1]	15.7	4.0	1.7	3.2	3.2	2.9	5.1
New capital	7.6	8.8	7.3	9.6	7.5	6.8	7.9
Short-term	3.9	3.3	1.9	3.6	3.8	3.0	2.0
Total taxable	.7	.7	.4	.7	.6	.7	.9

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

Municipal Markets

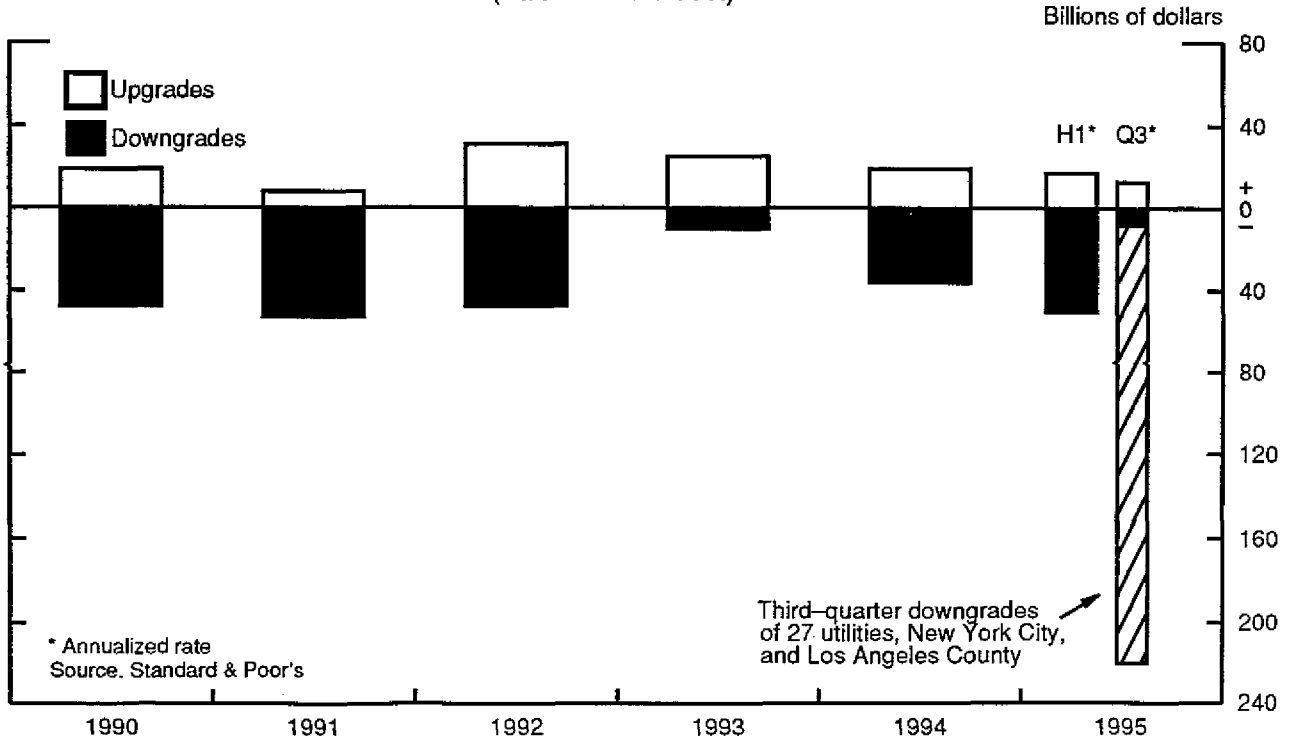
Ratio of Tax–Exempt to Taxable Yields at Two Maturities

(AAA–rated general obligation municipal debt relative to constant–maturity Treasury yields)



Long–Term Municipal Debt Rating Changes

(Value of rated debt)



continued to be heavy during the intermeeting period, and net issuance was negative in both September and October. Indeed, the stock of outstanding long-term tax-exempt bonds is expected to decline about $65 billion in 1995 as a result of heavy retirements and the low gross volume of new bonds.

Ratios of tax-exempt to taxable yields changed little over the intermeeting period (chart). For one-year securities, the ratio of AAA tax-exempt to Treasuries hovered near its average of the past few years, while the ratio for thirty-year AAA debt remained quite elevated at about 0.88. The high ratio for longer maturity debt owes largely to continuing discussion of tax reform proposals that would reduce or eliminate the tax advantage of income from municipal bonds. However, because any major change of the tax system is unlikely to take effect for a while, short-term municipal yields have not moved up.

Standard and Poor's downgraded almost $55 billion of municipal debt during the third quarter and upgraded only $3 billion (chart). However, almost $23 billion of the downgraded debt was confined to municipal utility companies, which have faced sharply increased competition in some regions as a result of recent measures to deregulate the electric power industry. S&P downgraded more than $25 billion of New York City's general obligation debt because of chronic budget problems and continued high debt levels. S&P also downgraded more than $5 billion of Los Angeles County debt in response to the county's large deficit for fiscal year 1996. The downgrades of New York City and Los Angeles County were widely anticipated by market participants and had little effect on their funding costs. In fact, both issuers raised significant amounts with little apparent trouble subsequent to the ratings actions.

TREASURY FINANCING
(Billions of dollars; total for period)

Item	1995 Q3	Q4[p]	Oct.[e]	Nov.[p]	Dec.[p]
Total surplus/deficit (-)	-40.1	-66.1	-32.3	-37.7	3.9
Means of financing deficit					
Net cash borrowing and repayments (-)	20.1	53.1	9.8	51.9	-8.6
Nonmarketable	-5.7	-5.9	-2.0	-1.7	-2.3
Marketable	25.8	59.1	11.8	53.6	-6.3
Bills	-5.9	30.1	-7.1	43.5	-6.3
Coupons	31.7	29.0	18.9	10.1	.0
Decrease in the cash balance	22.6	12.2	16.8	-1.3	-3.2
Other[1]	-2.5	.7	5.7	-12.8	7.9
Memo:					
Cash balance, end of period	37.9	25.7	21.2	22.5	25.7

Note. Data reported on a payment basis. Details may not sum to totals because of rounding.
p Projection.
e Estimate.
1. Accrued items, checks issued less checks paid, and other transactions.

NET CASH BORROWING OF GOVERNMENT-SPONSORED ENTERPRISES
(Billions of dollars)

Agency	Q2	1995 Q3	July	Aug.	Sept.
FHLBs	12.9	13.8	.0	5.2	8.6
FHLMC	6.8	3.1	2.9	.9	-.7
FNMA	12.3	6.3	-2.5	6.8	1.9
Farm Credit Banks	.0	1.9	.7	.3	.8
SLMA	-.3	.4	.1	.0	.3

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

Excluding the utilities, New York City, and Los Angeles County, only $2.5 billion of debt was downgraded.

As part of its strategy to remain below the current federal debt ceiling, the Treasury Department stopped taking orders for the sale of the state and local government series (SLGS) on October 18. These nonmarketable Treasury securities are used mainly as investments for the escrowed proceeds of advance refunding issues. Although they yield slightly less than marketable Treasuries, they can be tailored to match issuers' exact maturity and interest rate needs and thereby ease compliance with the "no arbitrage" restrictions on such issues.[1] Temporary suspension of sales of SLGS will probably have only a limited effect on refunding issuance because recent overall demand for SLGS has been fairly low. Refunding activity has been relatively light this year; moreover, many recent issuers reportedly have purchased open-market Treasuries rather than SLGS.

Treasury Financing

The debt subject to statutory limit is estimated to have been $4,896.5 billion by the end of October, $3.5 billion shy of the debt ceiling. On October 17, facing the prospect of exceeding its statutory borrowing authority by the end of October, the Treasury announced a sharp cutback in the size of that week's three-month bill auction. To avoid worsening the shortage of that bill, the Federal Reserve rolled over only $5.4 billion of the $6.3 billion of the System's maturing Treasury holdings at that week bill's auction. Nevertheless, this supply shortage was reflected in the price of the three-month bill, with its yield about 5 to 10 basis points below the smoothed bill yield curve for about a week. This supply effect

1. These restrictions require issuers to rebate to the Treasury any earnings on escrowed investments above what it is paying on the new, refunding bond.

has since disappeared, in part as it became clear to market participants that this bill would be reopened as a cash management bill.

In addition to suspending the sale of special issues to state and local governments, the Treasury halted the practice of issuing foreign add-ons at bill and note auctions, and has already called in the $2.3 billion of deposits held at depository institutions as compensating balances. The cut in bills permitted the Treasury to announce normal sizes and a timely settlement of end-of-October two- and five-year notes, as well as of two cash management bills totaling $14 billion, which were issued on November 3 when seasonal redemptions of nonmarketable debt held by government trust funds occurred. On November 6, the Treasury announced that it had to postpone the regular midquarter refunding auctions, stated to be held on November 7 and November 8, because Congress had not completed action on legislation to temporarily increase the statutory debt limit. The postponed auctions included $18 billion of three-year notes and $13.5 billion of ten-year notes. If a debt ceiling extension occurs any later than November 8 or November 9, then the settlement of the midquarter refunding would most likely have to be postponed. In this case, the Treasury is likely to raise new money by issuing a very short-term cash management bill structured so that it expires the same day the rescheduled midquarter refunding is to settle.

Absent an increase in the debt ceiling, the Treasury probably would deplete its cash balances and run out of borrowing authority by November 15 if it does not resort to gimmicks used in previous debt ceiling crises, such as underinvestment of trust funds to meet current outlays from such funds and replace them temporarily with

the issuance of special obligations that do not count as statutory debt under the borrowing constraints.

The staff forecast for Treasury financing in the fourth quarter assumes that there will be a permanent resolution to the debt-ceiling problem, without a default, by mid-December. In that forecast, the federal government is expected to finance the projected $66 billion fourth-quarter fiscal deficit partly by borrowing $53 billion from the public and by drawing down its cash balance by $12 billion. With no long-term bond scheduled for the upcoming midquarter refunding, the Treasury will rely on bills for half of the funds raised this quarter. It is also expected that the Treasury will auction four cash management bills, raising $28 billion, to help bridge upcoming seasonal financial needs.

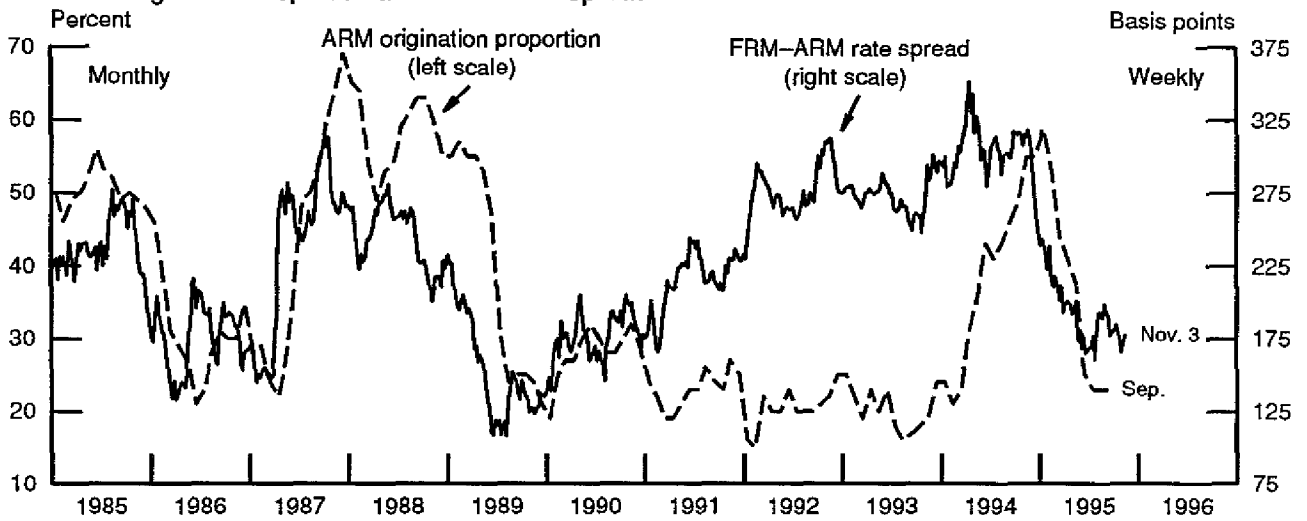
Agency Financing

Net borrowing by government-sponsored enterprises contracted slightly in the third quarter, and average spreads on GSE debt in the secondary market have widened slightly over the intermeeting period. Although the agencies continue to issue new debt, much of it is to fund outstanding debt being called to lower financing costs. About 85 percent of the new agency debt is callable. Borrowing by GSEs in the global bond market slowed considerably in September, after an active summer.

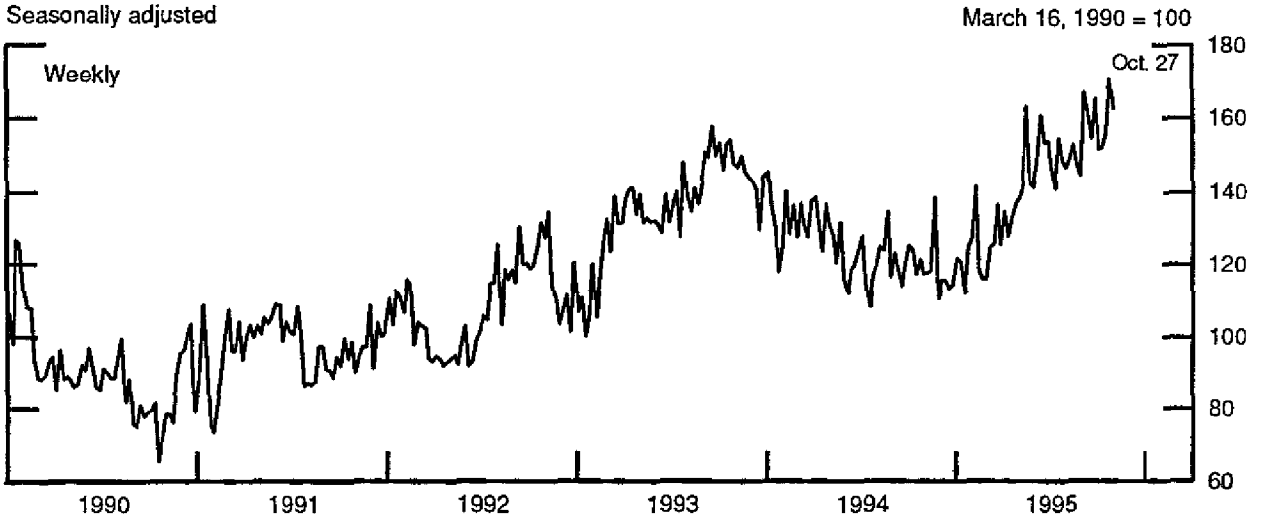
The Tennessee Valley Authority (TVA) has recently undertaken several steps to improve its financial condition, in part a response to a critical report issued by the Government Accounting Office (GAO). In 1994, the TVA's debt servicing costs ($1.9 billion) amounted to 35 percent of its revenues, or about double the debt service burden at neighboring utilities. Moreover, its nonproducing assets--largely nuclear power plants not in operation--have been treated as deferred assets so that the associated costs have not

Mortgage Market Indicators

ARM Origination Proportion and FRM–ARM Spread

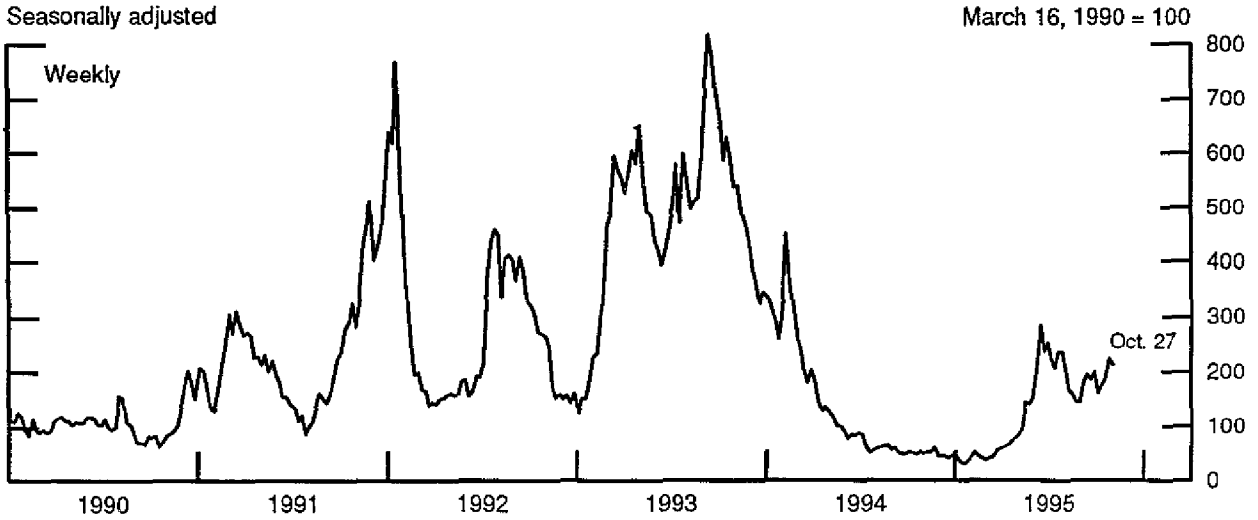


MBA Purchase Application Index



Note: Seasonally adjusted by Federal Reserve Board staff.

MBA Refinancing Application Index



Note: Seasonally adjusted by Federal Reserve Board staff.

been included in operating costs nor reflected in the TVA's electricity rates. The GAO views the high debt servicing costs and the large size of deferred assets as key factors that will put the TVA at a competitive disadvantage.

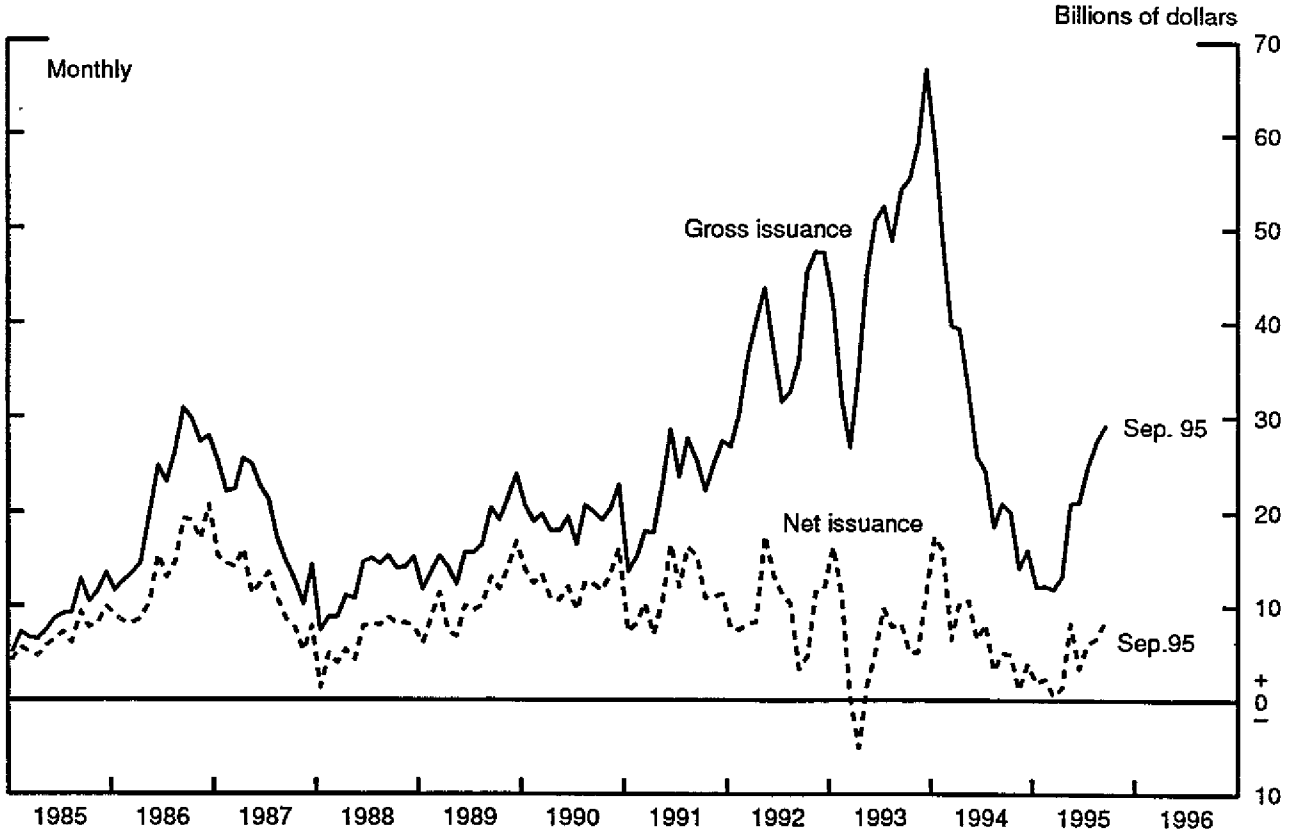
Of late, the TVA has substantially reduced the number of employees and has also refinanced some debt at a lower costs. However, there are few remaining areas for the TVA to reduce its costs. While the TVA is not currently facing any cash-flow problems, the GAO expects that, if the TVA's capital expenditures continue to exceed its net cash from operations to the tune of $1 billion annually, as occurred in 1994, the federal government "may be at risk for some portion of TVA's $26 billion debt."

Mortgage Markets

The commitment rate on thirty-year fixed-rate mortgages dropped to 7.38 percent in late October, its lowest level in eighteen months, before retracing slightly. On balance, last week it was down about 13 basis points from the reading in the week of the September FOMC meeting. The average initial rate on ARMs indexed to the one-year Treasury constant maturity yield has declined about 10 basis points on balance over the period, and the initial rate spread between FRMs and ARMs is just above its four-year low reached this past July (chart). Surveys of mortgage applications conducted by both the Mortgage Bankers Association and J.P. Morgan show slight increases recently in FRM applications as a share of total home loan applications.

In absolute terms, mortgage application volumes are at historically high levels. The MBA's home purchase index reached a record high in the week ended October 20, coinciding with the drop in mortgage commitment rates. In contrast, both the MBA and J.P. Morgan surveys report that the volume of refinancing applications

Issuance of Agency Mortgage Pass–Through Securities
(Not seasonally adjusted)



remains significantly below the recent peak reached in mid-July. Moreover, recent agency prepayment data show declines in prepayment rates for the month of September, suggesting that the surge in refinancings witnessed over the past six months will taper off unless spurred on by a further sizable drop in mortgage contract rates.

In the secondary market, the large FRM share of mortgage originations continues to be reflected in increased production of mortgage-backed securities. Although gross issuance of agency-backed pass-through securities has moved up steadily from the market

bottom in January, totaling $29.1 billion in September (chart), it is still substantially below the rate of issuance in 1993.

Despite the increased volume of pass-throughs, the agency CMO/REMIC market has remained mired at low issuance levels in recent months, with little sign of a near-term rebound. For the first nine months of 1995, issuance totaled only $20 billion, compared with $113 billion for the first nine months of 1994 and $324 billion for all of 1993. The continued lull in issuance of CMOs/REMICs appears to be the result of sparse investor demand, a consequence of many investors' painful experiences in the derivatives markets in the past couple years. The void created by the dropoff in CMO/REMIC production appears to have been filled, in part, by asset-backed securities (ABS), which are experiencing record issuance levels this year.

Consumer Credit

Growth of outstanding consumer installment credit slowed to a 6-1/2 percent seasonally adjusted annual rate in September, following an upward-revised 12-3/4 percent gain in August. For the third quarter as a whole, growth of consumer installment credit slowed to a 10 percent annual rate from the 15 percent pace of the first half. Revolving credit growth in September slipped to a single-digit pace for the first time since last December, while auto credit grew at a pace only slightly below that of August. Total consumer credit (installment plus noninstallment) also moderated a couple percentage points to a 9 percent growth rate in September.

Various reports over the intermeeting period suggest that credit performance of consumer loans likely has eroded further in recent months, albeit from fairly low delinquency levels. Indeed, most respondents to the November loan officer survey indicated that their banks' consumer loan delinquencies had increased this year,

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

Type of credit	1993	1994	1995 H1	1995 Q3	1995 Aug.[r]	1995 Sept.[p]	Memo: Outstanding Sept. 1995 (billions of dollars)
Installment	8.1	14.2	15.0	10.1	12.7	6.6	995.1
Auto	9.0	13.1	10.0	9.9	7.3	6.2	341.4
Revolving	11.0	16.7	23.4	11.2	14.0	8.9	384.0
Other	3.7	12.5	10.3	8.7	17.7	3.7	269.7
Noninstallment	-4.7	10.1	11.7	26.4	-4.8	49.2	65.8
Total	7.2	14.0	14.8	11.0	11.6	9.1	1,060.9

r Revised.
p Preliminary.

INTEREST RATES ON CONSUMER LOANS
(Annual percentage rate)

Type of loan	1993	1994	1994 Nov.	1995 Feb.	1995 May	1995 Aug.	1995 Sept.
At commercial banks[1]							
New cars (48 mo.)	8.1	8.1	8.8	9.7	9.8	9.4	n.a.
Personal (24 mo.)	13.5	13.2	13.6	14.1	14.0	13.8	n.a.
Credit cards	16.8	16.2	n.a.	n.a.	n.a.	n.a.	n.a.
Credit cards[2]							
All accounts	n.a.	n.a.	15.7	16.1	16.2	16.0	n.a.
Accounts assessed interest	n.a.	n.a.	15.8	15.3	16.2	15.9	n.a.
At auto finance cos.[3]							
New cars	9.5	9.8	10.5	11.9	11.4	10.9	10.8
Used cars	12.8	13.5	14.2	15.1	14.8	14.2	14.1

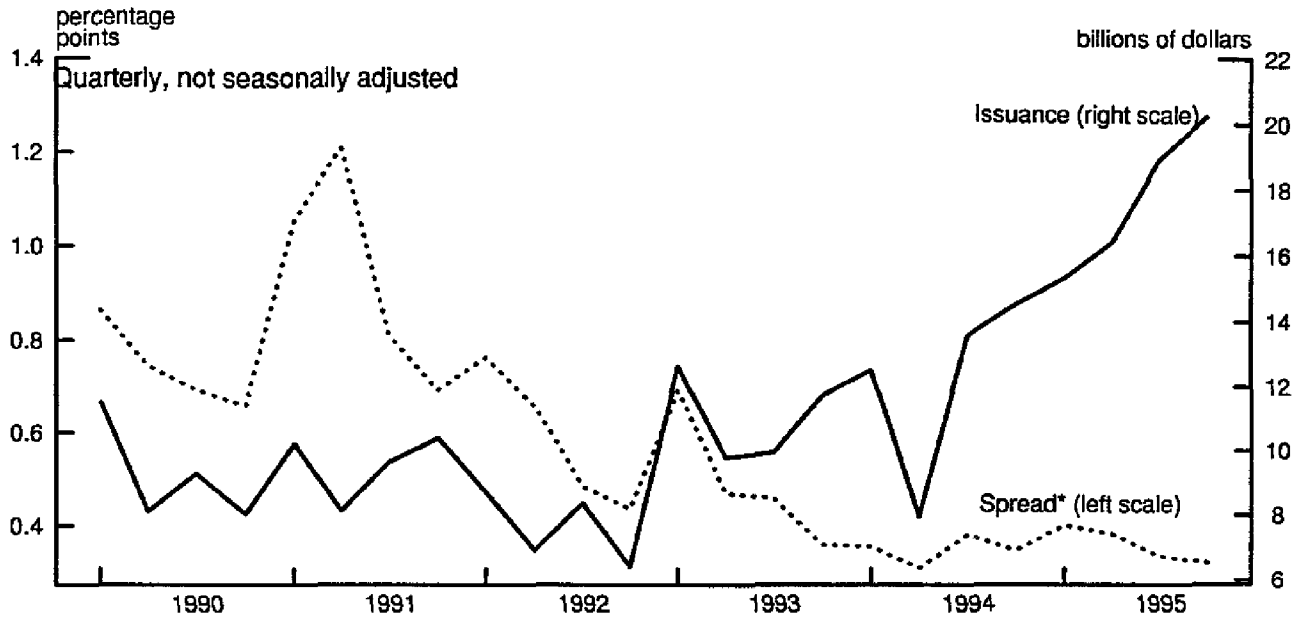
Note. Annual data are averages of quarterly data for commercial bank rates and of monthly data for auto finance company rates.
1. Average of "most common" rate charged for specified type and maturity during the first week of the middle month of each quarter.
2. The rate for *all accounts* is the stated APR averaged across all credit card accounts at all reporting banks. The rate for *accounts assessed interest* is the annualized ratio of total finance charges at all reporting banks to the total average daily balances against which the finance charges were assessed (excludes accounts for which no finance charges were assessed).
3. For monthly data, rate for all loans of each type made during the month regardless of maturity.
n.a. Not available.

which they attributed to several factors, including higher household debt burdens, greater willingness by households to declare bankruptcy, and slower growth in some markets. Although on net the willingness of surveyed banks to make consumer loans had not changed since August, a number of the respondents noted they had tightened lending standards and some had increased loan spreads, but these adjustments generally were small. These survey results are consistent with anecdotal reports of a growing number of institutional lenders undertaking reviews of their lending programs and standards. More broadly, as noted, investor concerns about the quality of lenders' portfolios contributed to some retrenchment of bank and other financial institution stock prices recently.

As noted above, securitization of consumer loans has been very strong so far this year; at $64-1/2 billion through mid-October, securitizations have already surpassed the record annual level set in 1994 (table). This rapid growth reflects both the rise in consumer loans outstanding as well as the hunger of investors for high-quality assets, evidenced, for example, by the narrowing of spreads on securities backed by credit-card receivables (chart).

Although growth has occurred in most major asset categories, credit card-backed securities have provided the biggest boost to total issuance in 1995, stimulated both by strong growth in outstanding credit card balances and by the need to re-securitize assets underlying maturing securitizations. In 1995, about $14 billion to $18 billion of existing securitizations are scheduled to be paid down in whole or in part. For banks, there is a need to "roll" these issues over in order to keep the underlying account balances from returning to the balance sheet and, thus, having to hold capital against the loans. For retailers and nonbank issuers

Gross Issuance of Consumer Asset-Backed Securities and Yield Spread



*Rate on new three-year issues minus three-year Treasury constant maturity.

Gross Public Issuance of Consumer Asset-Backed Securities
(Billions of dollars; not seasonally adjusted)

	Total	Automobile	Credit Cards	Other	Memo: Home Equity[1]
1990	35.6	11.6	22.5	1.5	5.6
1991	37.2	15.6	19.7	1.9	10.1
1992	34.6	17.4	13.8	3.4	7.1
1993	44.4	21.7	18.9	3.8	6.9
1994	53.8	14.6	30.8	8.4	9.4
1995[2]	64.6	18.8	39.6	6.4	11.7
1994:Q1	8.2	2.8	3.8	1.5	1.9
Q2	13.8	5.8	6.3	1.8	2.6
Q3	16.2	4.0	8.4	3.8	2.4
Q4	15.6	2.0	12.3	1.3	2.9
1995:Q1	16.8	3.9	10.1	2.8	3.6
Q2	19.0	4.5	14.4	.1	2.6
Q3	21.1	8.2	11.9	1.0	4.7
1995:Oct.[2]	7.8	2.2	3.1	2.5	.8

Note: Details may not add to totals due to rounding.
1. Home equity loans are not included in consumer installment credit.
2. Data are through October 27, 1995.

with less than top credit ratings on their debt, securitization provides a very attractive means of financing credit card programs.

ABS issuance has also been boosted by a sizable increase in offerings of securities backed by home equity loans. Notable among the third-quarter home equity issues were two that featured a Fannie Mae guarantee "wrapped" around the securities. A Fannie Mae "wrap" broadens the investor base for the securities to include a number of public entities and other investors whose investments are restricted to government or federal agency securities. For banks, the Fannie-backed securities carry a risk weight of 20 percent, compared with the 50 percent or 100 percent risk weights of traditional home equity loan securities. To date, Fannie Mae has done three home equity loan deals, totaling roughly $820 million.

INTERNATIONAL DEVELOPMENTS

U.S. International Trade in Goods and Services

In August, the deficit in goods and services narrowed markedly. Exports jumped sharply after falling in July, and imports were about unchanged following a substantial decline in July. For July-August combined, the deficit (at an annual rate) was significantly smaller than in the second quarter.

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

	1994	Annual rates 1995			Monthly rates 1995		
		Q1	Q2	Q3e/	Jun	Jul	Aug
Real NIPA 1/							
Net exports of G&S	-110.0	-118.5	-126.7	-125.8	--	--	--
Nominal BOP							
Net exports of G&S	-106.2	-116.0	-132.5	-120.0	-11.3	-11.2	-8.8
Goods, net	-166.1	-178.4	-195.2	-180.4	-16.5	-16.2	-13.8
Services, net	59.9	62.4	62.7	60.3	5.2	5.0	5.0

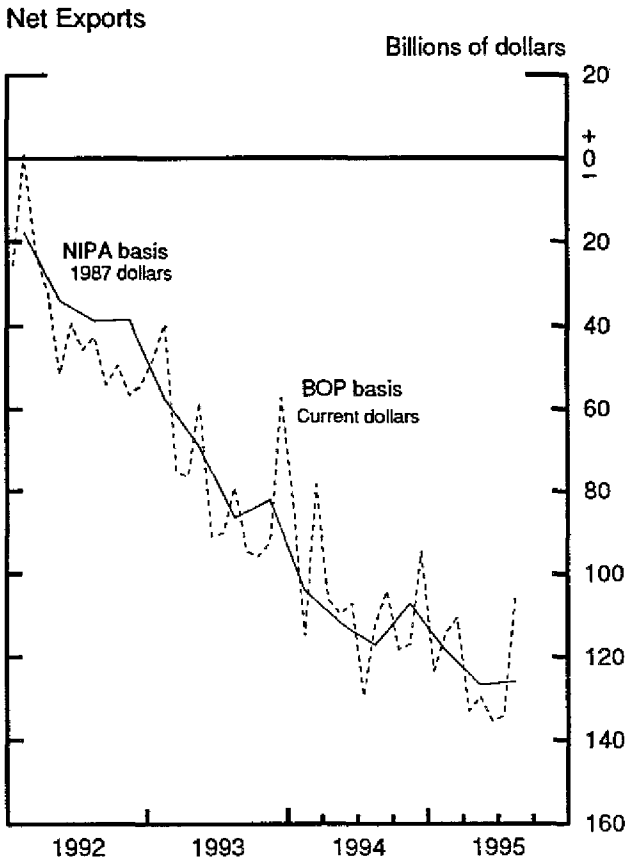
1. In billions of 1987 dollars.
e. NIPA data are FRB staff estimates; BOP data are two-month averages.
Source. U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

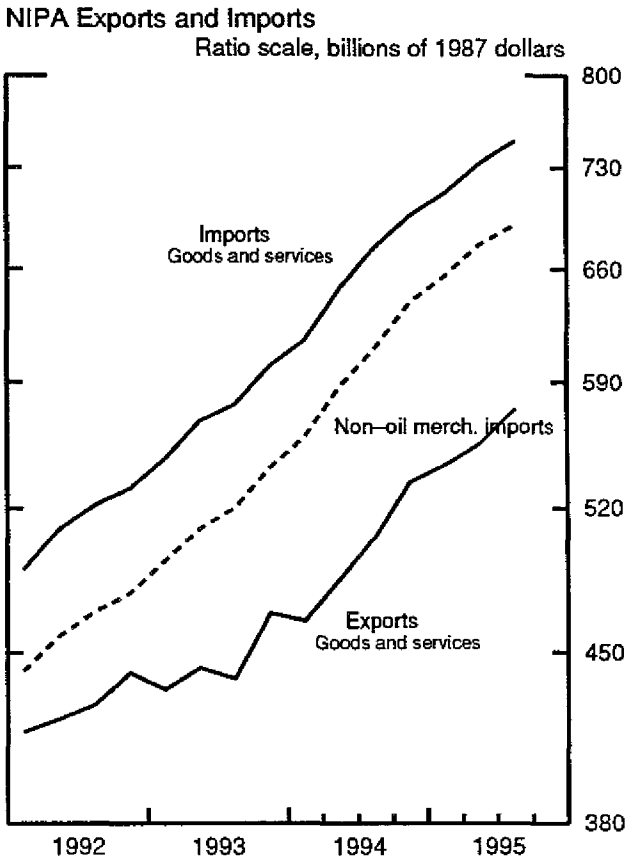
The level of exports of goods and services for July-August combined declined about 1/2 percent relative to the second quarter, as increases in exports of computers and agricultural products were more than offset by decreases in exports of aircraft, gold, and service receipts. Most of the changes in exports were due to quantities. The exceptions were agricultural products, where all of the increase was in prices, and industrial supplies, where quantity declines were exactly offset by price increases.

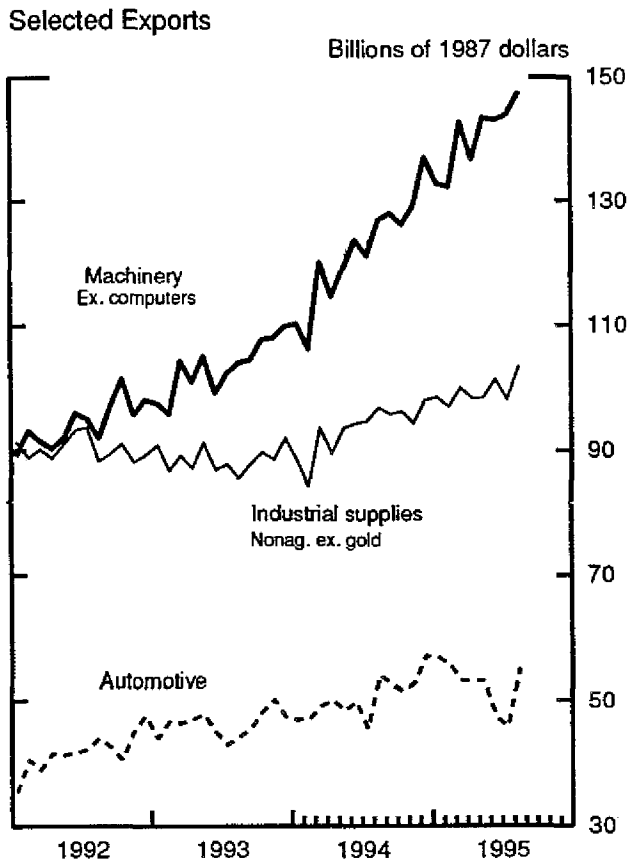
Imports of goods and services for July-August combined were about 2 percent lower than in the second quarter. Declines were recorded in most major import categories; notable exceptions were imported computers and semiconductors, which continued to rise sharply. Most of the decrease in non-oil imports reflected changes in quantities, as prices increased relative to the second quarter.

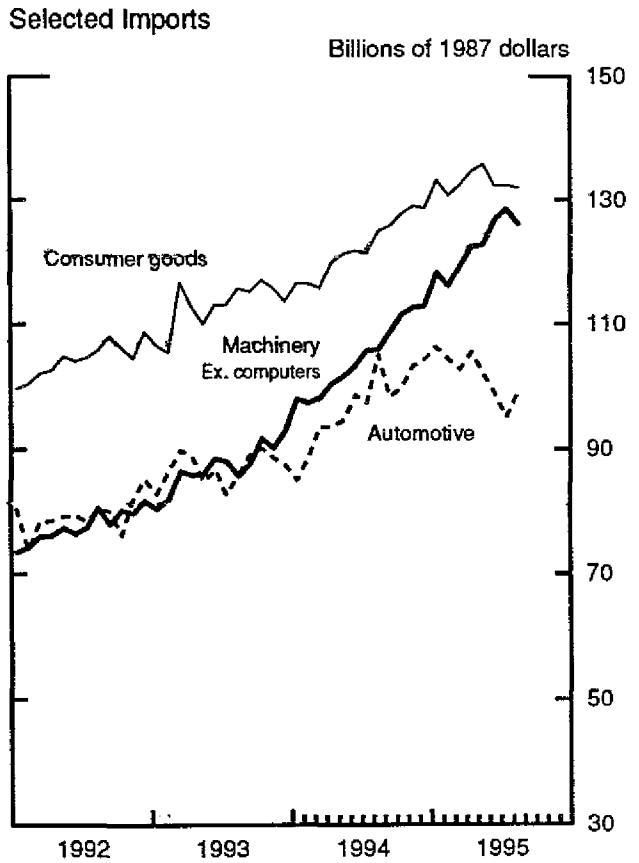
U.S. International Trade in Goods and Services

(Seasonally adjusted annual rate)









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

	Levels				Amount Change 1/			
	1995		1995		1995		1995	
	Q2	Q3e/	Jul	Aug	Q2	Q3e/	Jul	Aug
Exports of G&S	778.4	774.9	760.9	788.9	19.9	-3.5	-14.3	28.0
Goods exports	571.4	570.5	556.4	584.6	17.4	-0.9	-12.2	28.2
Agricultural	53.6	56.5	54.2	58.8	-2.5	2.8	3.2	4.6
Gold	7.7	3.3	3.9	2.6	2.1	-4.5	-4.7	-1.3
Computers	37.1	41.2	40.0	42.4	0.7	4.2	2.0	2.4
Other goods	473.0	469.5	458.3	480.8	17.0	-3.4	-12.7	22.5
Aircraft & pts	31.1	25.0	22.4	27.5	5.9	-6.1	-8.4	5.0
Semiconductors	32.6	35.0	34.3	35.6	2.6	2.3	-0.3	1.3
Other cap gds	129.9	132.9	131.5	134.2	4.7	2.9	1.1	2.7
Automotive	58.8	57.9	52.9	63.0	-4.7	-0.9	-1.7	10.1
to Canada	31.3	32.3	27.9	36.8	-4.5	1.0	-1.3	8.9
to Mexico	6.5	6.6	5.6	7.6	-0.7	0.1	-1.0	2.0
to ROW	21.0	19.0	19.4	18.6	0.5	-2.0	0.7	-0.8
Ind supplies	131.8	131.8	129.7	133.8	6.1	0.0	-5.0	4.1
Consumer goods	64.5	64.1	62.4	65.8	1.4	-0.4	-2.2	3.4
All other	24.2	22.9	25.0	20.9	1.0	-1.2	-1.0	-4.1
Services exports	207.0	204.4	204.5	204.3	2.5	-2.7	-2.1	-0.2
Imports of G&S	911.0	894.9	895.1	894.7	36.5	-16.0	-15.4	-0.4
Goods imports	766.6	750.9	751.2	750.6	34.2	-15.7	-15.3	-0.6
Petroleum	58.3	55.7	56.6	54.8	6.0	-2.6	-4.5	-1.8
Gold	10.8	2.1	2.0	2.3	6.4	-8.7	-8.5	0.3
Computers	53.0	57.1	55.2	59.1	2.2	4.2	0.1	3.8
Other goods	644.5	635.9	637.4	634.4	19.6	-8.6	-2.4	-3.0
Aircraft & pts	11.2	10.3	10.0	10.7	0.6	-0.8	-0.9	0.7
Semiconductors	37.2	41.3	40.9	41.8	5.3	4.1	1.1	0.9
Other cap gds	117.9	117.7	120.2	115.2	5.4	-0.2	1.3	-5.0
Automotive	128.6	122.7	120.2	125.2	-1.3	-5.9	-4.4	5.0
from Canada	42.8	42.9	34.2	51.7	-5.5	0.2	-6.9	17.5
from Mexico	17.6	17.2	16.1	18.4	-0.2	-0.4	-2.0	2.3
from ROW	68.2	62.5	69.9	55.1	4.4	-5.7	4.5	-14.8
Ind supplies	127.6	123.4	125.2	121.6	4.8	-4.2	0.6	-3.6
Consumer goods	163.1	161.5	161.6	161.4	4.0	-1.6	0.5	-0.2
Foods	32.7	32.9	32.9	32.9	-1.4	0.2	-0.1	-0.0
All other	26.2	26.0	26.3	25.6	2.1	-0.2	-0.5	-0.7
Services imports	144.4	144.1	144.0	144.2	2.3	-0.3	-0.1	0.2
Memo:								
Oil qty (mb/d)	9.10	9.50	9.57	9.44	0.15	0.41	-0.04	-0.12

1. Change from previous quarter or month.
e. Average of two months.
Source. U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

Oil Imports

The total quantity of oil imports is estimated to have risen in the third quarter due in part to a modest pickup in stockbuilding. Oil imports dipped in August, however, despite higher oil consumption. Preliminary Department of Energy statistics indicate that oil imports likely rebounded in September, as inventory accumulation resumed.

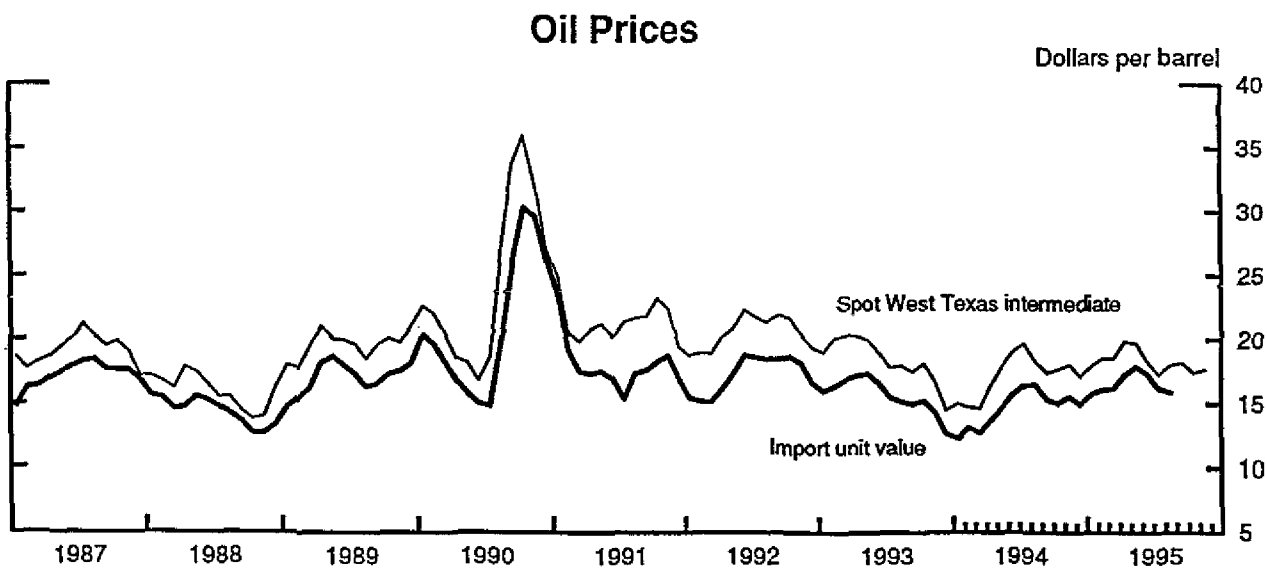
The price of imported oil rose in September, after falling in the previous three months. The earlier declines reflected concerns in world spot markets about an over-abundant world oil supply. These concerns abated, however, as spot WTI prices rose in August (reflected in September import prices) and again in September reflecting very lean U.S. inventories, uncertainty about the impact of recent hurricanes on Caribbean oil facilities, and increased tensions with Iraq (the defection of two high level Iraqi government officials in August and the ensuing U.S. military build-up in the Gulf Region). In October, however, spot oil prices fell back by almost $1.00 per barrel, in part because of a partial rebound in oil production in the Caribbean and the Gulf of Mexico, concerns about continued quota-busting by OPEC producers, and short-lived rumors about Iraq's acceptance of a limited U.N. oil sale for humanitarian purposes.

Prices of Merchandise Non-Oil Imports and Exports

The average price of U.S. non-oil imports rose significantly less in the third quarter than in recent quarters. Most categories of non-oil imports posted modest price increases; in particular, prices of non-oil industrial supplies, automotive products, and capital goods (excluding computers) slowed sharply from previous periods.

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

	Annual rates 1995			Monthly rates 1995		
	Q1	Q2	Q3	Jul	Aug	Sep
	----------BLS prices----------					
Merchandise imports	4.4	8.5	-1.9	-0.4	-0.3	0.1
Oil	15.2	36.3	-29.9	-6.4	-2.5	1.7
Non-oil	3.3	5.8	1.8	0.4	0.0	-0.2
Foods, feeds, bev.	-0.4	-3.8	0.9	0.5	0.4	-1.2
Ind supp ex oil	15.3	10.4	5.5	1.0	0.1	0.4
Computers	-3.5	-4.4	-2.1	0.0	-0.1	-0.7
Capital goods ex comp	0.6	9.5	0.2	0.0	-0.3	-0.4
Automotive products	0.7	5.2	2.0	0.3	-0.1	0.3
Consumer goods	1.3	3.4	1.2	0.1	0.1	-0.2
Memo:						
Oil imports ($/bbl)	16.01	17.55	16.05	16.20	15.90	...
Merchandise exports	8.6	7.1	1.0	0.3	-0.5	0.2
Agricultural	11.8	17.0	21.5	3.8	-1.4	2.9
Nonagricultural	8.3	6.0	-1.5	-0.2	-0.4	-0.2
Ind supp ex ag	23.5	13.8	-6.4	-0.7	-0.9	-0.8
Computers	-5.6	-2.4	-6.7	-0.4	-1.2	-0.5
Capital goods ex comp	3.0	3.9	2.2	0.2	0.1	0.1
Automotive products	1.0	-0.2	0.9	0.1	0.0	0.2
Consumer goods	1.9	2.9	0.7	0.2	0.0	0.0
	--------Prices in the NIPA accounts--------					
Fixed-weight						
Imports of gds & serv.	4.5	8.4	-1.3	...	...	...
Non-oil merch ex comp	3.6	5.5	1.9	...	...	...
Exports of gds & serv.	9.3	7.0	1.0	...	...	...
Nonag merch ex comp	9.7	6.3	-0.9	...	...	...



The average price of U.S. exports rose modestly in the third quarter, also significantly less than in recent quarters. Most of the increase stemmed from an upswing in the average price of agricultural products, especially grains. The price of non-agricultural exports fell in the third quarter, the first quarterly decline since 1993Q4. The decrease was the result of sharp declines in the price of exported industrial supplies, following four consecutive quarters of double-digit increases, and a continued fall in computer prices.

U.S. International Financial Transactions

Foreign private net purchases of U.S. Treasury securities (line 4) were extremely large in July and August. The United Kingdom, Japan, and the Caribbean financial centers accounted for the bulk of the net purchases. In the first eight months of 1995, recorded net private purchases by Japanese residents amounted to almost $36 billion, compared with $14 billion in all of 1994.

Foreign net purchases of U.S. corporate and agency bonds (line 4b) were also strong in July and August. More recent information indicates that new Eurobond issues by U.S. corporations fell somewhat in September from the very strong August pace. Foreigners showed renewed interest in the U.S. stock market in July and August (line 4c); net purchases in those two months amounted to more than cumulative net purchases in the previous six months or in all of 1994.

U.S. net purchases of foreign securities (line 5) were also strong in July and August. More than half of U.S. net purchases of foreign stocks (line 5b) during these months were from Japan. Purchases of stocks from other developed countries accounted for the bulk of the remainder, although there was some net investment in developing economies in Asia. Similarly, U.S. net purchases of

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

	1993	1994	1994		1995			
			Q3	Q4	Q1	Q2	July	Aug.
Official capital								
1. Change in foreign official reserve assets in U.S. (increase, +)	70.4	37.6	19.2	-.8	22.2	37.3	24.0	7.9
a. G-10 countries	30.1	28.9	8.9	-6.1	16.9	14.1	2.6	-1.0
b. OPEC countries	-5.1	-3.3	3.3	.4	.4	-.2	4.7	.6
c. All other countries	45.5	12.0	7.0	4.8	4.9	23.3	16.6	8.3
2. Change in U.S. official reserve assets (decrease, +)	-1.4	5.3	3.5	-.2	-5.3	-2.7	-2.5	.6
Private capital								
Banks								
3. Change in net foreign positions of banking offices in the U.S.[1]	17.1	102.9	9.8	17.9	-11.8	-23.4	4.0	-2.6
Securities[2]								
4. Foreign net purchases of U.S. securities (+)	105.8	92.8	19.3	36.5	46.2	51.5	27.4	37.8
a. Treasury securities[3]	24.8	34.6	5.6	26.0	30.1	30.5	16.4	27.1
b. Corporate and other bonds[4]	61.4	53.9	12.7	12.9	19.6	18.6	8.8	8.0
c. Corporate stocks	19.6	4.4	1.0	-2.4	-3.5	2.4	2.3	2.6
5. U.S. net purchases (-) of foreign securities	-143.1	-56.6	-10.0	-17.9	-7.9	-22.8	-13.2	-9.5
a. Bonds	-80.4	-9.3	-3.0	-8.5	-3.8	-12.4	-5.0	-2.6
b. Stocks	-62.7	-47.2	-7.0	-9.3	-4.1	-9.9	-8.2	-6.9
Other flows (quarterly data, s.a.)								
6. U.S. direct investment (-) abroad	-72.6	-49.4	-10.1	-11.9	-22.5	-16.1	n.a	n.a
7. Foreign direct investment in U.S.	41.1	49.4	19.7	19.6	17.2	11.3	n.a	n.a
8. Other (inflow, +)[5]	46.5	-16.5	.4	-13.6	-18.6	4.0	n.a	n.a
U.S. current account balance (s.a.)	-99.9	-151.2	-39.7	-43.3	-39.0	-43.6	n.a	n.a
Statistical discrepancy (s.a.)	36.0	-14.3	-12.1	13.7	19.5	4.5	n.a	n.a

Note. The sum of official capital, private capital, the current account balance, and the statistical discrepancy is zero. Details may not sum to totals because of rounding.

1. 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.

2. Includes commissions on securities transactions and therefore does not match exactly the data on U.S. international transactions published by the Department of Commerce.

3. Includes Treasury bills.

4. Includes U.S. goverment agency bonds.

5. 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 Survey of Current Business.

n.a. Not available. * Less than $50 million.

foreign bonds (line 5a) also were concentrated in the developed countries. However, U.S. investors did purchase over $1 billion in bonds from Mexico in July. The issue of $1 billion in two-year floating rate paper by Mexico in mid-July probably accounted for a large part of these recorded purchases by U.S. investors.

Foreign official assets in the United States (line 1) rose strongly in July, but rose by less in August. G-10 holdings (line 1a) showed little increase in August despite large reported intervention purchases of dollars by Japan. Information from FRBNY shows that heavy intervention in September also was not reflected in changes in reserve holdings at the FRBNY, as would typically be the case. Very large increases in U.S. holdings were reported for "other countries" (line 1c) in July and August, particularly Brazil and China, but also several other developing countries in Asia and Latin America.

There was little net change in the foreign positions of banking offices in the United States between the end of June and the end of August (line 3). However, monthly average data show net inflows into banks in the United States from their IBFs and own foreign offices in the third quarter of 1995. (See line 1 of the International Banking Data table.) These inflows were concentrated at Japanese-chartered banks and probably reflected their response to the premium they were being charged to borrow dollars in interbank markets.

INTERNATIONAL BANKING DATA[1]
(Billions of dollars)

	1992 Dec.	1993 Dec.	1994 Dec.	1995 Mar.	June	July	Aug.	Sep.
1. Net claims of U.S. banking offices (excluding IBFs) on own foreign offices and IBFS	-71.6	-122.1	-224.0	-242.7	-235.3	-235.0	-241.4	-244.3
a. U.S.-chartered banks	17.0	4.2	-70.1	-88.6	-88.7	-82.7	-87.9	-86.1
b. Foreign-chartered banks	-88.6	-126.3	-153.9	-154.1	-147.6	-152.2	-153.4	-158.2
2. Credit extended to U.S. nonbank residents								
a. By foreign branches of U.S. banks	24.8	21.8	23.1	23.5	25.2	25.2	25.3	25.7
b. By Caribbean offices of foreign-chartered banks	n.a.	90.9	78.4	80.3	85.3	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	90.0	77.8	85.6	90.5	92.3	93.6	94.9	94.6
b. At the Caribbean offices of foreign-chartered banks	n.a.	79.2	86.0	96.3	108.9	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	197	204	200	209	n.a.	n.a.	n.a.	n.a.
5. Eurodeposits of U.S. nonbank residents	235	229	260	270	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

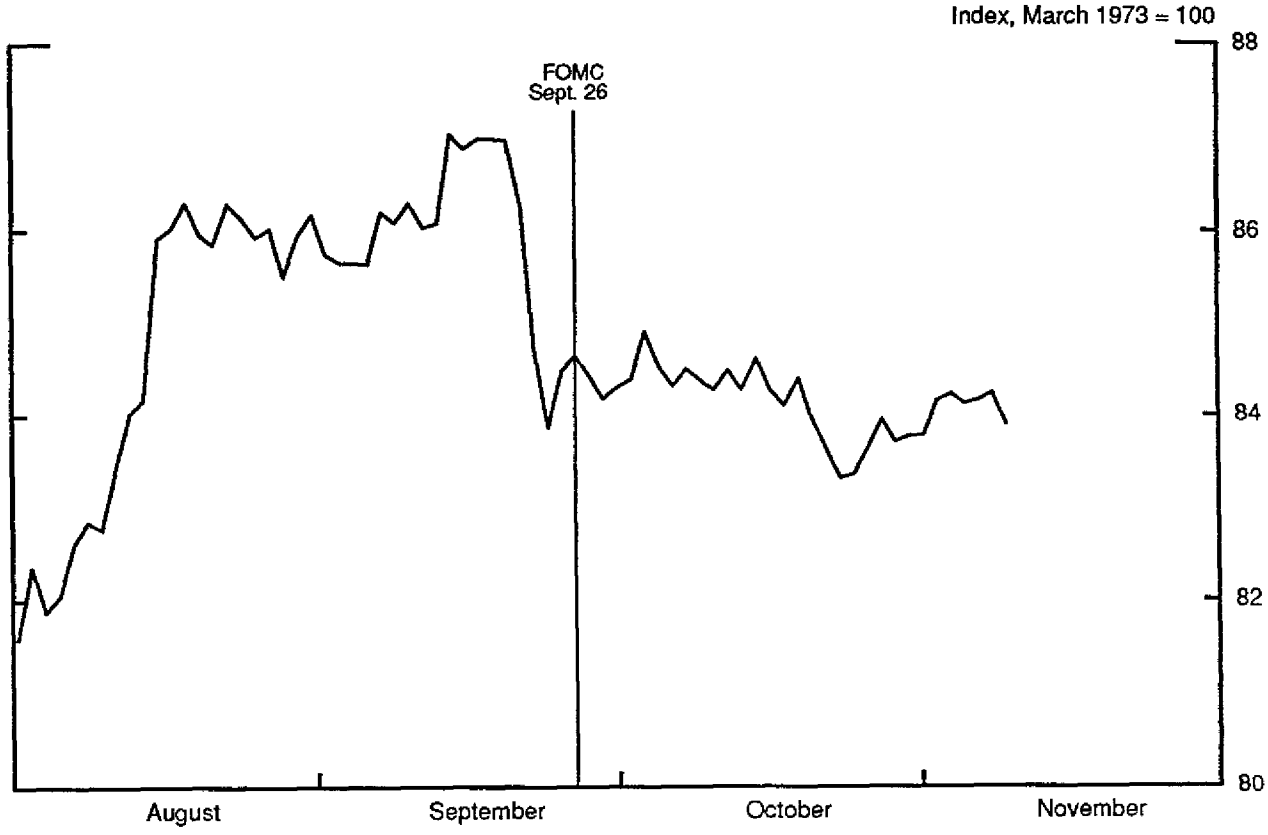
Foreign Exchange and Foreign Financial Markets

The weighted-average dollar has moved in a narrow range since the time of the September 26 FOMC meeting, declining about 3/4 percent on balance. The dollar has moved down 1/2 to 2 percent against most of the major European currencies but has risen nearly 1-1/2 percent against the yen.

Over the intermeeting period, the dollar has depreciated 1-1/2 percent against the mark, as the U.S.-German long-term interest rate differential moved against the dollar. During the period, the Bundesbank moved to reduce short-term interest rates in Germany, although perhaps somewhat less than had been expected, by ratcheting down its weekly repo rate in small steps a total of 12 basis points. The German three-month interbank interest rate edged down only 5 basis points during the period. At times during the intermeeting period, the mark was supported by concerns that some European countries, most notably France and Italy, would not be able to meet the Maastricht criteria for European Monetary Union by the deadline set forth in the treaty.

The dollar has declined about 1-1/2 percent against the French franc during the intermeeting period, leaving the franc little changed on balance against the mark. The franc had been lower during the period as concerns over the budget and political problems of the Chirac government came to the fore. Subsequent statements by French officials asserting that they were willing to take the policy stances needed to meet their budgetary and exchange rate objectives, along with reports that the Prime Minister would not be prosecuted for alleged improprieties in arranging family housing in Paris, seemed to stay the pressure on the franc. In the interim, however, French authorities suspended the 5-to-10-day emergency lending facility and reintroduced a 24-hour emergency

Weighted Average Exchange Value of the Dollar
(Daily data)



Interest Rates in Major Industrial Countries

	Three-month rates			Ten-year bond yields		
	Sept.26	Nov.8	Change	Sept.26	Nov.8	Change
Germany	4.00	3.95	-0.05	6.58	6.37	-0.21
Japan	0.50	0.56	0.06	2.78	2.91	0.13
United Kingdom	6.69	6.75	0.06	7.97	7.78	-0.19
Canada	6.55	6.10	-0.45	7.86	7.61	-0.25
France	6.12	6.02	-0.10	7.46	7.11	-0.35
Italy	10.50	10.63	0.13	11.50	11.62	0.12
Belgium	4.21	3.99	-0.22	7.09	6.84	-0.25
Netherlands	3.80	3.77	-0.03	6.62	6.46	-0.16
Switzerland	2.44	2.13	-0.31	4.13	3.81	-0.32
Sweden	8.96	8.70	-0.26	9.49	9.10	-0.39
Weighted-average foreign	5.05	4.98	-0.07	6.95	6.79	-0.16
United States	5.74	5.78[p]	0.04	6.28	5.96[p]	-0.32

Note. Change is in percentage points. p. Preliminary

lending facility at rates as high as 7.25 percent, 110 basis points above the previous 5-to-10-day rate. Later in the period, as the pressure on the franc subsided, the authorities moved the rate down 25 basis points to 7 percent.

The lira has declined nearly 1-1/2 percent on balance against the mark during the period, and short- and long-term interest rates in Italy moved up on net more than 10 basis points. The lira had declined more and interest rates had risen further, as prospects for the Dini government sank sharply ahead of a no-confidence vote on October 26. The later recovery of asset prices in Italy followed the dramatic, last-minute defeat of the no-confidence motion.

The yen weakened during the intermeeting period, as concerns over the financial problems of Japanese banks appeared at times to weigh on the currency, although the news in early November of the termination of Daiwa Bank operations in the United States did not seem to have created any further pressures on the yen or on the funding costs of Japanese banks. Somewhat surprisingly, the bellwether bond yield in Japan rose nearly 15 basis points during the period, despite widespread declines in long-term bond yields outside Japan and evidence of some flight-to-quality in the yields on Japanese government securities at the short end of the maturity spectrum. Reflecting part of the increase in the premium Japanese banks paid to raise funds during the period, the three-month CD rate in Japan edged up 6 basis points,

In recent months, a "Japan premium" has developed in both dollar and yen interbank markets. Japanese banks have paid a premium to borrow dollars in the interbank market since late July. During late October, the premium for three-month dollar deposits peaked at 50-70 basis points over rates paid by the most creditworthy banks; it has since declined to 30-40 basis points. Market commentary attributes the premium to Japanese banks' securing

funds over the year-end book closing well in advance, to avoid liquidity shortfalls. While Japanese banks have paid a premium for year-end funds in past years, this year's premium is larger and more persistent.

The maturity pattern of the premium confirms the importance of both a year-end and a more prolonged effect. The premium shows up most strongly at the three- and six-month maturities; for overnight and one-week deposits, there is a negligible premium, while one-month deposits carry a smaller premium. The combination of a smaller one-month premium and a roughly equal premium at three and six months implies a spike in the future one-month premium between one and three months out followed by a sustained positive premium between three and six months out.

The emergence of the premium appears to be having effects in other financial markets. The dollar/yen forward rate has been depressed as Japanese banks, faced with higher funding costs in dollars, buy dollars in the spot market and sell them forward, after the year-end. U.S. variable-rate municipal bonds issued with guarantees from Japanese banks are paying 0.2 percent more than bonds guaranteed by non-Japanese banks.

In recent weeks a premium has developed in yen funding markets as well. As of November 7, Japanese banks appear to be paying nearly 20 basis points more for one-month funding in the yen deposit market than non-Japanese banks and 25-30 basis points more for three-month funding in yen. An alternative measure of the credit risk assigned to Japanese banks, the spread between the three-month yen CD rate and the Japanese government treasury bill of comparable maturity, has widened from 10 basis points or less in early September to about 35 basis points on November 7.

The Canadian dollar has declined less than 1 percent on balance against the U.S. dollar, after having traded in a wide range

over the intermeeting period as expectations for the defeat of the Quebec sovereignty referendum waxed and waned. In the days immediately preceding the October 30 referendum, poll results showing the separatists moving ahead by a small margin prompted a decline of roughly 2 percent in the Canadian dollar. That drop was reversed immediately following the referendum, in which Quebec narrowly rejected the sovereignty proposal. The Canadian three-month interest rate moved synchronously with the exchange rate during the period, rising about 85 basis points in the days before the referendum and declining that amount and more immediately following the referendum. The extra decline in the three-month rate validated an immediate 25 basis point cut in the Bank of Canada's target range for the overnight rate and registered expectations of a further cut in the near term.

The Mexican peso has declined nearly 20 percent since the September FOMC meeting. Market commentary has focused on the lack of any clear indications of recovery in Mexican economic activity in the wake of the very sharp drop in second-quarter GDP announced in August, and investors may be concerned about the government's willingness to sustain its restrictive monetary policy stance. Mexican monetary authorities have so far responded to the recent pressure on the peso by refraining from exchange market intervention and maintaining unchanged bank reserve positions, allowing market interest rates to rise. The one-month interest rate in Mexico has risen roughly 20 percentage points during the intermeeting period, moving up to near the 55 percent level. Stock prices have continued to decline, with the major equity index declining another 6-1/2 percent during the intermeeting period.

The Swedish krona has risen more than 4 percent against the dollar, and Swedish short-term and long-term interest rates are down about 25-40 basis points from their levels at the time of the

September FOMC meeting, bolstered in part by better-than-expected inflation data.

. The Desk did not intervene for the U.S. monetary authorities during the period.

Developments in Foreign Industrial Countries

Economic growth remains subdued in the major foreign industrial countries. The Japanese economy has still shown little evidence of a sustained recovery, while growth in the European economies, with the exception of Italy, has continued to slow. However, the Canadian economy appears to have resumed a modest upward trend after contracting sharply earlier in the year.

Inflation abroad remains relatively low on average. Prices have continued to fall on a year-over-year basis at both the consumer and producer level in Japan, while consumer price inflation has declined further in Canada. In Europe, underlying inflation has been fairly stable in most countries, although the August increase in the French VAT as well as drought and currency depreciation in the United Kingdom have put some upward pressure on prices in recent months in those countries.

Major economic and financial uncertainties exist in a number of these countries. In Japan, concerns about the health of the banking sector persist and banks are paying a funding premium. In Europe, increased uncertainty about the ability of France to qualify for EMU on schedule as well as political turbulence in Italy have tended to put upward pressure on interest rates in those countries. Although last week's sovereignty referendum was defeated in Canada, the narrow margin suggests that the issue has not yet been resolved.

Individual country notes. In **Japan**, recent indicators suggest that private-sector activity remains weak, although some tentative signs of improvement have begun to appear. Industrial production fell in the third quarter after a flat second quarter, and the unemployment rate remained at a record level of 3.2 percent. However, machinery orders were a little higher on average in July and August than in the second quarter. Also, housing starts rose sharply in September from their very depressed August level, although they were still down for the third quarter on average. After registering a sizable decline in the second quarter, new car registrations--an important indicator of durable consumption--regained most of the lost ground in the third quarter. Meanwhile, prices have continued to fall. The October CPI for the Tokyo area was 0.8 percent below year-earlier levels, while wholesale prices were down 0.2 percent in September on the same basis.

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

	1995						
	Q1	Q2	Q3	July	Aug	Sept	Oct.
Industrial Production	1.3	0.0	-2.3	-2.7	2.5	-1.7	n.a.
Housing Starts	-1.9	-7.7	-1.2	2.8	-3.6	7.7	n.a.
Machinery Orders	5.0	-5.2	n.a.	-4.9	5.9	n.a.	n.a.
New Car Registrations	10.9	-8.9	6.4	-2.1	4.9	2.4	n.a.
Unemployment Rate (%)	3.0	3.1	3.2	3.2	3.2	3.2	n.a.
Job Offers Ratio[1]	0.66	0.63	0.60	0.61	0.61	0.60	n.a.
Business Sentiment[2]	-21	-16	-18	--	--	--	--
Consumer Prices[3]	0.0	-0.1	-0.2	-0.1	-0.4	-0.0	-0.8
Wholesale Prices[3]	-0.9	-1.7	-0.7	-0.8	-1.0	-0.2	n.a.

1. Level of indicator.
2. Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook.
3. Percent change from previous year, Tokyo area.

The Japanese current account surplus has continued to decline, registering $119 billion (SAAR) in the year through September, down

about $13 billion from the same period last year. In the year through September, the merchandise trade surplus (SAAR) was $114 billion, down about $8 billion from a year earlier.

In **Germany**, available data suggest that real activity has moderated somewhat from the 2-1/2 percent (SAAR) pace registered in the first half of this year. Virtually all indicators--including production, employment, prices, exports, and surveys of business and consumer confidence--point to sluggish growth. However, there is some uncertainty surrounding the interpretation of incoming evidence such as production, orders, and retail sales, given the redefinition of these series at the beginning of the year to achieve compliance with EU standards. Consumer price inflation has remained subdued, with the year-over-year rate just above 1-1/2 percent through October.

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

	1995						
	Q1	Q2	Q3	July	Aug	Sept	Oct
Industrial Production	-1.9	1.0	-1.2	1.7	-3.1	-1.9	n.a.
Orders	-4.0	0.6	n.a.	2.8	-2.4	n.a.	n.a.
Unemployment Rate (%)	9.3	9.3	9.4	9.3	9.4	9.5	9.6
Western Germany	8.2	8.2	8.4	8.3	8.4	8.4	8.4
Eastern Germany	13.8	13.7	14.0	13.8	13.8	14.3	14.3
Capacity Utilization[1]	85.2	85.9	85.4	--	--	--	--
Production Plans[1,2]	16.3	1.3	-0.3	0.0	-2.0	1.0	n.a.
Retail Sales[3]	-2.3	-3.0	n.a.	-4.0	-2.0	n.a.	n.a.
Consumer Prices[1,3]	2.0	1.9	1.7	1.9	1.5	1.6	1.6

1. Western Germany.
2. Percent of manufacturing firms planning to increase production in the next three months less those planning to decrease production.
3. Percent change from previous year.

The Bundesbank's targeted monetary aggregate M3 picked up in September, registering 1.5 percent growth (SAAR) relative to its base in the fourth quarter of last year. Although M3 growth will

most likely not reach the targeted range of 4 to 6 percent this year, the September pick-up was substantial, with the level of M3 balances more than 3/4 of one percentage point above its August value.

The Kohl government has announced a downward revision to expected tax revenue for this year and next. The revision is due mostly to subsidies in eastern Germany and refunds for earlier tax years and to a lesser extent to weaker-than-expected activity. In response to this shortfall in tax revenue, Finance Minister Waigel is requiring special approval for all federal government expenditures in excess of DM 1 million through the end of 1995 (the threshold rises to DM 10 million in 1996).

In **France**, monthly indicators suggest that economic activity slowed further in the third quarter and remains sluggish. The July/August level of industrial production (SA) was only slightly above that registered in the second quarter, while the unemployment rate was unchanged in August and up slightly in September. On the demand side, third-quarter spending on manufactured goods (equal to one-third of total consumption) was down sharply from its second-quarter level, although the drop in consumption was probably partly attributable to a two-percentage point increase in the VAT on August 1.

The business confidence survey by INSEE, the French statistical institute, indicates that business output declined sharply in September and fell slightly further in October. However, the survey also revealed that firms expect to increase output by the end of this year.

The August increase in the VAT has also resulted in a rise in the rate of year-over-year consumer price inflation in August and September to about 2 percent from 1-1/2 percent in July. However,

inflation exclusive of the VAT increase appears to have remained stable.

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

	1994	1995					
	Q4	Q1	Q2	Q3	July	Aug	Sept
Industrial Production	-0.0	1.1	0.5	n.a.	0.7	0.0[3]	n.a.
Capacity Utilization	84.2	84.8	84.8	n.a.	--	--	--
Unemployment Rate (%)[1]	12.0	11.8	11.6	11.4	11.4	11.4	11.5
Consumption of Manufactured Product	-0.1	-0.1	2.7	-0.8	-3.8	-0.1	0.1
Consumer Prices[2]	1.6	1.7	1.6	1.8	1.5	1.9	2.0

1. Break in series starting in March due to annual benchmark revision. Historical data are not yet available.
2. Percent change from previous year. Includes the increase in the VAT on August 1, 1995
3. INSEE releases a combined estimate for July and August due to the summer holiday.

The French trade performance has improved significantly this year relative to last year. The trade surplus continued to rise in August, and for the eight months through August was about $9 billion (SAAR) larger than over the same period one year earlier.

Recent data for the **United Kingdom** suggest that economic growth continued to slow in the third quarter, as real GDP rose a preliminary 2.0 percent (SAAR), slightly less than in the second quarter. Industrial production rose moderately in the third quarter, with most of the increase in the gas and oil extraction sector. On the demand side, retail sales were unchanged on balance in the third quarter. Forward-looking survey indicators are consistent with a softening trend. For example, the balance of firms expecting to increase output fell from +15 in July to +10 in October, according to the quarterly CBI survey. However, the

unemployment rate fell gradually throughout the third quarter to 8.1 percent in September.

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

	1994	1995					
	Q4	Q1	Q2	Q3	July	Aug	Sept
Real GDP	2.8	2.4	2.2	2.0	--	--	--
Non-oil GDP	2.7	1.9	2.7	2.0	--	--	--
Industrial Production	-0.1	0.7	0.2	0.4	0.6	-0.2	0.5
Retail Sales	0.3	-0.7	0.9	-0.0	0.4	-0.8	0.0
Unemployment Rate (%)	8.8	8.5	8.3	8.2	8.3	8.2	8.1
Consumer Prices[1]	2.2	2.7	2.7	2.9	2.8	2.9	3.1
Producer Input Prices[2]	8.6	11.1	10.8	9.5	10.1	9.0	9.2
Avg. Annual Earnings[2]	3.8	3.6	3.6	--	3.3	3.3	n.a.

1. Retail prices excluding mortgage interest payments. Percent change from previous year.
2. Percent change from previous year.

Inflation increased in the third quarter after remaining quite stable over the previous half-year. Targeted inflation, measured as the 12-month change in retail prices excluding mortgage interest payments, rose to 3.1 percent in September from 2.8 percent in July. The producer price index also continued to rise rapidly in the third quarter. The recent increase in consumer price inflation largely reflects upward pressure from both the pound's depreciation since the end of last year and this summer's drought, while growth in average earnings has slowed somewhat.

In **Italy**, real GDP declined a small amount in the second quarter (SAAR) following strong growth in the first quarter. However, the drop in GDP was concentrated in inventory investment, as final domestic demand and exports continued to grow rapidly. Investment growth was especially strong, while consumption showed a modest increase and government expenditures declined. Net exports

made a positive contribution to growth as exports continued to grow at a rapid pace. These data should be regarded as preliminary and are likely to be revised substantially, as has occurred in the past.

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

	1993	1994	1994		1995	
	Q4/Q4	Q4/Q4	Q3	Q4	Q1	Q2
GDP	-0.3	3.1	6.2	1.6	5.5	-1.5
Private Consumption	-1.1	1.9	1.3	1.5	0.4	1.3
Investment	-10.5	2.4	-2.6	7.2	5.3	10.1
Government Consumption	0.0	0.5	1.0	0.2	-1.9	-1.8
Exports	11.7	10.2	17.8	4.0	32.4	17.9
Imports	-5.3	14.7	14.3	13.5	8.9	10.6
Total Domestic Demand	-4.6	4.2	5.2	4.2	-0.7	-3.8
Net Exports (contribution)	4.4	-1.1	1.0	-2.6	6.2	2.2
Inv. Change(contribution)	-1.8	2.4	4.6	1.9	-1.7	-6.1

Monthly indicators suggest positive growth in the third quarter. Industrial production rose sharply in August and was nearly 4 percent above the second-quarter level on average in July and August. Consumer confidence also increased.

ITALIAN ECONOMIC INDICATORS
(Percent change from previous period except where noted, SA)

	1995						
	Q1	Q2	Q3	July	Aug	Sept	Oct.
Industrial Production	0.1	1.1	n.a.	0.9	6.2	n.a.	n.a.
Cap. Utilization (%)	78.2	78.6	n.a.	--	--	--	--
Unemployment Rate (%)	12.0	12.0	12.1	--	--	--	--
Consumer Confidence[1]	112.2	113.2	116.1	116.5	117.7	114.1	110.7
Bus. Sentiment[2] (%)	30	18	n.a.	18	21	n.a.	n.a.
Consumer Prices[3]	4.4	5.5	5.7	5.6	5.8	5.8	5.8
Wholesale Prices[3]	7.5	11.7	n.a.	11.5	10.8	n.a.	n.a.

1. Level of index, NSA.
2. Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook.
3. Percent change from previous year.

Inflation in Italy appears to have stabilized, but remains high. The year-over-year change in the consumer price index remained at 5.8 percent in October, the same rate as in the two previous months. Wholesale price inflation in August was down a little from the July level. However, wage inflation in September stood at 4.0 percent on a year-over-year basis, up from 3.2 percent in August.

On October 3, Prime Minister Dini presented the 1996 budget to parliament. The budget, which by law must be approved by the end of the year, includes a $20 billion deficit reduction package and calls for savings through a combination of tax rises and reductions in public expenditure. The 1996 budget deficit is projected to be 5.8 percent of GDP, down from an estimated 7.4 percent in 1995.

On October 26, Dini pledged to resign by the end of the year following the passage of the 1996 budget. His announcement came immediately before the government survived a vote of no-confidence instigated by Silvio Berlusconi, the leader of the center-right coalition. Berlusconi presented the no-confidence motion to parliament after the Senate passed a center-left initiated motion to oust Justice Minister Filippo Mancuso. National elections are now likely to be held before the end of March.

Indicators of economic activity in **Canada** suggest that growth resumed at a moderate pace in the third quarter after a sharp contraction in the second quarter. Both industrial production and retail sales were slightly above the second-quarter average in July and August, while employment rose in August after showing little change over the preceding half year, and increased further in September and October. As a result, the unemployment rate was 9.4 percent in October, a little below the third-quarter average. However, consumer and business confidence have remained weak.

Although the index of consumer attitudes registered a slight increase in the third quarter, it remained below 1994 levels. Business confidence slipped in the third quarter, primarily reflecting concerns over inventory buildup and excess capacity. Consumer price inflation has dropped back after a pickup in the second quarter, and was around 2-1/4 percent in both August and September.

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

	1995						
	Q1	Q2	Q3	July	Aug	Sept	Oct
Industrial Production	0.8	-0.5	n.a.	0.6	0.3	n.a.	n.a.
Manufacturing Survey:							
Shipments	3.6	-1.2	n.a.	-0.8	2.9	n.a.	n.a.
New Orders	3.4	-2.8	n.a.	2.2	0.2	n.a.	n.a.
Retail Sales	-0.1	0.2	n.a.	-0.1	0.6	n.a.	n.a.
Housing Starts	-10.0	-14.9	-3.3	-13.1	8.8	1.4	-10.9
Employment	0.3	0.1	0.1	-0.1	0.2	0.2	0.1
Unemployment Rate (%)	9.7	9.5	9.5	9.8	9.6	9.2	9.4
Consumer Prices[1]	1.6	2.7	2.4	2.5	2.3	2.3	n.a.
Consumer Attitudes	-10.9	0.4	1.7	--	--	--	--
Business Confidence[2]	-0.7	-12.3	-4.0	--	--	--	--

1. Percent change from year earlier.
2. NSA

On October 30, Quebec voters rejected the sovereignty referendum by a very narrow margin. Prime Minister Chretien has called for reconciliation with Quebec and a promise to bring about constitutional changes necessary to recognize the distinct character of Quebec society. However, separatist leaders have suggested another bid for independence should not be ruled out.

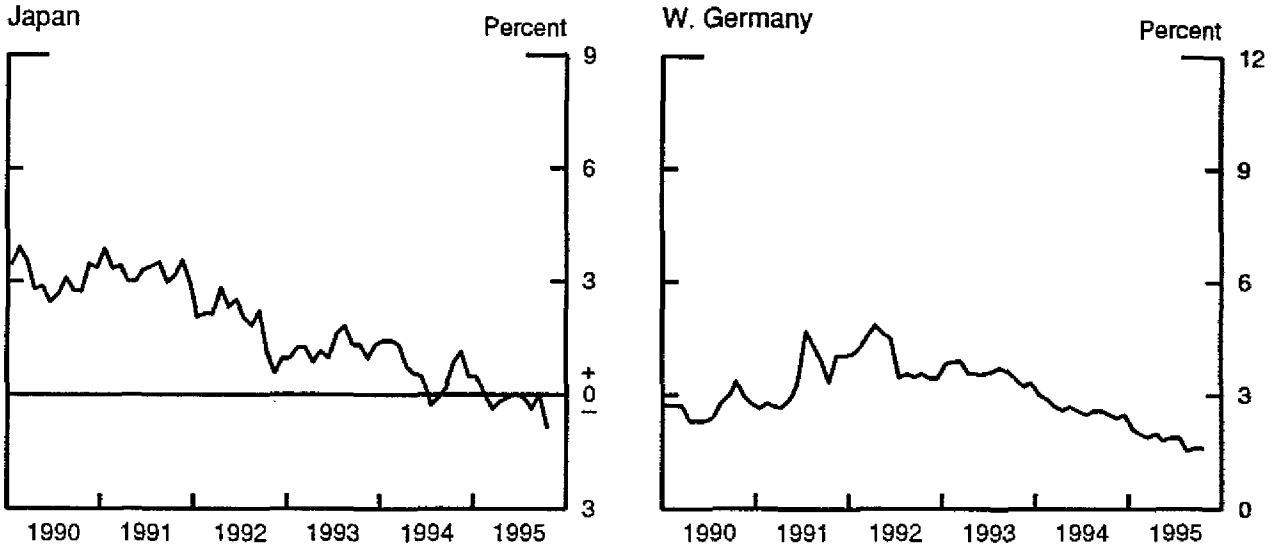
EXTERNAL BALANCES
(Billions of U.S. dollars, seasonally adjusted)

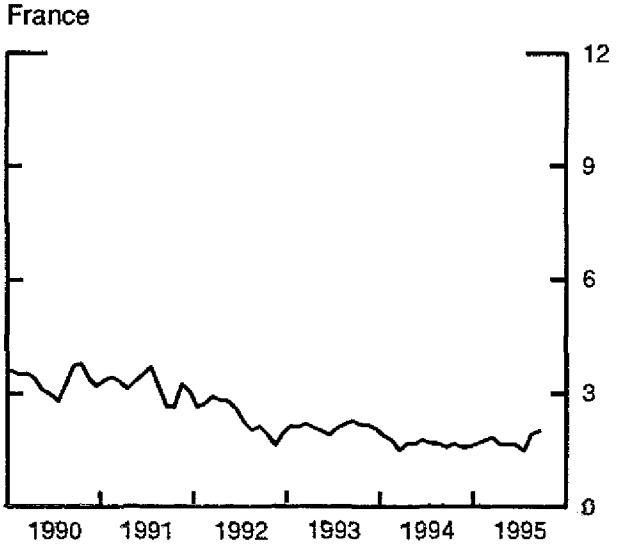
	1994	1994	1995					
		Q4	Q1	Q2	Q3	July	Aug	Sept
Japan: trade	120.7	29.7	27.3	32.7	25.3	8.1	8.6	8.6
current account	129.1	30.1	28.8	30.9	29.6	9.6	11.8	8.2
Germany: trade[1]	45.4	11.9	14.1	17.7	n.a.	4.5	5.3	n.a.
current account[1]	-21.7	-7.9	-3.5	-0.8	n.a.	-4.0	-3.3	n.a.
France: trade	15.1	4.9	5.7	6.0	n.a.	0.9	1.8	n.a.
current account[1]	8.1	2.6	7.5	n.a.	--	--	--	--
U.K.: trade	-16.2	-4.7	-3.2	-5.2	n.a.	-1.7	n.a.	n.a.
current account	-2.5	-0.8	-1.3	-3.8	--	--	--	--
Italy: trade	21.7	3.0	7.5	7.4	n.a.	1.7	n.a.	n.a.
current account[1]	15.6	4.8	2.6	7.8	n.a.	3.7	4.2	n.a.
Canada: trade	11.0	4.0	4.1	3.9	n.a.	1.1	2.0	n.a.
current account	-16.3	-2.9	-3.4	-4.0	--	--	--	--

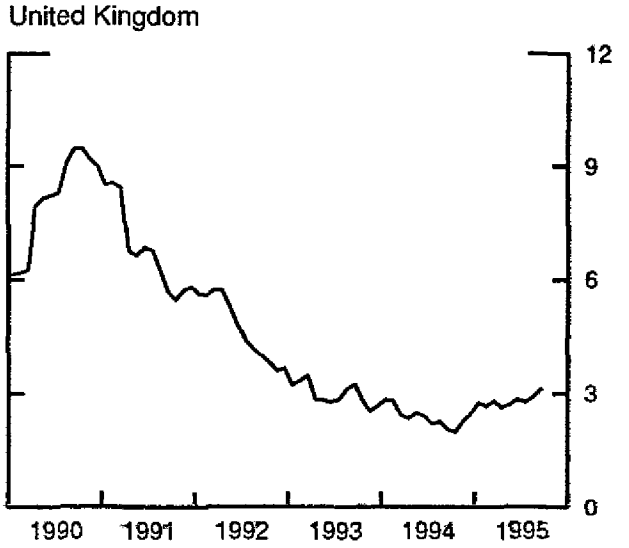
1. Not seasonally adjusted.
-- Data not available on a monthly basis.

Consumer Price Inflation in Selected Industrial Countries

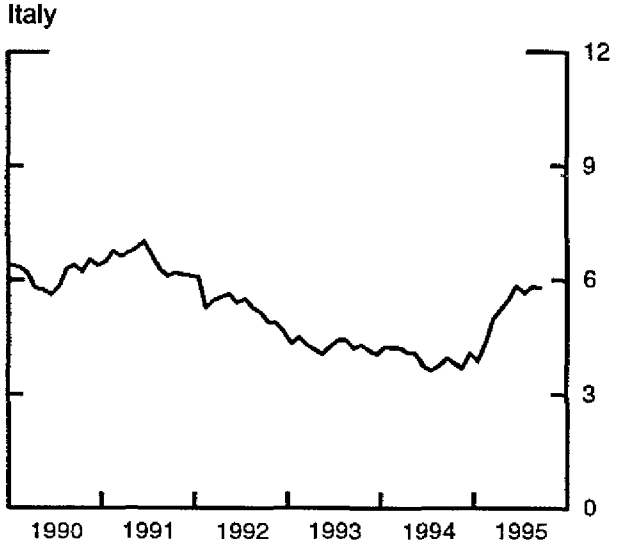
(12-month change)

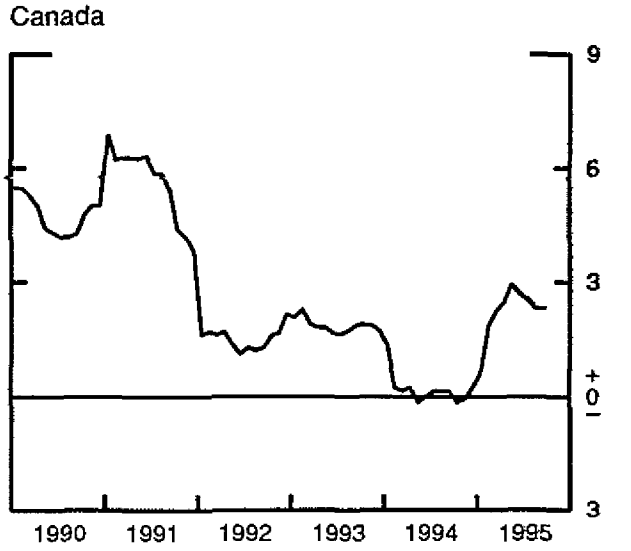






Note: Excludes mortgage interest payments.

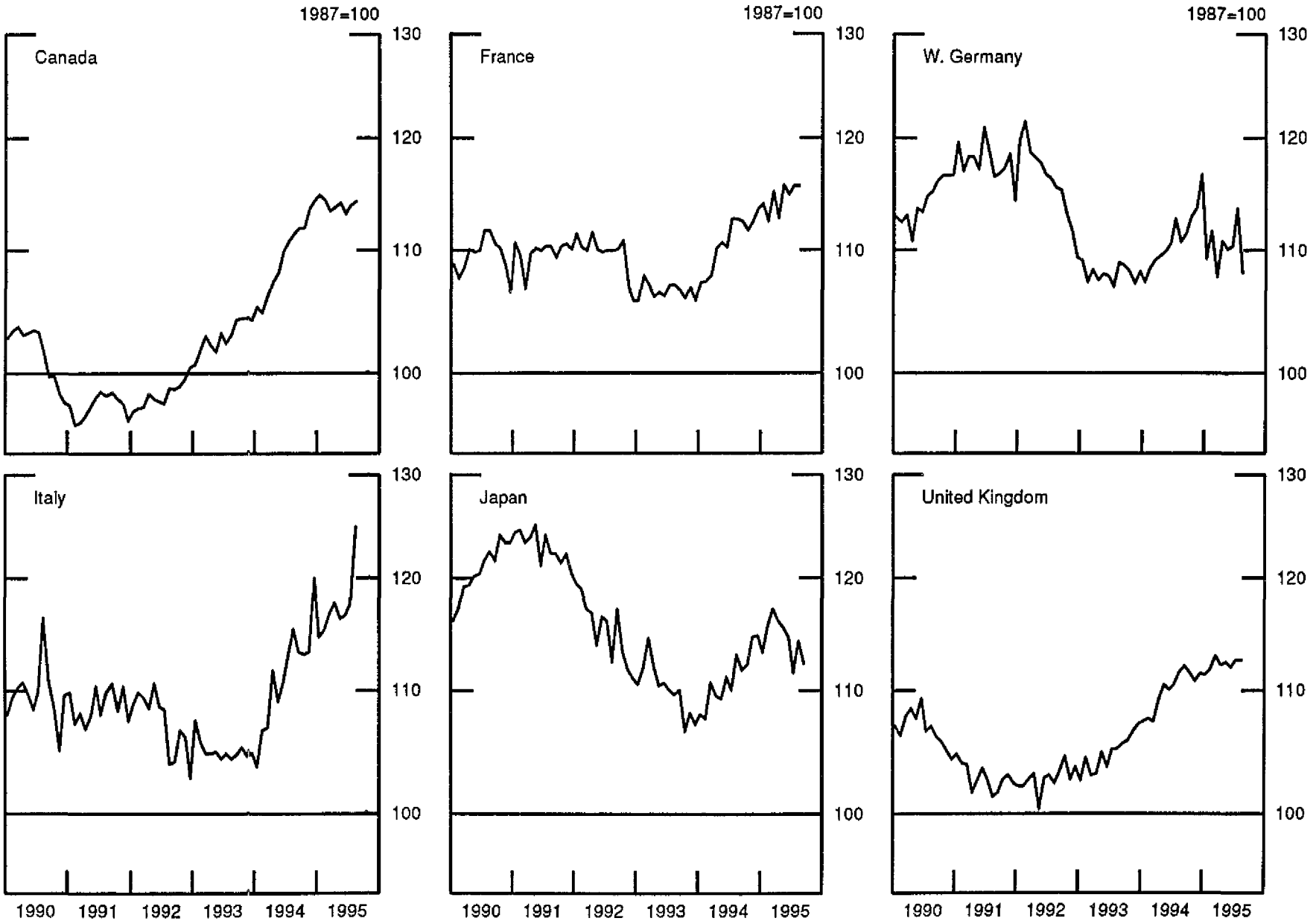




November 8, 1995

Industrial Production for Major Foreign Countries

Ratio Scale, Seasonally Adjusted, Monthly



Economic Situation in Other Countries

Economic activity in Mexico and Argentina appears to have remained weak in the third quarter following second-quarter declines in real GDP, while the slowdown in growth in Brazil that began in the second quarter probably continued into the third quarter. Growth remained strong in the major Asian developing countries, although the pace has moderated recently in China. In Russia, economic activity appears to have stabilized.

The contraction in economic activity in Mexico and Argentina, along with strong export growth, has contributed to the turnaround in these countries' trade balances. In Brazil, the trade balance moved into modest surplus in recent months after previously registering large deficits. However, in Venezuela, import growth was high and trade deficits have remained sizable. Both exports and imports grew rapidly in the Asian developing countries, while movements in trade balances have been mixed.

Inflation in Argentina and Brazil has continued to decline, but progress toward reducing inflation in Mexico and Venezuela appears to have slowed in recent months. Inflation in the Asian countries and in Russia continues to slow.

Individual country notes. In **Mexico**, monthly indicators suggest that economic activity remained depressed in the third quarter after contracting sharply in the second quarter. Industrial production was down about 12 percent from its year-earlier level in July, the same as the June decline, while the unemployment rate climbed to 7.5 percent by September. Inflation, after declining steadily from its April peak of 8 percent at a monthly rate, ticked up slightly to 2.1 percent in September, raising concerns that progress toward reducing inflation in the wake of last December's

devaluation of the peso may be slowing. Consumer prices increased by 1.1 percent during the first half of October.

In part reflecting the continued weakness of the economy, Mexico's trade performance remains strong. Over the first nine months of 1995, exports were 33 percent above their year-earlier level, while imports were down almost 8 percent. As a result, the trade surplus for the January-September period registered $5.4 billion compared with a $13.6 billion deficit for the same period in 1994.

MEXICAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1994	1995				
		Q2	Q3	Jul	Aug	Sep
Real GDP	3.5	-10.5	--	--	--	--
Industrial Production (s.a.)	3.8	-11.6	--	-11.9	--	--
Unemployment Rate (%)	3.2	6.5	7.5	7.3	7.6	7.5
Consumer Prices[1]	7.1	16.1	5.9	2.0	1.7	2.1
Trade Balance[2]	-18.5	2.4	2.3	0.7	0.7	0.9
Imports[2]	79.4	17.0	17.9	5.4	6.4	6.1
Exports[2]	60.8	19.5	20.2	6.1	7.1	7.0
Current Account[2]	-28.9	0.5	--	--	--	--

1. Percentage change from previous period.
2. Billions of U.S. dollars, n.s.a.

On October 29, representatives of government (including the Bank of Mexico), business, and labor in Mexico agreed on a new economic pact for 1996. The agreement seeks to achieve economic growth of at least three percent while keeping inflation to 20 percent. Unlike the pacts concluded in previous years, which stipulated the rate of depreciation of the exchange rate band, the current pact provides for a continuation of the floating exchange rate regime in the coming year. The agreement calls for a balanced budget in 1996--a slight decline from the 0.5 percent of GDP surplus targeted for 1995--with increases in investment spending and reductions in certain business taxes being offset by reductions in

current expenditures. As with previous pacts, the current agreement specifies increases in the minimum wage--10 percent increases in December 1995 and April 1996--and in public sector energy prices--a rise of 29 percent from December 1995 through the end of 1996.

In **Argentina**, consumer prices rose 2.3 percent in October from a year earlier. Real GDP fell 3.7 percent in the second quarter from a year earlier, and industrial production continued to decline in the third quarter. The drop in economic activity, in conjunction with a consumption boom in Brazil, contributed to a rapid turnaround in Argentina's trade deficit. In the first eight months of 1995, exports rose by 40 percent over a year earlier, while imports declined by 9.1 percent. However, the trade surplus peaked in June, and Brazil's recent slowdown suggests it will contribute significantly less to Argentina's export growth in the remainder of the year.

ARGENTINE ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1994	1995				
		Q1	Q2	Jul	Aug	Sep
Real GDP	7.4	3.1	-3.7	--	--	--
Industrial Production (nsa)	2.7	3.6	-4.6	-5.0	-7.9	-9.3
Unemployment Rate (%)[2]	11.7	--	18.6	--	--	--
Consumer Prices[1]	3.9	0.8	0.3	0.4	-0.2	0.2
Trade Balance[3]	-4.0	-0.2	1.9	0.6	0.3	--
Current Account[3]	-9.9	-1.0	--	--	--	--

1. Percentage change from previous period.
2. Unemployment figures available only in May and October of each year. The figure for 1994 is the average of the two surveys.
3. Billions of U.S. dollars, n.s.a.,current account under Q1 is for the first half of 1995.

Increased uncertainty about Finance Minister Cavallo's future, the prospects of the Convertibility Law, and the weakness of the Mexican peso led to a fall of 9.3 percent in the Buenos Aires stock market between October 18 and October 26. As of November 3, the stock market had recovered about 5 percent. Gross international

reserves fell from $14.7 billion at end-September to $13.3 billion at end-October, of which $0.7 billion are dollar-denominated Bonex bonds. The decline in reserves is partly due to a $1 billion buyback of domestic dollar-denominated bonds, reflecting the government's efforts to improve banking system liquidity. The monetary base was $11.4 billion at end-October, leaving $1.9 billion in excess international reserves.

In **Brazil**, indications are that economic activity has continued the slowdown that began in the second quarter. Monthly inflation has fallen further under the stabilization program, although seasonal effects were apparently responsible for some of the decline.

BRAZILIAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1994	1995				
		Q2	Q3	Jul	Aug	Sep
Real GDP	5.7	5.8	--	--	--	--
Industrial Production (s.a.)[1]	7.8	-7.5	--	-2.8	-2.7	--
Open Unemployment Rate (%)	5.1	4.5	4.8	4.8	4.9	4.8
Consumer Prices[1]	929	6.9	3.1	2.5	1.0	1.2
Trade Balance[2]	10.5	-2.0	0.8	0.0	0.3	0.5
Current Account[2]	-1.5	-6.0	--	--	--	--

1. Percentage change from previous period.
2. Billions of U.S. dollars, n.s.a.

Brazil recorded modest trade surpluses during August and September, after sizeable trade deficits during the first half of the year. International reserves (liquidity concept) continued to climb, reaching $49 billion at the end of September, compared with $34 billion in March 1995.

In September and October, the Central Bank reduced the overnight interest rate several times in response to the weakening of the economy. Since late August, the overnight rate has fallen from 57 to 44 percent.

In **Venezuela**, 12-month consumer price inflation was 51 percent in October, essentially unchanged from September. Real GDP grew 1.1 percent during the first half from a year earlier, largely due to 7.7 percent growth in the state-owned oil sector; the private sector, however, contracted by 2.6 percent during the first half. Venezuela registered a trade deficit of $3.2 billion for the first seven months of 1995, up from a deficit of $2.4 billion during the same period in 1994, reflecting a 26 percent increase in imports and an 18 percent increase in exports.

VENEZUELAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1994	1995				
		Q1	Q2	Jun	Jul	Aug
Real GDP	-3.3	1.6	--	--	--	--
Unemployment Rate (%)	8.5	11.4	--	--	--	--
Consumer Prices[1]	70.8	9.0	12.2	2.7	2.8	3.1
Trade Balance[2]	8.0	-1.0	-1.7	-0.7	-0.5	--

1. Percentage change from previous period.
2. Billions of U.S. dollars, n.s.a.

Venezuela began talks with the IMF in late September towards a stand-by arrangement that is expected to be approved in early 1996. Since the IMF program is likely to call for a devaluation of the exchange rate, the bolivar has been under strong downward pressure. The central bank's efforts to defend the exchange rate caused international reserves excluding gold to fall to $5.8 billion at the end of September from $7 billion at the end of June. To stem a further drop in foreign reserves, the government created a committee in mid-October to oversee foreign currency import requests and stagger the disbursal of dollars. On October 25, Venezuela introduced a dual exchange rate system. The new exchange rate for travelers and credit card expenses is now determined by the implicit exchange rate set by Brady bond prices on the Caracas Stock Exchange, currently about 286 bolivars per dollar, while all other

transactions will take place at the official exchange rate of 170 bolivars per dollar.

In **China**, real GDP growth and inflation continued to slow in the third quarter. Real GDP rose 9.8 percent in the first three quarters of 1995 from the year earlier period, somewhat below its 1994 pace. Consumer price inflation registered 14.4 percent in the twelve months ending in September, continuing its steady decline from its peak of 28 percent in October 1994.

China ran a trade surplus of $16.4 billion in the first three quarters of 1994, well above its surplus of $1.2 billion in the same period a year ago. The value of exports rose 35 percent over this period, while the value of imports rose 16 percent. At the end of September 1995, China's total reserves less gold reached $71 billion, up $19 billion from the end of 1994.

CHINESE ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1994	1995				
		Q2	Q3	Jul	Aug	Sep
Real GDP[1]	11.8	10.3	9.8	--	--	9.8
Industrial Production	22.0	16.8	--	16.2	14.0	--
Consumer Prices	25.5	18.3	15.2	16.7	14.5	14.4
Trade Balance[2]	5.2	6.1	3.2	1.1	0.9	1.1

1. Cumulative from the beginning of the year
2. Billions of U.S. dollars, n.s.a.

In **Taiwan**, industrial production strengthened in the third quarter, while consumer price inflation declined. The trade surplus in the first three quarters of 1995 declined somewhat from its year-earlier level, as the value of exports rose 23 percent while imports rose 26 percent. Taiwan's foreign exchange reserves, which peaked at $100 billion in June 1995, fell to $91 billion at the end of September.

TAIWAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1994	1995				
		Q2	Q3	Jul	Aug	Sep
Real GDP	6.5	6.5	--	--	--	--
Industrial Production	6.6	2.8	5.6	5.4	8.0	3.4
Consumer Prices[1]	2.6	4.7	2.0	3.9	1.7	2.0
Trade Balance[2]	12.0	0.3	2.4	0.7	1.0	0.7
Current Account[2]	6.0	-0.5	--	--	--	--

1. Percentage change from a year earlier.
2. Billions of U.S. dollars, n.s.a.

In **Korea**, economic activity continued to expand at a robust pace during the third quarter, as the recent cyclical upturn entered its third year. Despite rapid growth, inflation remained low by historical standards: consumer prices in October were 4.4 percent higher than their year-earlier level. Monetary policy appears to have become somewhat more accommodating during the past two months, as the central bank has allowed most of the runup in short-term interest rates that occurred last fall and in the early part of this year to be reversed.

Merchandise exports rose by 33 percent during the first three quarters of this year from their year-earlier level. Imports also expanded by 33 percent, largely due to a strong expansion of business investment. Because imports began from a higher base, this contributed to a substantial deterioration of Korea's current account balance over that period.

KOREAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1994	1995				
		Q2	Q3	Aug	Sept	Oct
Real GDP	8.4	9.6	--	--	--	--
Industrial Production	10.7	13.0	--	--	--	--
Consumer Prices	5.6	4.3	4.7	3.5	4.7	4.4
Trade Balance[1]	-3.1	-1.7	-0.8	-.4	-.3	--
Current Account[1]	-4.7	-2.0	-2.1	-.9	-.7	--

1. Billions of U.S. dollars, n.s.a.

In **Russia**, monthly consumer price inflation in September and October remained at 5 percent, and the ruble-dollar exchange rate continued to fluctuate around 4500. Real GDP and industrial production during the third quarter were essentially unchanged from their year-earlier levels, following four years of sharp declines. The Central Bank reduced its benchmark refinance rate from 15 percent to 14.2 percent a month in late October.

Russia has successfully completed six monthly reviews under its IMF stand-by arrangement. Through September, the government satisfied all of the program's quantitative indicative monthly targets. Notably, the fiscal deficit for the first nine months was held to 3 percent of GDP, well below the requirements of the IMF program. The government, however, is facing increased political pressure to ease economic policies, as mid-December's parliamentary elections approach. In an effort to obtain additional fiscal financing, the government has recently taken steps to reinvigorate its cash-based privatization program.

On November 8, President Yeltsin removed Mrs. Paramonova as Acting Central Bank Chairman. Alexander Khandruyev, one of her deputies, will serve as Acting Chairman until Yeltsin chooses a permanent candidate. Russian financial markets were calm immediately following the announcement.

RUSSIAN ECONOMIC INDICATORS
(Percent change from year earlier except where noted)

	1994	1995				
		Q2	Q3	Aug	Sep	Oct
Real GDP	-15	-2	-1	-1	-1	--
Industrial Production	-21	-3	1	0	0	--
Consumer Prices[1]	10	8	5	5	5	5
Ruble Depreciation[1]	9	-3	0	0	1	0
Trade Balance[2]	11.9	2.0	--	--	--	--
Current Account[2]	0.6	-0.8	--	--	--	--

1.Monthly Rate.
2.Billions of U.S. dollars, excludes intra-FSU transactions.