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MONEY MARKET IN MARCH

Money market pressures were relatively steady in March, despite the addition this year of substantial Treasury borrowing to the massive shifts of funds customarily resulting from the payment of corporate income taxes on March 15. The reserve positions of member banks for the country as a whole came under increasing pressure through the first half of the month, but in the week ended March 20 the usual rise in float and the net release of funds from the Treasury's balances at the Reserve Banks ahead of the actual collection of taxes caused net borrowed reserves to dip sharply. Both float and the Treasury's balance changed direction once more near the end of the month, and reserve positions again tightened. Federal Reserve open market operations released reserves to the market during the first three statement weeks and absorbed reserves in the final week. Total System holdings rose by 212 million over the four-week period ended March 27.

The wide swings in country-wide reserve positions over the month were accompanied by considerable shifts in the distribution of excess reserves and borrowings between New York and the rest of the country. In general, it appeared that the area outside New York experienced more of the impact of the aggregate reserve changes, while the New York banks, although under some pressure almost continuously, were not subjected to serious strain. Chicago banks, on the other hand, were an unusually important element in the net borrowings of all member banks, largely because of the special situation preceding the April 1 assessment of personal property taxes in Cook County. In the money market, the Federal funds rate held generally at 3 per cent despite the wide swings from day to day in aggregate reserve positions, dropping appreciably on only a few days after the Treasury's cash redemption on Friday, March 22, of 1.8 billion dollars of maturing tax anticipation certificates and bills.

Treasury borrowing during the month involved the sale of 3.4 billion dollars of notes and certificates of indebtedness and a total increase of 400 million dollars in the outstanding volume of Treasury bills. The two securities which had initially been issued during the February refunding were reopened, and subscribers were awarded 2,437 million dollars of 3⅜ per cent certificates due in February 1958 and 942 million dollars of 3½ per cent notes of May 1960. Prior to the announcement of the terms on March 14, prices of outstanding notes and bonds fluctuated unevenly in anticipation of the financing. The books were open for only one day, March 18. Both new issues were heavily oversubscribed, and the success of the cash financing helped to move quotations on outstanding bonds and notes generally higher through the rest of the month.

Yields on Treasury bills moved down during most of March, reflecting in part a persistent nonbank demand. The Treasury offered 1.8 billion dollars of new bills in the first two weekly auctions of the month, but beginning with the March 18 auction reverted to simply rolling over the 1.6 billion dollars of maturing issues. After the middle of the month, reinvestment demand from holders of Treasury notes maturing on March 15 and of tax anticipation bills and certificates maturing on March 22 put further downward pressure on bill yields. Over the month as a whole, rates on the longest outstanding Treasury bills fell by 32 basis-points to 2.96 per cent.

On March 19, dealers in bankers' acceptances announced that acceptance rates would be lowered by ¼ per cent, effective the following day, which brought quotations on 90-day acceptances, for example, to 3¼ per cent bid and 3⅛ per cent offered. This reduction, the first general

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move for the market as a whole since December 7, 1956, reflected the pressure of a continuing vigorous demand for acceptances against a relatively moderate supply.

Member Bank Reserve Positions

The first half of March was characterized by a progressive increase in reserve pressures, which were only moderately relaxed during the rest of the month. Average net borrowed reserves for the four weeks ended March 27 were thus 284 million dollars, or 159 million higher than in the preceding four weeks. During much of the period there were large-scale shifts in funds, largely as a result of corporate tax payments and Treasury debt operations, and these occasioned wide fluctuations in required reserves and Treasury deposits at Reserve Banks, although special handling of tax checks served to dampen the normal intramonthly swings in float.

As a result of the heavy volume of checks written in payment of corporate taxes due on March 15, the average level of float in the March 20 statement week increased by 265 million dollars, which contributed substantially to the easing of reserve positions. However, a special effort was made by the Internal Revenue Service and at Reserve Banks to speed up the processing of tax checks, and, partly in reflection of this program, the peak in float was much less pronounced than in comparable periods of other recent years. Indeed, the rate of advance in float from the low point earlier in the period to the midmonth peak was the lowest on record for the month of March. Toward the end of the period, after the peak had been passed, the usual month-end decline in float began and in the week ended March 27 siphoned off 206 million in reserves.

Table I
Changes in Factors Tending to Increase or Decrease Member Bank Reserves, March 1957
(In millions of dollars; (+) denotes increase, (−) decrease in excess reserves)

Factor	Daily averages—week ended				Net changes
	Mar. 6	Mar. 13	Mar. 20	Mar. 27	
Operating transactions					
Treasury operations*	−177	+ 12	+171	− 50	− 44
Federal Reserve float	− 38	−271	+265	−206	−250
Currency in circulation	− 22	− 44	+ 20	+ 87	+ 41
Gold and foreign account	+ 6	+ 32	− 2	− 34	+ 2
Other deposits, etc	+173	+ 13	− 7	− 7	+172
Total	− 58	−258	+448	−211	− 79
Direct Federal Reserve credit transactions					
Government securities:					
Direct market purchases or sales	+ 41	+ 39	+130	− 13	+197
Held under repurchase agreements	+ 18	+ 27	+ 69	− 71	+ 43
Loans, discounts, and advances:					
Member bank borrowings	+ 42	+124	− 97	+ 62	+131
Other	—	+ 1	− 1	—	—
Bankers' acceptances:					
Bought outright	− 4	− 1	+ 1	− 1	− 5
Under repurchase agreements	—	—	—	—	—
Total	+ 96	+191	+102	− 22	+367
Total reserves	+ 38	− 67	+550	−233	+288
Effect of change in required reserves†	− 35	+ 66	−374	+195	−148
Excess reserves†	+ 3	− 1	+176	− 38	+140
Daily average level of member bank:					
Borrowings from Reserve Banks	730	854	757	819	790‡
Excess reserves†	428	427	603	565	506‡

Note: Because of rounding, figures do not necessarily add to totals.
* Includes changes in Treasury currency and cash.
† These figures are estimated.
‡ Average for the four weeks ended March 27.

The swings in Treasury balances at Reserve Banks, unlike those of float, were unusually pronounced during March, supplying large amounts of reserves temporarily around the middle of the month and again on March 22 and withdrawing them during the rest of the period. The balances were substantially rebuilt in the March 6 statement week from the unusually low levels to which they had fallen in the latter part of February, and in the subsequent week they declined only slightly. In the early part of the week ended March 20, however, the level dropped sharply, as balances were drawn down by quarterly interest payments on outstanding Government debt and by the redemption of the 2⅞ per cent Treasury notes that had not been exchanged in the February refunding. In addition, commercial banks were permitted until March 20 to retain in Tax and Loan Accounts 50 per cent of all tax checks of more than $10,000. Average balances rose again in the week ended March 27, absorbing 50 million in reserves, but daily levels fluctuated over an unusually wide range. Commercial banks were permitted to retain only 25 per cent of the tax checks presented for collection March 20 through 22, thus shifting large amounts of reserves to Treasury accounts at Reserve Banks. Balances were substantially reduced by the redemption on March 22 of tax anticipation bills and certificates that had not been presented in payment of corporate profits taxes, but with the rapid processing of tax checks the Treasury was able to restore its balances at Reserve Banks to a more comfortable working level by the end of the month.

The effect of these swings in float and Treasury balances in March was partly offset by changes in required reserves. This was especially marked in the week ended March 20 when an increase in required reserves absorbed an additional 374 million dollars of reserves on average, reflecting the large expansion of business borrowing around the March 15 tax date. In the March 27 statement week, about half of the reserves absorbed in the preceding week were released by a decline in required reserves, again partially offsetting the impact of changes in float and Treasury balances.

Other regular market factors had relatively small influence on reserve positions during the month, while Federal Reserve open market operations added reserves on balance, although the average level of System holdings of Government securities was reduced somewhat in the closing statement week. System operations injected reserves both through outright purchases of Government securities and through repurchase agreements with Government securities dealers, particularly in the days just preceding and immediately following the March 15 tax date.

Government Securities Market

The market for Government securities was again dominated through much of the month by actual and prospective Treasury financing operations. An announcement was made on March 4 that the Treasury would come to market on or about March 18 with a new money offering, and on March 14 the terms of the financing were made public. A total of 3.0 billion dollars was offered by reopening the two securities that had been issued in the February refunding. Investors were offered an additional 2.25 billion dollars of the 3⅜ per cent certificates due February 14, 1958 and an additional 0.75 billion dollars of 3½ per cent Treasury notes of May 15, 1960. Subscription books were open only on Monday, March 18, with payment due on March 28. Commercial banks were permitted to credit Tax and Loan Accounts for their own and their customers' subscriptions. After some initial hesitancy, immediately following the announcement, the offering was well received by the market and was heavily oversubscribed. On March 20 the Treasury announced that subscribers for more than $100,000 would be allotted 31 per cent of their bids for the eleven-month certificates and 12 per cent of their bids for the three-year notes. Subscriptions of $100,000 or less were awarded in full. With the usual overallotment, a total of roughly 3.3 billion dollars was obtained through this operation, excluding about 100 million of the new issues purchased by Treasury agencies.

Prices of Treasury notes and bonds moved irregularly through the first half of March as the market awaited an announcement of the precise terms of the new Treasury offering. Activity was quite limited during this period, but, against the background of uncertainty generated by the impending financing operation, price quotations were moved up or down on several days by as much as ⅜ of a point. Quotations on Government bonds maturing after 1960 were marked down sharply following a Treasury announcement on March 14, coincident with the release of terms on the new borrowing, that a new long-term issue was being considered in exchange for 1.5 billion dollars of Series F and G Savings bonds due to mature during the rest of the year, and this prospect continued as a dampening influence for the remainder of the month. Mixed views about the business and credit outlook—and particularly the uncertainty regarding the likely magnitude of tax borrowing—also created instability in the market and restrained the volume of trading.

The strong interest that developed in the new offerings and their good behavior in "when-issued" trading injected a firm tone generally, and moderate offerings of the new issues by banks were readily absorbed by the market. On balance, prices of bonds callable after 1962 were marked as much as $^{26}/_{32}$ higher during March, although the 3¼'s of 1978-83 and the 3's of 1995 registered moderate declines of $^{12}/_{32}$ and $^{10}/_{32}$, respectively, reflecting market expectations that the Treasury might offer new issues of long maturity. Quotations on the outstanding 3½ per cent notes of 1960 dipped by $^{5}/_{32}$ to $99^{31}/_{32}$ bid following the announcement that the issue would be reopened but quickly steadied, and the notes traded around the par level while the books were open. After the books were closed, quotations firmed and held generally at $100^{3}/_{32}$ bid over the latter part of the month. The 3⅜ per cent certificates also remained relatively firm, trading slightly below par throughout the period but well above a price that might have been considered a break-even point for banks subscribing through credit to Tax and Loan Accounts.

Yields on Treasury bills declined during March. A surprisingly vigorous corporate demand developed early in the month, despite the approach of the March 15 tax date, and easily absorbed the moderate selling of commercial banks and some corporations. Tenders in the 1.8 billion dollar auction on March 11, for example, reached a new postwar record for a regular weekly offering. Some additional downward pressure continued to be put on yields by the special demand for short-term securities associated with the April 1 tax assessment on bank deposits in Cook County, Illinois. The market was also influenced by reinvestment demand from holders of maturing tax bills and certificates and 2⅞ per cent notes that had not been exchanged in the February refunding. In the weekly bill auctions, average issuing rates fell steadily through the month. From a rate of 3.288 per cent established in the auction of February 25, average yields moved down to 3.246 per cent in the auction of March 4, to 3.238 per cent on March 11, 3.041 per cent on March 17, and 3.034 per cent on March 25. In the first two auctions of the month, the new weekly issue of Treasury bills was continued at 1.8 billion dollars, or 200 million in excess of the maturing issue, but in succeeding weeks the offering was reduced to 1.6 billion dollars.

Other Securities Markets

Yields on high-grade corporate bonds continued largely unchanged during March. For outstanding municipal issues, on the other hand, rates moved up fairly sharply early in the month, continuing the trend established in the latter part of February. Municipal bond yields leveled off thereafter, however, and declined moderately toward the end of the month. Thus over March as a whole, average yields on outstanding high-grade municipal issues, as reflected in Moody's Aaa-rated index, moved up on balance from 2.83 per cent to 2.86 per cent. Average rates on similarly rated corporate bonds at the close of the month continued at the 3.66 per cent level prevailing at the end of February.

The volume of new offerings of corporate and municipal bonds in March was again large. Public offerings of corporate bonds for new capital reached an estimated total of 615 million dollars, compared with flotations of 465 million in February. The largest single issue was the 250 million dollar offering of long-term utility bonds, which were successfully reoffered on March 26 at 4.30 per cent. A large quantity of new municipal offerings was also brought to market, although the total of 420 million dollars for the month was somewhat below the volume of new issues in either January or February. The market for municipals continued to be congested during the first part of the month, and as a result a number of syndicates were terminated, while offering prices were substantially reduced for several other recent issues. Subsequently, however, renewed demand developed, and most new issues were quickly taken down. Dealer portfolios fell moderately over the month.

Member Bank Credit

Total loans at weekly reporting member banks expanded sharply during the four weeks ended March 20 (see Table II), reflecting the extensive business borrowing associated with quarterly payment of corporate income taxes. The advance of 1,367 million dollars in total loans was smaller, however, than in the corresponding period a year earlier when they rose by 2,092 million dollars. Business loans accounted for the great bulk of the expansion this year, rising by 1,239 million, but the increase fell short of last year's record advance by 271 million, or 18 per cent. Security loans and loans to "all others" (largely consumers) also rose, while real estate loans and agricultural loans declined.

Loans were increased on balance to each category of business borrowers except commodity dealers. For each group except sales finance companies and the food, liquor, and tobacco group, however, the expansion was smaller than in the comparable period of 1956. The increase in borrowing by sales finance companies was especially pronounced, amounting to 376 million in the four weeks ended March 20, compared with 168 million a year earlier.

Total investments at weekly reporting member banks rose by 311 million during the four weeks ended March 20, compared with an increase of 325 million dollars a year earlier. Holdings of Government securities advanced by 181 million on balance, as large increases in the weeks ended March 13 and March 20 more than offset net reductions in the preceding two weeks. Holdings of other securities increased by 130 million dollars over the period.

Table II

Weekly Changes in Principal Assets and Liabilities of the Weekly Reporting Member Banks

(In millions of dollars)

Item	Statement weeks ended				Change from Dec. 26, 1956 to Mar. 20, 1957
	Feb. 27	Mar. 6	Mar. 13	Mar. 20	
Assets					
Loans and investments:					
Loans:					
Commercial and industrial loans	− 39	+136	+ 403	+ 739	+ 301
Agricultural loans	+ 6	− 6	− 3	− 4	− 35
Security loans	+ 66	+ 39	—	+ 23	− 446
Real estate loans	− 4	− 26	+ 4	+ 6	− 106
All other loans (largely consumer)	+ 5	− 10	+ 21	+ 40	− 203
Total loans adjusted*	+ 31	+108	+ 423	+ 805	− 662
Investments:					
U.S. Government securities:					
Treasury bills	+ 35	−210	+ 119	+ 393	− 173
Other	−121	+ 19	+ 25	− 79	− 491
Total	− 86	−191	+ 144	+ 314	− 664
Other securities	+ 24	+ 20	+ 111	− 25	+ 148
Total investments	− 62	−171	+ 255	+ 289	− 516
Total loans and investments adjusted*	− 31	− 63	+ 678	+1,094	−1,178
Loans to banks	+335	−123	+ 172	− 75	+ 91
Loans adjusted* and "other" securities	+ 55	+128	+ 534	+ 780	− 514
Liabilities					
Demand deposits adjusted	+156	−579	+1,114	−1,201	−2,510
Time deposits except Government	+ 53	+114	+ 194	+ 91	+ 934
U. S. Government deposits	+ 37	−547	− 51	+2,106	+ 681
Interbank demand deposits:					
Domestic	−149	+370	− 121	+ 142	− 944
Foreign	+ 6	+ 8	− 26	+ 31	− 135

* Exclusive of loans to banks and after deduction of valuation reserves; figures for the individual loan classifications are shown gross and may not, therefore, add to the totals shown.

INTERNATIONAL MONETARY DEVELOPMENTS

Monetary Trends and Policies

United Kingdom. Interest rates, which had been declining since last December, moved upward somewhat in March. The average Treasury bill tender rate, which had fallen to 4.00 per cent on March 1, rose slightly at the second tender of the month and stood at 4.10 per cent on March 29. Government bond yields also increased during March, the yield of 2½ per cent Consols rising to 4.66 per cent on March 29 from 4.55 per cent at the end of February.

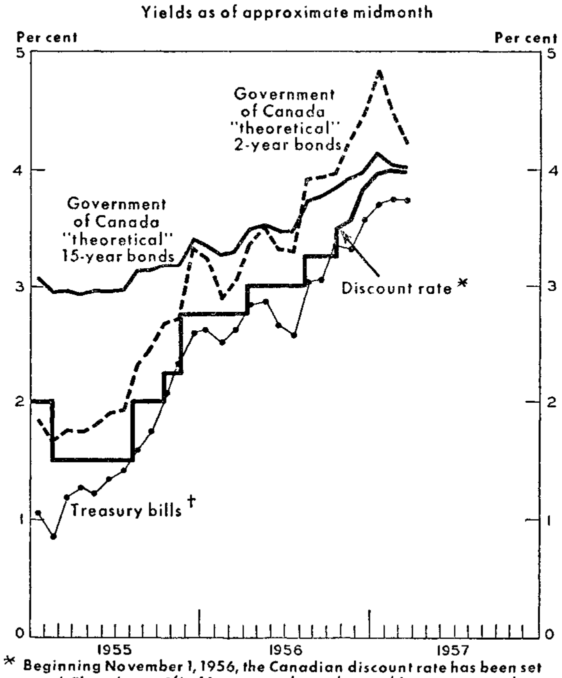
In the five weeks to February 20 the London clearing banks showed near-record declines in both deposits and liquid assets, owing to the substantial reduction in floating debt made possible by the seasonal budget surplus and by the increased market sales of government bonds preceding last month's reduction in the discount rate. The amount of tender bills outstanding has fallen by almost 700 million pounds in the first eleven weeks of this year, compared with a decline of about 300 million a year ago; most of this reduction in the floating debt took place prior to the lowering of the discount rate on February 7. The decline in liquid asset holdings, together with a more-than-seasonal increase in advances, put the banks' liquidity under greater pressure than has been experienced in many months; by February 20 the clearing banks' average liquidity ratio had fallen from 37.4 to 33.6 per cent, the lowest since last June and slightly less than in February 1956. Preliminary reports indicate that these trends continued in the four weeks to March 20, when the average liquidity ratio of the London clearing banks was further reduced to about 32.6 per cent.

The latest analysis of advances by the British Bankers' Association shows an increase of nearly 70 million pounds in the three months to February 1957, at which time bank loans were higher than a year previous for the first time since the banks were requested to reduce their advances in July 1955. While there was a substantial decline in the recourse to bank loans by the public utilities, advances to the private sector rose by more than 100 million pounds; nearly all classes of borrowers increased their loans, but about half of the net increase in advances went to the iron and steel and engineering industries, while the textile industry, the financial sector, and personal and professional borrowers also increased their borrowing substantially.

Canada. The decline in interest rates on government bonds generally leveled off in March, but the fall in bond yields that began early in February was extended to the Treasury bill market. The recovery in the government bond market had brought the yields on longest-term issues down 0.10 to 0.20 percentage points to the levels of late December, while the fall in interest rates on short-term bonds was much steeper, amounting to as much as 0.75 percentage points on maturities of less than two years (see chart). The differential between long and short-term bond yields was thus substantially narrowed; the more marked fluctuation in the short end of the market was also characteristic of the period of rising interest rates from mid-1956 to January of this year. The Treasury bill rate declined during March for the first time since November; on March 28 the average tender rate stood at 3.70 per cent. Along with these changes in the interest rate pattern, the chartered banks have added substantially to their government bond portfolios since early February; however, it should be noted that a major part of the very large reported increase in the banks' bond holdings during the last week in February was attributable to a change to valuing their portfolios at "amortized value" rather than at "not exceeding market value" as previously.

The liquidity of the chartered banks has continued at the comfortable level attained in February, and the banks have not added to their Treasury bill holdings; business loans continued what appears to be a more-than-seasonal decline. After discussions with the Bank of Canada, the chartered banks have agreed in principle to approve a total of not less than 150 million dollars of new housing loans in 1957; this is 10 million less than the amount of new housing loans approved last year. The anti-inflationary fiscal policy of the Canadian Government, which has lent powerful support to the policy of monetary restraint, is to continue in the fiscal year beginning April 1; last year there was a budget surplus of 282 million dollars and, despite

CANADIAN INTEREST RATES
Yields as of approximate midmonth



* Beginning November 1, 1956, the Canadian discount rate has been set each Thursday at 1/4 of 1 per cent above the week's average tender rate for Treasury bills. The rate shown on the chart during this period is for the same date as that for Treasury bills, i.e., the Thursday nearest the 15th of each month.
† Average tender rate for three-month Treasury bills.
Source: Bank of Canada, Statistical Summary.

some tax reductions and an increase in welfare payments, the new budgetary estimates call for another sizable surplus in 1956-7.

Japan. The Bank of Japan raised its basic discount rate from 7.3 to 7.665 per cent, effective March 20; the last previous change in the basic discount rate was an increase of about 1½ per cent in August 1955.[1] The increase in the discount rate was made simultaneously with an alteration in Japan's progressive discount rate system, reportedly intended to ease the seasonally very tight conditions on the money market; in recent months short-term interest rates have risen above 9 per cent. While the supply of funds has currently been reduced by unusually heavy tax payments connected with the general business prosperity, the underlying demand for credit has been swollen by an investment boom, the increased need for working capital, and the financing of a growing level of imports. The current money market tightness thus also reflects the rapid expansion of economic activity in Japan, which has been accompanied in the past few months by some signs of a building-up of inflationary pressures. The rise in industrial production of more than 18 per cent last year has strained capacity in several basic industries where supply bottlenecks have appeared, and unemployment has been reduced substantially. Very high levels of private investment in plant and equipment appear to be a major factor in the current expansion. That this expansion is putting heavy pressure on available resources is especially evidenced in a rise last year of almost 9 per cent in wholesale prices for producer goods; although consumer goods prices rose much less steeply, consumption has recently shown a marked upward trend, and in the past the retail price level has followed the wholesale price trend. The rise in demand has also been reflected in the large increase in imports, which has exceeded a substantial rise in exports. While there was still a surplus of nearly 300 million dollars' equivalent in the current account of the balance of payments last year (including United States special procurement), it was almost 200 million less than in 1955. The rapid expansion of economic activity has been accompanied by a substantial increase in bank credit; the rise in bank loans last year was three times as great as in 1955. In the light of these developments, the Bank of Japan declared in its *Monthly Review* for February that the "execution of a flexible monetary policy will constitute a major problem during the year 1957".

[1] The Bank of Japan maintains a progressive discount rate system under which the discount rate on commercial bills is the lowest rate at which the commercial banks can borrow from the central bank; other categories of central bank credit are subject to higher rates. Moreover, each bank can borrow only a certain maximum (determined by a complex formula based on the assets and liabilities of each bank) at the lowest rates, and must pay a higher rate for additional accommodation.

Latin America. Several countries have taken measures to tighten monetary policy in the past few months. In *Ecuador,* the Monetary Board at the end of December raised to a uniform 5 per cent the rate for central bank rediscounts and advances to the private banks; previously the rate had ranged from 3 to 5 per cent. At the same time, the maximum permissible rate on agricultural loans was raised to 9 per cent from 8, but the maximum rates on industrial and commercial loans of 9 and 10 per cent, respectively, were left unchanged. In *Bolivia,* a new supplementary reserve requirement designed to prevent additional excessive credit expansion was established in January as part of the government's stabilization program. The commercial banks and the banking department of the central bank must now maintain a reserve of 50 per cent against deposits in excess of the December 31, 1956 level; not only is this higher than the regular 40 per cent reserve requirement, but reserves are also defined in a more restrictive manner—only vault cash and sight deposits at the central bank qualify for the supplementary reserve requirement. In *Chile,* the central bank raised its progressive rediscount rate scale sharply in January; the rate was increased to 6 per cent from 4½ for those banks whose borrowing is equal to less than 50 per cent of their capital and reserves, progressive rates ranging up to 11 per cent are to be charged on rediscounts up to 100 per cent of the borrowing banks' capital and reserves, and the rate for rediscounts exceeding 100 per cent is to be equal to the borrowing banks' charge on the paper offered for rediscount. In other measures to restrict credit in Chile, the central bank has increased the interest rate on its own operations with the public to 14 per cent from 12, and has set monthly limits on credit expansion to prevent commercial bank loans from rising more than about 13 per cent in the first half of this year, which is substantially less than during the first six months of 1956.

Exchange Rates

American-account sterling moved within a relatively narrow range on either side of $2.79¾ during the first part of March, as good commercial demand at times overcame the depressing influence of the unsettled Middle East situation. In the latter part of the month, the rate moved lower, largely because of labor developments in Britain. The quotation declined to 2.78^{31}/_{32}$ on March 18, following the strike in Britain's shipbuilding industry, but shortly thereafter commercial demand for sterling reappeared and the rate improved as prospects brightened for an early settlement. When settlement negotiations reached a temporary impasse, however, and strikes spread, the rate again moved lower, declining to $2.78¾ on March 29.

In the forward market, discounts on three and six months' sterling narrowed to $^{1}/_{16}$ and $1\frac{7}{16}$ cents early in the month as forward sterling met with good commercial demand. After widening to as much as $1\frac{1}{8}$ and $2\frac{5}{32}$ cents shortly after the midmonth, the discounts again tended to narrow as demand for fairly substantial amounts of forward sterling again came into the market. At the month's end, the discounts stood at $^{27}/_{32}$ and $1\frac{25}{32}$ cents.

Good offerings from the Continent and reduced demand on the part of sugar interests led to generally lower rates for transferable sterling during March. After dropping to as low as $2.7580 on March 19, the rate recovered somewhat when there was some covering of short positions and a limited commercial demand reappeared. On March 29 transferable sterling was quoted at $2.7605. Securities sterling declined from an opening quotation of $2.62 to as low as $2.58½ on March 13 in a rather inactive market; during the latter part of the month the rate recovered somewhat, reflecting interest in certain British stocks, and on March 29 stood at $2.60¼.

The Canadian dollar moved to a new current high of $1.04¾ during March as it met with continued good investment demand from the United States, Britain, and the Continent. Substantial issues, both actual and proposed, of new Canadian securities were the major factor in the further strengthening of the Canadian dollar, although demand on the part of grain buyers was evident on occasion. On March 29 the Canadian dollar was quoted at $1.04\frac{9}{16}$.

CURRENT BUSINESS TRENDS

Since late in 1956, the United States economy has been marked by an essentially sideways movement in the total volume of activity, while the rising trend in wholesale prices has decidedly slackened. Following the strong advance in business activity that was registered last autumn, the less exuberant pace during the past few months has raised certain doubts about the economy's short-term prospects and even suggested to some observers that a general business downturn may be getting under way. Equally plausible interpretations have been advanced, however, to suggest that this is a natural and welcome breathing space, a period for correction and realignment among the many sectors of the economy after an unusually rapid upsurge in some of them. The latter views would, instead of fearing a downturn, express concern lest premature efforts to stimulate greater activity might interfere with the readjustments needed in costs and productivity, if there is to be hope that inflation can be avoided when expansion is resumed. No clear-cut choice between these interpretations, nor explicit support for any other views, can appropriately be expressed in this *Review,* but the importance of the questions which they suggest clearly calls for a close look at the recent record.

In large measure, the lessening of buoyancy in the economy thus far in 1957 seems to be linked with a slackened pace of inventory build-up. In turn, this has reflected easing tendencies or less-than-expected strength in some types of final demand. Thus, business spending for new plant and equipment has been increasing much more moderately than during most of last year, while the rate of housing starts has continued to drop, and total sales at retail stores have done little more than "hold their own" in recent months. A strong resurgence of new car sales, which was widely anticipated after last year's decline, has failed to develop thus far. Nevertheless, final demand has remained strong in the aggregate, and has continued to rise in such areas as government spending (Federal as well as State and local) and consumer outlays for services. Moreover, while the more comprehensive measures of wholesale prices have shown smaller increases or even slight declines in recent months, the consumer price index has continued to inch upward, and some of the factors that contributed to last year's increases—at both the retail and wholesale levels—still appear to be exerting upward pressure on the price structure.

Changing Patterns of Production and Employment

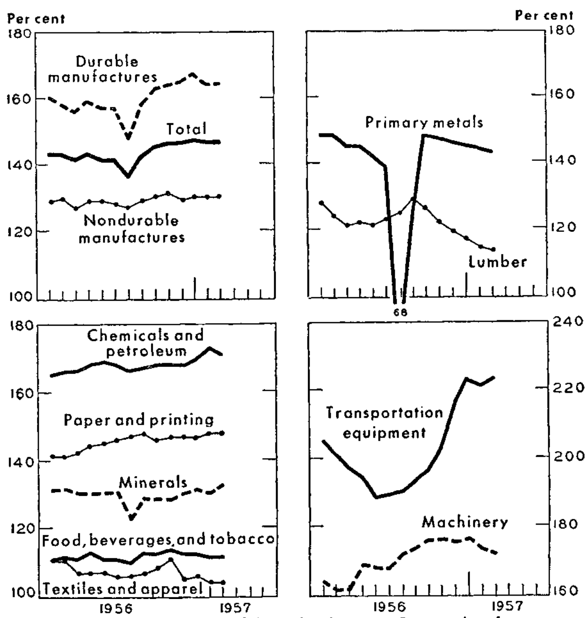
During the quarter just ended, the total output of goods and services seems to have made only a modest further advance, following the 10 billion dollar rise in gross national product to a seasonally adjusted annual rate of 424 billion in the final quarter of 1956. Moreover, in *real* terms, there has probably been little change in the aggregate volume of activity since last October or November.

This shift from rapid advance to near stability has stemmed from a number of related causes. Retail sales, for example, which were on a moderately (though irregularly) rising trend from spring through mid-autumn of last year, have increased only slightly since November, after seasonal adjustment. The rise in business outlays for new plant and equipment has slackened appreciably in the past two quarters, partly no doubt because further rapid increases are less likely to be sustained once record rates have already been reached. At the same time, the downward trend in residential building activity, after showing some signs of steadying in the middle of 1956, has become more pronounced. In turn, the reduced rate of home construction seems to have had some adverse effect on sales and output of household durable goods. Reflecting all of these developments but also overshadowing them because of its characteristically severe immediate impact, the rate of inventory build-up, insofar as that can adequately be appraised from available data, appears to have been curtailed sharply. There has been no evidence of widespread liquidation, however, with dramatic "unloading" limited mainly to a few types of durable consumer goods. In only a few instances does there seem to have been a significant involuntary piling-up of unsold goods.

The economy's recent sideways movement has perhaps been most clearly evident in the Federal Reserve index of industrial production. As may be seen in Chart I, the seasonally adjusted index remained at 146 per cent of the 1947-49 average from October through February, except for December when it reached 147 per cent. This plateau followed several months in which output had risen sharply, mainly as a result of the poststrike recovery in steel and related industries, the continued advance in machinery output, stepped-up production of automobiles, and a temporary upswing in textiles and apparel.

The rise in transportation equipment output continued strongly through the end of 1956, as automobile production advanced much more than seasonally after the model change-over period, and production of other types of transportation equipment increased further. Since December, however, there has been little change in this index; automobile sales failed to match the industry's earlier expectations, as selective buying apparently indicated some consumer disappointment with the new models, and producers have curtailed assembly schedules in order to avoid excessive inventories at the dealer level. Machinery output showed little change in late 1956 and then decreased somewhat in early 1957, reflecting the smaller rise in production of industrial equipment and actual declines in output of certain consumer durables (such as household appliances and television sets) that are included in this group. Some of these reductions were quite sharp, but they seem to have been undertaken primarily to correct overextended inventory positions rather than because of any drastic weakening in final consumer demand. At the same time, output of primary metals gradually edged downward after October. Copper production was reduced considerably, and the sharply rising trend in steel output leveled off and was followed by declines. Many steel-using firms completed rebuilding their inventories, while some others (in the auto industry, for example) reportedly decided to carry a smaller volume of stocks in relation to output, and some firms cut back their steel orders because of production declines. Lumber production, meanwhile, continued to decrease, largely as a result of the further reduction in residential building.

Chart I
INDUSTRIAL PRODUCTION AND SELECTED COMPONENTS, 1956-57
Seasonally adjusted, 1947-49=100



Source: Board of Governors of the Federal Reserve System; data for February 1957 are preliminary.

Among nondurable goods, textile and apparel output also has declined from the level reached late last autumn, but most other types of production have been sustained at high levels. Substantial increases were recorded for output of chemical and petroleum products, while the rate of mineral extraction (notably of crude oil) also staged a marked advance, achieving a new record in February. In part, this reflected the step-up in foreign demand for oil and the need to replace supplies imported from the Middle East, following the disruption of Suez Canal traffic.

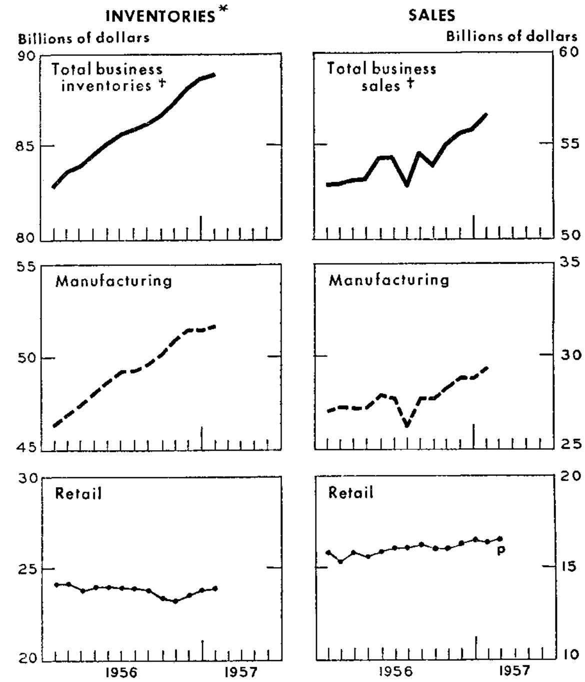
Broadly paralleling the steadier trend in production as a whole during recent months, employment aggregates also have shown little significant change after seasonal adjustment. Census Bureau estimates have indicated a somewhat larger-than-seasonal decrease in total employment since last summer's all-time record, but much of this weakening has been in the agricultural sector; the Bureau of Labor Statistics series on nonfarm employment has shown almost uninterrupted (though small) increases on a seasonally adjusted basis, reaching a new peak in February despite a slight decrease in manufacturing employment since December. At the same time, estimated unemployment has remained within the range prevailing since the spring of 1955.

The absence of any significant rise in unemployment during the past several months, which might have been expected as a consequence of normal labor force growth during a period of little change or even a slight easing in total employment, apparently reflects the fact that the labor force actually has contracted somewhat since last summer. Although the decrease has occurred primarily in the agricultural sector, for which estimates are typically subject to wide fluctuation, it is also apparent that the nonfarm labor force has not risen further (and may even have decreased slightly) following an unusually rapid rise from early 1955 through much of 1956. In the earlier period there were particularly marked increases in the number of part-time workers and others whose participation in the employment market tends to vary with general business conditions. Because of the lessening buoyancy in the economy's expansion during recent months, fewer persons entered the labor market and some who had previously sought only temporary employment may have withdrawn.

Inventory Trends

Although detailed inventory statistics are available only through the end of January, the latest data already reveal the slower growth in stocks that has apparently been so important in altering the recent business climate. While inventory data are generally somewhat inexact, they do provide reasonably reliable approximations of the major changes in this important component of the gross national product. As shown in Chart II, the estimated book value of total business inventories rose by only 200 million dollars in January, after seasonal adjustment, or at less than half of the average rate in the several preceding months. The January increase was estimated to be the smallest since early 1955 and, because rising prices account for some of the change, the physical volume of inventories may actually have shown no rise at all.

Chart II
BUSINESS INVENTORIES AND SALES, 1956-57
Seasonally adjusted



p Preliminary.
* End-of-month figures.
† Includes wholesale as well as retail and manufacturing trade.
Source: United States Department of Commerce

During 1956, accumulation was mainly at the manufacturing level, especially in the machinery industry and other durable goods lines. But in December and January there was almost no change in seasonally adjusted stocks of manufacturers, as the holdings of machinery producers and of metal-product and transportation-equipment firms (which had also been rising sharply) showed a slight decline for the two-month period. Although the book value of manufacturers' inventories did increase in February, the rise was quite small compared with those registered last autumn. On the other hand, retail inventories have been rising moderately since last October in contrast to the slight downtrend during much of 1956. Primarily, this has reflected the greater-than-seasonal rebuilding of automobile dealers' inventories from the unusually low level at the time when the new models were introduced last autumn. Auto dealers' stocks of new cars have climbed further since the end of January, but are still lower than in early 1956. At the same time, however, distributors of certain household durable goods hold much larger inventories than a year ago and have cut back their orders accordingly.

Even though total business inventories have grown to record size, they do not seem to be unduly large in relation to sales. Indeed, since the middle of last year the growth in stocks has been paralleled by sales increases (see Chart II), so that the ratio of end-of-month stocks to sales during the month, at 1.57 for January, was only slightly higher than a year earlier and was slightly lower than last June. Of course, if final sales were to weaken, then inventory levels that currently seem to be "in line" would quickly become burdensome, but the signs of slower accumulation in recent months are perhaps a reassuring indication of caution on the part of many businessmen.

Underlying Shifts in Demand

The current business scene bears some resemblance to the picture a year ago, in that offsetting increases and declines have produced a state of rough balance in the economy. The particular elements of strength and weakness, however, have been quite different in the two periods. Thus, business spending for new plant and equipment, shown in Chart III, was rising steeply throughout most of 1955 and 1956, but has advanced much more slowly in the past two quarters. Although capital outlays are scheduled to continue rising during the April-June period, results of a recent survey by the United States Department of Commerce and Securities and Exchange Commission suggest no further increase for the second half of the year.

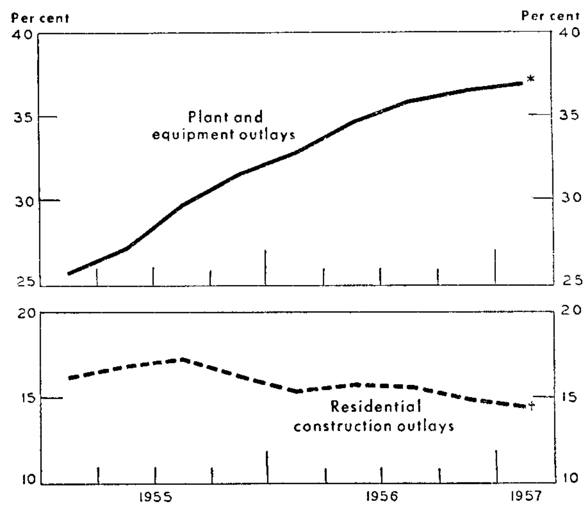
According to this survey, which was taken in late January and February, plans for all of 1957 call for plant and equipment outlays of 37.4 billion dollars—a rise of 6½ per cent over 1956, compared with last year's 22 per cent advance. In some industries, the increase in capital outlays for 1957 is scheduled to be as large or even larger than the expansion that occurred in 1956. (Most notable is the step-up planned by public utilities.) But in some other cases, such as the building of suburban shopping centers and other commercial construction, there may have been temporary overexpansion, and outlays this year are expected to be considerably lower than in 1956. Cutbacks are also planned by automobile producers, textile product manufacturers, and firms producing some types of building materials—industries where demand and production either declined or showed only a slight advance last year. Moreover, as already noted, the sheer size of the current rate of investment suggests that the economy may be nearing some limits upon its digestive capacity for absorbing further marked increases. In view of the long-term tendency for investment programs to be "bunched" together, sharp changes in the rate of capital expenditure growth are hardly surprising.

While the rise in business investment spending has been slackening, residential construction activity has continued the downtrend that has been in process, except for a brief interruption in mid-1956, since the latter part of 1955. Indeed, because of cost increases, the decline in housing outlays (shown in Chart III) does not fully measure the decrease in actual construction activity. The number of private nonfarm housing units started in February was at a seasonally adjusted annual rate of about 900,000, the lowest rate in several years (last year's total was 1.1 million). As was the case in 1956, the continued decline in housing starts this year has been concentrated in homes financed with Government-underwritten mortgages, on which maximum interest rates are set by law or Federal regulation. With business borrowers competing so strongly for funds, the guaranteed mortgages have become less and less attractive to investors.

Last December, the Federal Housing Administration (FHA) raised from 4½ to 5 per cent the maximum interest rate that may be charged on mortgages that it will insure, but the effect thus far on the total housing picture remains unclear. While the increased rate did improve somewhat the competitive position of FHA-insured mortgages, it seems to have made the mortgages guaranteed by the Veterans Administration an even less attractive investment. The high rate of mortgage purchases since last November by the Federal National Mortgage Association (FNMA) also seems to have supported home construction to only a limited degree, although the decline in such activity might well have been steeper in the absence of FNMA purchases. Advance indicators, such as the number of applications for Federally underwritten mortgages, do not suggest any early or dramatic upturn in home building, but some observers feel that the decline is not likely to proceed much further. This has been based partly on an anticipation of further Federal action to stimulate residential building activity. (Of course, it is still too early to observe any significant effects from the reduction in downpayment requirements on FHA-insured mortgages, announced at the end of March.) In addition, the view has been expressed that rising incomes may sustain demand while mortgage credit may become more readily obtainable if business demands for additional capital press less strongly against supplies of funds.

In assessing the business outlook for 1957, many analysts had counted on a powerful resurgence of new car sales to offset the effects of an expected slowdown in busi-

Chart III
OUTLAYS FOR PLANT AND EQUIPMENT AND FOR HOUSING, 1955-57
Seasonally adjusted annual rates



* Preliminary estimate for first quarter of 1957.
† Estimated on basis of January and February 1957 data.
Sources: United States Department of Commerce, Department of Labor, and Securities and Exchange Commission.

ness investment expansion and a further decline in residential construction. Auto sales did in fact show some improvement on a seasonally adjusted basis, when new models were introduced in the autumn, but the gain has apparently not been extended into 1957. Daily sales rates of new cars from January through mid-March averaged about 5 per cent below a year earlier, although total retail sales of automotive goods have been running somewhat higher than a year ago as a result of price increases and sales gains for some other automotive items. Despite the relatively modest and somewhat disappointing sales performance for new cars, however, developments in the automobile industry have not been exerting the major downward force on the economy that they did a year ago. At that time, dealers held record inventories of new cars and output was curtailed drastically as it became apparent that the usual spring upturn in sales was not developing. This year, many observers still expect some improvement in coming months. According to recent press reports, the automobile industry is scheduling production for the April-June quarter at a rate some 10 per cent lower than in the first three months of the year, but about 10 per cent higher than in the second quarter of 1956.

Meanwhile, certain other consumer "hard" goods industries (such as television set manufacturing) recently have been undergoing adjustments somewhat similar to those in the automobile industry last year; production has been cut back severely in order to reduce inventories that were amassed because of overoptimistic sales expectations. For the most part, however, sales of consumer goods have been well maintained, showing substantial increases over year-earlier figures that are only partially attributable to higher price tags. At the same time, outlays for a broad range of consumer services have apparently continued to rise vigorously, although this rise, too, has been partly dissipated in price advances. Preliminary results of the latest annual survey of consumer finances and expectations, published last month by the Board of Governors of the Federal Reserve System, indicate that consumers continue to be in a fairly optimistic frame of mind, both with regard to their own financial prospects and the outlook for the economy as a whole. Plans to buy durable goods were reported with about the same frequency as a year ago.

While the rate of business investment in inventories has declined and the rise in final demand from business and consumers has slackened since late 1956, government expenditures for goods and services have maintained a firm upward trend. The rise in State and local spending has been particularly evident in the new records set for outlays on highways, schools, and other facilities. Total public construction outlays in the first two months of this year averaged some 10 per cent higher (after seasonal adjustment) than in the first quarter of 1956 and about 7 per cent above the rate in the final quarter. Federal spending also has been running considerably ahead of the late 1956 and year-ago rates; in view of rising costs and increasingly complex defense requirements, a continued high rate of Federal spending seems assured.

Price Developments

Price trends in wholesale markets have been mixed in recent months, but have generally displayed the same "leveling-off" tendency that has been evident for over-all business activity. Thus, the index of wholesale industrial prices advanced from mid-January to mid-February by the smallest margin in several months, and this increase was largely a result of higher fuel costs; actually there were about as many declines as increases among major groups of prices. Moreover, the total index of industrial prices appears to have remained unchanged or possibly even declined slightly since mid-February, a development that was foreshadowed by the substantial drop from early December through February in prices of some industrial raw materials. These declines, particularly the sharp reductions in metal scrap prices, were closely related to the easing in supply conditions and the decreased rate of inventory build-up that has been evident in recent months.

Average farm prices have remained above their year-ago level, but by a narrower margin than in late 1956, since the recent trend has been sideways, in contrast to the strong rise experienced early last year. Acreage reductions, partly in connection with the "soil bank" program, are expected to exert a strengthening influence on some agricultural prices this year, although these effects may be offset because of the lower Federal price supports recently announced for a number of basic crops.

Even though wholesale prices have not maintained their earlier upward trend, average consumer prices continued to set new monthly highs at least through February. In part, the recent further advance in the consumer price index may be attributed to continued increases in service costs, which have been on a rising trend for a number of years. But retail costs of food, housefurnishings, and fuel, as well as a number of other goods, have also increased since the end of 1956. To some extent, these recent increases may be a delayed result of markups at the wholesale level, and if wholesale costs of consumer goods continue to register little change then prices charged to consumers for these items may also tend to level off. This would not follow necessarily, however, since retail prices also depend on distribution costs and retailers' margins.

Moreover, notwithstanding the many indications of a steadier trend in average wholesale prices, some of the factors that contributed to last year's increases are still present in modified form. Aggregate demand remains high and some industries have continued to operate at rates close to capacity (producers of heavy steel plate and structural shapes, for example). Wages are scheduled to rise during coming months in a number of key industries, and this may tend to set a pattern for the economy at large, although productivity gains might offset these labor-cost increases to a greater extent than in 1956. In addition, even though competition remains keen over wide areas of the economy, producers and distributors are striving to maintain and improve upon profit margins—which in some industries have narrowed considerably in relation to sales during the past year.

Conclusion

The course of business since the final months of 1956 strongly suggests that there has been no significant over-all expansion in the economy thus far in 1957. It is not by any means clear, however, that recent developments represent a prelude to recession, or that the upward price pressures in evidence throughout 1956 have fully abated. Contrariwise, there can be no positive assurance that the economy's expansion will shortly be resumed. It is nonetheless encouraging that much of the recent ebbing of buoyancy in total activity appears to be attributable to a lessened rate of inventory accumulation, while aggregate final demand has been maintained at an unprecedentedly high level.

SELECTED ECONOMIC INDICATORS
United States and Second Federal Reserve District

Item	Unit	1957		1956		Percentage change	
		February	January	December	February	Latest month from previous month	Latest month from year earlier
UNITED STATES							
Production and trade							
Industrial production*	1947-49= 100	146*p*	146	147	143	#	+ 2
Electric power output*	1947-49= 100	224	226	220	213	− 1	+ 5
Ton-miles of railway freight*	1947-49= 100	—	102*p*	112	108	− 9	− 9
Manufacturers' sales*	billions of $	29.2*p*	29.2	28.7	27.2	#	+ 7
Manufacturers' inventories*	billions of $	51.8*p*	51.5	51.4	46.9	+ 1	+10
Manufacturers' new orders, total*	billions of $	28.2*p*	28.9	28.8	27.6	− 2	+ 2
Manufacturers' new orders, durable goods*	billions of $	13.9*p*	14.4	14.5	14.1	− 3	− 1
Retail sales*	billions of $	16.5*p*	16.4*p*	16.5	15.3	+ 1	+ 8
Residential construction contracts*	1947-49= 100	—	n.a.	n.a.	318	n.a.	n.a.
Nonresidential construction contracts*	1947-49= 100	—	297	311	298	− 5	− 3
Prices, wages, and employment							
Basic commodity prices†	1947-49= 100	88.9	91.7	92.9	88.9	− 3	#
Wholesale prices†	1947-49= 100	117.0*p*	116.9	116.3	112.4	#	+ 4
Consumer prices†	1947-49= 100	118.7	118.2	118.0	114.6	#	+ 4
Personal income (annual rate)*	billions of $	—	335.2*p*	334.0	317.1	#	+ 6
Composite index of wages and salaries*	1947-49= 100	—	154*p*	154	146	#	+ 5
Nonagricultural employment*	thousands	52,151*p*	52,063*p*	52,072	51,127	#	+ 2
Manufacturing employment*	thousands	16,960*p*	17,030*p*	17,080	16,879	#	#
Average hours worked per week, manufacturing†	hours	40.2*p*	40.1	41.0	40.5	#	− 1
Unemployment	thousands	2,881	2,940	2,479	2,914	− 2	− 1
Unemployment‡	thousands	3,121	3,244	n.a.	n.a.	− 4	n.a.
Banking and finance							
Total investments of all commercial banks	millions of $	72,960*p*	73,660*p*	74,450*p*	75,810	− 1	− 4
Total loans of all commercial banks	millions of $	89,420*p*	89,010*p*	91,240*p*	82,540	#	+ 8
Total demand deposits adjusted	millions of $	106,780*p*	109,210*p*	110,650*p*	105,590	− 2	+ 1
Currency outside the Treasury and Federal Reserve Banks*	millions of $	30,811*p*	30,916	30,970	30,427	#	+ 1
Bank debits (337 centers)*	millions of $	81,175	82,754	76,576	76,852*r*	− 2	+ 6
Velocity of demand deposits (337 centers)*	1947-49= 100	143.8*p*	141.3	138.1	131.9	+ 2	+ 9
Consumer instalment credit outstanding†	millions of $	—	31,298	31,552	28,915	− 1	+ 8
United States Government finance (other than borrowing)							
Cash income	millions of $	7,427	4,886	5,899	7,089	+52	+ 5
Cash outgo	millions of $	6,802	5,599	7,448	5,600	+21	+21
National defense expenditures	millions of $	3,968	3,651	3,448	3,075	+ 9	+29
SECOND FEDERAL RESERVE DISTRICT							
Electric power output (New York and New Jersey)*	1947-49= 100	159	163	155	156	− 2	+ 2
Residential construction contracts*	1947-49= 100	—	n.a.	n.a.	252	n.a.	n.a.
Nonresidential construction contracts*	1947-49= 100	—	n.a.	n.a.	332	n.a.	n.a.
Consumer prices (New York City)†	1947-49= 100	115.9	115.6	115.5	112.1	#	+ 3
Nonagricultural employment*	thousands	7,804.8*p*	7,856.3	7,860.2	7,785.7	− 1	#
Manufacturing employment*	thousands	2,662.1*p*	2,696.0	2,698.3	2,687.5	− 1	− 1
Bank debits (New York City)*	millions of $	74,483	74,233	65,674	63,792	#	+17
Bank debits (Second District excluding New York City)*	millions of $	5,255	5,470	5,070	5,045	− 4	+ 4
Velocity of demand deposits (New York City)*	1947-49= 100	191.6	183.6	174.8	161.1	+ 4	+19
Department store sales*	1947-49= 100	115	119	116	105	− 3	+10
Department store stocks*	1947-49= 100	132	131	131	124	+ 1	+ 6

Note: Latest data available as of noon, April 1, 1957.

p Preliminary. *r* Revised.
n.a. Not available.
* Adjusted for seasonal variation.
† Seasonal variations believed to be minor; no adjustment made.
‡ New basis. Under a new Census Bureau definition, persons laid off temporarily and those waiting to begin new jobs within thirty days are classified as unemployed; formerly these persons were considered as employed. Both series will be published during 1957.
\# Change of less than 0.5 per cent.

Source: A description of these series and their sources is available from the Domestic Research Division, Federal Reserve Bank of New York, on request.