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CONFIDENTIAL (FR)

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

By the Staff
Board of Governors
of the Federal Reserve System

August 12, 1970

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SUMMARY AND OUTLOOK

Nonfinancial

The data now available for July on balance are consistent with the staff projection of a modest rise in real GNP in the third quarter.

Industrial production increased slightly in July, following a very small June decline, and was about 3 per cent below the peak level of a year earlier. Output of consumer goods was up slightly and production of both durable and nondurable materials advanced, but both business and defense equipment declined further. Retail sales increased almost 1 per cent in July following a relatively strong expansion for the second quarter as a whole. Unit sales of domestic autos, at an annual rate of 8.5 million units, were about the same as in June and 15 per cent above the average rate of the first five months of the year. New orders for durable goods leveled off in the second quarter following an extended period of decline; however, orders for producers' capital goods declined further. In recent months, inventories have been brought somewhat more closely into line with sales, but at midyear stock-sales ratios were still relatively high.

The labor market continued to ease in July. Nonfarm payroll employment dropped for the fourth successive month, with declines reported in most industries, and the unemployment rate moved back up to

5 per cent from 4.7 per cent in June. However, the work week in manufacturing increased slightly. Reductions of labor input in the spring were associated with a resumption of productivity increase for the private nonfarm economy as a whole, and the rise of unit labor costs slowed markedly. Increases in hourly compensation have averaged somewhat less in recent months than a year earlier. But new contracts have provided very large increases in wages and benefits, paced by the trucking and construction agreements.

Although seasonally adjusted wholesale prices of farm products and foods increased sharply from mid-June to mid-July, following three months of decline, there have been indications of selective easing of upward price pressures. Since mid-July, a number of farm product prices have declined, in some cases substantially. Moreover, prospective supplies of crops and livestock are large for the second half of this year. Wholesale prices of industrial commodities, seasonally adjusted, increased somewhat more slowly in July than in the first half of the year. Further weakness in prices of nonferrous metals resulted in the first decline in the metals and metal products group since November 1968. At the consumer level, some slowing of the rate of overall price increase occurred in the second quarter, mostly attributable to a relatively small increase in food prices and a leveling off of mortgage interest rates. On average, retail prices of other commodities and services continued to rise rapidly.

Outlook. Economic activity is expected to expand only moderately in the last half of this year, at about the same rate as previously projected. Consumer outlays and residential construction now seem likely to be stronger than expected earlier, but business fixed investment probably will be weaker. The recent strength in consumer spending, including purchases of autos, has led us to raise the projections in this area, and the saving rate is projected to decline perceptibly from the very high second quarter level. Similarly, the jump in housing starts in June and a very large inflow of funds into depositary institutions suggest that there may be a faster turnaround than we had allowed for in residential activity.

On the other hand, prospects for business fixed investment have become more bearish. The latest GNP figures for the first half show a leveling-off in business fixed investment in current dollars and an appreciable decline in real terms. Second half declines are now strongly suggested by recent reductions in contract awards for private non-residential construction, and the continued weakness in new orders for capital equipment.

Real growth in GNP seems likely to be somewhat more rapid in the first half of 1971 than previously projected, at about a 3 to 3-1/2 per cent annual rate. To a large extent, the upward revision reflects the stimulus of a less restrictive Federal Budget--including an assumed Federal pay raise next January 1--and the lagged effects of somewhat faster monetary expansion in the remainder of this year than occurred in the first half, when money supply rose at a 4 per cent annual rate. The projected rate of growth in real GNP, however, would probably still not be sufficient to absorb the increase in supplies of available resources, and the unemployment rate would likely rise above 5.5 per cent in the second quarter of 1971. In these circumstances, the rise in the GNP price deflator is still expected to ease to around a 3 per cent annual rate in the second quarter.

No allowance has been made in our projection for the very real possibility of an extended auto strike this fall. Such a strike, through its impact on output and incomes--and inventories and consumption--could depress the fourth quarter GNP increase appreciably, depending on which firm is struck and for how long. As output rebounds after a strike settlement, increases in the rate of inventory accumulation and in consumption would probably make up most or all of the fourth quarter shortfall.

Financial

The considerable decline in bond yields that began in late June appears to have stalled, and in some instances to have been reversed, by early August. The earlier rally in bond markets was triggered by a change in expectations about the future course of interest rates, reflecting prospects for only limited growth in economic activity, a reduced rate of inflation, a moderation of credit demands over the longer-run, and a more expansive monetary policy. More recently, with demands in long-term markets continuing very heavy, investors seem to be waiting for confirmation of these expectations. Similarly, cautious investor attitudes have affected short- and intermediate-term debt markets. The Treasury's mid-August refunding was relatively successful, but prices of the new issues have faded somewhat in recent days. In equity markets, prices have changed little on balance since mid-July in light trading.

Demands for bank credit by firms forced out of the commercial paper market seem to have abated, although some firms continue to use bank financing to meet maturing obligations as investors continue to be extremely quality-conscious. Partly as a consequence of reduced bank loan demands, banks have become less aggressive in bidding for 30-to-89 day CD's. They had increased their CD outstandings by nearly $5 billion from late June to the end of July, nearly all of which was in these shorter maturities.

Banking outlook. Over-all bank loan demand in the months immediately ahead is likely to be relatively moderate, barring any further disturbances to financial confidence. Loan demands of firms having difficulty selling commercial paper are likely to be modest, being limited possibly to a few lesser-rated names. Demands for loans other than those related to commercial paper and to security financing have been sluggish for the past two months. And with capital outlays being stretched out and cut back, with little increase indicated in inventory financing requirements, and with substantial capital market borrowing, business loan demands are not likely to pick up.

In this environment, bank willingness to bid for CD's should follow a more moderate course than in July. However, relatively strong time deposit inflows will likely be maintained by a continued sizable inflow of consumer-type deposits, with such deposit flows sustained in part by uncertainty concerning the financial and business outlook. Thus, with business loan demands limited, banks should be in a position to reduce their reliance on high-cost funds and to acquire an increasing volume of municipal securities and mortgages.

Security markets outlook. If banks acquire an enlarged volume of State and local government securities, municipal yields could edge down further. But such a downward yield tendency would probably be limited by a build-up in the volume of new issues, as many governmental units are no longer restrained by statutory rate ceilings. In the U. S. Government securities market, dealers have added about $1.3 billion to their inventories in the wake of the recent refunding, although there is no indication as yet that distribution of these holdings will present a significant problem. However, it seems probable that the Treasury will offer or announce a cash issue some time in September. Federally-sponsored credit agencies will continue to raise substantial funds over the rest of the quarter, but at a slower pace than in the first half of the year.

Corporate bond flotations are projected to remain unusually heavy through at least early fall, and above the rate projected in the last Greenbook. The forward calendar of offerings has been bolstered by several large industrial issues, which, together with a large amount of public utility offerings, may bring the dollar volume of total publicly offered bond issues in the third quarter above that in the preceding quarter exclusive of the exceptionally large AT&T financing. While such a volume of financing may generate some backing and filling of yields, we nevertheless anticipate a general drifting down in yields over time as signs of a lessening in inflation develop.

Mortgage markets. Net mortgage lending by thrift institutions is likely to increase further in the third quarter, and mortgage terms may ease somewhat. Although net savings inflows are not likely to be maintained at the unusually rapid July pace, consumer desires for depositary claims could remain strong in view of financial and economic uncertainties. With liquidity rebuilt, and favorable fund flows, S&L's and mutual savings banks are expected to accelerate their new mortgage commitment volume.

Balance of Payments

Presently available information throws little new light on second-quarter balance of payments developments. The trade balance showed a marked further improvement in June. For the second quarter as a whole, substantial capital outflows, including unrecorded flows of funds, were evidently a major factor in the very large overall deficit, measured either on the official settlements basis or on the liquidity basis before special transactions. These outflows, which presumably included movements into the Canadian dollar and the German mark, and perhaps into Euro-dollar deposits, seem to have slackened or even turned around since midyear--to judge by weekly over-all indicators which have been suggesting a marked shrinkage in the liquidity deficit in July, after allowance for adverse seasonality.

Since the relaxation of Regulation Q on June 24, outstanding liabilities of U. S. banks to their foreign branches have been sharply reduced. For most leading banks, these liabilities since the end of July have been close to May 1969 levels (the historical base levels). The repayment of these liabilities was a factor in the very large official settlements deficit experienced in July. The 3-month Euro-dollar rate has been in the 8 - to - 8/1/2 per cent range since the latter part of July, in contrast to rates over 9 per cent during June. Since the lowering of the German central bank's lending rates on July 16, there has been some decline in German money market rates, too. This easing of German rates may be partly seasonal, and it does not rule out the possibility of renewed upward pressures on Euro-dollar rates from the European side, which would encourage further Euro-dollar repayments by U. S. banks to their branches despite the impairment of reserve-free bases that would be entailed. Even without any new rise in Euro-dollar rates such repayments may continue if U. S. rates decline, and especially if U. S. banks become persuaded that they do not risk renewed pressures on their liquidity positions.

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SELECTED DOMESTIC NONFINANCIAL DATA

(Seasonally adjusted)

	1970				Per Cent Change* From		
	April	May	June	July	1 mo. ago	3 mos. ago	Year ago
Civilian labor force (mil.)	82.9	82.6	82.1	82.8	0.8	-0.1	2.5
Unemployment rate (%)	4.8	5.0	4.7	5.0	--	--	[3.5] 4/
Insured unempl. rate (%)	3.2	3.6	3.7	n.a.	--	--	[2.1] 4/
Nonfarm employment, payroll (mil.)	71.2	70.9	70.6	70.5	-0.2	-1.0	0.1
Manufacturing	19.8	19.6	19.5	19.4	-0.4	-2.0	-4.2
Nonmanufacturing	51.4	51.3	51.1	51.1	-0.1	-0.6	1.8
Industrial production (57-59=100)	170.0	169.1	168.8	169.2	0.2	-0.5	-3.1
Final products, total	168.5	167.8	167.1	167.2	0.1	-0.8	-3.2
Consumer goods	163.2	163.3	162.6	163.3	0.4	0.1	-0.7
Business equipment	193.0	188.7	188.3	186.9	-0.7	-3.2	-5.1
Materials	171.5	170.8	170.7	171.5	0.5	0.0	-2.8
Capacity util. rate, mfg.	78.8	77.7	77.1	n.a.	--	--	[84.7] 4/
Wholesale prices (57-59=100) 1/	116.6	116.8	117.0	117.7	0.6	0.9	3.9
Industrial commodities (FR) 5/	115.1	115.5	115.7	n.a.	0.2	0.9	4.0
Sensitive materials (FR)	116.6	116.9	115.9	114.7	-1.0	-1.6	2.8
Farm products, foods & feeds	117.6	117.0	117.5	119.3	1.5	1.4	3.3
Consumer prices (57-59=100 1/ 5/	134.0	134.6	135.2	n.a.	0.4	1.5	6.0
Food	132.0	132.4	132.7	n.a.	0.2	0.8	5.7
Commodities except food	121.6	122.3	122.8	n.a.	0.4	1.7	4.1
Services	153.4	154.1	155.0	n.a.	0.6	1.8	8.2
Hourly earnings, pvt. nonfarm ($)	3.19	3.20	3.21	3.22	0.3	0.9	5.6
Hourly earnings, mfg. ($)	3.32	3.34	3.36	3.37	0.3	1.5	5.3
Weekly earnings, mfg. ($)	132.60	132.93	133.73	134.74	0.8	1.6	3.5
Net spend. weekly earnings, mfg. (3 dependents 57-59 $) 1/ 5/	85.35	85.64	86.12	n.a.	0.6	-0.1	-1.8
Personal income ($ bil.) 2/ 5/	806.0	799.8	798.8	n.a.	-0.1	1.4	7.0
Retail sales, total ($ bil.)	30.5	30.5	30.4	30.6	0.7	0.3	5.3
Autos (million units) 2/	7.5	7.8	8.6	8.5	-1.4	14.0	-3.2
GAAF ($ bil.) 3/	8.5	8.3	8.2	8.3	0.5	-2.3	2.0
12 leaders, composite (1963=100) 5/	148.3	146.3	146.3	n.a.	0.0	-1.1	-3.5
Selected leading indicators:							
Housing starts, pvt. (thous.) 2/ 5/	1,224	1,225	1,358	n.a.	10.9	-2.4	-9.9
Factory workweek (hours)	40.0	39.8	39.8	39.9	0.3	-0.3	-1.7
Unempl. claims, initial (thous.) 5/	326	314	312	n.a.	0.5 6/	-16.5 6/	-56.5 6/
New orders, dur. goods, ($ bil.) 5/	28.6	29.5	29.6	n.a.	0.6	3.6	1.6
Machinery & equipment	6.0	6.2	6.2	n.a.	0.2	4.0	-4.7
Common stock prices (41-43=10)	85.95	76.06	75.59	75.72	0.2	-11.9	-20.1

* Based on unrounded data. 1/ Not seasonally adjusted. 2/ Annual rates.
3/ Gen'l. merchandise, apparel, and furniture and appliances. 4/ Actual figures.
5/ Per cent calculated to June 1970. 6/ Sign reversed.

SELECTED DOMESTIC FINANCIAL DATA

	Averages 1969 QIII	1969 QIV	1970 QI	1970 QII	1970 July	1970 Week ended July 29
Interest rates, per cent						
Federal funds	8.98	8.94	8.56	7.88	7.21	6.89
3-mo. Treasury bills	7.02	7.36	7.21	6.67	6.45	6.34
3-mo. Federal agencies	7.63	7.92	7.72	7.09	6.68	6.81
3-mo. Euro-dollars	10.89	10.48	9.26	8.87	8.76	8.34
3-mo. finance co. paper	7.74	7.89	7.94	7.41	7.64	7.80
4-6 mo. commercial paper	8.49	8.63	8.55	8.16	8.29	8.30
Bond buyer municipals	6.00	6.40	6.35	6.81	6.53	6.40
Aaa corporate-new issues	7.75	8.32	8.45	8.94	8.63	8.60
20-year Treasury bonds	6.34	6.71	6.78	7.14	6.92	6.86
FHA mortgages, 30-year	8.38	8.53	9.25	9.12	n.a.	--

	1969 QIII	1969 QIV	1970 QI	1970 QII	1970 July
Change in monetary aggregates (SAAR, per cent)					
Total reserves	- 9.3	1.4	- 2.9	2.6	4.1
Nonborrowed reserves	- 4.8	- 0.1	- 0.4	4.1	-18.1
Credit proxy	- 9.4	0.1	0.6	6.0	22.3
Credit proxy + nondep. funds	- 4.3	2.0	0.5	6.5	18.1
Money supply	-	1.2	3.8	4.2	4.1
Time and savings deposits	-13.3	--	0.4	13.8	35.2
Deposits at S&L's and MSB's	2.1	1.4	1.9	7.0	14.3
Bank credit, end-of-month	- 0.8	4.8	- 0.4	4.2	16.6
Treasury securities	-11.4	-20.5	-12.3	30.2	31.1
Other securities	- 7.2	4.5	9.5	9.9	8.0
Total loans	3.1	10.0	- 0.7	- 2.0	16.1
Business	7.0	7.7	- 4.5	1.5	4.6

	1969 QIII	1969 QIV	1970 QI	1970 QII	1970 July
Change in millions of dollars					
Commercial paper (SA)	3,329	3,151	3,185	2,104	n.a.
Bank related (NSA)	1,350	1,614	2,224	1,035	245

	1968 Year	1969 HI	1969 QII	1970 HI	1970 QII	1970 July
New security issues (NSA, $ mil.)						
Total corp. issues	21,965	13,572	7,354	17,944e	9,967e	2,900e
Public offerings	15,314	10,359	5,679	15,358e	8,634e	1,800e
State and local government bond offerings	16,574	11,881	3,648	7,816	3,711	1,300e
Fed. sponsored agency debt (change)	3,354	3,605	2,411	4,947	1,233	455e
Fed. gov't. debt (change)	15,300	-12,280	-12,437	-4,415	-6,396	5,900e

n.a. - Not available. e - Estimated. p - Preliminary.
SAAR - Seasonally adjusted annual rate. NSA - Not seasonally adjusted.

1/ Figure is for S&L's only, data for MSB's not available.

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U.S. Balance of Payments

In millions of dollars; seasonally adjusted

	1969 Year	1970p I	II	Apr.*	May*	June*
Coods and services, net 1/	1,950	885				
Trade balance 2/	638	518	848	181	237	430
Exports 2/	36,473	10,241	10,706	3,394	3,592	3,720
Imports 2/	-35,835	-9,723	-9,858	-3,213	-3,355	-3,290
Service balance	1,312	367				
Remittances and pensions	-1,191	-330				
Govt. grant & capital, net	-3,828	-837				
U.S. private capital	-5,374	-1,543				
Direct investment	-3,070	-1,304				
Foreign securities	-1,494	-159	19	-66	61	41
Banking claims	-541	170	-486	-117	-276	-151
Other	-269	-250				
Foreign capital	12,554	1,710				
Official foreign, liquid	-525	3,028	450	-343	368	503
Official reserve holders, nonliquid	-996	-422	506	67	131	283
Other official foreign, nonliquid	259	-66				
Foreign commercial banks, liquid	9,434	-1,717	13	935	-351	-656
New direct investment issues 3/	1,029	155	306			
U.S. corporate stocks	1,565	-85	-126	8	-198	64
Other	1,788	817				
U.S. monetary reserves (inc.-)	-1,187	481	1,022	431	754	-163
Gold stock	-967	-44	14	1	2	11
Special drawing rights	--	-53	-37	-6	1	-32
IMF gold tranche	-1,034	-253	227	67	150	10
Convertible currencies	814	831	818	369	601	-152
Errors and omissions	-2,924	-366				
BALANCES (deficit -) 4/						
Official settlements, S.A.		-3,087	-1,978			
" " , N.S.A.	2,708	-2,825	-2,063	-155	-1,253	-623
Liquidity, S.A.		-1,767	-1,504			
" , N.S.A.	-7,221	-1,677	-1,497	-1,008	-707	218
Adjusted over-all, S.A.		-1,370	-1,991			
" " , N.S.A.	-6,726	-1,288	-1,991	-1,090	-902	33
Financed by: 5/						
Liab. to comm. banks	9,434	-1,537	-72	935	-351	-656
Official settlements	-2,708	2,825	2,063	155	1,253	623

* Only exports and imports are seasonally adjusted.

1/ Equals "net exports" in the GNP, except for latest revisions.

2/ Balance of payments basis which differs a little from Census basis.

3/ New issues sold abroad by U.S. direct investors.

4/ Excludes initial allocation of SDRs on January 1, 1970; total $867 million, quarterly S.A., $217 million.

5/ Minus sign indicates decrease in net liabilities. Data not seasonally adjusted.

THE ECONOMIC PICTURE IN DETAIL

Domestic Nonfinancial Scene

Gross national product. Most recent economic data continue to suggest a resumption of a moderate rate of real growth in the current quarter. We anticipate an increase of $13.5 billion in GNP--about the same as projected last month--as compared with a $10.6 billion rise last quarter. This is expected to produce a gain of about 1-1/2 per cent annual rate in real terms, on the assumption that the rise in the deflator moderates slightly further to a 4 per cent rate.

Although similar overall in total to our last projection, the composition of the current third quarter GNP increase has been changed somewhat. Consumer demand has shown greater strength than anticipated and some unexpectedly early signs of recovery are evident now in construction activity. On the other hand, business fixed investment is now projected to turn down this quarter, earlier than formerly expected.

CHANGES IN GNP AND RELATED ITEMS, 1970
(Seasonally adjusted, annual rates)

	2nd Quarter (Preliminary)	Third Quarter Projection of 7/15/70	Current Projection
	----------Billions of dollars----------		
GNP	10.6	13.7	13.5
Final sales	9.6	13.2	13.8
Personal consumption	11.1	9.5	11.5
Residential construction	- .6	1.0	.5
Business fixed investment	.1	1.0	- .5
Net exports	.3	.3	.6
Federal purchases	-2.7	- .6	- .6
State and local purchases	1.3	3.0	2.3
Inventory change	1.0	.5	- .3
	----------Per cent----------		
Real GNP	.3	1.6	1.6
GNP deflator	4.2	4.0	4.0

The strengthened projection of personal consumption expenditures for this quarter reflects in part a continued advance in retail sales in July, following a relatively strong pick-up in the second quarter. Unit sales of new domestic autos last month averaged 8.5 million, annual rate, about half a million above the second quarter rate of sales, and well above our last Greenbook projections for the third quarter. Nondurable sales in general have also been somewhat stronger than we had earlier projected.

The removal on July 1 of the remainder of the tax surcharge, estimated at about $3.8 billion, annual rate, will strengthen disposable income this quarter. In addition, some decline from the abnormally high second quarter saving rate of 7.6 per cent also seems probable. As a result, we have revised third quarter consumer expenditures upward by $2 billion.

The recent rebound in housing starts and the enlarged inflows of funds into savings and loan associations also suggest that the long-awaited upturn in residential construction activity may be taking place earlier than anticipated. Our starts projection has been adjusted upward slightly to 1,350 units for the third quarter and expenditures are now expected to increase by $0.5 billion, rather than remain unchanged at the second quarter level as previously projected. Some additional strength has also been evident in net exports, largely as a result of an expansion of machinery and agricultural exports.

On the other hand, we now expect a decline in business fixed investment spending to begin in the third rather than in the fourth quarter. Revised GNP data which became available in July showed investment spending as unchanged in the first half from the level of the fourth quarter of 1969 instead of rising steadily as earlier estimated. With production and new orders for machinery and equipment continuing to decline and private nonresidential building contracts running below year-ago levels, we now project a dip of $0.5 billion in business fixed investment for this quarter, rather than a rise of $1 billion.

The rate of growth is expected to increase further in the fourth quarter, about as we had been assuming earlier, with real GNP projected to rise by 2.7 per cent, annual rate. Although further weakening of capital outlays appears probable, consumption seems likely to continue expanding at close to the increased third quarter rate. A strong gain in residential construction expenditures is expected as the greater availability of funds begins to have increasing effect, and easier financial markets should also permit some faster expansion in outlays by States and localities. With final sales rising, some modest increase in inventory accumulation may occur, despite the dampening effect of reduced capital expenditures and defense outlays.

These projections assume no auto strike. A prolonged strike at a major producer beginning in mid-September could markedly affect the pattern of activity in late 1970 and early 1971. Gains in production, income, inventories and to a lesser extent consumption would likely be below current estimates particularly for the fourth quarter. But if settlement were reached by year-end, the first quarter would show a much stronger rise than we had projected.

Real growth is now projected to increase at a slightly faster pace in the first half of 1971 than we had earlier anticipated. Partly this results from the assumption of a somewhat more rapid rate of monetary growth for the remainder of this year than occurred in the first half, which should lead to easing financial conditions and an increasing impetus to economic activity in 1971. Further, the

Federal deficit (NIA basis) is expected to be larger and hence more stimulative during the first half of next year than we had formerly thought, mainly because of increased expenditures. We have newly incorporated in our current projections a 6 per cent Federal pay raise in January in line with the Administration's recent proposal with respect to comparability of Federal and industry pay. This pay raise would add some $2.6 billion to disposable income, and should help to support continued relatively strong gains in consumption. The somewhat easier credit market conditions associated with more rapid money supply growth should encourage additional outlays for residential construction and expenditures by States and localities, and may also contribute to the moderate rise in inventory investment that is projected. Declines in business fixed investment and defense spending will limit expansion of activity, but with other major expansionary forces at work, we now expect first and second quarter GNP gains of $18.2 billion and $16.0 billion, respectively as compared with the earlier $15.6 and $14.9 billion increases.

Our basic price assumptions are little changed, with the increase in the GNP implicit price deflator projected to moderate to a 3 per cent rate by mid-1971. In real terms, the economy is projected to be growing at an annual rate of 3 to 3-1/2 per cent in early 1971, still significantly below its long-term potential. With the economy now operating well below its potential, and productivity expected to recover further, we still expect substantial slack in the demand for labor and other resources. Unemployment seems likely to move moderately higher, with job opportunities particularly scarce for new entrants to the labor force. Assuming near-normal labor force growth, the unemployment rate could rise above 5-1/2 per cent by mid-1971.

CHANGES IN GNP AND RELATED ITEMS, 1971
(Seasonally adjusted, annual rates)

	First Quarter		Second Quarter	
	Proj. of 7/15/70	Current Proj.	Proj. of 7/15/70	Current Proj.
	Billions of dollars			
GNP	15.6	18.2	14.9	16.0
Final sales	15.1	17.9	14.4	14.5
Personal consumption	10.0	11.0	11.1	11.0
Residéntial construction	2.4	2.4	1.3	1.1
Business fixed investment	-1.5	-1.5	-1.5	-1.5
Net exports	1.0	.6	.0	.1
Federal purchases	- .3	1.9	.0	.0
State and local purchases	3.5	3.5	3.5	3.8
Inventory change	.5	.3	.5	1.5
	Per cent			
Real GNP	3.0	3.2	3.0	3.3
GNP deflator	3.2	4.1 1/	2.8	3.0

1/ Excluding effects of Federal pay increase, 3.2 per cent per year.

Industrial production. Industrial production rose 0.2 per cent in July, following a similar decline in June, and at 169.2 was 3 per cent below a year earlier. Increases in output of consumer goods and materials more than offset further declines in production of business and defense equipment.

GROSS NATIONAL PRODUCT AND RELATED ITEMS
(Quarterly figures are seasonally adjusted. Expenditures and income figures are billions of dollars, with quarterly figures at annual rates.)

	1969	1970 Proj.	1970 I	1970 IIp	1970 III (Projected)	1970 IV (Projected)	1971 I (Projected)	1971 II (Projected)
Gross National Product	931.4	978.0	959.5	970.1	983.6	998.8	1017.0	1033.0
Final purchases	922.9	975.7	957.9	967.5	981.3	996.1	1014.0	1028.5
Private	710.7	755.7	738.3	749.2	761.3	774.1	786.6	797.3
Excluding net exports	708.8	751.6	734.8	745.4	756.9	769.4	781.3	791.9
Personal consumption expenditures	577.5	619.9	603.1	614.2	625.7	636.5	647.5	658.5
Durable goods	90.0	92.4	89.1	91.8	93.7	95.0	96.2	97.0
Nondurable goods	245.8	264.7	258.8	262.1	266.7	271.0	275.5	280.0
Services	241.6	262.8	255.2	260.2	265.3	270.5	276.0	281.5
Gross private domestic investment	139.8	134.0	133.2	133.8	133.5	135.6	136.8	137.9
Residential construction	32.0	29.6	29.1	28.5	29.0	31.7	34.1	35.2
Business fixed investment	99.3	102.2	102.6	102.7	102.2	101.2	99.7	98.2
Change in business inventories	8.5	2.3	1.6	2.6	2.3	2.7	3.0	4.5
Nonfarm	8.0	1.9	.9	2.1	2.1	2.5	3.0	4.5
Net exports of goods and services	1.9	4.1	3.5	3.8	4.4	4.7	5.3	5.4
Gov't. purchases of goods & services	212.2	220.0	219.6	218.3	220.0	222.0	227.4	231.2
Federal	101.3	99.7	102.3	99.6	99.0	98.0	99.9	99.9
Defense	78.8	76.5	79.3	77.1	75.8	73.7	74.0	72.9
Other	22.6	23.3	23.0	22.5	23.2	24.3	25.9	27.0
State & local	110.8	120.3	117.4	118.7	121.0	124.0	127.5	131.3
Gross national product in constant (1958) dollars	727.1	726.9	723.8	724.3	727.2	732.1	738.0	744.1
GNP implicit deflator (1958 = 100)	128.1	134.6	132.6	133.9	135.3	136.4	137.8	138.8
Personal income	748.9	803.5	782.3	801.5	809.3	820.8	833.8	846.5
Wages and salaries	509.0	542.9	531.9	539.8	546.5	553.2	564.5	572.8
Disposable income	631.6	686.2	665.3	684.0	693.3	702.3	712.5	722.7
Personal saving	37.6	48.5	44.8	52.1	49.6	47.4	46.3	45.2
Saving rate (per cent)	6.0	7.1	6.7	7.6	7.2	6.7	6.5	6.3
Corporate profits before tax	91.2	83.6	82.6	83.0	83.7	85.2	83.7	85.7
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	200.6	196.6	195.9	196.7	195.4	198.4	205.6	209.1
Expenditures	191.3	206.9	197.7	210.6	209.2	210.1	215.2	218.5
Surplus or deficit (-)	9.3	-10.3	-1.7	-13.9	-13.8	-11.7	-9.6	-9.4
High employment surplus or deficit (-)	4.5	-.5	3.2	-3.6	-3.0	1.4	5.7	5.6
Total labor force (millions)	84.2	86.0	85.8	85.7	86.1	86.5	86.9	87.3
Armed forces "	3.5	3.2	3.3	3.2	3.2	3.1	3.1	3.0
Civilian labor force "	80.7	82.8	82.4	82.5	82.9	83.4	83.8	84.3
Unemployment rate (per cent)	3.5	4.8	4.1	4.8	5.1	5.3	5.5	5.7
Nonfarm payroll employment (millions)	70.3	70.9	71.1	70.9	70.7	71.0	71.4	71.8
Manufacturing	20.2	19.6	20.0	19.6	19.4	19.5	19.5	19.6
Industrial production (1957-59=100)	172.8	170.3	170.7	169.3	170.0	171.1	172.4	174.0
Capacity utilization, manufacturing (per cent)	83.7	78.0	79.8	77.9	77.3	76.8	76.6	76.6
Housing starts, private (millions A.R.)	1.47	1.34	1.25	1.27	1.35	1.50	1.57	1.63
Sales new domestic autos (millions, A.R.)	8.46	8.08	7.35	7.95	8.50	8.50	8.60	8.75

CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1969	1970 Proj.	1970 I	1970 IIp	1970 Projected III	1970 Projected IV	1971 Projected I	1971 Projected II
	Billions of Dollars							
Gross National Product	66.4	46.6	7.8	10.6	13.5	15.2	18.2	16.0
Inventory change	0.9	-6.2	-5.6	1.0	-0.3	0.4	0.3	1.5
Final purchases	65.5	52.8	13.4	9.6	13.8	14.8	17.9	14.5
Private	53.5	45.0	10.1	10.9	12.1	12.8	12.5	10.7
Excluding net exports	54.1	42.8	9.2	10.6	11.5	12.5	11.9	10.6
Net exports	-0.6	2.2	0.9	0.3	0.6	0.3	0.6	0.1
Government	12.0	7.8	3.3	-1.3	1.7	2.0	5.4	3.8
GNP in constant (1958) dollars	19.9	-0.2	-5.4	0.5	2.9	4.9	5.9	6.1
Final purchases	19.6	4.9	-0.5	-0.7	3.4	4.4	5.6	4.7
Private	20.1	10.7	1.1	2.6	4.2	4.8	5.0	3.9
	In Per Cent Per Year							
Gross National Product	7.7	5.0	3.3	4.4	5.6	6.2	7.3	6.3
Final purchases	7.6	5.7	5.7	4.0	5.7	6.0	7.2	5.7
Private	8.1	6.3	5.5	5.9	6.5	6.7	6.5	5.4
Personal consumption expenditures	7.8	7.3	7.1	7.4	7.5	6.9	6.9	6.8
Durable goods	7.1	2.7	-7.5	12.1	8.3	5.5	5.1	3.3
Nondurable goods	6.8	7.7	10.8	5.1	7.0	6.4	6.6	6.5
Services	9.0	8.8	8.6	7.8	7.8	7.8	8.1	8.0
Gross private domestic investment	10.5	-4.1	-20.0	1.8	-0.9	6.3	3.5	3.2
Residential construction	5.6	-7.5	-17.1	-8.2	7.0	37.2	30.3	12.9
Business fixed investment	12.0	2.9	0.0	0.4	-1.9	-3.9	-5.9	-6.0
Gov't. purchases of goods & services	6.0	3.7	6.1	-2.4	3.1	3.6	9.7	6.7
Federal	1.8	-1.6	0.8	-10.6	-2.4	-4.0	7.8	0.0
Defense	1.0	-2.9	2.5	-11.1	-6.7	-11.1	1.6	-5.9
Other	5.1	3.1	-5.2	-8.7	12.4	19.0	26.3	17.0
State & local	10 0	8.6	11.2	4.4	7.7	9.9	11.3	11.9
GNP in constant (1958) dollars	2.8	0.0	-3.0	0.3	1.6	2.7	3.2	3.3
Final purchases	2.8	0.7	-0.4	-0.4	1.9	2.4	3.1	2.6
Private	3.6	1.9	0.8	1.8	2.9	3.3	3.4	2.6
GNP implicit deflator	4.7	5.1	6.4 1/	4.2	4.0	3.5	4.1 2/	3.0
Personal income	8.7	7.3	6.1	9.8	3.9	5.7	6.3	6.1
Wages and salaries	9.5	6.7	5.0	5.9	5.0	4.9	8.2	5.9
Disposable income	6.8	8.6	9.0	11.2	5.4	5.2	5.8	5.7
Corporate profits before tax	2.8	-8.3	-26.7	1.9	3.4	7.2	-7.0	9.6
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	14.4	-2.0	-12.1	1.6	-2.6	6.1	14.5	6.8
Expenditures	5.3	8.2	3.7	26.1	-2.7	1.7	9.7	6.1
Nonfarm payroll employment	3.5	0.9	1.7	-1.1	-1.1	1.7	2.3	2.2
Manufacturing	2.0	-3.0	-2.0	-8.0	-4.1	-2.1	0.0	2.0
Industrial production	4.4	-1.4	-2.8	-3.3	1.7	2.6	3.0	3.7
Housing starts, private	-2.7	-8.5	-31.0	5.4	25.5	44.4	20.0	12.7
Sales new domestic autos	-1.9	-4.6	-38.1	32.3	27.8	0.0	4.7	7.0

1/ Excluding effects of Federal pay increase, 5.5 per cent per year.

2/ Excluding effects of Federal pay increase, 3.2 per cent per year.

Auto assemblies, after allowance for the model changeover period, were at an annual rate of 8.5 million units, about the same as in June but 7 per cent below a year earlier. Production schedules for August and September are set at the July rate. Output of television sets, appliances, and consumer nondurable goods increased in July, but production of furniture declined further. Output declines were widespread among the equipment industries, including industrial and commercial equipment and aircraft. Production of farm equipment and trucks, however, changed little. Among materials, output of steel, consumer durable parts for further processing, and most nondurable materials increased, but production of construction materials continued to decline.

INDUSTRIAL PRODUCTION
Per cent changes

	June 1970 to July 1970	July 1969 to July 1970
Total index	.2	- 3.1
Consumer goods	.4	- .7
Durables	1.3	- 4.6
Autos	.5	- 8.3
Home goods	1.6	- 2.6
Nondurables	.4	1.0
Business equipment	- .7	- 5.1
Defense equipment	-2.5	-20.5
Materials	.5	- 2.8
Construction	- .5	- 3.7
Metal goods	.7	- 5.3
Nondurables	.7	- .8

Retail sales. Advance retail sales data indicate that July sales were 0.7 per cent higher than in June. Retail sales in the second quarter as a whole had risen more than in any quarter for two years. The thrust came in April, when retroactive social security and Federal pay increases were received. Similarly, July sales volume may have benefited from the ending of the surtax at mid-year.

Sales at durable goods outlets rose 0.8 per cent in July, with both the automotive group and the broad lumber, building materials, and hardware group up about 1.5 per cent. Sales at nondurable goods stores rose 0.6 per cent, with all major types of stores except restaurants reporting increases.

RETAIL SALES, 1970
Per cent Change from Previous Period

	QI	QII	May	June	July*
Total	1.0	2.4	- .1	- .2	.7
Durable	-2.5	3.1	- .2	.2	.8
Automotive	5.2	2.8	-2.2	1.2	1.6
Furniture & appliance	5.1	.6	-1.3	- .3	-.6
Nondurable	2.5	2.1	- .1	- .4	.6
Food group	3.6	1.7	.3	.9	.8
Dept. stores	.6	3.3	-3.0	-1.6	.5
Total, deflated by all commodities CPI	- .3	1.2	- .6	- .4	--

* Advance, unpublished report.

Unit auto sales and stocks. Sales of new domestic autos in July were at an annual rate of 8.5 million units, down only 1.5 per cent from the improved June rate and 3 per cent below a year earlier. Unit sales in June and July were 15 per cent above the average rate prevailing in the first 5 months of 1970.

Dealers' stocks of new domestic autos rose slightly during July and at the end of the month represented 52 days supply, compared with 53 days a year earlier.

Production of compact cars increased steadily from January to June, both absolutely and relative to total output, suggesting that the improvement in sales to a significant extent has reflected growing demand for small cars.

AUTO ASSEMBLIES
Monthly output, thousands

Years	Total	Compacts	Other	Compacts, as per cent of total
January	601.6	67.1	534.5	11.2
June	806.8	121.8	685.0	15.1
Per cent change Jan. to June	34.1	81.5	28.2	--

Consumer credit. Consumer instalment credit outstanding rose at a seasonally adjusted annual rate of $5.3 billion in June. This was the largest monthly advance since last November and lifted the average rate of increase for the second quarter as a whole to $4.6 billion, up somewhat from the $4.0 billion rate in the first quarter. Despite the most recent gain, the rise in instalment credit during the first half of 1970 was less than one-half the $9.0 billion rate in the first half of last year, and was also well below the $7.2 billion rate in the latter half of 1969.

Extensions and repayments of instalment credit both declined substantially in June after posting very large increases in May. The reductions were centered in personal loans and nonautomotive consumer goods--the same categories that had moved up sharply in May. For the second quarter as a whole, total extensions of instalment credit, which had declined for three straight quarters, rose to a level slightly above the year-earlier peak; over-the-year increases in personal loans and nonautomotive consumer goods more than offset reductions in the automobile and repair and modernization groups.

NET CHANGE IN CONSUMER INSTALMENT CREDIT OUTSTANDING
(Billions of dollars, seasonally adjusted annual rates)

	Total	Automobile	Other Consumer goods	Personal Loans	Home repair and Modernization
1969--QI	$8.3	$2.7	$2.5	$3.0	$ .2
QII	9.6	3.1	2.9	3.2	.4
QIII	7.7	1.9	2.6	3.1	.0
QIV	6.8	2.0	2.4	2.6	- .2
1970--QI	4.0	.0	2.4	1.7	.0
QII	4.6	.2	2.3	1.9	.1

Consumer buying expectations. The July Census survey of buying intentions--like the latest Michigan Survey Research Center and National Industrial Conference Board surveys--on the whole suggested little improvement in the consumer outlook. There was a rather substantial recovery in the index of expected house purchases, which rose from 87.9 to 92.9, but the July figure is still the second lowest in the 15 quarters for which this index has been computed. Income expectations worsened: fewer respondents expected a substantial increase in income (the chance of increase declined to 18.2 from 19.9 in April) and more families expected a substantially lower income (7.3 vs. 7.0 in the April survey).

Auto purchase plans for the next six months are unchanged from the last survey and, according to Census analysts, not significantly different from a year earlier. Because of the poor past performance of the index, the Census Bureau has changed its method of computation, and the auto series in its present form has yet to be evaluated. The latest Michigan and NICB indicators of expected auto purchases were lower than in the spring.

HOUSEHOLD PURCHASE AND INCOME EXPECTATIONS

	1969		1970		
	July	October	Jan.	April	July
Indexes of expected house and new car purchases (Jan.-Apr. 1967=100, seasonally adjusted)					
Houses (new and used)	93.9	96.7	93.6	87.9	92.9
New cars	104.3	103.1	106.0	105.8	105.8
Expected change in income (average chance in 100)					
Substantial increase	18.6	17.6	20.1	19.9	18.2
Substantial decrease	5.6	6.0	6.3	7.0	7.3

<u>Manufacturers' orders</u>. New orders for durable goods rose 0.6 per cent in June, according to preliminary data--slightly more than indicated by the advance report. It was the second straight month of increase. Shipments also increased, and the backlog of durable goods orders dropped 1 per cent for the sixth month in a row.

In the second quarter as a whole, durable goods orders increased half a per cent, after their sharp (6.5 per cent) first-quarter decline. The rise occurred in major consumer goods and materials industries. Defense orders changed little; in the first half of this year they averaged 20 per cent below the levels of late 1968- early 1969. Orders for capital equipment continued to drop in the second quarter and were 8 per cent below the high reached in the fourth quarter of last year.

CHANGES IN VALUE OF MANUFACTURERS' NEW ORDERS
(Seasonally adjusted, changes in averages of monthly data, millions of dollars)

	IQ 1970 from IVQ 1969	IIQ 1970 from IQ 1970
Manufacturing, total	-1,973	234
Durable	-2,027	180
Nondurable	54	54
Selected groups:		
Home goods and apparel	- 67	144
Household durables	- 39	68
Defense products	- 392	-51
Capital equipment	- 280	-416
Producers' capital goods industries*	- 212	-175
Automotive equipment	- 557	312
Construction materials	- 290	122
Iron and steel	- 294	223

* Formerly titled "machinery and equipment.

The second-quarter increase in durable goods orders was smaller than that in the second quarter of 1967, when orders increased nearly 5 per cent in both current and constant dollars. The increase in the second quarter of 1970 amounted to less than 1 per cent in current dollars, and a slight decline is indicated after correction for price increase.

Inventories. The book value of business inventories rose at a $4.2 billion rate in June, after changing little in May. A decline in durable manufacturer's stocks was more than offset by a sharp increase at both durable and nondurable goods retailers.

For the quarter as a whole, book value growth at manufacturing and trade establishments was slightly above the first-quarter rate. Moreover, with the slowing rate of increase in the wholesale price index, the valuation adjustment is likely to be lower than in the first quarter.

Growth of durable manufacturers' inventories slowed further in the second quarter, with stocks declining at the defense, automotive, and household durables industries. Retail auto dealers' stocks were rebuilt somewhat after the first quarter's rapid liquidation.

CHANGE IN BOOK VALUE OF BUSINESS INVENTORIES
(Seasonally adjusted annual rates, billions of dollars)

	1970				
	QI	QII Prel.	April	May	June Prel.
Manufacturing and trade, total	4.7	5.1	11.1	- .1	4.2
Manufacturing, total	4.1	3.4	10.3	1.8	-1.8
Durable	2.9	.6	5.1	- .9	-2.3
Nondurable	1.2	2.8	5.2	2.7	.5
Trade, total	.6	1.7	.8	-1.9	6.0
Wholesale	1.9	.8	1.2	.6	.6
Retail	-1.3	.9	- .4	-2.5	5.4
Durable	-2.3	.3	- .7	-1.0	2.5
Automotive	-1.8	1.1	.2	.9	2.1
Nonautomotive	- .5	- .8	- .9	-1.9	.4
Nondurable	1.0	.6	.3	-1.5	2.9

The over-all inventory-sales ratio was cut in June, as declines continued at durable and nondurable manufacturing and wholesale trade. Inventories rose relative to sales throughout the major retail groups, however. The recent slowdown of investment inventory has brought stocks into better alignment with sales, and recent ratios for the cyclically significant durable manufacturing and total trade groups are comparable to those of mid-1967 and other periods when the economy was on the verge of renewed expansion. The ratio of durable manufacturers' inventories to unfilled orders rose further, however, and is at the highest point since its historical peak in November 1962.

INVENTORY RATIOS

	1967		1970	
	May	June	May	June (prel.)
Inventories to sales:				
Manufacturing and trade, total	1.59	1.57	1.58	1.57
Manufacturing, total	1.79	1.78	1.76	1.74
Durable	2.11	2.08	2.13	2.11
Nondurable	1.41	1.41	1.32	1.30
Trade, total	1.37	1.35	1.37	1.38
Wholesale	1.22	1.20	1.21	1.20
Retail	1.47	1.44	1.48	1.50
Durable	2.02	1.95	2.13	2.15
Automotive	1.51	1.43	1.78	1.79
Nonautomotive	2.74	2.70	2.63	2.66
Nondurable	1.21	1.20	1.20	1.22
Inventories to unfilled orders, durable manufacturing	.681	.673	.789	.795

Cyclical indicators. In June, the preliminary leading indicator composite was unchanged from a downward-revised May level. The index released to the press was off a tenth of a point, but the series has since been revised by inclusion of the slight June increase in contracts and orders for plant and equipment. The six-month decline in the leading composite during the current economic slowdown is now calculated at 3.7 per cent, greater than the comparable 1960-61 drop but less than the declines in the other postwar recessions. June changes in coincident and lagging composites were small.

COMPOSITE CYCLICAL INDICATORS
1963 = 100

		12 Leading Indicators	5 Coincident Indicators	6 Lagging Indicators
1969:	December	151.9	173.7	200.9 (H)
1970:	January	149.4	173.2	200.0
	February	150.4	173.4	199.3
	March	148.0	173.5	198.3
	April	148.3	173.7 (H)	198.5
	May	146.3	172.6	198.5
	June (prel.)	146.3	172.8	198.3

(H) Current high value.

Leading series declining in June were housing permits, materials prices, stock prices, and the ratio of price to unit labor costs. The workweek was unchanged. Upward influences were provided by slight increases in durable goods new orders and contracts and orders for plant and equipment, by a drop in initial unemployment claims, and by the trend adjustment which contributes an increase of .35 per cent each month. The principal reason for May's downward revision appears to have been the sharp drop in the preliminary inventory data.

Preliminary data for July indicate an increase in common stock prices and the manufacturing workweek and a decline in initial unemployment claims, but a further decline in industrial materials prices.

Construction and real estate. Total outlays for new construction put in place remained virtually unchanged in July, according to preliminary Census estimates. At a seasonally adjusted annual rate of $89.0 billion, the July figure was 2 per cent below a year earlier; in constant dollars, however, the year-over-year decline amounted to more than 7 per cent. Private residential construction expenditures, reflecting the higher level of June starts, apparently halted the downward trend of the past three months. In the public sector, State and local outlays continued near the reduced April rate.

NEW CONSTRUCTION PUT IN PLACE
(Confidential FRB)

	July 1970 ($ billions) 1/	Per cent change from June 1970	Per cent change from July 1969
Total	89.0	--	- 2
Private	62.1	--	- 2
Residential	27.9	+1	- 8
Nonresidential	34.2	--	+ 4
Public	26.9	--	- 3
Federal	3.3	+1	+ 5
State and local	23.6	--	- 4

1/ Seasonally adjusted annual rates; preliminary. Data for the most recent month (July) are confidential Census Bureau extrapolations. In no case should public reference be made to them.

Tending to support recent indications of some improvement in the market for homes, seasonally adjusted sales of new single-family homes by merchant builders rose in June to the highest rate in over a year. As a result of this increase, the builders' sales/stock ratio improved further during the month. The available data continues to suggest that buyers are still concentrating on lower priced homes and that some change in the mix of builders' inventories, toward more lower priced units, is occurring. The average price of used homes sold rose again in June, but a drop in the demand for higher-priced homes and some downward shading in the asking prices of such units helped to hold the average price of used homes sold to no more than 5 per cent above the level of a year ago.

Labor market. The labor market continued to ease in July. Unemployment moved back up to 5 per cent of the labor force and nonfarm payroll employment declined further along a broad front.

All of the July increase in unemployment occurred among adults, with especially sharp rises for women and 20-24 year-old men, for whom unemployment had declined in June. Teenage unemployment was little changed in July, but their seasonally adjusted labor force and employment levels continued well below the average of the January-May period; the shortage of jobs has apparently deterred some youngsters from seeking work this summer.

The unemployment rate for adult men rose slightly in July as did the rate for married men. Rates for these overlapping groups were about twice as high as in early 1969 and were still edging up. Unemployment in manufacturing continued to increase, and the closely-related rate for blue-collar workers rose to 6.6 per cent, its highest level in over six years. Long-term unemployment also continued to

SELECTED UNEMPLOYMENT RATES
(Seasonally adjusted)

	1969	1970		
	July	May	June	July
Total	3.5	5.0	4.7	5.0
Men aged 20 to 24	5.3	7.7	7.2	9.1
Men aged 25 and over	1.7	2.9	2.9	3.0
Women aged 20 and over	3.7	5.1	4.5	5.0
Teenagers	12.2	14.3	14.6	13.9
Insured unemployed	2.2	3.6	3.7	3.7*
White-collar workers	2.2	2.8	2.6	3.1
Blue-collar workers	3.8	6.2	6.3	6.6

* Estimated monthly average.

edge higher. Over the past year, the number of persons unemployed for 15 weeks or longer has increased from 400,000 to 700,000 (seasonally adjusted).

The civilian labor force, which had declined somewhat in May and June--almost entirely among adult women and teenagers--rose sharply in July. Despite the July pickup, the labor force was no higher than in March and April. A slowing of labor force growth--especially among more marginal workers--has occurred in each of the postwar downturns, presumably because the increasing scarcity of job openings discouraged some workers from seeking jobs.

Payroll employment. Nonfarm payroll employment, which had been rising through April, fell by a total of 700,000 in the next three months (adjusted for changes in strike activity) and in July was little higher than a year earlier. The drop in total employment since April has reflected both continued large declines in manufacturing and the emergence of reductions in services, trade and construction. The reductions in manufacturing employment continue to include office and supervisory workers as well as production workers. In addition, the Federal government has been cutting back civilian defense employment and dismissing temporary workers hired for the 1970 Census.

NONFARM PAYROLL EMPLOYMENT, 1970*
(Seasonally adjusted, in thousands)

	Total	Manufacturing	Nonmanufacturing
Change from prior month:			
January	150	-64	214
February	33	-209	242
March	113	7	106
April	21	-146	167
May	-214	-175	-39
June	-306	-108	-198
July	-194	-103	-91

* Adjusted to exclude effects of major strikes.

The downtrend in manufacturing employment, which began last fall and intensified in the early months of 1970, may be easing somewhat. The average workweek--a fairly reliable leading indicator--has held at a little less than 40 hours for the past three months. And although employment declines were evident in June and July in most of the 21 manufacturing industries, the over-all declines were somewhat smaller than in April and May.

Earnings. Since January, hourly earnings of nonsupervisory workers in the private nonfarm sector have increased 2.9 per cent, compared with a 3.4 per cent advance in the corresponding period of 1969. Hourly earnings in July were 17 cents, or 5.6 per cent, higher than a year earlier. So far this year, weekly earnings have advanced 4.3 per cent, as compared with a 5.0 per cent gain last year. The moderation of the rate of growth of both hourly and weekly earnings largely reflects the sharp reductions of overtime work at premium pay and the heavy layoffs of high-wage workers in the durable goods manufacturing industries (both factors tend to depress the average earnings figures).

Productivity. Output per manhour increased at an annual rate of 3.3 per cent in the private nonfarm economy in the second quarter. The increase resulted from a sharp drop in employment and working hours while real output leveled off. Both output and productivity had declined in the first quarter. As a result of the rise in productivity and the smaller gains in earnings, noted above, the increase in unit labor costs slowed sharply in the second quarter.

PRODUCTIVITY AND UNIT LABOR COSTS, PRIVATE NONFARM ECONOMY
(Seasonally adjusted)

	Compensation per manhour	Output per manhour	Unit labor costs
Change from previous quarter, annual rate:			
1969: I	5.5	-1.5	7.1
II	5.8	-0.4	6.3
III	7.3	.6	6.6
IV	7.7	.3	7.3
1970: I	6.6	-2.9	9.8
II	5.6	3.3	2.2

Industrial relations. Wage and benefit increases provided by major collective bargaining settlements were much larger in the second quarter of 1970 than in the first--up an average of 11 per cent a year--and the number of workers covered was also substantially greater. For the first half as a whole the annual rate of increase in wages and benefits averaged nearly 10 per cent over the life of the contract for all major contracts in private nonfarm industries. Increases averaged about 8 per cent in 1969 and 6.5 per cent in 1968.

WAGE AND BENEFIT INCREASES
IN PRIVATE NONFARM CONTRACT SETTLEMENTS
(Mean increases in per cent)

	Year		1970		
	1968	1969	IQ	IIQ	1st Half
Wages and Benefits: 1/	6.5	8.2	8.0	10.9	9.7
Wage Rates 2/					
First Year:	7.4	9.2	10.2	15.4	13.4
Manufacturing	7.0	7.9	8.2	8.4	8.3
Nonmanufacturing	7.8	10.8	12.8	17.4	16.2
Average over the life of contract:	5.9	7.6	7.7	10.6	9.5
Manufacturing	5.2	6.0	5.5	6.6	6.0
Nonmanufacturing	6.5	9.3	10.7	11.8	11.4

1/ Based on settlements covering 5,000 or more workers.
2/ Based on settlements covering 1,000 or more workers.

Settlements in nonmanufacturing activities continued to provide much larger wage increases than in manufacturing. The wage increase in nonmanufacturing mainly reflected the very large construction and trucking industry settlements. In the trucking settlement, wage and benefit increases together averaged about 13 per cent annually; first-year wage increases alone totaled 85 cents, or 22-1/2 per cent. Construction workers covered by new contracts during the second quarter received wage increases averaging about 18 per cent in the first year.

With most of the 1970 collective bargaining schedule in manufacturing lying ahead, pressure on wages may intensify in this important sector. Only one-fourth of the 2.7 million workers covered by major contracts to be reopened this year negotiated new agreements during the first six months. Of the remaining 2 million workers, more than 700,000 are employees of General Motors, Ford and Chrysler where contracts expire September 14. The auto industry settlement will probably set the wage pattern for the auto supplier plants and in the farm and construction equipment industries.

Unemployment insurance legislation. The President on August 10 approved legislation which extends coverage of the State unemployment insurance programs and automatically triggers an extension of the number of weeks of benefits during periods of high unemployment nationally or at the State level. The Act will be effective at the national level January 1, 1972. The Federal government will pay one half the cost of the extended benefit program.

About 4.7 million workers will be newly covered, mainly employees of small firms, private nonprofit organizations, State hospitals and institutions of higher education. Extension of benefits will be automatically triggered for all States when the seasonally adjusted national rate of insured unemployment reaches 4.5 per cent for three consecutive months. (This rate was 3.7 per cent in June, the latest figure available.) Provision is also made for extension of benefits in individual States with high unemployment when the overall rate is not high enough to trigger a national extension. For individual States, the automatic trigger occurs when the State's unemployment rate for 13 consecutive weeks is 120 per cent or more of the rate for the corresponding period in each of the two preceding years and is 4 per cent or more.

Generally, workers covered by unemployment compensation will receive 13 additional weeks of benefits if unemployment goes above the prescribed rate. In several States rates are now high enough to trigger automatically the extension of benefits, but such extension awaits passage of enabling legislation by the State before the program becomes effective. In times of nationwide recession, also, the new legislation will eliminate the necessity for enacting a temporary extension of benefits, as was done in 1958 and 1961.

Wholesale prices. Wholesale prices rose at a seasonally adjusted annual rate of 6.0 per cent in July (July 9th to July 14th), with prices of farm and food products up 16.0 per cent and those for industrial commodities up 3.2 per cent. A slower rate of increase in industrial commotities than over the previous 3 months to a large extent reflected weakness in prices of metals. However, the number of increases (112) in the 228 product classes prepared by the BLS was somewhat larger in July than the average for the preceding 3 months (98).

WHOLESALE PRICES
(Seasonally adjusted percentage changes at annual rates)

	June '69 to Dec. '69	Dec. '69 to Mar. '70	Mar. '70 to June '70	June '70 to July '70
All commodities	4.2	4.0	1.0	6.0
Farm products, and processed foods and feeds	5.4	6.6	-10.3	16.0
Industrial commodities	4.1	3.4	4.3	3.2
Metals and metal products (unadj.)	10.0	10.3	6.6	- 0.9
Machinery and equipment (unadj.)	5.6	3.9	3.2	5.8

The July increase in prices of farm and food products more than offset declines posted from March to June. However, many of the commodity prices that had risen sharply in July have since receded, as shown in the table below.

Percentage Changes in Spot Prices of Selected Agricultural Commodities

	June 9 to July 14	July 14 to August 6
Coffee	0.9	2.3
Sugar	- 0.9	0.6
Eggs	12.8	-20.5
Broilers	3.6	-10.5
Hogs	6.7	- 9.3
Steers	3.3	- 0.3
Wheat	- 1.9	3.1
Corn	2.8	- 2.3
Soybeans	4.7	- 5.2

Source: Wall Street Journal. Spot price changes may vary from those which may be shown by the BLS for the same or similar commodities.

The trend of wholesale foods prices is still expected to be down over the months ahead, although prices of major crops may fluctuate. Prices of red meat, especially of pork, are expected to be lower this fall, with the largest pig crop in 27 years in prospect.

Among industrial commodities, an increase of 0.5 per cent in prices of machinery and equipment from June to July was larger than in any month since last January. Prices of fuels and chemicals also moved up, and increases were posted for tires and paper products. Coal prices are still rising, and prices for natural gas are under growing pressure, with additions to supply failing to keep up with rapidly growing demand. Further advances in prices of residual fuels (up more than 5 per cent in July) are likely as demand increases while supply and distribution problems persist.

On the other hand, the metals and metal products group declined for the first time in over a year and one-half, as nonferrous metals prices fell for the second successive month--reflecting cuts for lead and copper mill products. Since mid-July, further cuts have been made in the prices of brass mill products as a result of a drop in price for dealer copper and in reaction to increased competition from imports. Dealer copper and copper scrap were recently selling for less than producer copper--for the first time in seven years. The price of lead was reduced recently by another 1/2 cent a pound, following by about a month a cut in July. Steel scrap receded somewhat from recent high levels, probably reflecting lower operating rates in the steel industry. Lumber and wood products prices declined further in July as did prices of hides and skins and crude natural rubber.

Consumer prices. The slower rise in the CPI over the second quarter was mainly attributable to a much more moderate rise in food prices than earlier and to a leveling off in mortgage interest rates, which had risen very sharply in the first quarter. Indeed, both seasonally adjusted food prices and mortgage interest rates declined in June. However, there was little change through midyear in the basic trend of retail prices of non-food commodities or of service costs. The 7 per cent rate of increase in service prices in the second quarter was close to the average for last year--when interest costs were rising rapidly.

Despite the fact that a seasonal (or perhaps more than seasonal) increase in food prices will probably show up in the July CPI a tendency toward stability in prices of foods for home use is likely in the second half of the year, reflecting rising supplies of such important foods as pork, poultry, eggs, and potatoes. Such a leveling off would tend to moderate the advance in consumer prices, even if services and non-food commodities should continue to rise at recent rates.

The acceleration in non-food commodity prices last quarter (and in June) mainly reflects large jumps in used car prices. New car prices have been fairly stable; apparel price increases speeded up since last quarter from the first quarter pace, when price increases were exceptionally small owing to January sales.

Used car prices may decline soon, if last year's experience is any guide. Last year, after a spectacular rise between January and April, such prices started down and lost most of the previous gain by early this year. (This series is too short for seasonal adjustment.) On the other hand, the fall rise in new car prices will probably be larger this year than last. The nominal rise, judging from the Ford announcement, will not only be larger, but in addition, the service warranty is being withdrawn adding to the price increase after allowance for quality change.

CHANGES IN CONSUMER PRICES

(Seasonally adjusted annual rates)

	June '69 to Sept. '69	Sept. '69 to Dec. '69	Dec. '69 to March '70	March '70 to June '70	May '70 to June '70
All items	5.3	6.2	6.1	5.7	4.5
Food	6.0	10.0	5.2	1.2	- 4.5
Non-food commodities	2.8	4.2	2.9	6.2	4.9
Apparel	4.6	5.2	2.4	3.5	4.6
New cars	.2	3.8	2.5	1.2	0
Services	7.5	6.3	10.8	7.1	7.0
Medical care	7.3	1.4	9.7	8.1	8.7
Mortgage interest rates	9.8	4.1	26.6	.5	- .8
Add					
Addendum:					
Services less home finance	5.8	5.3	7.5	7.7	6.5
Used cars- (not adjusted)	-21.2	8.2	-20.3	49.0	42.3

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Price indexes for the GNP. The GNP implicit price deflator rose at an annual rate of 4.9 per cent in the fourth quarter of 1969 and at a rate of 6.4 per cent in the first quarter of 1970. But the increase in the second quarter was down to 4.2 per cent, a rate considerably below the average for 1969. While the retroactive Federal government pay increase accounts in large part for the step up in the first quarter, the deflator for the private economy (which excludes government salaries) also shows a pattern similar to the overall deflator--from a rise of 5.3 per cent in the first quarter and 4.1 per cent in the second. This pattern of change in the implicit deflator in the past two quarters reflects in the main shifts in the composition of the GNP rather than a changing rate of price increase.

The implicit deflator was not designed to measure price changes but is rather a byproduct of the transaction of current dollar GNP to constant dollar GNP. The implicit weights are, in concept, current period quantities valued at base year (1958) prices; the weights thus change--to a varying degree--from quarter to quarter. Shifts in weights towards components that have increased more rapidly in price since 1958 result in a higher index than would fixed weights and vice versa. Thus, changes in the deflator are to a varying extent independent of current price movements. For example, autos have increased relatively little in price since 1958, and are consequently deflated by an index of only 107, compared with an index of 134 for the GNP as a whole and indexes as high as 139 for consumer services and 148 for non-residential construction. When consumer demand for autos declines as a proportion of GNP, as it did in the first quarter, the rate of increase in the overall GNP deflator is raised on this account. The increase in the implicit GNP deflator in the first quarter would have been 6.0 per cent instead of 6.4 per cent if auto purchases had been the same percentage of GNP as in the fourth quarter.

The OBE has supplied us with confidential estimates of price change for the GNP based on chain weights.[1/] These are useful for comparing prices in two adjacent quarters since they measure the quarterly change in prices assuming that the composition of expenditures in the second quarter is unchanged from the actual composition in the first.[2/]

1/ For a detailed account of the GNP implicit deflator and comparisons with fixed weight and chain indexes in 1965-1968, see "Alternative Measures of Price Change for GNP" by Allen H. Yound and Claudia Markins, Survey of Current Business, March, 1969.

It should be noted that this article commented as follows: "The implicit deflator for the GNP has increased at the same rate as fixed weighted prices indexes over the past 3 years [IV-1965 to IV-1968]. Within this span, however, the alternative price measures have on occasion moved differently from the delator."

2/ A chain-weighted price index differs from a fixed base-year-weighted index such as the CPI and WPI. For a change between two adjacent quarters, the two indexes would be equivalent if the composition of expenditures in the first of the two quarters were the same as in the base year of the fixed weighted index.

As may be seen in the table, the rates of increase of the chain-weighted price index for the gross private product show a fairly steady price increase over the last three quarters, at an annual rate of 4.7 - 4.8 per cent.

COMPARISON OF GNP DEFLATORS WITH CHAIN INDEX

Changes from preceding quarter,
Seasonally adjusted annual rates, in per cent

	1969		1970			
	IV Q		I Q		II Q	
	Implicit Deflator	Chain Index	Implicit Deflator	Chain Index	Implicit Deflator	Chain Index
Gross national product	4.9	4.9	6.4	5.9	4.2	4.8
Gross private product	4.6	4.7	5.3	4.7	4.1	4.8
Personal consumption expenditures	4.8	4.9	5.1	4.8	4.5	4.8
Durable goods	2.3	2.6	3.0	2.6	2.0	2.0
Nondurable goods	5.5	5.6	4.5	4.7	4.4	4.4
Services	5.0	5.0	5.7	5.8	6.0	6.2
Business fixed investment	3.0	3.7	5.0	4.4	2.7	4.5
Non-residential structures	4.2	4.6	4.7	4.3	4.3	5.5
Producers' durable equipment	4.2	4.4	5.6	4.7	2.5	4.0
Residential structures	1.0	1.0	3.8	3.8	4.6	4.6
Government purchases	6.0	5.9	11.3	10.3	7.0	5.1

Farm production prospects. The crop report released at 3:00 p.m. on August 11 can be expected to spark a mildly bullish reaction in future markets even though the small declines in prospects for feed grains and soybeans were not entirely unexpected. Based on August 1 conditions, the corn crop is forecast at 4.7 billion bushels, 3 per cent above last year's record but 3 per cent below the July 1 forecast. Output of the four feed grains is expected to be about the same as last year and possibly a little less than anticipated utilization if exports equal those of last year. A soybean crop of 1.1 billion bushels, nearly the same as last year, is forecast.

The index of total crop output is forecast at 121 (1957-59 = 100), the same as last year's record and yields are down a little, as shown in the table. Aside from the close balance in supply and demand prospects for feed grains and soybeans, August 1 prospects are relatively favorable. Smaller food grains and processing vegetable crops reflect planned adjustments to prospective needs. In the south, a 10 per cent larger cotton crop is in prospect and a record peanut crop. Tobacco is expected to equal last year's output.

Prospects are mixed for the fresh market crops which have a direct impact on retail prices. Summer vegetable and melon crops are larger than last year. Marketings from the short early summer potato crop will soon be supplemented by the more ample late summer crop. Output of sweet potatoes is smaller than last year and so is output of nearly all of the deciduous fruits. Plentiful citrus fruits are in prospect for the 1970/71 season starting in September.

Total output of farm products in 1970 is expected to top last year's record by a narrow margin if the August 1 crop forecast is realized. But much of the critical growing season lies ahead and substantial changes between the August 1 forecast and the final harvest may occur. Record livestock output seems to be assured. Liveweight production of meat animals is estimated to be 5 per cent larger than last year but it should be pointed out that marketings for slaughter (another concept) will be up a little less than 2 per cent. More turkeys and broilers are being raised this year than last and egg production will average above last year if anticipated increases in the latter part of the year occur. Milk production is likely to remain the same as in 1968 and 1969.

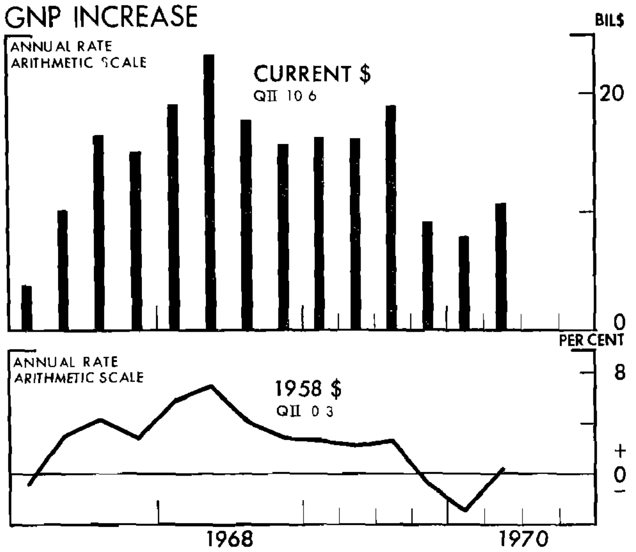
INDEX NUMBERS OF FARM OUTPUT AND RELATED VAIRABLES
(1957-59 = 100)

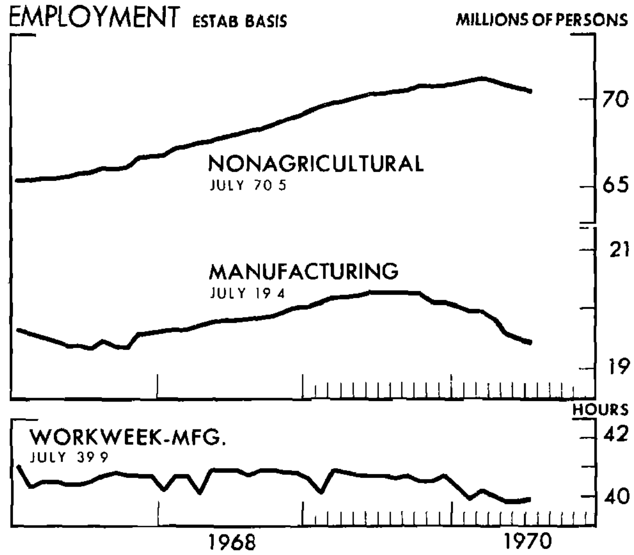
Item	1969	1970 1/ Estimate	Per cent change
Farm output	121	122	.8
All livestock products	118	121	2.5
Meat animals	122	128	4.9
Dairy products	98	98	0
Poultry and eggs	139	142	2.2
All crops	121	121	0
Feed grains	123	123	0
Food grains	130	121	-6.9
Cotton	82	90	9.8
Tobacco	104	104	0
Oil crops	196	195	- .5
Acreage for harvest (59 crops)	90	91	.9
Yield per acre (28 crops)	132	130	-1.5

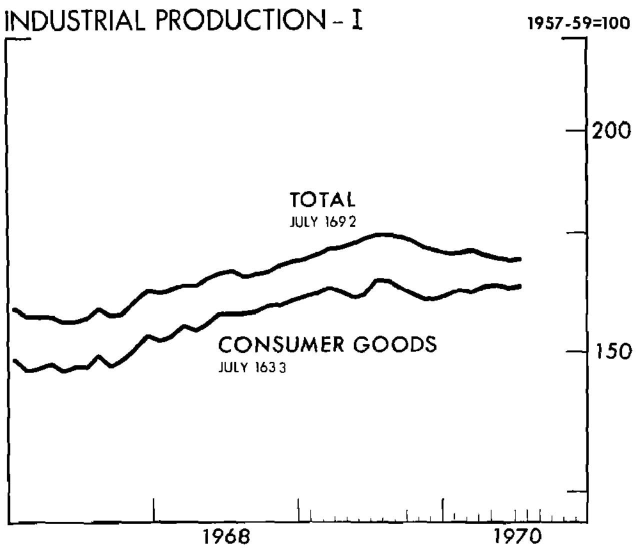
1/ The crop indexes are estimates of the Crop Reporting Board and are based on August 1, 1970, conditions. The livestock product and total farm output indexes are estimates prepared by Donald Durost of the Economic Research Service of the USDA.

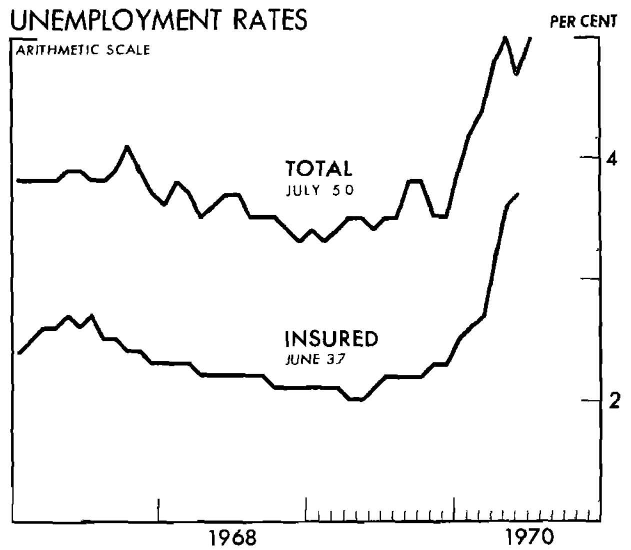
ECONOMIC DEVELOPMENTS - UNITED STATES

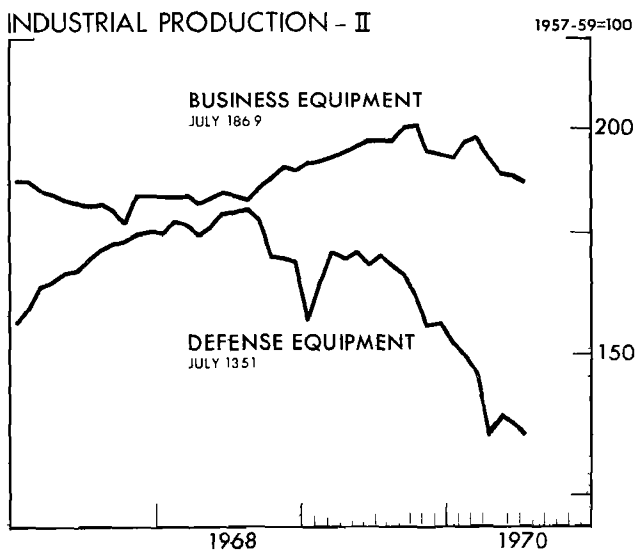
SEASONALLY ADJUSTED, RATIO SCALE

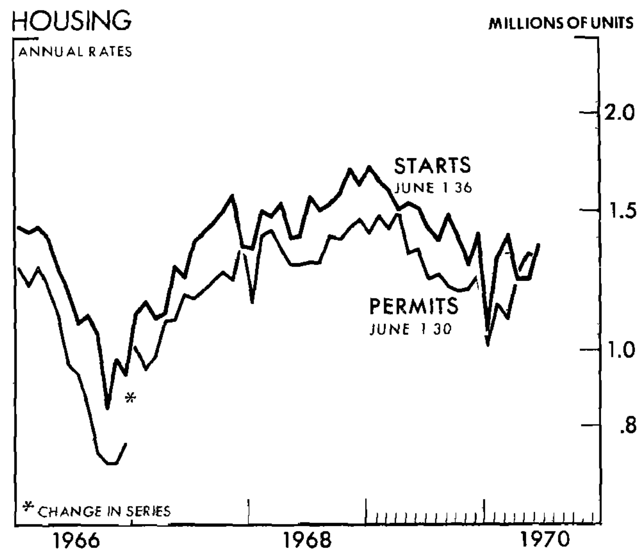








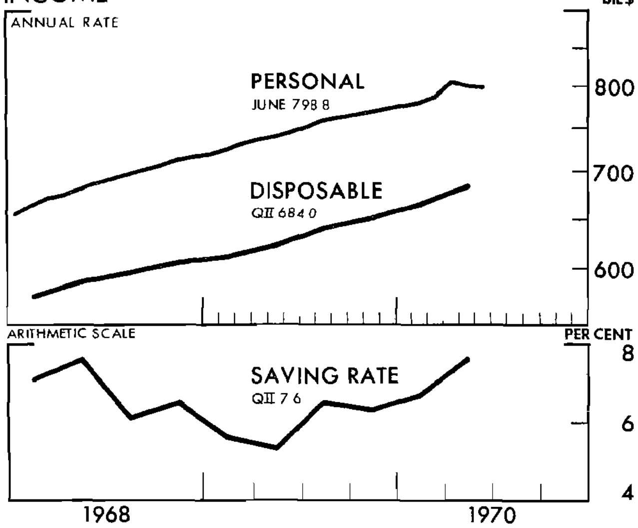




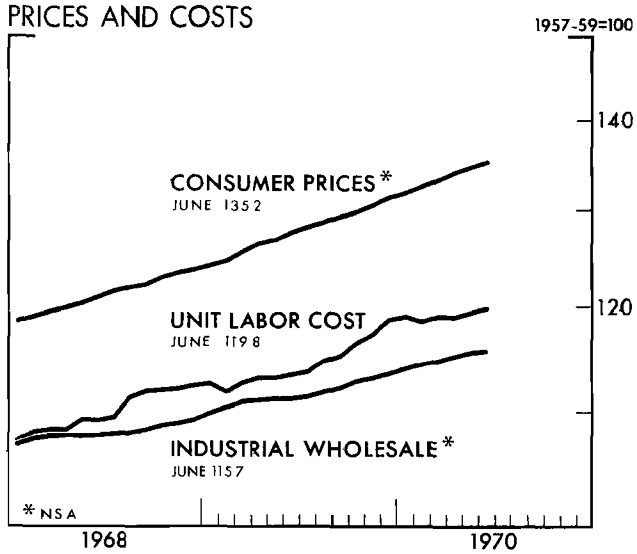
ECONOMIC DEVELOPMENTS - UNITED STATES

SEASONALLY ADJUSTED, RATIO SCALE

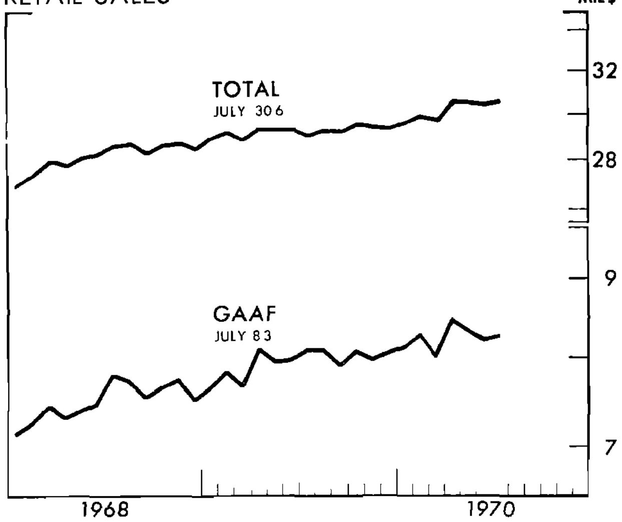
INCOME



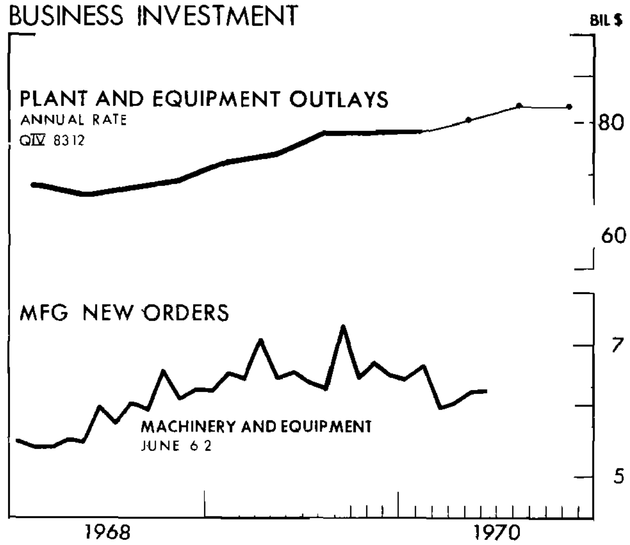
PRICES AND COSTS



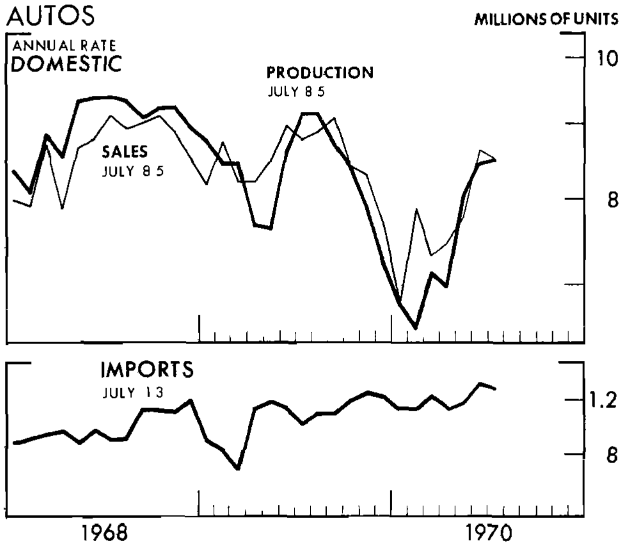
RETAIL SALES



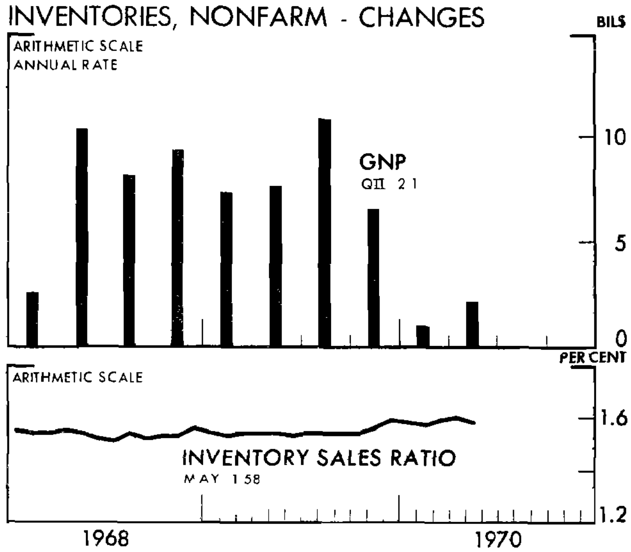
BUSINESS INVESTMENT



AUTOS



INVENTORIES, NONFARM - CHANGES



THE ECONOMIC PICTURE IN DETAIL

Domestic Financial Situation

Monetary aggregates. The money supply increased at a 4.1 per cent annual rate in July, close to the average rate of increase during the second quarter of the year. Money balances ballooned in the first two weeks of the month (presumably in part reflecting a buildup in response to the abrupt shift of investors away from the commercial paper market) receded sharply during the middle of the month, then advanced again toward month-end.

MONETARY AGGREGATES
(Seasonally adjusted percentage changes, at annual rates) 1/

	1970			
	QI	QIIp	June	July
Money stock	3.8	4.2	-1.8	4.1
Commercial bank time and savings deposits	.4	13.8	8.4	35.2
Member bank deposits	.6	6.0	5.8	22.3
Member bank deposits plus nondeposit sources 2/	.5	6.5	7.0	18.1

1/ Based on monthly average of daily figures for deposits and monthly average of weekly figures for nondeposit funds. Quarterly changes are calculated from the average amounts outstanding in the last month of each quarter.

2/ Includes all deposits subject to reserve requirements plus the following nondeposit sources: commercial paper issued by a holding company or bank affiliate; loans or participation in pools of loans sold under repurchase agreement to other than banks and other than banks' own affiliates or subsidiaries; Euro-dollars borrowed directly through brokers or dealers; liabilities to banks' own branches in U.S. territories and possessions; and liabilities to banks' own foreign branches.

p--preliminary

While growth in the money stock was moderate in July, a very large advance was recorded in total commercial bank deposits, primarily because of an exceptionally strong expansion in time and savings deposits. Inflows of funds into large CD's paced the time deposit expansion. On a seasonally unadjusted basis, the volume of outstanding CD's increased nearly $5.0 billion at large commercial banks in the 5 weeks following the suspension of ceiling rates on short-term CD's on June 24. Inflows into consumer-type deposits and "other" time deposits at weekly reporting banks were also quite strong during this period, probably in part reflecting a shift by consumers toward less risky forms of saving. Country member banks also shared in the step-up of incoming deposit funds, recording an increase in total time and savings deposits for the 5 weeks ending July 29 that was more than 3 times as large as the expansion in the preceding 5-week period.

NET CHANGE IN TIME AND SAVINGS DEPOSITS
(Billions of dollars, not seasonally adjusted)

	May 20-June 24 1/		June 24-July 29 1/	
	1967-69 average	1970	1967-69 average	1970
Weekly reporting banks				
Total time and savings	-.1	.1	.4	6.8
Consumer-type	.5	.4	.2	1.1
CD's	-.6	-.1	.5	4.9
All other time	--	-.2	-.3	.8
Country banks				
Total time and savings	.3	.5	.8	1.7

1/ Dates are for 1970; comparable dates used for other years.

Commercial banks used part of their incoming deposit funds to reduce other liabilities in July and the credit proxy adjusted for non-deposit sources increased at a somewhat slower pace than total member bank deposits. The main decline was in bank borrowing from foreign branches, but borrowing from other sources outside the U.S. was also reduced and loan RP's continued to edge downward. Outstanding commercial paper issued by holding companies and affiliates declined during the early part of the month, extending a downtrend prevailing since early June, but this trend was reversed as the month progressed, and on balance bank-related commercial paper indebtedness showed a fairly strong increase for the month.

Bank credit. Commercial bank credit adjusted for loan sales to affiliates and subsidiaries rose sharply in July after having remained essentially unchanged in June. Substantial acquisitions of U.S. Treasury securities, an unusually large rise in loans to finance companies, and an increase in loans to security dealers were primarily responsible for the step-up in bank credit growth. In contrast to these developments, acquisitions of other security holdings remained moderate, as in other recent months, and comparatively small gains were recorded in business, real estate and consumer loans.

COMMERCIAL BANK CREDIT ADJUSTED
TO INCLUDE LOAN SALES TO AFFILIATES 1/
(Seasonally adjusted percentage changes, at annual rates)

	1969	1970			
	2nd half	QI	QIIr	June r	July
Total loans & investments 2/	2.9	2.5	5.3	.9	16.6
U.S. Govt. securities	-15.6	-12.3	30.2	18.0	31.1
Other securities	- 1.4	9.5	9.9	6.5	8.0
Total loans 2/	7.8	3.4	- .3	-3.4	16.1
Business loans 3/	9.5	5.5	5.8	4.3	3.2

1/ Last Wednesday of month series.
2/ Includes outright sales of loans by banks to their own holding companies, affiliates, subsidiaries, and foreign branches.
3/ Includes outright sales of business loans by banks to their own holding companies, affiliates, subsidiaries, and foreign branches.
r - Revised.

The expansion in holdings of U.S. Treasury securities was associated with the sale by the Treasury of two tax anticipation bills. Full credit to tax and loan accounts was accepted in payment. Commercail banks acquired nearly all of the $4-3/4 billion total of bills sold and by month-end still retained a substantial volume of these securities. The growth in loans to nonbank financial institutions occurred primarily during the early weeks of the month when many of these firms encountered difficulty in rolling over their commercial paper indebtedness. After the middle of the month, the rate of growth in these loans slowed and in the final week of the month a fairly sizable reduction was recorded.

Growth in business loans (adjusted for loan sales) was weaker than the advance recorded in June which in turn failed to match the average rate of growth recorded for the second quarter as a whole. The continued weakness displayed by July loan data appears particularly significant in view of the fillup to business loan demand provided by refinancings of commercial paper, some of which appears to have involved nonfinancial firms. An easing in business loan demand, however, is hardly surprising in view of the slowdown in economic activity. Rates of change in business loans have lagged behind changes in general economic activity in other post-war periods of economic slack, although the exact timing has not been predictable. Moreover, the recent slowing seems consistent with the modest rate of inventory investment, heavy corporate borrowing in the bond market, and growing indication of a cutback in business spending on fixed investment.

Other short-term credit markets. Outstanding commercial paper continued to decline during July. While we do not have data for the last two days of the month, a preliminary estimate suggests a seasonally adjusted decline of $1.4 billion in outstandings in July, as compared with a drop of $993 million in June. Seasonally unadjusted data, however, show an overall July decrease of about $200 million in outstandings as compared with a fall of $1.9 billion in June.

Dealers report that the market is still wary of anything other than top-rated paper. Large finance companies generally have had no difficulty in rolling over their maturing paper and in some cases they have picked up sizable amounts of new money. But in the dealer-placed market those firms with lower-grade paper outstanding are being encouraged to line up alternative sources of financing. Dealers have in some cases bought back paper, and dealer holdings may decline for a few more weeks as such paper matures.

Rates on commercial paper, finance paper and bankers' acceptances maturing in 30 days or less fell 25 basis points from July 22 to August 5, after rising in the first part of July. Some reduction in rates has also been visible in daily quotations on other maturities of commercial paper and finance paper. This softening has occurred in conjunction with the downward movement in rates on 60-89 day certificates of deposit. The spread between commercial and finance paper, on the one hand, and Treasury bills on the other had become particularly wide around midyear, but has narrowed again recently as bill rates have moved up partly under the weight of heavy dealer positions arising from the Treasury tax bill financings in July.

COMMERCIAL AND FINANCE COMPANY PAPER
(End-of-month data, in millions of dollars)

	May	June	July 1/
		Amounts outstanding	
Total commercial and finance paper 2/	39,503	38,510p	37,102e
Bank related 3/	7,465	7,468	7,713p
Nonbank related 4/			
Placed through dealers	12,969	12,486p	11,658e
Placed directly	19,069	18,556p	17,731e
		Net change	
Total commercial and finance paper 2/	1,227	-993p	-1,408e
Bank related 3/	923	3	245p
Nonbank related 4/			
Placed through dealers	808	-483p	-828e
Placed directly	-504	-513p	-825e

e/ Estimated. p/ Preliminary.
1/ Weekly data. The end-of-month data, for other than bank related, will differ somewhat from the July 29 data because of the 2 day difference in dating.
2/ Combines seasonally adjusted nonbank-related paper and seasonally unadjusted bank-related paper.
3/ Seasonally unadjusted. 4/ Seasonally adjusted.

SELECTED SHORT-TERM INTEREST RATES
(Wednesday Quotation - Discount Basis)

	1969 Nov.-Dec. highs 1/	June 24	July 22	Aug. 5	Net change (July 22-Aug. 5)
1-month					
Commercial paper	9.25 (12/31)	8.25	8.38	8.13	-.25
Finance paper	9.00 (12/31)	7.75	8.00	7.75	-.25
Bankers' acceptances	9.00 (12/31)	8.00	7.88	7.63	-.25
Certificate of deposit--new issue 2/	6.25	7.75	7.75	7.63	-.12
Treasury bill	7.54 (12/31)	6.10	6.09	6.30	.21
3-month					
Commercial paper	9.25 (12/31)	8.63	8.75	8.75	--
Finance paper	8.13 (12/31)	7.75	7.75	7.75	--
Bankers' acceptances	9.00 (12/31)	7.75	7.63	7.38	-.25
Certificate of deposit--new issue 2/	6.50	8.00	8.00	7.75	.25
Treasury bill	8.00 (12/29)	6.62	6.35	6.50	.15
6-month					
Bankers' acceptances	9.00 (12/31)	7.75	7.63	7.38	-.25
Treasury bill	8.09 (12/29)	6.84	6.38	6.65	.27
12-month					
Prime municipals 2/	6.25 (12/12)	5.20	4.44	4.30	-.14
Treasury bill	7.86 (11/24)	7.07	6.60	6.66	.06

1/ Dates of highs in parentheses; latest date used if high occurred on more than one date.
2/ Investment yield basis.

Source: Wall Street Journal's Money Rates for commercial and finance paper and bankers' acceptances; all other data from the Federal Reserve Bank of New York.

Nonbank depositary intermediaries. Continuing the pattern shown during the June-July reinvestment period, deposit growth during the whole month of July is estimated on the basis of sample data to have been strong at both savings banks and savings and loan associations, and exceptionally so at S&L's. Unadjusted for seasonality, the S&L inflow was actually the largest achieved during any July since at least 1955, and was fairly well geographically distributed.[1/] One reason for these unusually large inflows to both bank and nonbank institutions in the face of persistent adverse yield differentials between deposits and market securities may be a desire on the part of consumers to acquire deposit-type assets in view of uncertainties with respect to financial and economic conditions.[2/]

DEPOSIT GROWTH AT NONBANK THRIFT INSTITUTIONS
(Seasonally adjusted annual rates, in per cent)

	Mutual Savings Banks	Savings and Loan Associations	Both
1969 - QI	6.1	6.0	6.0
QII	4.3	3.7	3.9
QIII	2.0	2.1	2.1
QIV	3.3	.4	1.4
1970 - QI	2.6	1.5	1.9
QII p/	6.4	7.4	7.1
April*	6.6	8.6	8.0
May*	6.4	5.6	5.9
June* p/	6.0	7.9	7.3
July* e/	6.1	14.3	11.6

* Monthly patterns may not be significant because of difficulties with seasonal adjustment.
p/ Preliminary.
e/ Estimates based upon sample data.

1/ The New England and Pittsburgh FHLB districts had small outflows, according to sample data.

2/ In Massachusetts, the State Banking Commissioner, exercising newly-granted authority, set rate ceilings on deposits at uninsured nonbank thrift institutions. The only change effected by this action was a reduction in regular account rates by 25 basis points to 5.25 per cent, which is still 25 basis points above the ceilings elsewhere in the country. The FDIC and the FHLB have followed suit, so that all nonbank institutions in the State are now subject to the same ceiling rates.

The general improvement in savings and loan associations' deposit growth that has been maintained since February has afforded them the opportunity to rebuild liquidity. In sharp contrast to the previous two years, their total liquid assets increased during the first half of this year by $1.5 billion--nearly all of which represented Agency issues. Correspondingly, S&L borrowing activity has been very modest--and continued so during July--although repayments have been minimized by the FHLBB's subsidization of rates on advances guaranteed to remain outstanding for at least one year. New mortgage commitments were made at an advanced pace during May and June, but the net increase in mortgages has not yet reflected all of this buildup.

INSURED SAVINGS AND LOAN ASSOCIATIONS
Sources and Uses of Funds
(Billions of dollars, not seasonally adjusted)

	First Quarter			Second Quarter		
	1968	1969	1970	1968	1969	1970
Sources						
Deposit accounts net 1/	1.6	1.8	.4	2.0	1.4	2.7
Borrowed funds net	-.2	-.1	.3	.7	1.1	.5
Subtotal	1.4	1.7	.7	2.7	2.5	3.2
Gross mortgage repayments	3.4	3.4	3.0	3.7	3.8	3.4
Other sources net 2/	.8	1.0	.4	-.2	.1	.1
Total	5.6	6.1	4.1	6.2	6.4	6.7
Uses						
Cash and Governments net	.2	.2	-.2	--	-.7	.3
Other liquid assets net 3/	.3	.4	.7	-.1	--	.7
Gross mortgage acquisitions	5.1	5.5	3.6	6.3	7.1	5.7
Total	5.6	6.1	4.1	6.2	6.4	6.7
Memo: Net increase in mortgages	1.7	2.1	.6	2.6	3.3	2.3

1/ Includes interest credited.
2/ Includes the net changes in loans in process, reserves and surplus, and accrual of dividends. Netted out from that total are the net changes in other uses of funds.
3/ Reflects primarily Federal Agency issues, but also includes time CD's and State and local government securities.

The Federal Home Loan Bank System continues to maintain a large liquid balance of nearly $2 billion--$300 million of which will be used temporarily to purchase mortgages already committed to the System's GNMA-backed security, but which will be replaced as soon as the proceeds of the security issue are received. Nevertheless, the Home Loan Bank System continues to plnn to raise a substantial amount of new money during the balance of this year--presumably to maintain a large liquidity position readily available to advance to member institutions.

Life insurance companies. Although the rate of expansion moderated, policy loan increases continued to divert a large volume of life insurance funds from alternative investments during the second quarter.1/ This pattern had been anticipated by life insurance companies when, at the end of the first quarter, they projected their second quarter sources of funds available for investment acquisitions.

NET INCREASE IN POLICY LOANS AT 15 LIFE INSURANCE COMPANIES*
(Millions of dollars)

	First Quarter	Second Quarter
1965	80	102
1966	126	210
1967	190	162
1968	181	247
1969	269	414
1970	461	413

* These companies account for 65 per cent of policy loans held by the industry.

1/ Incomplete data for the month of July suggest that this trend of policy loan behavior probably continued.

Thus, although the policy loan increase that actually occurred during the second quarter was still extremely large by historical standards, it probably caused no disruption in the investment plans of life companies. An increase much in excess of estimates would, of course, have represented a prior claim on cash flow available to meet commitment disbursements, and therefore could have had destabilizing potential.

Life insurance companies have maintained a markedly reduced volume of new commitment activity, in accord with projections of continued pressure on funds available for commitment disbursements. The low volume of new commitments reflects not only the absolute reduction in projected available funds, but also an attempt to rebuild a recently-narrowed margin between those projected flows and scheduled commitment takedowns.

NEW COMMITMENTS MADE BY LIFE INSURANCE COMPANIES
TO ACQUIRE CORPORATE DIRECT PLACEMENTS*
(Millions of dollars)

	First Quarter	Second Quarter
1965	969	1,373
1966	1,365	1,093
1967	612	1,277
1968	813	831
1969	716	721
1970	376	499p

* Sample of companies representing two-thirds of industry assets.
CONFIDENTIAL
p/ Preliminary.

Mortgage market. With net savings flows exceptionally strong last month, the availability of mortgage funds probably increased further, although July data on nonbank thrift institution lending commitments are not yet available.

During the second quarter, there was a modest upturn in net mortgage debt formation to a seasonally adjusted annual rate of around $23 billion--the first increase in 5 quarters. While net expansion in outstanding residential mortgage debt was still unusually low and failed to recoup fully the first-quarter decline, it apparently accounted for all of the rise in the second-quarter total. Savings and loan associations, bolstered by improved deposit flows, accounted for most of the seasonally adjusted increase in net residential mortgage lending, in contrast to the quite depressed first-quarter performance for this important lender group. With new mortgage commitments rising sharply at S&L's, by the end of June the backlog of their outstanding commitments available for takedown in the future reached the highest level in 8 months. Although FNMA's net addition to its mortgage portfolio remained quite large in the second quarter, it was below earlier peaks. Meanwhile, net expansion in the mortgage portfolios of other major lender groups, including commercial banks, generally continued limited.

NET MORTGAGE DEBT FORMATION
(Billions of dollars, seasonally adjusted annual rates)

	1969				1970	
	QI	QII	QIII	QIV	QI	QIIp
Total	30.4	28.5	27.0	25.6	20.7	22.8
Type of Property						
Residential	22.1	21.2	20.0	18.6	14.2	16.7
Nonresidential	8.3	7.3	7.1	7.1	6.5	6.1
Type of Holder						
Savings and loan asso.	10.6	11.1	8.9	7.0	4.4	7.5
Mutual savings banks	3.1	2.9	1.9	2.2	1.5	2.3
Commercial banks	7.8	6.2	3.4	3.3	2.7	2.2
Life insurance companies	1.8	2.2	2.2	1.8	2.3	2.3
FNMA-GNMA	2.1	2.8	5.5	7.1	6.3	5.5
Other	5.0	3.3	5.1	4.2	3.5	3.0

p/- Preliminary

MORTGAGE COMMITMENTS OUTSTANDING AT SELECTED THRIFT INSTITUTIONS
(Billions of dollars, seasonally adjusted)

End of quarter	Savings and loan associations 1/			Mutual savings banks (New York State)			Total		
	1968	1969	1970	1968	1969	1970	1968	1969	1970
QI	6.1	7.0	5.2	2.5	3.3	2.5	8.6	10.3	7.6
QII	5.9	7.0	6.1	2.6	3.2	2.1	8.5	10.2	8.2
QIII	6.2	6.4		2.9	2.8		9.2	9.2	
QIV	6.6	5.8		3.1	2.6		9.7	8.4	

1/ Data include loans in process.

As an indication of some further improvement in underlying mortgage supply conditions, yields on 6-month forward commitments in

FNMA's latest (August 10) bi-weekly auction to purchase Government underwritten home mortgages continued downward to 9.03 per cent. This was 30 basis points below the high recorded near the end of June, and by a slim margin represented the lowest yield level since last December. Offerings to FNMA increased further as originators sought to replace lower-priced commitments obtained earlier this year with new ones at higher prices.

FNMA AUCTION

	Amount of total offers		Implicit private market yield on 6-month commitments
	Received	Accepted	
	(Millions of dollars)		(Per cent)
Weekly Auction			
1969 high	$410 (6/16)	$152 (9/8)	8.87 (12/29)
1970 high	705 (1/5)	151 (1/12)	9.36 (1/12)
May 11	269	102	9.07
18	300	136	9.13
25	290	145	9.18
June 1	224	114	9.24
Bi-weekly Auction			
1970 high	581 (1/26)	298 (1/26)	9.33 (6/29)
June 15	250	128	9.30
29	156	99	9.33
July 13	286	113	9.21
27	324	150	9.12
Aug. 10	441	180	9.03

NOTE: Average secondary market yield after allowance for commitment fee and required purchase and holding of FNMA stock, assuming prepayment period of 15 years for 30-year Government-underwritten mortgages. Yields shown are gross, before deduction of fee paid by investors to servicers of 50 basis points prior to August 10 auction, and 38 basis points thereafter. At least partially offsetting the effect of the reduction in servicing fees on bid prices and gross yields in the August 10 auction was another FNMA regulatory change permitting mortgage servicers to retain all escrow funds received on mortgages serviced under the reduced fee schedule. Under earlier practice, FNMA had retained most of these funds itself.

Corporate and municipal securities markets. Prices generally rose in the corporate and municipal securities markets during July, but the rally which brought long-term yields down 90 to 95 basis points this summer lost momentum in late July and early in August. On balance, yields leveled off during this period in both markets. Institutional investors continued to be selective, and yields on lower-grade corporate bonds turned up more and faster than those on high-grade issues. Meanwhile, after mid-July, stock prices showed no basic trend and trading volume stayed relatively light throughout the period.

BOND YIELDS AND STOCK PRICES

	New Aaa Corporate Bonds 1/	Long-term State and Local Bonds 2/	Stock Prices 3/ NYSE	Stock Prices 3/ AMEX
1969				
Low	6.90 (2/21)	4.82 (2/23)	49.31 (7/29)	25.97 (8/13)
High	8.85 (12/5)	6.90 (12/18)	59.16 (5/16)	32.91 (1/3)
1970				
Low	8.20 (2/27)	5.95 (3/12)	37.69 (5/26)	19.36 (5/26)
High	9.30 (6/18)	7.12 (5/28)	52.36 (1/5)	27.02 (1/8)
Week of:				
July 3	9.02	6.79	39.64	19.95
10	8.70	6.59	40.54	19.93
17	8.58	6.60	42.15	20.19
24	8.38	6.28	42.28	20.32
31	8.60	6.40	42.43	20.50
August 7	8.35	6.25	41.97	20.37

1/ With call protection (includes some issues with 10-year protection).
2/ Bond Buyer (mixed qualities).
3/ Prices as of the day shown.

In the corporate bond market, a further build-up in the calendar of new issues seemed to be a factor causing the recent rally to stall. New public issues of corporate bonds in July had amounted to slightly more than $1.8 billion, down only marginally from the June total, as favorable market conditions in July encouraged a number of industrial firms to enter the market. And the forward calendar of new offerings has risen in recent days. The staff now estimates August public bond offerings at $1.8 billion, with the September estimate remaining unchanged at $1.8 billion.

For the third quarter, total corporate security offerings are now expected to average about $2.8 billion a month. This volume is exceeded only by that of the second quarter, which included the outsized AT&T issue; excluding that issue, the estimated third quarter pace would set a new record.

CORPORATE SECURITY OFFERINGS
(Monthly or monthly averages, in millions of dollars)

	Bonds			
	Public Offerings	Private Placements	Stocks	Total
1969	1,061	468	700	2,229
1970 - QI	1,525	420	712	2,659
QII	2,308e 1/	444e	569e	3,322e 1/
QIII	1,800e	433e	583e	2,816e
July	1,800e	400e	650e	2,850e
August	1,800e	400e	500e	2,700e
September	1,800e	500e	600e	2,900e

e/ Estimated.
1/ The second quarter "Public Offerings" and "Total" figures include the $1.5 billion AT&T offering. The monthly average for the second quarter "Public Bond Offerings" and "Total Security Offerings" excluding AT&T would be $1,808(e) million and $2,822(e) million, respectively.

Long-term debt issues by State and local governments totalled over $1.3 billion in July. While this pace of new offerings continues above that of 1969, the forward calendar has not yet increased, despite the sizable decline in yields since late May. There are reports that the improvement in tax-exempt yields during a large part of July was associated with professional trading and dealer stocking of shelves in anticipation of further price rises. Banks are reported to have increased their purchases in early August, and the resultant optimism has apparently led dealers (including dealer banks) to maintain, if not expand, their already large positions.

STATE AND LOCAL GOVERNMENT OFFERINGS
(Monthly or monthly averages, in millions of dollars)

1969 -	Year	990
1970 -	QI	1,368
	QII	1,237
	QIII	1,333e
	July	1,300e
	August	1,300e
	September	1,400e

e/ Estimated.

Corporate profits in manufacturing. The seasonally adjusted annual rate of corporate profits before taxes apparently increased slightly in the second quarter, following a sharp decline in the first quarter. While profits remained well below 1969 levels, the year-to-year decline was not quite so large in the second quarter as in the first quarter. Compilations of the published after-tax earnings of large companies showed a similar narrowing in the 1969-70 decline, a fact that is generally being interpreted as signifying a "bottoming-out" in the first quarter of this year.

However, it should be noted that these relatively favorable developments reflect, to a considerable extent, the marked improvement in the second quarter of profits in two major manufacturing industries--motor vehicles and electrical machinery--that had accounted for much of the first quarter decline. As may be seen in the table, year-to-year declines in other manufacturing industries were still deepening through the second quarter. These comparisons lend support to a view that the base for renewed growth in corporate profits has not yet been laid. Staff projections of another very slight rise in total profits before tax (SAAR) in the third quarter are consistent with this view.

CORPORATE PROFITS BEFORE TAXES
(Year-to-year percentage changes)

	1969	1970	
	QIV	QI	QIIp
All corporations (Dept. of Commerce)	- 3.1	-11.2	-10.9
Manufacturing corps. (FTC-SEC):			
All industries	- 3.7	-14.4	-13.7
Motor vehicles and electrical mach.	-20.7	-37.2	-11.2
All other manufacturing groups	1.2	-8.3	-14.2
Durable goods	- 2.9	-16.5	-22.5
Nondurable goods	4.6	-2.0	-7.1

p - Preliminary.

Government securities market. Yields on Treasury notes and bonds have fluctuated fairly narrowly over the past few weeks as market attention has been focused on the progress of the Treasury's August refinancing operation. Treasury bill rates have risen somewhat on balance, however, as dealers have become a little chary about the size of their positions, particularly in longer bills.

WEEKLY AVERAGE MARKET YIELDS ON U.S. GOVERNMENT AND AGENCY SECURITIES 1/
(Per cent)

	1970		Week ending			
	Highs	Lows	July 21	July 28	Aug. 4	Aug. 11
Bills						
1-month	7.84 (1/28)	6.02 (6/24)	6.16	6.09	6.27	6.34
3-month	7.93 (1/16)	6.08 (3/24)	6.40	6.35	6.40	6.50
6-month	7.99 (1/5)	6.18 (3/23)	6.46	6.42	6.49	6.65
1-year	7.62 (1/30)	6.20 (4/13)	6.61	6.48	6.54	6.65
Coupons						
3-year	8.42 (1/7)	6.87 (3/25)	7.55	7.52	7.53	7.56
5-year	8.30 (1/7)	7.05 (3/25)	7.54	7.56	7.60	7.65
7-year	8.12 (4/26)	6.98 (3/25)	7.60	7.56	7.58	7.63
10-year	8.22 (5/26)	6.90 (2/27)	7.46	7.37	7.39	7.46
20-year	7.73 (5/26)	6.55 (2/27)	6.94	6.87	6.92	7.01
Agencies						
6-month	8.65 (1/27)	7.17 (4/15)	7.31	7.31	7.34	7.43
1-year	8.75 (1/2)	7.46 (4/14)	7.65	7.57	7.58	7.62
3-year	8.54 (1/2)	7.75 (3/25)	8.05	7.96	7.95	7.98
5-year	8.43 (1/15)	7.78 (3/25)	8.16	8.04	8.02	8.05

1/ Latest dates of high or low rates in parentheses and refer to single dates.

The Treasury's refunding operation was moderately successful and raised a total of $1.9 billion of new cash, near the upper end of the $1.5-$2.0 billion range generally expected. A total of $1.1 billion of the \$5.6 billion publicly held maturing issues (just under 20 per cent) was not exchanged into the two longer 7-3/4 per cent issues. Cash subscriptions to the 7-1/2 per cent, 18-month note were very large, however; and the issue was over-allotted by nearly 10 per cent, increasing its size to \$3.0 billion. An allotment ratio of 9-1/2 per cent was set for subscriptions in excess of \$200,000; a total of \$1.2 billion of subscriptions for less than \$200,000 was awarded in full.

Dealers' positions in Treasury securities have been swollen in recent weeks by the various Treasury financing operations, including the two tax anticipation bill auctions in early and mid-July which in the first instance were taken up by banks. Dealer bill positions reached a peak of just under \$4.0 billion on July 28. Some reduction in these positions has been effected most recently, but market reports indicate that bill demand has not been up to the expectations of a number of participants. Thus, despite a 50 basis point decline in financing costs over the past two or three weeks, there has been some tendency for dealers to cut prices and for bill rates to drift generally higher. Most recently, dealer positions have been swollen by \$1.25 billion of awards of new notes in the mid-August refunding, including about \$550 million of the 7-year, \$450 million of the 3-1/2-year, and \$250 million of the 18-month issue.

DEALER POSITIONS IN GOVERNMENT AND AGENCY SECURITIES
(In millions of dollars)

	July (daily average)	July 20	July 27	Aug. 3	Aug. 10
Treasury securities					
Total	3,259	3,044	4,251	4,316	4,527
Treasury bills (total)	2,633	2,465	3,583	2,920	2,721
Due in 92 days or less	458	288	283	481	460
93 days or over	2,176	2,178	3,300	2,439	2,262
Treasury notes and bonds (total)	626	579	668	1,397	1,806
Due within 1 year	466	396	542	1,388	221
1-5 years	-23	-17	-44	-102	806
over 5 years	183	200	170	111	778
Agency securities					
Total	827	890	1,021	908	775
Due within 1-year	561	581	694	638	540
other 1 year	266	309	328	270	235

Yield changes in the market for Federal agency securities have also been small since mid-July, but on long maturities spreads between these securities and comparable maturity Treasury obligations have narrowed by around 20 basis points, perhaps reflecting some of the shift in investor demands away from the commercial paper market. New issues by FNMA and FHLB raised $400 million and $215 million in new money in the latter half of July and early August at yields of around 7.90 per cent, about 20-25 basis points lower than on the last issues by these agencies. Other new issue activity has been confined largely to rolling over maturing issues with small pay-downs or only marginal amounts of new money raised.

<u>Federal finance</u>. At the present time the Board Staff is projecting a fiscal 1971 federal deficit of $11.7 billion, on a unified budget basis, about $10.4 billion more than the deficit forecast by the Administration in the May 19 budget review. The staff's estimate of receipts is nearly $5.0 billion lower than the Administration's revised estimate, largely because of lower income assumptions; the remaining difference between the Staff and Budget Bureau projections reflects the higher level of expenditures in the Staff estimates.

The Staff estimate of fiscal 1971 receipts remains at $199.4 billion, as in the last Greenbook, though an apparent shortfall in recent corporate tax receipts suggests that a downward revision in the forecast may eventually be necessary. The Staff's estimate of budget outlays for the current fiscal year has been increased by $1.8 billion since the last Greenbook as a result of (1) the expected Congressional overriding of the President's veto of the education appropriation bill which includes $.5 billion above the budget request, and (2) the Administration's recent proposals, relating to comparability in Federal pay, which implicitly include a pay hike in January 1971 that would add $1.3 billion to fiscal 1971 outlays. Considerable uncertainty exists with respect to the forecast of outlays, however, since Congress has yet to act on most of the regular appropriations bills for the current fiscal year.

In regard to the fiscal year just completed, final figures indicate that the budget deficit was $3.0 billion, about as projected by the Staff, though our estimates of both receipts and outlays for June were approximately $.6 billion too high.

Turning to the national income accounts concepts, the Staff projects a $10.3 billion federal deficit in calendar 1970 and an $11.1 billion deficit in fiscal year 1971. The increase in the size of the Federal sector deficit at annual rates is expected to have topped out in the second quarter of calendar 1970; thereafter the deficit is expected to remain at high, though somewhat lower, levels through the second quarter of 1971.

Despite the discretionary increases in spending included in the staff estimate for the current fiscal year, the forecast of the high employment budget indicates that fiscal policy will still be turning somewhat more restrictive as the fiscal year progresses. The high employment budget is expected to move from a $.8 billion deficit in the July-December period of 1970 to a $5.7 billion surplus in the first half of calendar 1971. This shift reflects mainly the anticipated speed-up in estate and gift taxes ($1.5 billion), the scheduled hike in social security taxes in January ($5.8 billion) and the fact that federal outlays still are not projected to be rising quite as fast as revenues if the economy were growing at its full potential.

The Staff estimates that the end-of-August cash balance at the Treasury will be about $6.3 billion. The Treasury raised $1.9 billion of net new money in the recent refinancing and cash borrowing operation. There may be additional cash borrowing in early September though it is not yet clear whether it will be early or late in the month. As indicated in earlier Greenbooks, Treasury net cash borrowing in the second half of 1970 is expected to be somewhat larger than in recent years.

PROJECTION OF TREASURY CASH OUTLOOK
(In billions of dollars)

	July	Aug.	Sept.	Oct.
Total net borrowing:	5.9	2.1	-.7	4.1
Weekly and monthly bills	.5	.3	--	--
Tax bills	4.8	--	--	--
Coupon issues	--	3.0	--	--
As yet unspecified new borrowing	--	--	1.2	4.1
Other (agency, debt repayment, etc.)	.6	-1.2	-1.9	--
Plus: Other net financial sources[a/]	-.3	-.2	.2	.6
Plus: Budget surplus or deficit (-)	-6.2	-3.0	2.0	-6.5
Equals: Change in cash balance	-.6[b/]	-1.1	1.5	-1.8
Memoranda: Level of cash balance, end of period	7.4[b/]	6.3	7.8	6.0
Derivation of budget surplus or deficit:				
Budget receipts	12.5	15.2	19.6	11.9
Budget outlays	18.7	18.2	17.6	18.4
Maturing coupon issues held by public	--	5.6	--	--

a/ Checks issued less checks paid and other accrual items.
b/ Actual.

FEDERAL BUDGET AND FEDERAL SECTOR IN NATIONAL INCOME ACCOUNTS
(In billions of dollars)

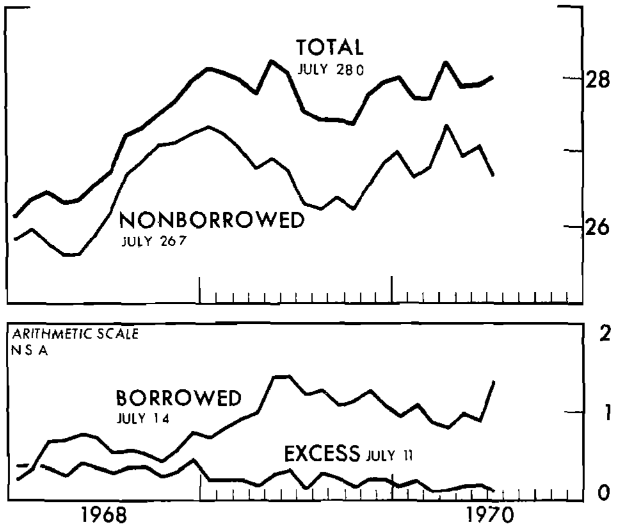
	Fiscal Year 1970*	Calendar Year 1970 F.R. Board	Fiscal Year 1971 Revised Budget 1/	Fiscal Year 1971 F. R. Board	Calendar Quarters 1970 I*	1970 II*	1970 IIIe/	1970 IVe/	1971 Ie/	1971 IIe/
Federal Budget										
(Quarterly data, unadjusted)										
Surplus/deficit	-2.9	-10.2	-1.3	-11.7	-3.5	8.7	-7.2	-8.2	-5.6	9.3
Receipts	193.8	193.3	204.3	199.4	44.4	58.7	47.3	42.9	46.6	62.6
Outlays	196.8	203.4	205.6	211.1	47.8	50.0	54.5	51.1	52.2	53.3
Means of financing:										
Net borrowing from the public 2/	3.8	10.2		11.0	2.0	-6.4	7.3	7.3	4.0	-7.6
Decrease in cash operating balance	-2.1	-.9		1.3	-1.6	-1.1	.2	1.6	.1	-.6
Other 3/	1.2	1.0	n.a.	-.6	3.1	-1.1	-.3	-.7	1.5	-1.1
Cash operating balance, end of period	8.0	6.2		6.7	6.9	8.0	7.8	6.2	6.1	6.7
National Income Sector										
(Seasonally adjusted annual rate)										
Surplus/deficit	-.3	-10.3	n.a.	-11.1	-1.7	-13.9	-13.8	-11.7	-9.6	-9.4
Receipts	198.9	196.6	n.a.	202.1	195.9	196.7	195.4	198.4	205.6	209.1
Expenditures	199.2	206.9	208.3	213.3	197.7	210.6	209.2	210.1	215.2	218.5
High employment budget surplus/deficit 4/	2.1	-.5	n.a.	2.4	3.2	-3.6	-3.0	1.4	5.7	5.6

e--projected
n.a.--not available
1/ Official Budget Revision: May 19, 1970
2/ Excludes effect of reclassification of $1.6 billion of CCC certificates of interest, as of July 1, 1969. This reclassification increased Federal debt, but is not treated as borrowing from the public.
3/ Includes such items as depsit fund accounts and clearing accounts.
4/ Estimated by Federal Reserve Board Staff. Since the last Greenbook, the high employment figures have been revised in line with recent revisions in the historical national income accounts.
* Actual

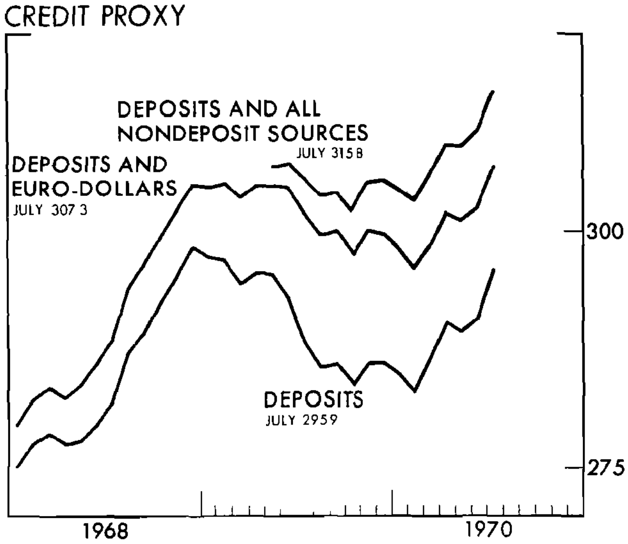
FINANCIAL DEVELOPMENTS - UNITED STATES

BILLIONS OF DOLLARS, SEASONALLY ADJUSTED, RATIO SCALE

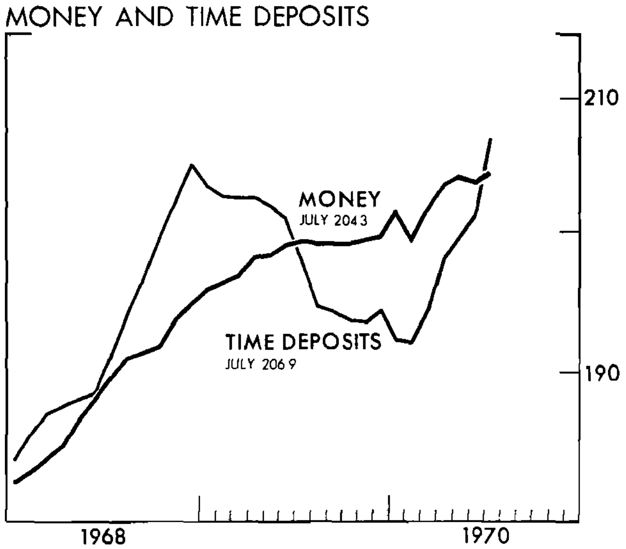
BANK RESERVES



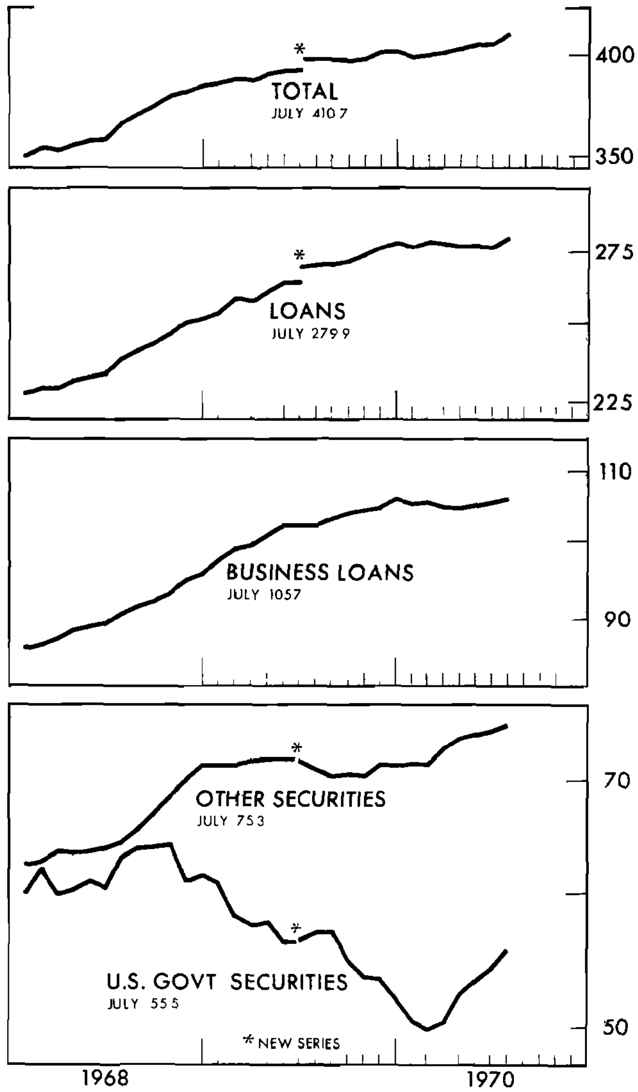
CREDIT PROXY



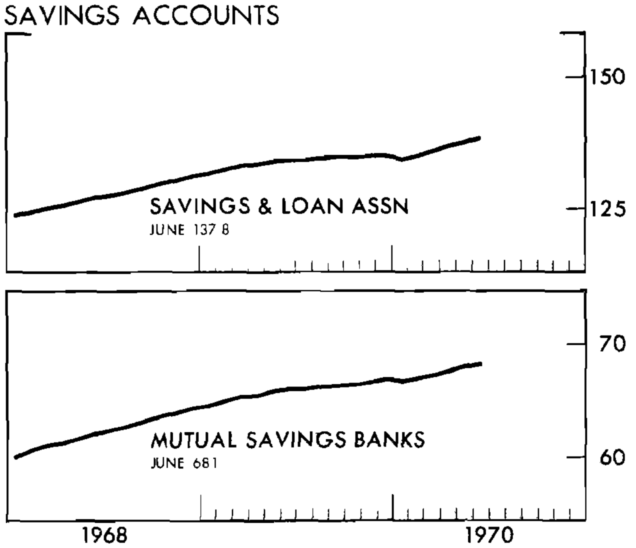
MONEY AND TIME DEPOSITS



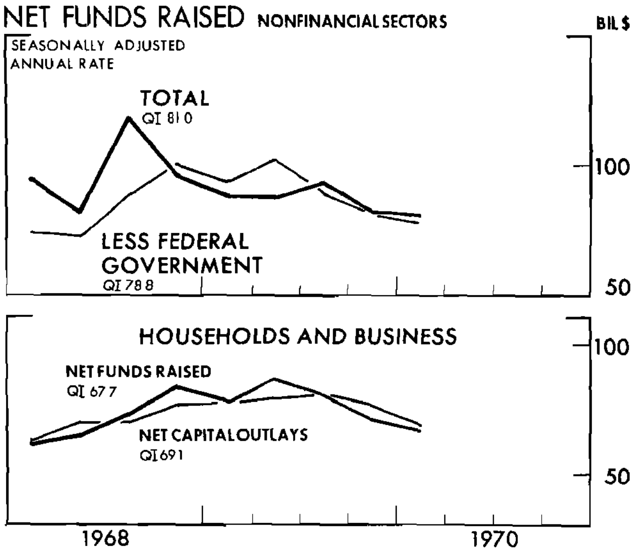
BANK CREDIT

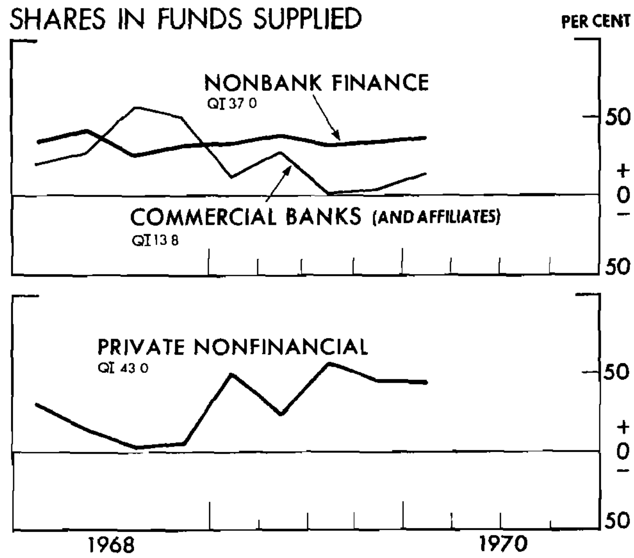


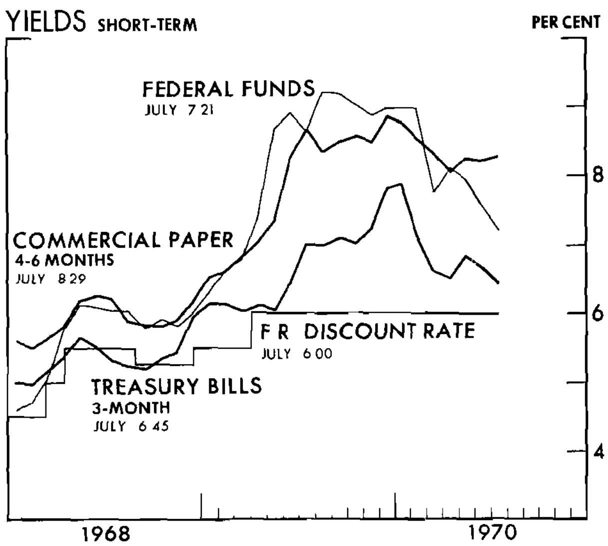
SAVINGS ACCOUNTS

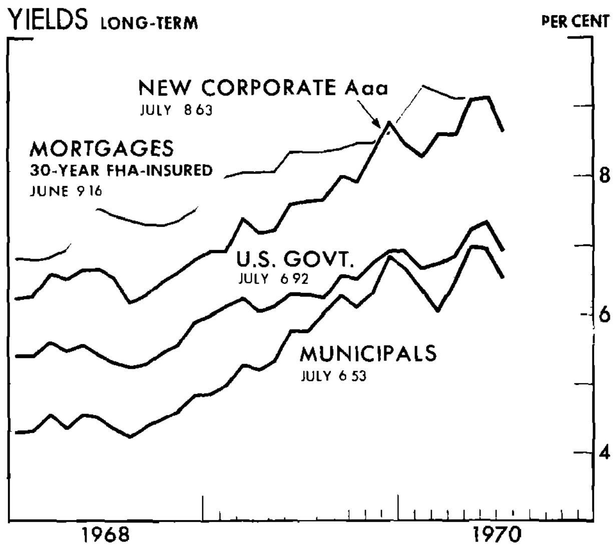


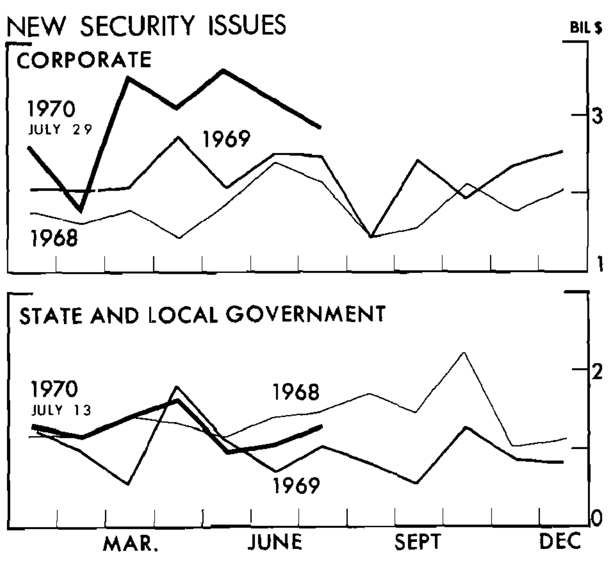
FINANCIAL DEVELOPMENTS - UNITED STATES

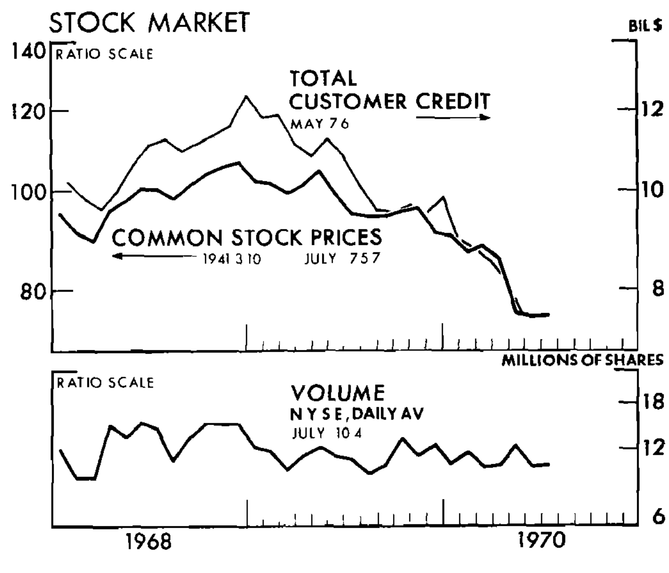












THE ECONOMIC PICTURE IN DETAIL

International Developments

U.S. balance of payments. The data now available for the first-half balance of payments (shown in the following table) are scheduled to be published by the Commerce Department on August 17. As noted in the last Green Book, the overall results before special transactions and the allocation of SDRs show a rise in the liquidity deficit to $2.2 billion for the second quarter, and the balance settled by official reserve transactions in the second quarter was about the same.

A principal feature of the accounts recently has been the strength of exports, discussed in some detail in a following section. Another helpful feature in the second quarter was the extraordinarily small amount of new foreign bonds sold in this market -- about $100 million. However, indications are that the capital outflow to purchase new foreign bonds is rising sharply in the current quarter and may exceed $500 million. That total would include several large issues by Canadian borrowers and a large issue by the World Bank.

Foreign transactions in U.S. corporate securities (both in U.S. and foreign markets) resulted in a net inflow of about $300 million in the second quarter -- about the same as in the first but far below the $800 million quarterly average of 1969. Trading in

U.S. BALANCE OF PAYMENTS 1/
(millions of dollars, seasonally adjusted)

	1968	1969			1970		
	Year	Year	1H	2H	1H	Qtr.1	Qtr.2
Merchandise excluding military							
Exports	33,588	36,473	17,057	19,416	20,947	10,241	10,706
Imports	-32,964	-35,835	-17,182	-18,653	-19,581	-9,723	-9,858
Net	624	638	-125	763	1,366	518	848
Cash receipts for military sales	966	1,449	558	891	418	198	220
U.S. purchases (-) of foreign securities	-1,254	-1,494	-858	-636	-140	-159	19
U.S. banking claims (increase, -)	253	-541	-434	-107	-316	170	-486
Foreign purchases of U.S. corp. stocks	2,096	1,565	904	661	-211	-85	-126
Foreign purchases of other U.S. sec., excluding Treasury issues	2,293	1,547	849	698	816	382	434
Selected Government transactions, total	2,885	-804	-221	-583	396	-304	700
Nonscheduled debt repayments	269	-87	78	-165	203	88	115
Nonliquid U.S. bank liabilities 2/	606	-676	-223	-453	-365	-150	-215
Nonliquid U.S. Government liabilities	2,010	-41	-76	35	558	-242	800
Liquid liabilities to commercial banks abroad	3,387	9,434	7,757	1,677	-1,704	-1,717	13
Liquid liab. to other private foreign accounts. 3/	423	-501	-173	-328	-6	-25	19
Liquid liab. to foreign reserve holders	-3,101	-525	-2,084	1,559	3,478	3,028	450
U.S. reserve assets (increase, -)	-880	-1,187	-347	-840	1,069	264	805
Allocation of SDRs	--	--	--	--	434	217	217
Other transactions (derived as residual)	-7,692	-9,581	-5,826	-3,755	-5,600	-2,487	-3,11[illegible]
Balances (deficit, -) 4/							
Official settlements balance	1,641	2,708	2,768	-60	-4,631	-2,870	-1,761
Liquidity balance	171	-7,221	-5,153	-2,068	-2,837	-1,550	-1,287
Adjusted over-all balance	-1,746	-6,726	-4,989	-1,737	-2,927	-1,153	-1,774

p/ Preliminary. r/ Revised.
1/ Items available for second quarter of 1970 as of August 11, 1970.
2/ Chiefly to foreign reserve holders and international institution.
3/ Including international institutions.
4/ Includes initial allocation of SDRs in first and second quarters of 1970.

U.S. corporate stocks recovered to a net inflow of about $60 million in June, following a heavy sell-off in May. Although there was some reduction in foreign purchases of bonds in the U.S. market, foreign purchases of new issues of U.S. corporations offered in Europe rose to about $300 million, the largest quarterly total since early in 1969. About two-thirds of the proceeds were intended for use in the United States rather than as financing for foreign affiliates. Rates in the Euro-bond market hardened during the second quarter, and indications are that borrowings in that market by U.S. companies will drop off once again.

Claims on foreigners reported by U.S. banks rose about $500 million in the second quarter, largely in claims on Canada and Japan ($200 million each). In the case of Canada the rise in claims is presumably part of the overall inflow attracted by high interest rates and the prospect of revaluation -- a large part of the flow reflected activities of the banks' customers and of the U.S. agencies of foreign banks. In the case of Japan the outflow may be partly seasonal -- there was a comparable outflow last year -- but it is surprising in view of the intention of the Japanese authorities to reduce the use of foreign borrowing by Japanese banks. Outflows by U.S. banks chargeable to their VFCR ceilings were still quite small in the second quarter and reflected mainly export credits.

After taking account of known transactions in the second quarter, the residual -- representing such major categories as U.S.

Government aid and military activities, and direct investment capital and income accounts -- showed about $3.0 billion of net payments. This is about as large as in the periods of heavy recorded and unrecorded capital outflows last year, and suggests that capital outflows were larger than in the first quarter of the year.

Preliminary weekly data for July suggest that the liquidity measure seasonally adjusted, registered a much smaller deficit than in other recent months. However, a very large deficit persisted on the official settlements measure as liabilities to commercial banks abroad fell off sharply between June 24, when Regulation Q was relaxed, and the end of July.

Euro-dollar market. Euro-dollar interest rates declined fairly rapidly in the latter half of July. The three-month deposit rate, for example, declined to an average of 8.36 per cent in the week ended July 29, compared to more than 9.5 per cent in mid-June. In August, through the 12th, rates for Euro-dollar funds of three-month maturity and longer have remained rather stable, and rates for one-month maturity and less have advanced moderately. The call deposit rate averaged 7.53 per cent in the week ended August 12, after dropping below 7 per cent in late July. (See table).

The marked decline in Euro-dollar rates during the latter half of July reflected a sharp reduction in American bank takings from the market as the banks replaced part of their Euro-dollar liabilities with less expensive funds in the domestic CD market. Liabilities of U.S. banks to their foreign branches fell by $1.5 billion from July 15 to August 5; of this total decline, however, only $0.25 billion occurred in the week ended August 5, and later data available through Monday, August 10, show a moderate increase. On August 5, liabilities to foreign branches (including participations in domestic loans) were $10.8 billion, $0.5 billion above the average of the four Wednesdays in the May 1969 base period. This difference was more than accounted for by borrowings by banks using the three per cent of deposit base, indicating that some of those banks using the historical base had dipped below their base levels.

By the end of July rates in the Euro-dollar market had fallen to levels not substantially above the cost of funds to U.S. banks in the domestic CD market and the Federal funds market. One-month Euro-dollar rates have averaged about 8 per cent thus far in August; the banks giving the highest offering rates for 30-59 day CD's have been paying about 7-3/4 per cent since late July. The differential between the call Euro-dollar rate and the Federal funds rate has been quite narrow ever since mid-July (See table).

SELECTED EURO-DOLLAR AND U.S. MONEY MARKET RATES
(weekly average of daily figures)

Average for week ending Wednesday	(1) Call Euro-$ Deposit	(2) Federal Funds	(3) (1)-(2) Differential	(4) 3-month Euro-$ Deposit	(5) 3-month Treasury Bill	(6) =(4)-(5) Differential
Jul. 1	8.78	7.23	1.55	9.00	6.43	2.57
8	8.60	7.34	1.26	9.18	6.61	2.57
15	7.83	7.59	0.24	8.98	6.53	2.45
22	7.08	7.16	-0.08	8.65	6.38	2.27
29	6.95	6.89	0.06	8.36	6.34	2.02
Aug. 5	7.13	6.93	0.20	8.37	6.43	1.94
12	7.53	6.88p	0.64	8.33	6.44p	1.89

<u>Foreign exchange markets</u>. After coming under considerable pressure in the foreign exchange markets during the second half of July as a result of the decline in Euro-dollar interest rates, the dollar firmed somewhat in the first two weeks of August. Intervention purchases of dollars by major foreign central banks, which totaled nearly $1.2 billion in the latter half of July, abated sharply after the end of the month.

The decline in Euro-dollar interest rates during July, combined with still tight credit conditions in Germany, led to sizable flows of funds into marks, and the Bundesbank purchased $400 million in spot market intervention during the last half of the month, when it also purchased $64 million for future delivery. In early August, however, German money market rates declined relative to Euro-dollar rates, reducing the covered interest differential in favor of mark investments. So far this month the Bundesbank has purchased only a small amount of dollars.

The Dutch guilder was in strong demand in late July, partly as a result of a very large conversion of foreign currencies by a Dutch oil company. An OECD report on the Dutch economy, released at about this same time, suggested that the guilder should have been revalued last fall, stimulating discussion in the press of the possibility of a future guilder revaluation. As a result of this discussion, the guilder remained firm following the completion of the oil company conversion. The Netherlands Bank has purchased $168 million since mid-July, and the System has provided cover for $125 million of these purchases by drawing that amount on the reciprocal swap facility.

The Belgian franc, reflecting Belgium's strong basic balance of payments, has been at or near its ceiling since mid-July, though it eased somewhat after month-end. The National Bank of Belgium purchased $93 million from July 15 to August 12, and the System provided exchange guarantees for these uncovered dollars by drawing $65 million on the reciprocal swap facility. The System's outstanding indebtedness on that line is now $95 million.

The French franc was very firm in late July, partly as a result of the bunching of conversions of export receipts prior to the August vacation period in France. The Bank of France purchased $175 million in the latter half of the month. After month-end the franc exchange rate eased, and Bank of France dollar purchases in early August were very small.

The last two weeks of July saw a temporary respite in the selling pressures on the Italian lira, and the Bank of Italy purchased a small amount of dollars. Paradoxically, after the formation of a new government in early August, selling pressure resumed, and the Bank of Italy sold over $100 million in support operations.

Month-end liquidity needs of Swiss commercial banks pushed the Swiss franc exchange rate to the ceiling in the last week of July, and the Swiss National Bank purchased $120 million. The exchange rate declined markedly after month-end.

The Canadian dollar advanced strongly in late July and early August, touching a high of 98 cents at one point. Factors strengthening the Canadian dollar included the conversion of proceeds of a large bond issue and seasonal strength in an already strong balance of payments on current account. The Bank of Canada purchased just over (U.S.) $50 million in moderating the rise in the exchange rate, then, in the second week of August, sold a small amount of U.S. dollars as the rate slid back to 97.5 cents.

Sterling rallied briefly around month-end with the settlement of the British dock strike, and the Bank of England purchased $135 million in two days. Since month-end, sterling has moved in a narrow range on light volume, and the Bank of England has purchased only a small amount of dollars.

U.S. foreign trade. In June, the export surplus rose to $5.2 billion at a seasonally adjusted annual rate (balance of payments basis). The surplus in the second quarter of 1970, $3.4 billion at an annual rate, was the highest since the third quarter of 1967.

The trade balance has improved steadily since mid-1969, buoyed by a marked rise in exports. Exports in the first six months

U.S. MERCHANDISE TRADE 1/

(Billions of dollars; seasonally adjusted annual rates)

	1968	1969			1970		
	Year	Year	1H	2H	1HP	Q-1P	Q-2P
Exports, total	33.6	36.5	34.1	38.8	41.9	40.8	42.9
By type							
Agricultural	6.3	6.0	5.5	6.5	6.9	6.7	7.2
Nonagricultural	27.3	30.5	28.6	32.3	34.9	34.1	35.7
By area							
Canada	8.1	9.2	9.0	9.4	9.2	9.3	9.1
Western Europe	10.5	11.6	10.6	12.6	14.3	13.7	14.9
Japan	3.0	3.5	3.1	3.9	4.6	4.5	4.7
All other	11.9	12.2	11.3	12.9	13.8	13.4	14.2
Imports, total	33.0	35.8	34.4	37.3	39.1	38.7	39.5
By area							
Canada	8.6	10.0	9.7	10.2	10.7	10.8	10.7
Western Europe	10.2	10.2	9.7	10.7	10.8	10.6	11.1
Japan	4.1	4.9	4.6	5.1	5.6	5.5	5.6
All other	10.1	10.7	10.3	11.2	12.0	11.8	12.1
Balance	+0.6	+0.6	-0.2	+1.5	+2.7	+2.1	+3.4
By area							
Canada	-0.5	-0.8	-0.7	-0.8	-1.5	-1.5	-1.6
Western Europe	+0.3	+1.4	+0.9	+1.9	+3.5	+3.1	+3.8
Japan	-1.1	-1.4	-1.5	-1.2	-1.0	-1.0	-0.9
All other	+1.8	+1.5	+1.0	+1.7	+1.8	+1.6	+2.1

1/ Balance of payments basis.
p/ Preliminary
Note: Details may not add to totals because of rounding.

of 1970 ($41.9 billion at an annual rate, balance of payments basis) about 8 per cent greater than in the second half of 1969. This generally reflects the high level of demand abroad. The first-half import increase was more moderate -- almost 5 per cent greater than in the second half of 1969.

A large part of the advance in exports from the latter half of 1969 to the first half of 1970 resulted from a considerable increase in shipments of goods to Western Europe. Exports to Japan, primarily non-agricultural, also recorded sizable gains in the first half. On the other hand, shipments to Canada declined slightly.

Canada and Japan accounted for most of the increase in first-half imports. At the same time, arrivals of goods from Western Europe were sluggish.

As a result of these changes in the geographical distribution of exports and imports, the U.S. trade balance with Canada deteriorated sharply in the first half of 1970, while the balance with each of the other major areas -- Japan, Western Europe; Australia, New Zealand and South Africa; Latin America; and all other countries as a group -- either remained the same or improved.

Exports in the second quarter of 1970 were at a $42.9 billion annual rate (balance of payments basis), an increase of over 5 per cent from the first quarter.

Both agricultural and non-agricultural exports registered substantial gains in the second quarter. The surge in agricultural products from the already high first quarter level occurred primarily in soybeans, cotton, and PL-430 shipments of rice to Korea. During the rest of 1970, agricultural exports are expected to continue at a high level but not as high as in the second quarter.

Among the non-agricultural commodities, machinery exports performed well in the second quarter; after falling in April, they recovered in May and rose significantly in June. In the second half of this year they are expected to rise further. A sharp upswing -- from a very low first-quarter level -- occurred in automobile shipments to Canada in the April-June period, as Canadian car sales improved slightly. Deliveries of civilian aircraft, while higher for the second quarter as a whole, declined abruptly in June and will probably continue to fall off somewhat during the remainder of 1970. The expected rise in machinery exports in the second half, however, should more than compensate for the anticipated shortfall in aircraft deliveries. Continued strength was shown in exports of non-agricultural industrial supplies -- especially coal, steel scrap, steel products, and fuels and lubricants -- although exports of chemicals declined slightly. Exports of steel products actually fell in June, but showed an extremely strong overall increase for the second quarter because of the abnormally high levels in April and May.

Imports in June declined 2 per cent from the relatively high May level, but for the second quarter as a whole imports ($39.5 billion at an annual rate, balance of payments basis) were 2 per cent above the level of the first quarter.

The second-quarter increase was largely based on increased automotive imports, as deliveries from Europe and Japan continued to respond to strong U.S. demand for foreign-type cars. While automotive shipments from Canada picked up in the second quarter -- U.S. sales of American-type cars improved slightly -- they were still about 7 per cent less in the first half of 1970 than in the second half of 1969. Iron and steel imports increased in the second quarter from first quarter levels but showed no significant advance for the first half of 1970 over the last half of 1969. Fuels and lubricants declined from the first quarter but were still imported at a higher rate than in the last half of 1969. Second quarter increases were also recorded for coffee, metals, nonelectric machinery and consumer goods. Part of the strength in imports continues to reflect the relatively high prices of coffee and nonferrous metals. Coffee prices continued to rise throughout the second quarter while import prices of nonferrous metals remained generally high.

Imports, therefore, have continued at high levels throughout the first half of 1970 despite a slowing in the domestic economy. The ratio of imports to GNP rose to 4.1 per cent in the second quarter.

In other recent periods of economic slowdown (i.e., in 1960-61 or even in 1967) the import-GNP ratio leveled off or fell. Several factors may help explain why imports have remained as strong as they have in the first half of 1970. The bulk of the U.S. slowdown has resulted from lower Federal government expenditures and smaller business inventories, while domestic expenditures on consumer goods have continued to grow. Since highly finished goods (automobiles, other nonfood consumer goods, and capital equipment) now comprise a larger share of U.S. imports than in any earlier period (55 per cent in the first half of this year), continued U.S. demand for these products have sustained aggregate imports. In particular, the upward trend in imports of autos from Canada and elsewhere has remained strong. Persistently high domestic prices have encouraged a shift by both consumers and producers toward lower-priced imported products; at the same time, incomes have remained high encouraging the importation of more luxury-type consumer goods.

Foreign trade of major industrial countries. In the first half of this year, world trade expanded rapidly, particularly among industrial countries. Imports of a number of industrial countries expanded faster than their exports. However, increases in the trade balances of France, the United States, Canada and Japan outweighed in the aggregate decreases for the other industrial countries.

In each case where trade balances have increased, this has been largely the result of stabilization measures, which in Canada and the United States have caused the economy to operate with a considerable degree of slack; in France, they were combined with a devaluation last year and have removed excess demand. In Japan also, restrictive demand management actions halted the decline in the still large trade surplus last year, and increases in exports are once more outrunning those in imports. Buoyant external demand was an added factor in the reversal of trade balance trends from declines to increases for these countries.

For most other countries, rapid expansion of exports has added to general demand pressures. Differential developments in trade positions resulted largely from differential responses of import demand. Germany, like Japan, is continuing to maintain a large trade surplus as the increase in German imports has not been large enough--despite internal excess demand and a revaluation of the DM--to exceed significantly the rise in exports. Still, import

TRADE BALANCES OF MAJOR INDUSTRIAL COUNTRIES
(millions of U.S. dollars, seasonally adjusted, annual rates)

	1967	1968	1969 1st H.	1969 2nd H.	1970 a/ 1st H.
United Kingdom	-1,256	-1,276	- 706	+ 245	- 288
Germany	+4,380	+4,692	+3,558	+4,636	+3,650
France	-1,020	-1,284	-2,268	-2,466	- 900
Italy	-1,116	- 72	+ 30	-1,476	-1,590
Netherlands	-1,056	- 948	- 924	-1,110	-1,400
Belgium-Lux.	- 132	- 144	- 84	+ 240	+ 150
Japan	-1,221	- 15	+1,264	+ 562	+ 720
Canada	+ 524	+1,273	+ 775	+ 830	+2,532
Sweden	- 180	- 180	- 162	- 252	- 400
United States	+3,860	+ 624	- 250	+1,520	+2,740 b/

a/ Reflects Board staff estimates of seasonal adjustment for June, except for U.S., U.K. and Canada. Balance for Belgium-Luxembourg relates to the period January-April at an annual rate, with Board staff estimate of seasonal factor for April. For Sweden, seasonal factor estimated for second quarter.
b/ Adjustment to balance of payments basis estimated for second quarter.

Note: Trade balances equal exports f.o.b. minus imports c.i.f. except for Canada, the U.K. and the United States, where both exports and imports are f.o.b. (U.S. data on balance of payments basis, which excludes military export sales).

demand is clearly responding to higher incomes, and the trade surplus, in the longer run, is likely to decrease, albeit slowly.

Despite large increases in exports, the Dutch and Swedish trade deficits widened considerably this year, as imports responded sharply to internal demand and price pressures. In Belgium, too, a revival of import demand caused the trade surplus to narrow. The sharp deterioration in Italy's trade balance resulted from continuing labor difficulties which have not only held back exports, but have also caused a shift to imports in order to satisfy rapid rises in internal demand.

Only the United Kingdom has not fully shared in the increased export activity, although the economy is operating at less than full capacity. Exports have risen only slightly since the end of last year, while imports have rebounded. As a result, the emergence of a British trade surplus from mid-1969 proved to be short-lived and since April, 1970 there have once more been successive monthly deficits.

Trade among industrial countries expanded faster than world trade in the first half of 1970. Imports of OECD countries from the rest of the world during January-April, 1970 were 11 per cent above the first half of 1969, while intra-OECD trade expanded by more than 20 per cent. OECD exports to other countries grew by 16 per cent over the period, so that the trade surplus of the non-OECD countries has narrowed considerably.

The steady improvement in the British trade balance, which had begun in the second half of 1968, came to a halt early this year. The slim surplus which had emerged in the second half of 1969 had turned into a deficit once more by the second quarter of 1970 (on an f.o.b.-f.o.b. basis). The second quarter deficit, at an annual rate of almost $900 million, compares with surpluses averaging $250 million in the preceding three quarters, but is still well below the rate of annual deficits recorded in the 1964-1968 period. Although British exports to the Continent and the sterling area have been buoyant, exports to the U.S. declined sharply in the second quarter while those to Canada remained roughly the same.

Given relatively high employment, a trade deficit would normally be expected for Britain, but the current deterioration in the trade balance has taken place at a time when the pace of economic activity has been below potential. In fact, GDP fell in the first quarter of this year and probably did not grow much--if at all--in the second quarter. Despite the sluggishness in domestic output, imports have grown at an accelerating rate since the beginning of the year, while exports have been increasing only slightly. Imports rose by about 7-1/4 per cent in the second quarter of 1970 (excluding U.S. military aircraft financed by the Export-Import Bank), over three times as fast as in the first quarter, with about one-third of this rise accounted for by rising unit values. The less than 3 per cent rise in exports since the end of last year was almost entirely the result of rising unit values.

Although several "special" factors--anticipation of a dock strike, a bulge in imports from Canada following the end of strikes there, and deliveries of jumbo jets in May and June--have contributed to the re-emergence of the trade deficit, Britain's trade situation gives cause for concern. New export orders for machinery and equipment declined last spring (although orders on hand were still increasing slightly). The rapid rise in imports, which has been concentrated primarily in finished manufactures and industrial materials, probably reflects some inventory accumulation and the response of final demand to rising prices. Despite the rise in imports, the Government announced last month that the import deposit requirement--which affects slightly less than half of total British imports--would be lowered from 30 to 20 per cent, effective September 1, and totally removed in December.

The revaluation of the mark has thus far not led to a decrease in the German trade surplus. The surplus during the first half of this year was at an annual rate of $3.6 billion, virtually the same as during the first 6 months of 1969. This is well below the $4-1/2 billion rate of 1967-68 and of the second half of 1969. But the 1967-68 surpluses were recorded at a time when the economy was operating well below capacity and the second half of 1969 was distorted by pre-revaluation flows. This year's surplus, although inflated somewhat by the short-run "terms of trade" effect of the parity change, is being achieved at very high pressures upon industrial capacity. Foreign demand for German output has not yet been significantly affected by the higher prices of German goods. The volume of German exports during the first 4 months of this year was over 8.5 per cent higher than in the corresponding 1969 period. Imports have risen at a somewhat faster rate, reflecting the strong domestic expansion, but from a lower base. A very large order backlog still exists in the export sector, and the expected moderation of domestic demand and price pressures during the remainder of the year is likely to slow import growth. Thus, only little shrinkage in the surplus can be expected during the course of this year.

The prices of German exports, in marks, were continuing to rise last spring--in April-May they were 2.5 per cent higher than in September--as German producers passed on some of their substantial increases in labor and other production costs. The revaluation, partially offset by border tax adjustments, added roughly 5 per cent to the foreign currency costs of German goods. On the import side, foreign suppliers to Germany have raised their prices in their own currencies since the DM revaluation, so that the DM prices of German imports in May were down only 1.4 per cent from September.

There has been no marked change in the direction of German trade since the revaluation. The other EEC member countries are continuing to increase their share of the German market, with Dutch and Belgian exporters enjoying the most significant gains. French exports to Germany have not shown particular strength relative to the other EEC countries this year even though French exporters have the benefit of the franc devaluation as well as the upvaluation of the mark.

The U.S. share in both German exports and imports is only about 10 per cent, but there has been a rather substantial swing toward bilateral surplus for the United States. German data sources indicate that in January-May of this year, the U.S. ran a $160 million surplus with Germany, whereas in 1968 and 1969, the U.S. had run trade deficits of approximately $500 million and $100 million, respectively. A large increase in U.S. exports to Germany--particularly of metals and civilian aircraft--was largely responsible for this reversal.

A strong rise in French exports, combined with only a moderate increase in imports, resulted in a virtual balance of the French trade account (f.o.b.-f.o.b. basis) with the non-franc area during the first half of this year. During the corresponding 1969 period, there had been a trade deficit on this basis of $1.8 billion at an annual rate. (In the table, the balance is shown with imports on a c.i.f. basis and inclusive of trade with the franc area.)

The rise in French exports (17 per cent in the first 5 months of this year as compared with a year earlier) was more or less in line with the rate of expansion of total OECD trade. France does not seem to have improved her share in total trade despite the 11.1 per cent devaluation of the French franc in August last year. French exporters have absorbed the devaluation advantage in profit margins rather than passing it on in price decreases. Thus, unit values of French exports in May 1970 were 13-1/2 per cent higher than in July 1969. The smallness of the rise in imports can be attributed to a drawing down of imported stocks built up last summer prior to the franc and mark parity changes, to severe installment credit controls implemented last September which have damped down demand for consumer durables, and to the extra rise in franc prices of imports owing to devaluation.

Italy's trade deficit for the first half of 1970 was at an annual rate of nearly $1.6 billion (with imports valued c.i.f.). While only slightly larger than the $1.5 billion deficit registered in the second half of last year, this compares to a near-zero balance in the trade account during the first 6 months of 1969.

Labor difficulties have held industrial production well below its potential level and have affected the foreign trade balance primarily by restricting exports. Despite an appreciable rise in exports in the second quarter, the total for the first half was only 7.7 per cent more than a year earlier, which compares with a 23 per cent rise for January-June 1969 relative to the comparable 1968 period. The export products that have been most adversely affected this year have been textiles, paper, metals, chemicals and motor vehicles.

Internal demand has been rising quite rapidly in Italy, and with industrial production constrained in a number of sectors, there has been a very swift increase in the demand for imports of manufactured and semimanufactured goods. Particularly noteworthy increases have occurred in imports of iron and steel, motor vehicles, and copper and copper alloys. The limited rise in domestic production, however, has tended to depress imports of some industrial materials such as textile fibers, iron ore and scrap metals. Total imports in the first half showed a year-to-year rise of over 21 per cent.

The principal changes in the regional distribution of Italian exports have been a decline in the proportion going to France since the devaluation of the franc a year ago--which mainly reflects the unwinding of anticipatory purchases by French importers before the parity change--and an increase in the relative importance of the German market--a result of boom conditions there and, perhaps to some extent, of the mark revaluation. The relatively small increase in imports of raw materials was the main reason why the share of the less developed countries in total Italian imports decreased somewhat after mid-1969.

For the first 6 months of the year, the Netherlands had a very large trade deficit of roughly $1.4 billion, at an annual rate. While the value of Dutch exports was 20 per cent higher in this period than in the first half of 1969, Dutch imports were 22 per cent higher--reflecting the large import content of Dutch exports, stockbuilding, and domestic demand for comsumer goods. The prices of imported goods have risen almost 6 per cent since the revaluation of the German mark. Since imports are equal in value to about one-third of Dutch GNP, this has no doubt added importantly to the price pressures being experienced in the domestic economy.

The growing importance of the other EEC countries as suppliers and customers continues to characterize Dutch trade. These countries account for roughly 60 per cent of Dutch imports and exports, Germany alone about 30 per cent. There has been an exceptionally rapid rise this year in sales to Germany, which were up over 35 per cent from the first half of 1969.

The substantial deterioration in Sweden's foreign trade position since mid-1969 reflects an excess demand situation which economic policy has thus far not been able to restrain successfully. During January-June, 1970 the trade deficit ran at an annual rate of $400 million, which compares to a deficit of $162 million during the comparable 1969 period. Although exports increased in value by 17 per cent, imports rose about 23 per cent. The rise in imports from Germany, the U.K., Denmark and the U.S. was particularly large. There is as yet no indication that this high import growth rate, which reflects domestic demand and price pressures, is slowing. There may even be an acceleration during the remainder of this year if Swedish consumers substantially increase their purchases before the scheduled increase in the value-added tax at the end of this year.

The Belgium-Luxembourg Economic Union registered a trade surplus of $150 million at an annual rate during the first 4 months of this year. Imports had virtually ceased to expand after mid-1969, reflecting a moderate slowdown in the expansion of internal demand, the cessation of speculative purchases from Germany after the mark was revalued, and inventory adjustments of imported industrial materials. The surplus that developed then has been narrowed this year by renewed import growth--probably a result of a higher rate of inventory accumulation rather than an acceleration of domestic economic activity as a whole.

Japan's trade surplus widened once more in the first half of this year to approximately $720 million at an annual rate from $560 million in the preceding half year (imports valued c.i.f.). Exports rose sharply, particularly to the EEC countries, which now purchase roughly 6 per cent of total Japanese exports. Trade with the United States, Japan's largest single trading partner, has represented a smaller proportion of total exports (about 30 per cent) and a larger proportion of imports (about 29 per cent) in the last few years.

Japan recently has experienced substantial gains in its exports of electrical machinery and automobiles. A decline of 18 per cent in exports of iron and steel to the U.S. in 1969 was more than offset by a three-fold rise in sales to Western Europe.

Continued strong domestic demand during the second half of 1969 contributed to a large rise in raw materials imports, particularly metals. Imports of coal and ores from Oceania, Southeast Asia and Latin America increased markedly. There were also large increases in imports of certain manufactured goods such as computers and aircraft, and certain foodstuffs, such as meat and marine products.

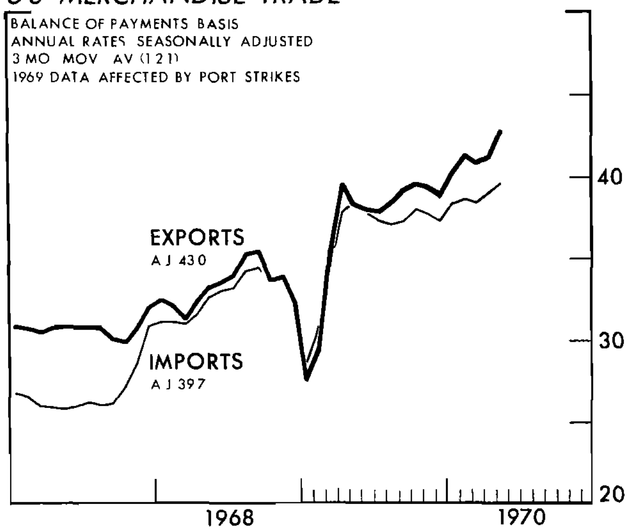
The Canadian trade surplus in the first half of 1970 ran at an annual rate of $2.5 billion, very much higher than that registered in the first half of 1969. Exports increased by 16 per cent, while imports rose less than 2 per cent. A marked easing of demand pressures in Canada and relatively high levels of demand in Western Europe and continued growth in import demand in the United States have been the primary factors behind this substantial change in the Canadian trade account. Increased sales of wheat and the unwinding of the effects of strikes which had occurred in important export industries, such as nickel and iron ore, in 1969, were also factors in the improvement. Rapidly growing exports of automobiles and parts added further to Canada's trade balance. The large surplus provided one of the main sources of the exchange inflows which preceded the floating of the Canadian dollar on June 1.

Canada's foreign trade continues to be predominantly with the United States; approximately 75 per cent of Canadian imports come from the U.S., and about 68 per cent of Canada's exports are sold in the American market. Items covered by the 1965 automobile agreement now represent over 25 per cent of U.S.-Canadian trade, compared to less than 20 per cent in 1967 and just over 10 per cent in 1965. Exports of crude oil to the U.S. have also sharply expanded in recent years, although this source of export growth may be ended by recent U.S. restrictions on oil imports from Canada.

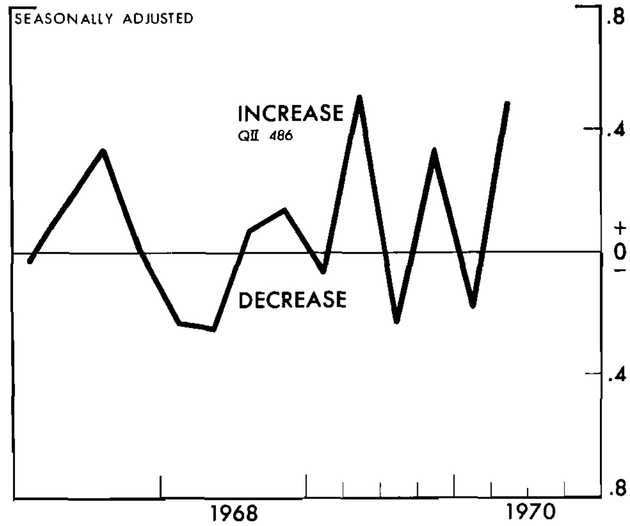
U.S. AND INTERNATIONAL ECONOMIC DEVELOPMENTS

BILLIONS OF DOLLARS

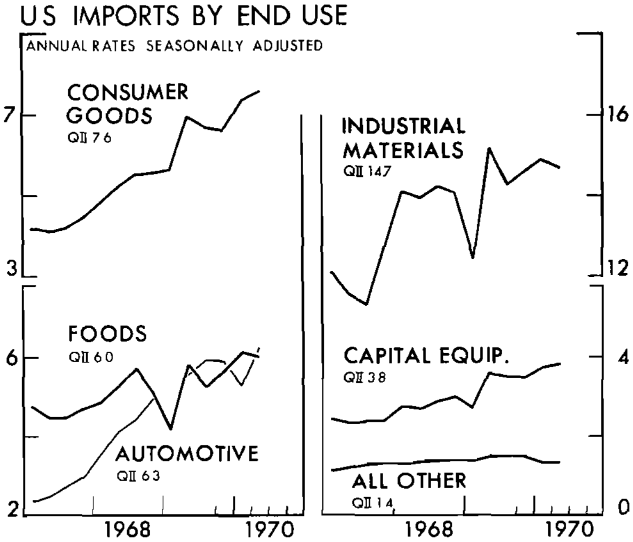
US MERCHANDISE TRADE



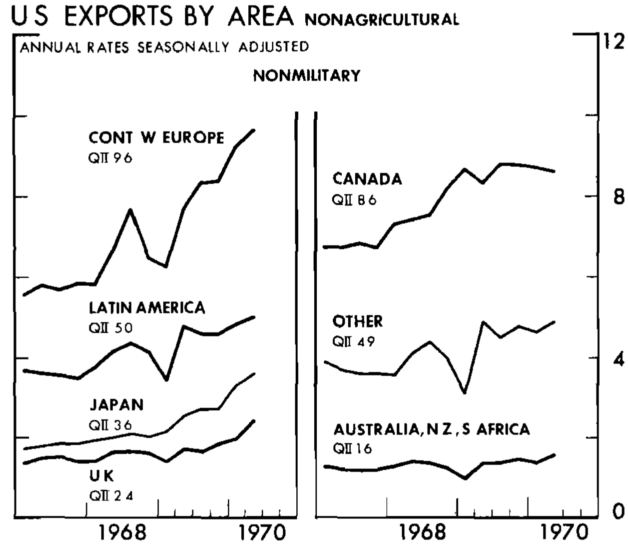
US BANKS FOREIGN CLAIMS



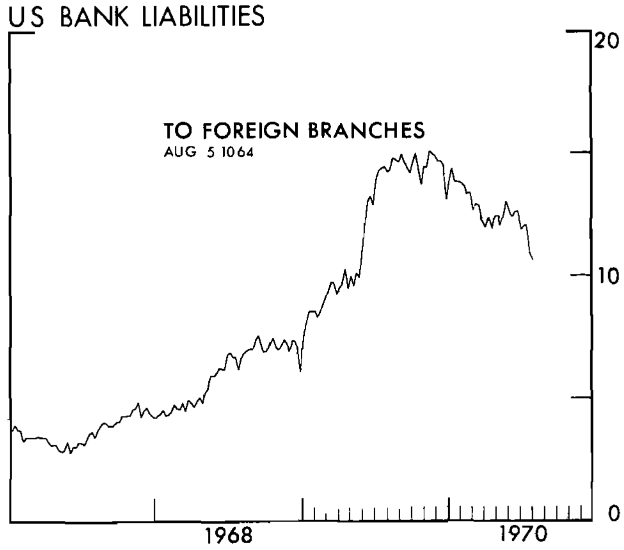
US IMPORTS BY END USE



US EXPORTS BY AREA NONAGRICULTURAL



US BANK LIABILITIES



90-DAY RATES