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CURRENT ECONOMIC AND FINANCIAL CONDITIONS

By the Staff
Board of Governors
of the Federal Reserve System

June 14, 1972

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DOMESTIC NONFINANCIAL SCENE

June 14, 1972

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SELECTED DOMESTIC NONFINANCIAL DATA
AVAILABLE SINCE PRECEDING GREENBOOK
(Seasonally adjusted)

	Latest Data-1972			Per Cent Change From		
	Period	Release Date	Data	Preceding Period	Three Periods Earlier	Year Earlier
						(At annual rates)
Unemployment rate (%)	May	6/2	5.9	[5.9] ^{1/}	[5.7] ^{1/}	[6.1] ^{1/}
Nonfarm employment, payroll (mil.)	May	6/2	72.5	3.4	4.2	2.4
Manufacturing	May	6/2	19.0	5.9	5.8	1.4
Nonmanufacturing	May	6/2	53.5	2.6	3.6	2.8
Private nonfarm:						
Average weekly hours (hours)	May	6/2	37.0	[37.2] ^{1/}	[37.2] ^{1/}	[36.9] ^{1/}
Hourly earnings (\$)	May	6/2	3.61	3.3	6.8	5.9
Output per manhour (1967=100)	QI ^{1/}	5/26	109.4	3.9	--	3.4
Compensation per manhour (1967=100)	QI ^{1/}	5/26	136.8	9.4	--	6.6
Unit labor cost (1967=100)	QI ^{1/}	5/26	125.1	5.3	--	3.1
Manufacturing:						
Average weekly hours (hours)	May	6/2	40.5	[40.8] ^{1/}	[40.5] ^{1/}	[40.0] ^{1/}
Unit labor cost (1967=100)	Apr.	5/25	120.7	10.0	9.5	4.1
Industrial production (1967=100)	May	6/14	111.6	5.4	8.0	4.3
Consumer goods	May	6/14	121.2	10.0	8.8	4.8
Business equipment	May	6/14	101.5	8.3	11.3	7.5
Defense & space equipment	May	6/14	76.2	-1.6	4.8	-0.9
Materials	May	6/14	113.1	-3.2	9.4	3.9
Wholesale prices (1967=100)	May	6/2	117.9	5.4	3.4	3.9
Industrial commodities	May	6/2	117.5	4.2	4.2	3.4
Farm products & foods and feeds	May	6/2	119.4	8.7	1.3	5.0
Consumer prices (1967=100)	Apr.	5/19	124.3	2.0	3.1	3.4
Food	Apr.	5/19	122.5	-1.0	7.0	3.9
Commodities except food	Apr.	5/19	118.6	2.0	2.4	2.3
Services ^{2/}	Apr.	5/19	132.4	3.6	2.7	4.4
						(Not at annual rates)
Retail sales, total (\$ bil.)	May	6/9	36.8	2.3	4.1	9.8
GAF	May	6/9	9.9	3.4	4.6	12.1
Auto sales, total (mil. units) ^{3/}	May	6/6	11.13	6.2	9.9	12.4
Domestic models	May	6/6	9.60	6.4	10.3	14.0
Foreign models	May	6/6	1.53	4.7	7.1	3.8
Plant & equipment expen. (\$ bil.) ^{4/}	1972	6/2	89.61	--	--	10.3
Mfrs. new orders dur. goods (\$ bil.)	Apr.	5/31	35.5	1.2	1.1	17.4
Capital equipment	Apr.	5/31	9.1	1.4	3.7	18.6
Defense products	Apr.	5/31	1.9	11.1	-37.7	29.8
Leading indicators (1967=100)	Apr.	5/25	140.2	1.4	4.4	12.8

^{1/} Actual data.

^{2/} Not seasonally adjusted.

^{3/} At annual rate

^{4/} Planned--Commerce survey (the February, 1972 survey indicated an increase of 10.7 per cent).

THE ECONOMIC PICTURE IN DETAIL

Domestic Nonfinancial Scene

Summary. The overall economic situation continues strongly expansive. Retail sales rose sharply in May, according to the advance report, and were substantially above the first-quarter average. Strength was widespread among durable and nondurable goods. Sales of domestic-type autos accelerated to an annual rate of 9.6 million units, the highest this year, and sales of imported models were at a 1.5 million rate.

Industrial production rose 0.5 per cent further in May, with gains in consumer goods, business equipment, and materials. Total industrial output was 2 per cent above the first quarter average and virtually back to its pre-recession high in September 1969. Manufacturers' new orders for durable goods rose further in April, with orders for capital equipment up for the seventh consecutive month. Book value of manufacturing and trade stocks increased only moderately in April, according to the preliminary estimates, and the stocks/sales ratio was the lowest in six years.

Employment showed a further strong gain in May, but the unemployment rate--reflecting another large addition to the civilian labor force--remained at 5.9 per cent for the third consecutive month. In manufacturing, the rise in employment continued sizable, but the workweek declined following the sharp April advance. The rise in average hourly earnings in the private nonfarm economy was reported to be small in May, bringing the average increase since January down to an

annual rate of 4.7 per cent, compared with 6.7 per cent in the pre-freeze months of 1971.

Wholesale prices rose substantially in May. Prices of industrial commodities increased at an annual rate of more than 4 per cent, about the average rate prevailing since last November. Prices of farm products and foods were up sharply, following little change in April. The consumer price index, which had been stable in March, increased quite moderately in April.

Outlook. Recent economic data support the staff projection of a step-up in the rate of real GNP growth this quarter. Current expectations are for a 6.5 per cent annual rate of gain, compared with 5.6 per cent in the first quarter. Further acceleration is projected in the second half of this year, to an average of around 7-1/2 per cent.^{1/} The monetary aggregates are assumed to grow at rates consistent with a 6 per cent expansion in M_1 during this period, and this is expected to be associated with some increase in short-term interest rates.

The rise in the GNP deflator is expected to slow in the current quarter, and to moderate somewhat further in the second half of the year--to an annual rate of about 3-1/2 per cent. The anticipated slowing reflects a moderation in the rise in unit labor costs. The staff is now projecting the unemployment rate at 5.3 per cent in the fourth quarter, about the same as in the greenbook four weeks ago.

^{1/} Projections through calendar year 1973 are being distributed separately and will be described in detail in the Chart Show.

STAFF GNP PROJECTIONS

	Change in Nominal GNP \$ billion		Per cent increase, annual rate				Unemployment Rate	
	5/17/72	Current	Real GNP		Private GNP fixed weight price index		5/17/72	Current
			5/17/72	Current	5/17/72	Current		
<u>Actual</u>								
1971-IV	19.5	19.5	5.8	5.8	1.8	1.8	5.9	5.9
1972-I	30.7	30.7	5.6	5.6	4.4	4.4	5.8	5.8
<u>Projected</u>								
1972-II	30.2	28.9	6.9	6.4	4.0	4.0	5.7	5.8
1972-III	32.3	31.5	7.9	7.7	3.4	3.4	5.5	5.6
1972-IV	32.7	31.8	7.8	7.5	3.4	3.4	5.2	5.3

The staff GNP projection for the second and subsequent quarters is slightly lower than four weeks ago, as can be seen in the table. The downward revision is primarily attributable to the smaller increase now projected for business capital outlays--12.6 per cent from 1971 to 1972, rather than the 14.0 per cent of the preceding projection. In this sector, staff expectations have been reduced as a result of the latest Commerce Survey, which indicated a smaller increase than did the recent McGraw-Hill survey. Projections for other demand sectors have changed very little.

For the current quarter, in addition to the smaller increase projected for business fixed investment, we now expect somewhat less improvement in net exports than earlier. However, consumer spending is

at least as strong as we have been projecting, and inventory investment is still expected to be appreciably larger than the close-to-zero figure of the first quarter.

In the second half of the year, all demand sectors are expansive--except for residential construction, which appears to be near or at its peak now. The staff still expects a rise in defense outlays in lagged response to the recent escalation in Vietnam and a rise of 12-1/2 per cent in social security benefits, effective July 1. Recent official statements on defense spending and Congressional developments with respect to social security legislation appear to support these assumptions.

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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.)

	1971	1972 Proj.	1971		1972 Projected			
			III	IV	I	II	III	IV
Gross National Product	1046.8	1149.0	1053.4	1072.9	1103.6	1132.5	1164.0	1195.8
Final purchases	1044.5	1142.7	1054.6	1070.4	1103.0	1129.0	1156.0	1182.8
Private	811.5	883.9	820.8	829.6	853.4	873.7	894.3	914.1
Excluding net exports	811.5	887.8	820.8	834.2	859.6	878.5	897.2	915.8
Personal consumption expenditures	662.1	715.7	668.8	677.2	691.8	707.2	723.3	740.4
Durable goods	100.5	112.2	102.8	103.6	107.6	110.6	113.6	117.0
Nondurable goods	278.6	298.2	280.2	283.3	288.0	294.6	301.5	308.7
Services	282.9	305.3	285.8	290.3	296.2	302.0	308.2	314.7
Gross private domestic investment	151.6	178.4	150.8	159.4	168.3	174.8	181.9	188.4
Residential construction	40.6	49.7	42.7	44.4	49.0	50.3	50.4	48.9
Business fixed investment	108.7	122.4	109.3	112.6	118.7	121.0	123.5	126.5
Change in business inventories	2.2	6.3	-1.2	2.4	0.6	3.5	8.0	13.0
Nonfarm	1.7	6.1	-2.0	2.0	0.1	3.3	8.0	13.0
Net exports of goods and services ^{1/}	0.0	-3.9	0.0	-4.6	-6.2	-4.8	-2.9	-1.7
Exports	65.3	70.5	68.2	60.4	69.2	68.9	70.8	73.2
Imports	65.3	74.4	68.2	65.0	75.4	73.7	73.7	74.9
Gov't. purchases of goods and services	233.0	258.8	233.8	240.8	249.6	255.3	261.7	268.7
Federal	97.6	107.3	97.6	100.3	104.9	106.3	108.2	109.7
Defense	71.4	77.5	70.2	71.4	75.8	76.8	78.0	79.5
Other	26.2	29.7	27.4	28.9	29.0	29.5	30.2	30.2
State & local	135.5	151.6	136.2	140.5	144.8	149.0	153.5	159.0
Gross national product in constant (1958) dollars	739.4	781.9	740.7	751.3	761.6	773.8	788.7	803.4
GNP implicit deflator (1958 = 100)	141.6	146.9	142.2	142.8	144.9	146.3	147.6	148.8
Personal income	857.0	931.7	864.6	876.7	900.1	917.8	943.9	965.0
Wage and salary disbursements	574.2	629.6	577.3	587.0	608.9	621.5	636.1	652.0
Disposable income	741.3	793.9	748.5	755.0	764.3	781.8	806.1	823.5
Personal saving	60.5	59.0	61.0	59.0	53.5	55.4	63.4	63.5
Saving rate (per cent)	8.2	7.4	8.1	7.8	7.0	7.1	7.9	7.7
Corporate profits before tax	85.5	100.9	85.8	86.0	91.6	96.0	104.0	112.0
Corp. cash flow, net of div (domestic)	81.0	97.4	82.4	85.6	90.0	94.0	100.1	105.5
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	198.8	227.4	197.8	203.0	222.1	224.0	228.6	235.0
Expenditures	221.9	248.8	224.6	228.7	235.5	244.1	255.7	259.9
Surplus or deficit (-)	-23.1	-21.4	-26.7	-25.7	-13.3	-20.1	-27.1	-24.9
High employment surplus or deficit (-)	2.9	-2.0	1.3	6.6	8.3	0.3	-8.1	-8.7
Total labor force (millions)	86.9	89.1	87.0	87.7	88.4	88.8	89.3	89.7
Armed forces "	2.8	2.4	2.8	2.7	2.5	2.4	2.4	2.4
Civilian labor force "	84.1	86.6	84.2	85.0	85.9	86.4	86.9	87.3
Unemployment rate (per cent)	5.9	5.6	6.0	5.9	5.8	5.8	5.6	5.3
Nonfarm payroll employment (millions)	70.7	72.7	70.6	71.0	71.8	72.4	73.0	73.6
Manufacturing	18.6	19.0	18.5	18.6	18.7	18.9	19.1	19.3
Industrial production (1967 = 100)	106.3	113.1	105.9	107.0	109.3	111.6	114.4	117.2
Capacity utilization, manufacturing (per cent)	74.6	76.7	74.1	74.1	74.9	76.2	77.3	78.3
Housing starts, private (millions, A.R.)	2.05	2.28	2.11	2.24	2.51	2.30	2.20	2.10
Sales new autos (millions, A.R.)	10.13	10.65	10.29	10.47	10.09	10.75	10.75	11.00
Domestic models	8.68	9.17	8.76	9.20	8.69	9.25	9.25	9.50
Foreign models	1.46	1.48	1.53	1.27	1.40	1.50	1.50	1.50

^{1/} The projected GNP exports and imports of goods and services, and their net, are based on quarter-to-quarter changes projected in balance of payments exports and imports, shown below. These are consistent with revised '71-IV figures not yet incorporated in the GNP accounts.

Net exports of goods and services	0.8	-1.3	0.2	-2.1	-3.6	-2.3	-0.3	0.9
Exports	66.0	72.8	68.3	62.7	71.5	71.2	73.1	75.5
Imports	65.2	74.1	68.1	64.8	75.1	73.4	73.4	74.6

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CHANGES IN GROSS NATIONAL PRODUCT
AND RELATED ITEMS

	1971	1972 Proj.	1971		1972			
			III	IV	I	Projected		
						II	III	IV
-----Billions Of Dollars-----								
Gross National Product	72.7	102.2	13.4	19.5	30.7	28.9	31.5	31.8
Inventory change	-0.6	4.1	-5.8	3.6	-1.8	2.9	4.5	5.0
Final purchases	73.2	98.2	19.2	15.8	32.6	26.0	27.0	26.8
Private	59.6	72.4	15.0	8.8	23.8	20.3	20.6	19.8
Excluding net exports	63.2	76.3	15.1	13.4	25.4	18.9	18.7	18.6
Net exports	-3.6	-3.9	-0.1	-4.6	-1.6	1.4	1.9	1.2
Government	13.6	25.8	4.2	7.0	8.8	5.7	6.4	7.0
GNP in constant (1958) dollars	19.4	42.5	4.9	10.6	10.3	12.2	14.9	14.7
Final purchases	19.6	39.1	9.5	7.7	12.4	9.4	10.9	10.3
Private	19.8	32.0	6.9	4.1	10.9	8.3	8.9	8.6
-----Per Cent Per Year-----								
Gross National Product	7.5	9.8	5.2 ^{1/}	7.6 ^{1/}	12.0 ^{1/}	10.5	11.1	10.9
Final purchases	7.5	9.4	7.4	6.0	12.2	9.4	9.6	9.3
Private	7.9	8.9	7.4	4.3	11.5	9.5	9.4	8.9
Personal consumption expenditures	7.5	8.1	7.0	5.0	8.6	8.9	9.1	9.5
Durable goods	13.4	11.6	14.9	3.1	15.4	11.2	10.8	12.0
Nondurable goods	5.3	7.0	3.5	4.4	6.6	9.2	9.4	9.6
Services	7.8	7.9	7.6	6.3	8.1	7.8	8.2	8.4
Gross private domestic investment	12.0	17.7	-5.5	22.8	22.3	15.4	16.2	14.3
Residential construction	33.6	22.4	27.0	15.9	41.4	10.6	0.8	-11.9
Business fixed investment	6.5	12.6	3.7	12.1	21.7	7.8	8.3	9.7
Gov't. purchases of goods & services	6.2	11.1	7.3	12.0	14.6	9.1	10.0	10.7
Federal	0.4	9.9	6.7	11.1	18.3	5.3	7.1	5.5
Defense	-5.3	8.5	-6.7	6.8	24.6	5.3	6.3	7.7
Other	19.6	13.4	45.5	21.9	1.4	6.9	9.5	0.0
State & local	10.9	11.9	7.8	12.6	12.2	11.6	12.1	14.3
GNP in constant (1958) dollars	2.7	5.7	2.7 ^{1/}	5.8 ^{1/}	5.6 ^{1/}	6.4	7.7	7.5
Final purchases	2.7	5.3	5.2	4.2	6.6	5.0	5.7	5.3
Private	3.4	5.3	4.6	2.7	7.2	5.4	5.7	5.4
GNP implicit deflator	4.7	3.8	2.5 ^{1/}	1.7 ^{1/3/}	6.0 ^{1/4/}	4.0	3.4	3.4
Private GNP fixed weight index ^{2/}	5.3	3.6	3.6 ^{1/}	1.8 ^{1/}	4.4 ^{1/}	4.0	3.4	3.4
Personal income	6.6	8.7	5.2	5.6	10.7	7.9	11.4	8.9
Wage and salary disbursements	6.1	9.6	4.4	6.7	14.9	8.3	9.4	10.0
Disposable income	7.8	7.1	4.8	3.5	4.9	9.2	12.4	8.6
Corporate profits before tax	13.4	18.0	-5.1	0.9	26.0	19.2	33.3	30.8
Federal government receipts and expenditures (N.I.A. basis)								
Receipts	3.8	14.4	0.2	10.5	37.6	3.4	8.2	11.2
Expenditures	8.2	12.1	5.8	7.3	11.9	14.6	19.0	6.6
Nonfarm payroll employment	0.1	2.8	-0.2	2.2	4.3	3.4	3.3	3.4
Manufacturing	-3.9	2.3	-2.5	0.9	2.5	5.3	3.9	4.2
Industrial production	-0.4	6.4	-3.4	4.2	8.6	8.4	10.0	9.8
Housing starts, private	43.4	11.2	22.2	24.2	47.8	-33.5	-17.4	-18.2
Sales new autos	21.3	5.2	19.1	7.4	-14.5	26.2	0.0	9.3
Domestic models	21.9	5.7	22.7	20.1	-22.2	25.8	0.0	10.8
Foreign models	18.7	1.5	-0.8	-66.4	37.9	30.0	0.0	0.0

^{1/} At compound rates.^{2/} Using expenditures in 1967 as weights.^{3/} Excluding the first \$1.2 billion, annual rate, of the volunteer army pay increase, 1.2 per cent per year.^{4/} Excluding the remaining \$1.2 billion, annual rate, of the volunteer army pay increase and the general Federal employees pay increase, 4.3 per cent per year.

Industrial production. Industrial production rose 0.5 per cent further in May to 111.6 per cent (1967=100). This was 4.3 per cent above a year earlier and only 0.3 per cent below the previous high in September 1969. Gains in May were widespread among consumer goods, business equipment, and durable materials. The indexes for February, March, and April were revised up slightly--by 0.2 percentage point in each month. Since last December, the index has advanced at an annual rate of nearly 9 per cent.

Output of most appliances, furniture, and consumer nondurable goods increased in May. Auto assemblies, however, were off a little from April, despite strong retail sales in May, and were at an annual rate of 8.8 million units compared with a 9.0 million unit rate in April. Production of most business equipment industries rose further in May; the total was 7.5 per cent above the low of a year earlier but still 8 per cent below the 1969 peak. Output of defense equipment was unchanged in May. Production of construction products, steel, and other durable goods materials increased, while nondurable materials changed little.

INDUSTRIAL PRODUCTION
(1967=100, seasonally adjusted)

	Per cent changes				
	1972		April 1972	May 1971	Sept.*1969
	April(r)	May(e)	to May 1972	to May 1972	to May 1972
Total index	111.1	111.6	.5	4.3	- .3
Consumer goods	120.2	121.2	.8	4.8	7.9
Autos	114.3	111.3	-2.6	2.8	-4.5
Home goods	121.0	122.2	1.0	7.3	9.5
Apparel & staples	119.4	120.2	.7	4.4	8.0
Business equipment	100.8	101.5	.7	7.5	-8.0
Defense equipment	76.3	76.2	-.1	-.9	-25.4
Intermediate products	116.6	117.3	.6	3.3	4.6
Construction products	116.4	117.0	.5	1.3	-1.7
Materials, total	113.4	113.1	-.3	3.9	-1.1
Durable	108.0	108.6	.6	3.6	-5.5
Steel	103.5	105.5	1.9	-6.6	-9.8
Nondurable	119.8	119.7	-.1	6.1	5.2

* Pre-recession peak for total index.

Retail sales. Sales in May rose 2.3 per cent from April to a new high, 3.5 per cent above the first quarter average and 9.8 per cent above a year earlier. Strength was widespread in May but durable goods sales were relatively stronger than nondurable, with an increase from the first quarter average of 4.6 per cent largely reflecting a 7.2 per cent increase in the sales of the automotive group. Furniture and appliances sales rebounded after an April drop, and were 17 per cent above a year earlier.

Nondurable goods sales in May were up 1.8 per cent from April and 2.9 per cent from the first quarter, led by general merchandise group. Food sales were also strong, with an advance of 3.1 per cent from the first quarter average.

RETAIL SALES, 1972
(Seasonally adjusted, percentage change)

	<u>QIV to</u> <u>QI</u>	<u>QI to</u> <u>May</u>	<u>Feb. to</u> <u>March</u>	<u>March to</u> <u>April</u>	<u>April to</u> <u>May</u>
Total sales	1.2	3.5	3.1	-1.3	2.3
Durable goods	.3	4.6	5.5	-2.1	3.3
Automotive	-3.1	7.2	5.7	- .9	3.7
Furniture and appliances	9.2	.6	3.0	-3.5	2.4
Nondurable goods	1.6	2.9	2.0	- .9	1.8
Food	1.7	3.1	.7	- .3	1.7
General merchandise	2.3	4.6	2.1	-1.0	3.7
Total, less autos and nonconsumption items	2.1	3.1	2.3	- .9	1.9
GAAF	3.0	4.1	2.1	-1.0	3.4
Real* sales	.3	NA	3.0	-1.3	NA

* Deflated by all commodities CPI, seasonally adjusted.

Unit sales of consumer durables. Sales of new domestic-type autos in May were at an annual rate of 9.6 million units, 6 per cent above a month earlier and 14 per cent above a year earlier. April-May sales were at a 9.3 million unit rate compared with an 8.7 million unit rate in the first quarter. Dealer inventories at the end of May were at a 52 day supply, down 5 per cent from a month earlier and 10 per cent from a year ago. The decline in the stock-sales ratio resulted

from the higher sales rate, since stocks in absolute terms were the same as last month and above those of a year earlier.

May sales of imported autos were at a 1.5 million unit rate, up 5 per cent from both a month and a year earlier. The import share of total sales was 14 per cent, the same as in April but below the 16 per cent of May last year.

According to partially complete data, unit purchases of major home appliances by retailers fell 6 per cent between April and May but were 9 per cent above a year ago. With the exception of freezers, which showed another sharp monthly gain, dealer purchases of other items declined from April levels. Compared with a year earlier, however, all items showed gains, except air conditioners. Similar trends held for unit purchases of TVs, which in May were below a month earlier but up from a year ago. Purchases of monochrome sets were 20 per cent above May 1971 while color set purchases were up 4 per cent.

UNIT PURCHASES BY RETAILERS OF SELECTED HOME GOODS
(Seasonally adjusted, 1967=100)

	<u>1971</u>	<u>1972</u>		<u>Per cent change</u>		
	May	March	April	May	Month ago	Year ago
TVs ^{1/}	123	121	141	131	-7	6
Radios	105	83	105	89	-15	-15
Home appliances ^{2/}	126	129	146	137p	-6	9

^{1/} Includes foreign-made units sold under U.S. brand names. Foreign-made sold under foreign brands are not included.

^{2/} Weighted average of indexes for air conditioners, dishwashers, dryers, freezers, electric ranges, gas ranges, refrigerators, washing machines, and vacuum cleaners. Weights are 1967 values of retail sales.

Conference Board Survey of Consumer Expectations and Intentions.

The March-April Conference Board survey was somewhat weaker than the previous bi-monthly report which had indicated a significant improvement in some of the more important consumer attitudes and was in sharp contrast to recent retail sales reports. In the latest survey--taken at the end of March and in early April--an increased percentage of households reported present business conditions were bad and there was a sharp drop in households expecting an increase in income. Present employment conditions were appraised somewhat better, however; this was also true of business conditions expected six months hence.

Buying plans for autos within the next six months were lower, with purchase plans declining from 7.7 per cent of households in January-February to 7.2 in March-April. A year earlier 8.6 per cent of households were planning to buy a car. Intentions to purchase major appliances dropped sharply, compared with both the previous survey and a year earlier. Plans to purchase a house remained relatively high.

CONSUMER EXPECTATIONS AND INTENTIONS^{1/}
(Seasonally adjusted)

	1971				1972	
	March- April	July- August	September- October	November- December	January- February	March- April
<u>Appraisal of Present Situation</u>						
Business Conditions						
Good	13.1	14.8	15.1	15.4	20.9	21.0
Bad	34.3	28.9	28.1	26.5	19.8	21.2
Employment						
Jobs plentiful	5.9	7.6	6.5	6.8	8.9	9.8
Jobs hard to get	45.0	43.1	42.7	41.5	39.4	38.6
<u>Expectations for Six Months Hence</u>						
Business Conditions						
Better	25.4	26.2	25.9	25.3	24.7	26.3
Worse	13.0	10.4	10.5	8.4	6.1	7.5
Employment						
More jobs	21.7	21.9	20.3	20.5	20.4	20.2
Fewer jobs	21.0	18.3	19.2	16.0	16.2	16.3
Income						
Increase	23.8	23.1	24.2	24.8	28.2	23.7
Decrease	7.2	7.3	7.8	6.9	6.0	6.3
<u>Plans to Buy Within Six Months</u>						
Automobile						
Yes	8.6	8.4	7.9	8.1	7.7	7.2
New	5.3	4.7	4.6	4.5	4.7	4.2
Home						
Yes	3.0	3.4	3.2	3.1	3.8	3.8
Major appliances						
Total plans	39.2	35.0	37.9	37.5	37.4	32.4

^{1/} Source: Conference Board Survey of Consumer Expectations and Intentions.

Cyclical indicators. The Census trend-adjusted composite index of leading indicators rose 1.4 per cent in April (p), after an upward-revised 1.9 per cent increase in March. The coincident and lagging composites also rose.

Leading series increasing in April were the manufacturing workweek, initial claims for unemployment insurance (inverted), new orders for durable goods, contracts and orders for plant and equipment, housing permits, industrial materials prices, and common stock prices. The only series to decline was the ratio of price to unit labor cost in manufacturing, as the index of unit labor costs increased faster than the price index.

CHANGES IN COMPOSITE CYCLICAL INDICATORS
April 1972 (p)

	Per cent change from:	
	Previous month	Three months earlier
12 Leading (trend adjusted)	1.4	4.4
12 Leading, prior to trend adjustment	1.2	3.3
5 Coincident	.8	2.5
5 Coincident, deflated	.7	2.1
6 Lagging	1.3	2.1

April was the tenth consecutive month of increase for the leading composite, which is now 23 per cent above November, 1970. This rise is similar to the 17-month increases from the 1954 and 1958 troughs and greater than the increase from the 1961 trough. However, the amount of increase from the trough does not appear to be highly correlated with the strength or duration of expansion in the following period.

Manufacturers' orders and shipments. New orders for durable goods rose 1.2 per cent from March to April (p), following a 1.7 per cent increase in March. Orders for capital equipment--which had declined according to the earlier advance report--now are shown to have risen for the seventh straight month. April orders for all major groups except defense were above the first quarter average.

MANUFACTURERS' NEW ORDERS FOR DURABLE GOODS
(Per cent change)

	April from March (p)	April from Q1 average (p)
Durable goods, total	1.2	1.7
Primary metals	- .9	2.6
Motor vehicles & parts	2.5	2.5
Household durables	.9	7.7
Defense products	11.1	-12.3
Capital equipment	1.4	2.4
Construction and other durables	- .3	1.7

Shipments rose 1.9 per cent in April but were still below incoming orders, and the order backlog rose 0.3 per cent--a somewhat lower rate of increase than in the previous five months. The order backlog for capital equipment rose for the third straight month.

Inventories. Book value of business inventories rose at a \$6.6 billion annual rate in April (p) following an upward-revised March increase of \$5.4 billion. Trade stocks rose sharply, especially at wholesale. The increase in wholesale stocks followed a slight decline in March and reflected, in part, restocking by auto and other importers following the end of the dock strike. Partly offsetting this was a decline in manufacturing.

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

	1971	1972		
	Q IV	Q I (r)	March (r)	April (p)
Manufacturing and trade	4.1	5.5	5.4	6.6
Manufacturing, total	1.1	2.8	2.5	-1.9
Durable	-1.3	2.8	2.2	- .9
Nondurable	2.4	- .1	.4	-1.0
Trade, total	2.9	2.7	2.8	8.5
Wholesale	4.4	1.0	- .1	4.7
Retail	-1.5	1.7	2.9	3.9

NOTE: Detail may not add to total because of rounding.

The inventory-sales ratio for manufacturing and trade was unchanged in April from a downward-revised March level of 1.47--the lowest level in six years. The trade ratio increased--reflecting in part both the jump in stocks in wholesale trade and the temporary decline in retail sales in April--but the manufacturing ratio declined. The ratio of inventories to unfilled orders at durable goods manufacturers declined further.

INVENTORY RATIOS

	1971		1972	
	March	April	March (r)	April (p)
<u>Inventories to sales:</u>				
Manufacturing and trade	1.56	1.56	1.47	1.47
Manufacturing, total	1.74	1.74	1.61	1.59
Durable	2.06	2.08	1.88	1.84
Nondurable	1.35	1.34	1.28	1.28
Trade, total	1.37	1.37	1.33	1.35
Wholesale	1.24	1.24	1.22	1.23
Retail	1.45	1.45	1.40	1.42
<u>Inventories to unfilled orders:</u>				
Durable manufacturing	.823	.834	.837	.833

Construction and real estate. Seasonally adjusted outlays for new construction changed little in May from a downward revised but still record rate now reported for April. Residential construction declined for the second consecutive month, but the May rate remained above the advanced first quarter level. Outlays for private non-residential construction edged higher, while those for public construction showed essentially no change.

Despite little further rise so far this year, construction costs in May were about 5 per cent above a year earlier, according to the Census Bureau's composite index. This compared with a corresponding year to year increase of 7 per cent in May of last year.

NEW CONSTRUCTION PUT IN PLACE
(Seasonally adjusted annual rates, in billions of dollars)

	1971		1972		
	QI	QIV	QI	Apr.p/	May <u>1</u> /
Total	102.0	115.7	121.1	122.6	122.1
Private	71.4	84.6	89.7	91.5	90.9
Residential	36.6	46.9	51.5	52.5	51.6
Nonresidential	34.8	37.6	38.2	39.0	39.4
Public	30.6	31.1	31.4	31.1	31.2
State and local	26.8	27.0	26.9	26.9	26.9
Federal	3.8	4.1	4.5	4.2	4.3

1/ Data for May 1972 are confidential Census Bureau extrapolations. In no case should public reference be made to them.

Seasonally adjusted sales of new homes by merchant builders turned upward again in April to virtually the record rate in the first quarter. As a result, while stocks of homes for sale increased somewhat

further, they amounted to only 5.5 months' supply in April compared with 5.9 months' in March. The improved sales rate in April was associated with a shift toward less expensive units. Even so, at \$26,700, the median price for new homes sold continued above that for homes still awaiting sale. Moreover, unlike prices of new homes sold, prices of existing homes sold in April rose somewhat further to a median of \$26,450.

NEW SINGLE-FAMILY HOMES SOLD AND FOR SALE

	Homes sold <u>1/</u> (Thousands of units)	Homes for sale <u>2/</u> (Thousands of units)	Median price of:	
			Homes sold (Thousands of dollars)	Homes for sale (Thousands of dollars)
<u>1971</u>				
QIII	666	265	25.3	26.1
QIV	682	284	25.5	25.9
<u>1972</u>				
QI	698	317	26.1	26.1
February (r)	724	309	26.3	26.2
March (r)	648	317	27.3	26.1
April (p)	697	320	26.7	26.4

1/ SAAR.

2/ SA, end of period.

Anticipated plant and equipment spending. The May Commerce capital expenditures survey indicates that business now plans a 10.3 per cent increase in 1972 spending for new plant and equipment as compared to an actual increase of only 2 per cent in 1971. This is essentially unchanged from the 10.5 per cent planned increase reported

in the February Commerce survey but is well below the 14.5 per cent rise shown in the April McGraw-Hill survey. Manufacturers now anticipate a 5-1/2 per cent gain--down from the earlier reported 9 per cent rise--with durable goods producers' plans up 11 per cent instead of 14 per cent. There was a small upward revision in plans of nonmanufacturing concerns.

ANTICIPATED 1972 EXPENDITURES FOR NEW PLANT
AND EQUIPMENT BY U.S. BUSINESS
(Per cent change from 1971)

	Comm-SEC (Dec. 1971)	McGraw-Hill (Feb. 1972)	Commerce (Feb. 1972)	McGraw-Hill (Apr. 1972)	Commerce (May '72)
All business	9.1	11.4	10.5	14.5	10.3
Manufacturing	4.0	12.0	8.7	15.1	5.6
Durable goods	5.1	13.1	13.9	14.8	11.3
Nondurable goods	3.0	11.1	4.2	15.4	.6
Nonmanufacturing	12.1	11.0	11.6	14.1	13.1
Transportation	18.3	23.6	16.0	31.6	14.4
Electric utilities	16.1	8.0	13.4	11.0	13.2
Communication	12.8 <u>1/</u>	10.0	14.2 <u>1/</u>	8.0	14.2 <u>1/</u>
Commercial and other	7.3 <u>1/</u>	11.0	8.1 <u>1/</u>	13.0	11.9 <u>1/</u>

1/ Confidential, not published separately.

The Commerce survey further reports that overall spending is anticipated to rise sharply in the first half of 1972 with a slowing to about a 4 per cent annual rate of increase in the second half.

In contrast, the Conference Board survey of new capital appropriations by 1,000 large manufacturing concerns indicated considerable renewed strength--with an 11 per cent rise in the first quarter following a decline of 2 per cent in the fourth quarter. The rise in first quarter appropriations was largely in nondurable goods where the increase was 18 per cent; in durable goods, the increase was 5 per cent.

This increase in new appropriations should offer some support to spending by manufacturers in the second half of the year if historical performance is a guide. Substantial second half gains in outlays, however, would require a further appropriations rise in the second quarter.

Labor market. The labor market continued to strengthen in May. Payroll employment increased by 210,000--about the same as in April (revised up by 100,000). About half the increase was in manufacturing industries with the largest gains in durable goods particularly major metal-using industries. The number of jobs has increased rapidly since August, at an annual rate of 2.6 million. Factory employment, which has displayed no growth in 1971, has accelerated since December, but still remains 1.3 million below the high reached in the summer of 1969. Accompanying the recent increase in factory jobs has been a gain in the workweek; although down in May to 40.5 hours, it was about half an hour above the average for the fourth quarter of 1971.

NONFARM PAYROLL EMPLOYMENT
(Seasonally adjusted)

	Jan. 1971 - Aug. 1971	Aug. 1971 - May 1972	Dec. 1971 - May 1972
	--Change in thousands, annual rates--		
Total	129	2,595	3,096
Manufacturing	-497	669	943
Production workers	-309	627	881
Nonmanufacturing	626	1,925	2,153
Federal government	- 19	24	- 2
State and local government	231	580	622

Unemployment and labor force. The unemployment rate was unchanged in May at 5.9 per cent for the third consecutive month, as both total employment and the civilian labor force increased by about 200,000. The jobless rate for adult males was unchanged while the rate for adult females moved up, returning to the level of last fall; the volatile teenage rate dropped sharply, due entirely to a decline in unemployment among teenage girls.

SELECTED UNEMPLOYMENT RATES
(Seasonally adjusted)

	1971		1972	
	May	November	April	May
Total	6.1	6.0	5.9	5.9
Men 20 years and over	4.5	4.4	4.3	4.3
Women 20 years and over	5.9	5.8	5.4	5.9
Teenagers	17.4	16.7	17.3	15.7
Households heads	3.8	3.6	3.4	3.6
White workers	5.6	5.6	5.4	5.3
Negro workers	10.5	9.4	9.6	10.7

After showing virtually no change in the first half of 1971, the civilian labor force has grown rapidly, and in May was 2.1 million above a year earlier. About two-thirds of the increase occurred among women and teenagers, apparently due in part to a return of so-called "discouraged workers" to active job seeking. Large increases in the labor force are not unusual in this stage of a recovery when job opportunities are increasing.

Earnings. Average hourly earnings of production workers on private nonfarm payrolls (adjusted for inter-industry shifts) increased at an annual rate of 5.8 per cent from last August (just before the freeze) to May; during the pre-freeze months of 1971, earnings rose at an annual rate of 6.7 per cent. Since this January, earnings have risen at only a 4.7 per cent annual rate, but this figure is strongly influenced by the usually small April-to-May increase--3.5 per cent (annual rate). Recent increases in manufacturing have been near the Pay Board guideline of 5.5 per cent while the rise in trade, finance and services has been much smaller.

HOURLY EARNINGS INDEX*
(Per cent change; seasonally adjusted, annual rate)

	Jan. 1971- Aug. 1971	Aug. 1971- May 1972	Jan. 1972- May 1972
Private nonfarm	6.7	5.8	4.7
Manufacturing	6.1	6.2	5.7
Mining	8.0	6.5	3.1
Construction	9.0	6.0	4.8
Transportation & P.U.	8.0	9.7	6.8
Trade	6.5	4.1	2.5
Finance	7.6	4.2	3.7
Services	4.4	5.5	3.6

* Adjusted for inter-industry shifts and, in manufacturing only, for overtime hours.

Meat prices. In May, beef and pork prices at the farm and wholesale levels reversed their earlier decline. They continued to rise after the WPI pricing date in the second week of the month, reaching levels by late May and early June that were around their February peaks. Retail prices--according to the Department of Agriculture's chainstore sample (confidential)--fell from their February-March peak through the first week of May. The CPI, which is priced during the first week of the month, may reflect this low for May and then begin in June to reflect the advances at farm and wholesale levels; some of this increase, however, would reflect the usual seasonal rise in retail beef and pork prices after April to a peak in August.

BEEF AND PORK--ESTIMATED PRICES AND MARGINS
Indexes 1/, 1967=100

	1971						Percentage change <u>1/</u>
	Nov.	Feb.	Mar.	Apr.	May <u>2/</u>	Nov. 1971 to May 1972 <u>2/</u>	
Beef							
Retail value	128.7	140.2	140.2	135.6	133.9	4.0	
Carcass value <u>3/</u>	130.6	139.1	133.0	130.1	135.9	4.1	
Net farm value	132.6	141.5	135.7	132.5	137.2	3.5	
Spread:							
Farm-retail	121.6	137.8	148.3	141.2	128.0	5.3	
Carcass-retail	123.7	143.1	158.6	149.6	128.9	4.2	
Pork							
Retail value	106.2	121.0	118.2	116.4	116.1	9.3	
Wholesale value	105.6	122.5	117.9	113.2	118.6	12.3	
Net farm value	97.4	132.8	120.1	116.1	129.6	33.1	
Spread:							
Farm-retail	115.7	108.3	116.0	116.7	101.5	-12.3	
Wholesale-retail	108.3	115.9	119.1	126.8	107.6	-.6	

1/ Calculated from USDA dollars-and-cents estimates for choice beef and pork.

2/ Not for publication; preliminary four-week estimates based on chainstore sample for retail prices. (Department of Agriculture).

3/ Average wholesale price multiplied by "carcass equivalent" (the average carcass weight required per pound of retail beef sold).

Retail meat prices tend to lag wholesale prices and to fluctuate less. Between November and February, however, retail beef prices rose about parallel with wholesale prices and then, more typically, declined less. Margins therefore rose sharply and, although they have since declined, still appear well above last November levels and nearly 30 per cent above those in 1967. The advance in retail beef prices in the next few months may be significantly less than recent increases in farm and wholesale prices if widening of margins is limited. (The margin--or spread--between beef prices at the farm and at retail, as estimated by the Department of Agriculture, has averaged 34 per cent of retail prices over the past decade). In addition, the usual seasonal rise amounts to 1.4 per cent between April and August.

Some improvement in margins for pork can be expected in view of the squeeze indicated by the preliminary (confidential) May estimates. Seasonal influences, as measured for the CPI, however, allow for an increase in pork prices of about 4 per cent between April and their August high.

For the second half of the year, the Department of Agriculture still expects an improvement in beef supplies; projections will be revised in mid-July taking into account new cattle-on-feed data. So far this year, marketings have been smaller than projected on the basis of recent cattle-on-feed reports; the hypothesis is that the cattle are being fed longer in view of the profitable feeding margin and this will eventually help swell marketings.

Wholesale prices. Wholesale prices increased at a seasonally adjusted annual rate of 5.6 per cent from April to May, close to the average rate of rise in the first six months of Phase II.

Industrial commodities continued to rise at about the post-freeze annual rate of 4.1 per cent. Advances for textile products, lumber and plywood, machinery and equipment, and fuels and power contributed most to the rise although increases were widespread.

Prices of consumer and producer non-food finished goods increased more slowly in May than in April, but the rates of increase since the end of last year's freeze still exceed those for the pre-freeze period in 1971. Crude materials prices have advanced rapidly since November; in May, higher prices for cattle hides and a less-than-seasonal decline for nonferrous scrap mainly accounted for the large increase.

The May advance in the index of farm and food products, at a rate of 9.5 per cent, included large increases for livestock, meat, eggs, cotton, and wool. More recently prices of livestock and meat have climbed further.

WHOLESALE PRICES

(Percentage changes, at seasonally adjusted annual rates)

	Pre-stab. period	Phase I	Phase II		Phase I + Phase II
	Dec. 1970 to Aug. 1971	Aug. 1971 to Nov. 1971	Nov. 1971 to May 1972	Apr. 1972 to May 1972	Aug. 1971 to May 1972
All commodities	5.2	-.2	5.2	5.6	3.4
Farm products ^{1/}	6.5	1.1	7.8	9.5	5.5
Industrial commodities	4.7	-.5	4.1	4.3	2.6
Crude material ^{2/}	3.3	2.3	8.8	15.1	6.6
Intermediate materials ^{3/}	6.5	-.7	4.4	6.3	2.7
Finished goods ^{4/}	2.7	-.9	3.3	2.1	1.9
Producer	3.7	-2.0	4.3	2.0	2.2
Consumer	2.2	-.4	3.1	2.1	1.9

^{1/} Farm products and processed foods and feeds.^{2/} Excludes foods, plant and animal fibers, oilseeds, and leaf tobacco.^{3/} Excludes intermediate materials for food manufacturing and manufactured animal feeds.^{4/} Excludes foods.

Increases in prices of industrial commodities have been widespread during Phase II, with a few groups showing especially sharp advances. Those five groups (out of 13) with the largest contributions to the increase on a seasonally unadjusted basis accounted for 68 per cent of the rise in the six months following the freeze compared with 83 per cent in the six months prior to the freeze. Estimates using seasonally adjusted data suggest, however, that the proportion of prices showing increases was not so different in the two periods.

PERCENTAGE CONTRIBUTIONS TO THE INCREASE IN PRICE
OF INDUSTRIAL COMMODITIES

	Feb. 1971 to Aug. 1971 (Seasonally unadjusted)	Nov. 1971 to May 1972
Metals and metal products	31.6	17.4
Lumber and wood products	22.3	14.2
Textile products and apparel	11.0	12.4
Machinery and equipment	9.9	12.1
Nonmetallic minerals products	8.2	--
Transportation equipment	--	<u>11.4</u>
	<u>83.0</u>	<u>67.5</u>

DOMESTIC FINANCIAL SITUATION

II-T-1

SELECTED DOMESTIC FINANCIAL DATA
(Dollar amounts in billions)

Indicator	Latest data		Net change from			
	Period	Level	Month ago	Three months ago	Year ago	
<u>Monetary and credit aggregates</u>			<u>SAAR (per cent)</u>			
Total reserves	May	32.9	8.4	15.9	8.7	
Reserves available (RPD's)	May	30.0	7.9	10.3	7.4	
Money supply						
M1	May	235.7	3.6	7.8	5.3	
M2	May	486.5	8.7	9.2	8.9	
M3	May	759.1	10.2	11.8	11.5	
Time and savings deposits (Less CDs)	May	250.8	13.1	10.6	12.6	
CDs (dollar change)	May	36.2	1.5	2.4	7.7	
Savings flows (S&Ls + MSBs)	May	272.6	12.9	16.5	16.3	
Bank credit (end of month)	May	516.5	17.7	13.2	12.4	
<u>Market yields and stock prices</u>			<u>Percentage or index points</u>			
Federal funds	wk. endg. 6/7	4.48	.24	1.05	.29	
Treasury bill (90 day)	" 6/7	3.86	.25	.34	-.57	
Commercial paper (90-119 day)	" 6/7	4.48	-.02	.60	-.75	
New corporate bonds Aaa	" 6/9	7.25	-.03	.11	-.80	
Municipal bonds (Bond Buyer) 1 day	6/8	5.32	-.07	.14	-.69	
FNMA auction yield	wk. endg. 6/12	7.62	-.01	.08	-.29	
Dividends/price ratio (Common stocks)	6/7	2.88	-.04	.02	.21	
NYSE index (12/31/65=50)	end of day 6/14	59.66	.19	-.33	4.30	
<u>Credit demands</u>			<u>Net change or gross offerings</u>			
			<u>Current month</u>	<u>Year to date</u>		
			<u>1972</u>	<u>1971</u>	<u>1972</u>	<u>1971</u>
Business loans at commercial banks (dollar change)	May		1.1	0.9	5.1	2.8
Consumer instalment credit outstanding	April		1.1	0.7	4.1	1.3
Mortgage debt outst. (major holders)	April		4.3 ^e	3.1	15.0 ^e	10.3
Corporate bonds (public offerings)	June		1.6 ^e	2.1	8.6 ^e	12.6
Municipal long-term bonds (gross offerings)	June		1.9 ^e	2.2	9.9 ^e	10.9
Federally sponsored Agcy. (net borrowing)	June		0.6 ^e	-0.4	2.0 ^e	-2.0
U.S. Treasury (net cash borrowing)	June		-3.8 ^e	-3.1	-2.4 ^e	3.2
Total of above items			6.8	5.5	42.3	39.1

e - Estimated.

DOMESTIC FINANCIAL SITUATION

Interest rates have changed little on balance since the last Committee meeting, although the Federal funds rate has edged higher. In the corporate and tax-exempt bond markets, underwriters in May had been pricing issues aggressively in view of the moderating forward calendar of public offerings. Although investor hesitancy led to an accumulation of underwriter inventories and syndicate terminations in early June, the resultant increase in yields simply returned rates to their mid-May levels.

Total deposit growth at banks continued to be rapid in May, even though expansion in private demand balances moderated further, as total time and savings deposit growth accelerated to the most rapid rate since January. As in April, outstanding negotiable CD's rose sharply in May, particularly at those banks experiencing sustained business loan demands; anticipation of June tax date run-offs also appeared to be a factor in these sales. Other time deposits continued their post-April-tax-date strength, suggesting that at least some of the slowdown of such inflows in March-April was associated with final payments on personal income taxes. The most recent survey of time and savings deposits indicates no significant change in bank offering rates on consumer-type CD's.

With funds inflows large, all categories of bank loans and investments rose in May. Banks stepped up their purchases of longer-term municipals, real estate and consumer loans continued to expand rapidly, and business loans outside of New York City showed significant growth for the fifth consecutive month.

Inflows to the nonbank thrift institutions, on the other hand, appear to be moderating somewhat. Nevertheless, outstanding mortgage commitments at savings and loan associations rose further in April, and mortgage credit remains readily available. In mid-June the lessening of earlier marginal pressures in the mortgage market was evidenced by a leveling off in FNMA auction yields and a decline in lender demands for forward commitments from FNMA.

Outlook. The projected increase in the pace of economic activity, along with renewed Treasury demands on the securities markets, is likely to be associated with upward pressures on short-term interest rates as the third quarter progresses. While the amount of net cash borrowing that the Treasury will need to undertake in the third quarter is uncertain, the staff feels that it could be as large as \$9 billion, financed mainly in the short-term area. The increased bill supply, when coupled with the current unusually large spread of the Federal funds rate over the 3-month Treasury bill, suggests that the largest increase in market rates is likely to occur in the bill market.

Barring a significant change in investor expectations regarding inflation or monetary policy, rising short-term rates this summer may have a less than usual impact on long-term rates. The spread between short- and long-term rates is quite wide and capital market credit demands--particularly public bond offerings--are likely to remain significantly below the first quarter pace as the refinancing of bank and other short-term borrowing by corporations of the past two years now appears to be over. In contrast to public corporate bond offerings, tax-exempt volume is expected to remain large, and some additional upward

rate pressure could develop in this market, particularly if bank funds are diverted by business loan demands, Treasury issues, or a reduced rate of deposit inflows.

As inventory and other working capital needs of businesses expand, business loan demands at banks should continue to be relatively strong this summer. Although bank inflows of time and savings deposits other than CD's are likely to slow from their recent pace as short-term market interest rates rise, banks have ample portfolio liquidity and access to negotiable CD's to meet these increased business loan demands and simultaneously to absorb some of the Treasury's new issues. However, as short-term rates rise, upward pressure on the prime rate is likely to develop.

With short-term market rates rising, inflows to nonbank thrift institutions this summer should also remain below the unusually rapid pace of earlier this year. Nevertheless, with mortgage credit demands expected to abate along with the anticipated reduction in housing starts, mortgage interest rates should be under only modest upward pressure in the immediate months ahead. Consequently, the Federal housing agencies are unlikely to be called upon for any substantial increase in market support operations this summer.

Monetary Aggregates. Growth in M_1 decelerated further in May to an annual rate of about 3.5 per cent. While M_1 growth has been moderating since early April, the slowdown in May appears to be largely associated with delayed processing of individual income tax payment checks by Internal Revenue. Had these checks cleared shortly after receipt instead of early May, private demand balances would have been

lower in late April and higher in early May. Over April-May combined, M_1 expanded at a 5.7 per cent rate, and for the first five months of the year grew at a 7.9 per cent rate.

MONETARY AGGREGATES
(Seasonally adjusted changes)

	1971		1972			
	QIII	QIV	QI	March	April	May p
	<u>Per cent at annual rates</u>					
M_1 (Currency plus private demand deposits)	3.7	1.1	9.3	11.9	8.2	3.6
M_2 (M_1 plus commercial bank time and savings deposits other than large CD.'s)	4.4	8.0	13.3	11.6	7.7	8.7
M_3 (M_2 plus savings deposits at mutual savings banks and S&L's)	7.8	9.6	15.5	13.8	11.1	10.2
Adjusted bank credit proxy	7.6	9.7	11.3	17.7	13.9	15.0
Time and savings deposits at commercial banks						
a. Total	8.2	15.9	14.8	7.8	12.4	17.8
b. Other than large CD.'s	5.3	14.7	17.1	10.8	7.8	13.1
	<u>Billions of dollars^{1/}</u>					
Memorandum:						
a. U.S. Government demand deposits	2.3	-.4	.1	2.4	1.3	--
b. Negotiable CD.'s	2.3	1.8	-.1	-.4	1.3	1.5
c. Nondeposit sources of funds	-.4	--	-.3	.1	-.2	.2

p Preliminary and partially estimated.

1/ Month-to-month and last-month-in-quarter to last-month-in-quarter changes in averages, not annualized.

Since the April tax date, inflows of consumer-type time deposits have been strong in almost all parts of the country, despite essentially unchanged differentials between yields on market instruments and bank offering rates. This rapid deposit growth follows a slowing in March and early April, when individuals needed funds to meet large income tax payments. Time and savings deposits other than CD's grew at a 13 per cent rate in May, bringing the month's expansion of M_2 to about an 8.5 per cent rate.

Net sales of large CD's also continued strong in May, with expansion broadly based at banks outside New York City, where business loans continued to show strength; in early June New York banks also increased their CD's significantly. Some of the CD growth--particularly the most recent expansion in New York--may reflect bank positioning for large expected CD run-offs around the June tax-date.

With moderation of growth in private demand balances more than offset by rapid expansion in total time and savings deposits, and with Treasury balances not declining from their high level, the adjusted credit proxy in May expanded at a rapid rate (15.0 per cent) for the third consecutive month. For the first five months of 1972, this measure of growth in total member bank funds has grown at a 12.7 per cent annual rate.

Bank Credit. Growth in bank credit, as measured by the last-Wednesday-of-month series, rebounded to over an 18 per cent rate in May, following a sharp drop in April. Since the April growth rate had been distorted by credit movements late in that month, the 11 per cent rate of growth for April and May combined is probably more indicative

of growth trends in this series. Increases were large in all categories of earning assets in May. Growth in security loans, not shown separately in the table, showed substantial growth as both dealer inventory positions and margin credit increased.

COMMERCIAL BANK CREDIT ADJUSTED FOR LOANS
SOLD TO AFFILIATES 1/
(Seasonally adjusted changes at annual percentage rates)

	1971		1972			
	QIII	QIV	QI	Apr.	May	Apr.-May
Total loans & investments ^{2/}	9.7	11.1	15.1	3.6	18.4	11.0
U.S. Treasury securities	-18.5	5.3	9.9	3.9	7.7	5.8
Other securities	12.0	20.1	16.1	-1.1	23.2	11.0
Total loans <u>2/</u>	14.7	9.4	15.7	5.0	18.8	12.0
Business loans <u>2/</u>	14.4	-3.4	9.6	12.0	10.9	11.5
Real estate loans	14.2	14.2	14.7	14.2	16.9	15.6
Consumer loans	13.3	13.6	11.7	8.5	10.6	9.6

1/ Last-Wednesday-of-month series.

2/ Includes outstanding amounts of loans reported as sold outright by banks to their own holding companies, affiliates, subsidiaries, and foreign branches.

Business loans continued the growth pattern that began early this year, with substantial expansion at banks outside of New York City and relative weakness at large New York City banks. The small increase in business loans at these latter institutions presumably reflects the previous high level of market financing and improved cash flows of large corporations, and their resultant high liquidity and reduced need to seek bank credit. Press reports and market analysts have suggested that the weakness in business loans at New York City banks also reflects substantial repayments by foreign and domestic borrowers of loans obtained last summer to speculate against the dollar. Staff

analysis of the industrial categories of loans thought to be associated with such speculation last year^{1/} fails to find confirmation of this hypothesis, although our data are not adequate for drawing firm conclusions. Repayments of such loans so far this year have held back net growth in all business loans--perhaps by 1.5 per cent (annual rate)--but reductions of loans in these categories were just as large outside as in New York City.

GROWTH IN BUSINESS LOANS ADJUSTED FOR LOANS
SOLD TO AFFILIATES ^{1/}
First Five Months of the Year, 1968-72
(Billions of dollars, not seasonally adjusted)

	1968	1969	1970	1971	1972
Large banks in New York City ^{2/}	-.9	.1	.2	-.9	-.9
Other large banks ^{2/}	<u>.5</u>	<u>2.7</u>	<u>-.4</u>	<u>-.2</u>	<u>1.3</u>
Total large banks ^{2/}	-.4	2.8	-.2	-1.1	.4
All other banks ^{3/}	<u>.7</u>	<u>1.3</u>	<u>.8</u>	<u>.8</u>	<u>1.3</u>
Total all banks	<u>.3</u>	<u>4.1</u>	<u>.6</u>	<u>-.3</u>	<u>1.7</u>

^{1/} Includes outstanding amounts of business loans reported as sold outright by banks to their own holding companies, affiliates, subsidiaries, and foreign branches.

^{2/} Weekly reporting banks.

^{3/} Estimated.

^{1/} Foreign commercial and industrial loans, bankers' acceptances, and loans to firms in wholesale trade.

Even with the weakness at New York City banks, aggregate business loans so far this year have shown significant growth, as shown in the table. Although a step-up in bank credit demands is to be expected with the expansion in economic activity and the moderation in capital market financing, the growth in total business loans appears to be somewhat larger than might be expected in the light of corporate financial positions and expenditures. This strength may be reflecting a more rapid growth in the book value of inventories than indicated by preliminary data. In addition, it could be associated with nonfinancial corporate hesitancy to use the commercial paper market after their 1970 experience; outstanding dealer placed commercial paper, after declining from 1970 to mid-1971, has been essentially unchanged for about a year.

Consumer credit. The April increase in consumer instalment credit outstanding amounted to nearly \$13.2 billion, seasonally adjusted annual rate. This advance followed a record \$16.4 billion rise in March. All types of credit showed substantial further growth in April, but the rate of expansion moderated for the three largest categories-- automobile, other consumer goods, and personal loans.

Extensions of instalment credit decreased slightly from March but remained well above any other previous month. Extensions of automobile credit increased for the fourth month in a row, but this rise was more than offset by decreases in non-automotive goods and personal loans. Repayments on outstanding debt edged up to a new high in April.

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
1971 - QI	2.7	.4	.6	1.7	.1
QII	6.7	2.3	1.8	2.3	.3
QIII	10.3	3.7	2.8	3.5	.3
QIV	12.4	4.5	4.0	3.5	.3
1972 QI	11.9	4.1	4.0	3.4	.4
April	13.2	5.1	3.5	3.9	.6

Nonbank financial institutions and mortgage markets. Savings inflows to nonbank thrift institutions slowed during May, according to estimates based on sample data, but an average of April and May probably provides a better measure of recent experience. This average shows a less pronounced moderation in inflows than suggested by the May figure alone.

Although commercial banks experienced an increase in deposit growth during May, there is little likelihood that this represented a shift of funds out of thrift institutions, since some loss in yield would accompany the transfer of funds to commercial banks.

The seasonally adjusted volume of outstanding commitments at the thrift institutions continued to rise in April. However, new commitment activity slowed somewhat from the extraordinarily high March pace. Reflecting a rise in commitments earlier in the year, total mortgage debt held by the major financial institutions and by FNMA and GNMA increased at a seasonally adjusted monthly rate of \$4.3 billion in April, 2 per cent more than in March. One measure of the

quality of residential mortgage debt held, the average delinquency rate, improved in the first quarter, according to the Mortgage Bankers Association.

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

	Mutual savings banks	Savings and loan associations	Both
1971 - QI	16.3	24.6	21.9
QII	15.0	18.4	17.3
QIII	9.6	15.7	13.7
QIV	10.6	13.8	12.8
1972 - QI	14.3	23.4	20.5
March*	15.8	20.5	19.0
April * p/	11.5	17.7	15.8
May* e/	9.0	10.5	10.0
April-May average e/	10.3	14.2	13.0

*/ Monthly patterns may not be significant because of difficulties with seasonal adjustment.

p/ Preliminary.

e/ Estimated on the basis of sample data.

Interest rates on home mortgage loans edged slightly higher in May. In the primary market for new conventional home loans, the average contract rate remained at 7.60 per cent, but the rate on existing home loans rose slightly to 7.70 per cent. In the secondary market for Government-underwritten loans, the average yield edged up 3 basis points to 7.53 per cent. More recent mortgage market indicators suggest an easing of upward pressure on mortgage rates. In the June 12 auction of FNMA forward commitments, the average yield was unchanged at 7.62 per cent and the amount sought was sharply lower.

AVERAGE RATES AND YIELDS ON NEW-HOME MORTGAGES

	Primary market: Conventional loans		Secondary market: FHA-insured loans		
	Level (per cent)	Spread (basis points)	Level (per cent)	Spread (basis points)	Discounts (points)
1971 - Low	7.55	-36	7.32	-36	2.5e
High	7.95	71	7.97	56e	7.8
Dec.	7.70	60	7.59	50	4.8
1972 - Jan.	7.60	53	7.49	42	4.0
Feb.	7.60	44	7.46	30	3.8
March	7.55	33	7.45	23	3.7
April	7.60	29	7.50	19	4.1
May	7.60	39	7.53	32	4.3

NOTE: FHA series: interest rates on conventional first mortgages (excluding additional initial fees and charges) are rounded by FHA to the nearest 5 basis points. On FHA loans carrying the 7 per cent ceiling rate in effect since mid-February 1971, a change of 1.0 points in discount is associated with a change of 12 to 14 basis points in yield. Gross yield spread is average mortgage return, before deducting servicing costs, minus average yield on new issues of high-grade corporate bonds with 5-year call protection.

Long-term securities. Long-term security yields fell about 15 to 20 basis points during the last three weeks of May, but this decline was almost completely offset by a turnaround in rates in early June. While underwriters, encouraged by apparent moderation in the forward public bond calendar, continued to price aggressively throughout May, investors became increasingly reluctant to acquire long-term bonds at those levels. Investor expectations apparently were adversely affected by increases in a number of short-term rates, particularly on Federal funds, and the rise in the May wholesale price index. A series of syndicate terminations in early June resulted in the return of corporate and municipal yield indexes to their early May levels.

SELECTED LONG-TERM INTEREST RATES
(Per cent)

	New Aaa corporate bonds 1/	Long-term State and local bonds	U.S. Gov't. (10-year constant maturity)
<u>1971</u>			
Low	6.76 (1/25)	4.97 (10/21)	5.42 (3/26)
High	8.23 (5/21)	6.23 (6/24)	6.89 (7/30)
<u>1972</u>			
Low	6.36 (1/14)	4.99 (1/14)	5.87 (1/14)
High	7.42 (4/4)	5.54 (4/4)	6.22 (4/21)
Week of:			
May 5	7.20	5.35	6.16
12	7.23	5.39	6.18
19	7.25	5.29	6.14
26	7.19	5.19	6.05
June 2	7.09	5.15	6.05
9	7.25	5.31	6.12

1/ With call protection (includes some issues with 10-year protection).

2/ Bond Buyer (mixed qualities).

p/ Preliminary.

Stock prices since the end of May have declined on balance, following appreciable increases in the last 3 weeks of May. Press reports indicate investors may have been concerned about the increased pressure for tax reform, the outcome of the Presidential primaries, and the sharp run-up in gold prices. Volume on all exchanges has remained moderate, with trading on the NYSE averaging 15.3 million shares daily during May and somewhat less most recently.

With industrial corporations virtually absent from the market, public bond offerings in May were about \$1.6 billion. The staff estimates that June public bond volume will be \$1.5 billion,

and the July total could be as low as \$1.2 billion. At least two large previously scheduled issues were placed privately in May, and negotiations for a number of such placements by other industrial corporations have been announced recently. Since no information on the takedown pattern of these private placements is available, the estimates of current and future private bond volume are subject to an unusual degree of uncertainty. Staff estimates indicate a continued high level of corporate stock and private bond issues in May and June, as shown in the accompanying table. Total corporate securities offerings are expected to show some seasonal decline in July.

SELECTED STOCK PRICE INDEXES
(Per cent change)

	D-J Industrials	NYSE	AMEX	NASDAQ
March 29 - April 12	+3.6	+3.6	+2.7	+4.4
April 12 - May 9	-4.3	-5.3	-5.1	-5.5
May 9 - June 12	+1.3	+2.1	+1.3	-3.7
June 1 - June 12	-2.5	-2.4	-1.4	-2.1

CORPORATE AND MUNICIPAL LONG-TERM SECURITY OFFERINGS
(Monthly or monthly averages, in millions of dollars)

	1971	First quarter	1972		
			May ^{e/}	June ^{f/}	July ^{f/}
Corporate securities - Total	3,758	3,268	3,300	3,500	2,600
Public bonds	2,065	1,787	1,600	1,500	1,200
Privately placed bonds	613	531	700	800	550
Stock	1,080	950	1,000	1,200	850
State and local gov't, securities	2,080	1,985	1,870	1,900	1,800

^{e/} Estimated.

^{f/} Forecast.

Yields on long-term municipal bonds, after declining almost 25 basis points during May, rose sharply in the second week of June and now stand at about the level prevailing just before the May 23 Committee meeting. Both commercial banks and casualty insurance companies continued to acquire tax-exempt bonds at a high rate during May. In recent days, however, yields on tax-exempts have risen in response to the same factors influencing other long-term markets.

The May volume of State and local long-term offerings was almost \$1.9 billion, with a number of revenue bonds brought to market, apparently in response to the rate declines in late May. The staff expects June volume to remain close to the May level, as several large pre-refunding offerings have been accelerated by the issuance of Treasury regulations about arbitrage bonds, which became effective in July. The impact of these rulings on future volume of pre-refunding issues is indeterminate at this time.

Short-term security markets. Most short-term rates have drifted up slightly since early June. However, over the inter-meeting interval they have generally increased by less than the 1/4 per cent rise in the Federal funds rate.

Rate advances averaging about 1/8 per cent in the commercial paper market have been accompanied by an increase of about \$700 million in the volume of non-bank related commercial paper in May on a seasonally adjusted basis. The entire increase occurred in directly placed paper. The overall increase for the January to May period now totals about \$450 million, \$400 million of which has been in directly-placed paper.

The bill rate, however, is now quoted around 3.84 per cent, about the same as at the time of the last meeting. Upward rate pressure in this market was moderated by the Treasury's decision (announced May 31) not to refund the maturing \$1.2 billion June 15 bond, which is expected to generate demand for bills, and indications that new cash will not be needed until well into July. Also, the supply of bills will be reduced by the runoff of June tax bills.

Desk activity in the open market for System Account has been unusually light since about mid-April. The last bill purchase on an outright basis in the market was on April 14. For some of the period since then the reserve effect of swings in the Treasury's balance at the Federal Reserve has lessened the need for Desk action. System activity in the form of market transactions was also reduced by direct bill purchases from foreign accounts; some of these accounts were selling bills and switching into coupon issues.

SELECTED SHORT TERM INTEREST RATES
(Per cent)

	1972			Basis point change May 24 - June 13
	May 24	June 7	June 13	
Federal funds	4.24 ^{1/}	4.48 ^{1/}	4.48 ^{2/}	24
Treasury bills				
3 month	3.84	3.88	3.84	--
6 month	4.21	4.26	4.23	2
1 year	4.51	4.61	4.59	8
Federal agency				
1 year	4.93	4.96	4.96	3
Commercial paper				
90-119 day	4.38	4.50	4.50 ^{3/}	12
60-89 day CD's	4.38	4.38	4.38 ^{3/}	--

^{1/} Weekly average.

^{2/} 6-day average.

^{3/} Latest available data are for June 7.

Federal finance. The mid-year Budget review, released June 5, projects unified budget deficits of \$26.0 billion in the current fiscal year and \$27.0 billion in fiscal year 1973. Compared to the January Budget, the mid-year review anticipates faster growth in receipts in fiscal 1972 and a slower increase in fiscal 1973, largely as a result of overwithholding this year and larger refunds next spring. However, the projected budget deficit will not significantly increase from fiscal 1972 to fiscal 1973, because of plans to reduce sharply the rate of growth of outlays from 10.2 per cent in fiscal 1972 to 7.3 per cent in fiscal 1973. An even sharper deceleration in spending growth had been estimated in the January Budget. The NIA translation of the unified budget, however, indicates a different pattern of expenditures. Applying the timing adjustments incorporated in the January Budget to the outlays shown in the mid-year review suggests that NIA expenditures may increase by about 11 per cent in fiscal 1973.

The Staff estimates of both receipts and outlays (unified budget basis) for fiscal 1973 are about \$2.0 billion higher than those shown in the mid-year review. The Staff projects higher outlays for defense (\$2.0 billion), social security benefits (\$3.0 billion) and interest (\$1.0 billion) but lower amounts for revenue sharing (-\$2.2 billion), unemployment compensation (-\$1.0 billion) and other grants (-\$0.8 billion). Our estimate of defense outlays reflects Secretary Laird's recent statement that accelerated activity in the

Vietnam war may require additional budget authority in fiscal 1973 with the amount depending on the duration of expanded military activity.

The Senate Finance Committee recently approved a 10 per cent social security benefit hike but many Senators are committed to a 20 per cent increase. This recommended social security boost is incorporated in the broad Social Security-Welfare bill which is now scheduled for extensive Senate debate beginning mid-July. While the eventual costs of this Senate Committee bill are very large, the effect on outlays is spread out over a considerable period, with the family welfare program scheduled for start as late as January 1974. As compared to staff projections for fiscal 1973, the major addition of the Senate measure would be a boost in Federal welfare benefits to the aged, blind and disabled that would become effective with passage of the bill. Under new matching formulas the Federal government would provide a larger share of this type of welfare cost and Federal spending would increase at an annual rate of \$4.4 billion while State outlays are estimated to decrease by \$2.4 billion. During the last half of calendar year 1973, there would also be additional costs for social security and medicare benefits totaling perhaps \$3.0 billion. In addition, Senate Committee provisions would yield \$3.0 billion more in payroll taxes, beginning in January 1973, than assumed in the Staff projection.

The Staff estimate assumes a 12.5 per cent social security benefit increase, rather than the 5 per cent shown in the Budget or the 10 per cent increase proposed by the Senate Committee.

The staff also assumes that the social security benefit hike and revenue sharing will be retroactive to July 1, 1972. The mid-year budget review assumes that revenue sharing will be retroactive to January 1, 1972. In the Staff projections retroactive payments are made in late September, but unless the social benefit hike is enacted within the next few weeks, further slippage of the retroactive social securities payments is likely.

On the receipts side, the staff assumes that the retroactive (to January 1972) increase in the social security wage base, which adds \$2.3 billion to the Administration estimate of fiscal 1973 receipts, will be postponed until January 1973. Our higher estimate of fiscal 1973 receipts is due mostly to higher income assumptions.

As shown in the table below, the high employment budget as measured by the staff, showed little change from the last half of calendar 1971 to the first half of calendar 1972. The shift toward deficit in the first half of 1972 that was anticipated in the January Budget did not develop because the scheduled tax cuts and stepped-up expenditures were largely offset by the unanticipated overwithholding.

STAFF ESTIMATE OF ACTUAL AND HIGH
EMPLOYMENT SURPLUS/DEFICIT (-)
(Billions of dollars, annual rates, NIA accounts)

<u>Calendar years</u>	<u>NIA deficit</u>	<u>High employment surplus/deficit</u>
1971 H-2	-26.2	4.0
1972 H-1 _e	-16.9	4.3
H-2 _e	-26.0	-8.3
1973 H-1 _e	-32.0	-17.5
H-2 _e	-13.3	1.0

e - estimated.

From the first to the second half of this calendar year, however, the high employment budget is expected to shift toward deficit by nearly \$13 billion. This shift reflects the rapid increase in expenditures--especially for Vietnam, social security and revenue sharing--and some reduction in overwithholding. To a large extent the further shift toward deficit in the first half of 1973 reflects the net reduction in receipts because of large refunds resulting from overwithholding. By the last half of 1973, however, our projections suggest a marked reduction in fiscal stimulus. Of course, this estimate rests on the assumption that Congress will not institute new expenditure programs beyond the measures discussed above.

It should be noted that traditionally the high employment budget has incorporated the full effect of temporary tax and expenditure changes.^{1/} However, the economic impact of such temporary measures is less certain than that of permanent tax or expenditure adjustments and, thus, the high employment budget may not accurately reflect the degree of fiscal stimulus. Similarly the revenue effect of the investment tax credit may be a poor indicator of the amount of stimulation provided by that measure.

¹ The Administration has not revised its estimate of high employment receipts (unified budget basis) as a result of overwithholding and, hence, the shift toward deficit in fiscal 1973, shown in the Staff projections, does not appear in the Administration high employment estimates.

The Treasury's cash balance at the end of this fiscal year is now expected to be about \$7.8 billion, about \$.6 billion higher than estimated in the May 17 Greenbook. The Staff continues to expect that the Treasury will need to raise large amounts of funds, perhaps \$18 billion, in the second half of this calendar year. In the near-term the Treasury has some flexibility because it still holds about \$1.5 billion of Treasury bills previously acquired from the German central bank in an exchange of special issues for marketable issues. These bills can be sold at the Treasury's discretion. Nevertheless, Treasury borrowing in July and August may total \$8-9 billion, with the first financing not expected until the second half of July.

PROJECTION OF TREASURY CASH OUTLOOK
(In billions of dollars)

	May	June	July	Aug.
Total net borrowing	- .4	-3.8	4.8	3.7
Weekly and monthly bills	- .2	- .4	--	--
Tax bills	--	-3.0	--	--
Coupon issues	- .7	-1.2	--	- .3
As yet unspecified new borrowing	--	--	4.0	4.0
Other (debt repayments, etc.)	.5	0.8	.8	--
Plus: <u>Other net financial sources</u> ^{a/}	1.8 ^{b/}	--	- .4	- .7
Plus: <u>Budget surplus or deficit (-)</u>	-3.4	1.9	-6.2	-3.2
Equals: <u>Change in cash balance</u>	-2.0 ^{c/}	-1.9	-1.8	- .2
Memoranda: Level of cash balance end of period	9.7 ^{c/}	7.8	6.0	5.8
Derivation of budget surplus or deficit:				
Budget receipts	16.5	24.8	14.8	18.5
Budget outlays	19.9	22.9	21.0	21.7
Maturing coupon issues held by public	2.4 ^{d/}	1.1	--	2.3
Net agency borrowing	.4	.6	.3	.4

^{a/} Checks issued less checks paid and other accrual items.

^{b/} Includes \$0.8 billion of capital gains from gold revaluation.

^{c/} Actual.

^{d/} The Treasury auctioned \$1.8 billion of notes and bonds in a partial refunding of the \$2.4 billion maturing. The remaining \$700 million was redeemed in cash.

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

	Fiscal 1972 e/		Fiscal 1973 e/		Calendar Year 1972 1/	Calendar Quarters					
	Mid-year F.R.		Mid-year F.R.			F. R. B. Staff Estimates					
	Review Board		Review Board			1972				1973	
						I*	II	III	IV	I	II
Federal Budget											
(Quarterly data, unadjusted)											
Surplus/deficit	-26.0	-24.5	-27.0	-26.5	-23.5	-10.5	4.5	-8.4	-9.1	-12.5	3.5
Receipts	207.0	207.0	223.0	225.5	222.6	48.1	65.8	57.2	51.5	50.9	66.
Outlays	233.0	231.5	250.0	252.0	246.2	58.6	61.4	65.6	60.6	63.4	62.5
Means of financing:											
Net borrowing from the public	n.a.	19.2	n.a.	25.3	15.6	3.9	-6.3	9.2	8.8	8.3	-1.0
Decrease in cash operating balance	n.a.	1.0	n.a.	.5	3.7	3.6	-.1	-.7	.9	2.2	-1.9
Other 2/	n.a.	4.3	n.a.	.7	4.3	3.0	2.0	-.1	-.6	2.0	-.6
Cash operating balance, end of period	n.a.	7.8	n.a.	7.3	7.6	7.7	7.8	8.5	7.6	5.4	7.3
Memo: Net agency borrowing ^{3/}	n.a.	5.2	n.a.	n.e.	n.e.	.4	1.5	1.1	n.e.	n.e.	n.e.
National Income Sector											
(Seasonally adjusted annual rate)											
Surplus/deficit	n.a.	-21.5	n.a.	-29.0	-21.4	-13.3	-20.1	-27.1	-24.9	-29.6	-34.4
Receipts	n.a.	211.7	n.a.	232.5	227.4	222.1	224.0	228.6	235.0	234.9	231.6
Expenditures	n.a.	233.2	n.a.	261.5	248.8	235.5	244.1	255.7	259.9	264.5	266.
High employment surplus/deficit (NIA basis) 1/	n.a.	4.1	n.a.	-12.8	-2.0	8.3	.3	-8.1	-8.7	-15.1	-19.4

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* Actual e--projected n.e.--not estimated n.a.--not available

1/ Estimated by F. R. Board Staff.

2/ Includes such items as deposit fund accounts and clearing accounts.

3/ Federally-sponsored credit agencies, i.e., Federal Home Loan Banks, Federal National Mortgage Assn., Federal Land Banks, Federal Intermediate Credit Banks, and Banks for Cooperatives.

INTERNATIONAL DEVELOPMENTS

6/14/72

III -- T - 1
 U.S. Balance of Payments
 In millions of dollars; seasonally adjusted

	1971	1972 ^{P/}			
	Year	Q1	Feb.*	Mar.*	Apr.*
<u>Goods and services, net</u> 1/	727	-1,147			
Trade balance 2/	-2,689	-1,673	-628	-655	-735
Exports 2/	42,770	11,809	3,793	3,835	3,711
Imports 2/	-45,459	-13,482	-4,421	-4,490	-4,446
Service balance	3,416				
<u>Remittances and pensions</u>	-1,529	-387			
<u>Govt. grants & capital, net</u>	-3,937	-802			
<u>U.S. private capital (- = outflow)</u>	-9,782	-2,879			
Direct investment abroad	-4,765	-994			
Foreign securities	-909	-388	-81	-46	42
Bank-reported claims -- liquid	-566	-518	-215	-174	318
" " " other	-2,372	-764	-296	-367	-184
Nonbank-reported claims -- liquid	-506	-175	-83	-137	
" " " other	-664	-40			
<u>Foreign capital (excl. reserve trans.)</u>	-5,037	1,280			
Direct investment in U.S.	-68	-335			
U.S. corporate stocks	849	679	153	273	80
New U.S. direct investment issues	1,161	309			
Other U.S. securities (excl. U.S. Govt.)	272	78			
Liquid liabilities to:	-6,691	528	183	-5	868
Commercial banks abroad	-6,908	438	202	58	929
Of which liab. to branches	(-4,942)	(-238)	(-425)	(331)	(437)
Other private foreigners	-465	61	42	-1	46
Intl. & regional institutions	682	29	-61	-62	-107
Other nonliquid liabilities	-560	21			
<u>Reserve liab. to foreign official institutions</u>	27,417	2,848	772	1,011	277
<u>U.S. monetary reserves (increase, -)</u>	3,065	607	549	60	-15
Gold stock	866	544	544	--	--
Special drawing rights 3/	468	--	--	--	7
IMF gold tranche	1,350	-1	5	-4	195
Convertible currencies	381	64	--	64	-217
<u>Errors and omissions</u>	-10,928	480			
<u>BALANCES (deficit -) 3/</u>					
Official settlements, S.A.		-3,455			
" " " " , N.S.A.	-30,482	-3,258	-1,321	-1,071	-262
Net liquidity, S.A.		-3,290			
" " " " , N.S.A.	-22,719	-3,075	-1,206	-755	
Liquidity, S.A. 4/		-3,983			
" " " " , N.S.A.	-23,791	-3,824	-1,504	-1,066	-1,130

* Monthly, 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/ Excludes allocations of SDRs as follows: \$717 million on 1/1/71 and \$710 million on 1/1/72.

4/ Measured by changes in U.S. monetary reserves, all liabilities to foreign official reserve agencies and liquid liabilities to commercial banks and other foreigners.

NOTE - First quarter data are preliminary and Strictly Confidential (F³).

INTERNATIONAL DEVELOPMENTS

Summary and outlook. The improvement in the U.S. balance of payments noted four weeks ago has been maintained since then. In the four weeks through June 7 there were surpluses on both the official settlements basis and the net liquidity basis, the former over \$400 million and the latter apparently at least as large.

The latest available merchandise trade data are for April. These show an even larger excess of imports that month than in February or March. Publication of the April trade results late in May may have been a factor in the recent weakening of exchange market quotations for the dollar. Nevertheless, in the first week of June, despite large repayments of liabilities by commercial banks to their branches and other banks abroad, foreign official reserves showed little increase in total over the week.

It appears virtually certain that some unwinding of last year's shift in leads and lags of commercial payments, along with other unidentified transactions as well as known short-term inflows, is helping to equilibrate international receipts and payments, which otherwise would be tending to produce large monthly deficits in the U.S. balance of payments. Possibly these equilibrating inflows have become much larger than earlier in the year.

In the first quarter of this year -- according to preliminary data to be published near the end of June -- there was a deficit on current and long-term capital accounts of \$3.3 billion and net outflows of recorded short-term capital amounting to \$0.7 billion. The over-all

deficit (before SDR allocation) was nevertheless no more than \$3.5 billion, as the errors and omissions account showed a positive balance (of \$0.5 billion) for the first time in several years.

The outlook as described four weeks ago included a gradual improvement in the current account extending on into 1973-74; and further net private capital inflows in coming months, so long as confidence in the viability of the Smithsonian realignment holds and interest rate relationships remain about as at present. No significant change in this description of the outlook is needed now, but the disappointingly poor April trade results lead us to change the estimate of net exports of goods and services in the current half year from about minus \$2-1/2 billion (annual rate) to about minus \$3 billion. The recent experience also casts some doubt on the considerable improvement expected later this year. The staff's present net export projection for the second half year is a small positive balance (less than \$1/2 billion, annual rate).

U.S. balance of payments. Preliminary data for April and May indicate a considerable improvement in the overall balance on the official settlements basis in these months. In April the balance was a small deficit of \$250 million; in May the balance shifted into a surplus on the order of \$500 million. These balances compare with a monthly average deficit of \$1.1 billion in the first quarter. Since the trade deficit increased further in April (described below) and foreign purchases of U.S. stocks in April fell from the very high

levels of the first quarter, it would appear that little of this improvement can be attributed to a decrease in the deficit on current account and long-term capital transactions, which amounted to about \$3-1/4 billion in the first quarter.

Some part of the improvement in April and May stemmed from inflows of short-term capital, which more than offset the continuing large deficit on current account and long-term capital transactions. U.S. banks reduced their claims on foreigners in April, though weekly data show no further reduction in May. Probably more important was the reversal of last year's unrecorded outflow. Preliminary confidential data for the first quarter accounts show net "errors and omissions" positive by \$500 million, compared with the exceptionally high negative quarterly average of \$2.7 billion in 1971. Such reflows may have risen in April and May as advance payments for imports were worked down and interest rates shifted in a favorable direction. If confidence in the new exchange rate structure is sustained, even larger positive "errors and omissions" in the months ahead should help to equilibrate the overall balance.

Another factor reducing the official settlements deficit in April was a sizable increase in liabilities to foreign branches of U.S. banks and in liabilities reported by U.S. agencies of foreign banks. There appears to have been a further inflow of short-term funds from foreign banks in May, but on a reduced scale. In the

first week of June, however, there was a reduction of nearly \$500 million in liabilities to foreign banks, of which about half was a reduction in liabilities to foreign branches at the end of a reserve computation period. Nevertheless, there was little change in that week in aggregate liabilities to foreign official accounts.

Other data available on first quarter transactions indicate that the outflow of U.S. capital for direct investment abroad was about \$1 billion, still substantial but less than the \$1-1/4 billion outflow recorded in each of the first and second quarters of 1971. There was also a large outflow of funds -- about \$300 million -- from foreign direct investors in the United States, principally by Japanese trading companies. These companies were also responsible for large outflows of funds last year -- probably in order to pay in advance for imports when the yen was expected to be revalued. These outflows should be reversed in the course of the year.

U.S. foreign trade. The U.S. trade deficit in April increased further over the very high deficits of the preceding two months. Imports in April dipped only slightly from the very strong level in March while exports fell more sharply, principally because of much lower deliveries of commercial aircraft.

Prices of both exports and imports -- as measured by unit values -- rose at about equal rates in April so that the effect of prices on the trade balance was not significant. The rise in the

April import unit-value index was less than the rise in either February and March, and was mainly in prices of foodstuffs and semi-finished materials; prices of imports of finished manufactures were unchanged. In February and March, finished manufactures did account for most of the overall increase in import unit values, but the March-April level of the index for this group was up only 6 percent from a year earlier. This was less of a rise than in each of the preceding two 12-month periods.

For the four months January-April the trade deficit was at an annual rate of about \$7 billion (balance of payments basis) compared with a \$4-1/2 billion rate in the last half of 1971. Imports in the first four months averaged about 16 percent higher than in the second half of 1971; exports were about 11 percent higher. The levels of both exports and imports in the first four months were inflated, to some degree, by a catchup in shipments delayed by dock strikes.

Although trade movements in the first four months of this year were distorted by the effects of dock strikes, it appears that much of the current strength in exports is in shipments to Canada (affected only slightly by the strikes), particularly in machinery and automotive equipment. Exports to Western Europe in January-April were little changed from those of a year ago while increased deliveries of aircraft accounted for most of the rise in exports to Japan.

The rise in imports this year has been widespread, covering all major product categories. The sharp expansion in domestic

automobile sales has resulted in increasing entries of cars from Canada. While sales of foreign cars (other than those from Canada) in the United States in the first five months have slipped below year-earlier levels, imports have risen, resulting in larger inventories. Though some of the inventory increase probably stems from the introduction of new models, part of the increase probably was involuntary. Deliveries of light trucks, made in Japan for Ford and General Motors, also boosted imports of automotive equipment this year. Imports of other consumer goods, as well as capital equipment (office machines, textile machinery) also are up sharply this year. While imports of textiles continued their long-term uptrend in the first three months of this year, there was a sharp drop in arrivals in April, probably reflecting the first effects of the "voluntary" textile agreement reached at the beginning of the year. Much of the increase in imports of industrial materials this year has been in petroleum and lumber.

Merchandise imports in the first four months were much greater than can be readily explained by the economic variables normally used in forecasting equations. Possibly such temporary factors as heavy bunching of deliveries of goods ordered and paid for last year may help to explain this development.

Foreign exchange markets. Over the past month, the dollar weakened against most major currencies, and, as of June 14, is

generally at its lowest levels since early March. The release of U.S. trade figures for April -- showing a further increase in the trade deficit -- combined with the Commerce Department's forecast that the 1972 trade deficit would exceed last year's and press reports of statements by Under Secretary Volcker which seemed not to rule out further devaluations of the dollar, all tended to weaken confidence and depress exchange rates for the dollar.

Exchange rates for the Canadian dollar and the French franc have been particularly firm in recent weeks, reflecting tight money market conditions in Canada and France, as well as the general weakness of the dollar. The Canadian dollar reached a high of \$1.0263 on June 9, nearly 2 percent higher than a month ago. During that one-month period the Bank of Canada purchased \$260 million. On June 12, the Canadian dollar backed off as Canadian banks, under pressure from the government, lowered their rates paid on large term deposits to 5-1/2 percent from as high as 6-1/4 percent, and the Bank of Canada sold \$35 million, moderating the decline in the Canadian dollar's exchange rate. Subsequently, however, the rate rebounded and the Bank of Canada again purchased U.S. dollars in the market.

The French franc has been at or close to its ceiling for the past three weeks, and Bank of France intervention purchases have amounted to \$140 million. On June 2, the Bank of France,

concerned about excessive domestic monetary expansion, announced an increase in marginal reserve requirements on certain commercial bank assets.

In contrast to other European currencies, sterling has eased against the dollar in the past month, mainly in response to an actual and prospective further reduction in the U.K. trade and current account balances. As of June 14, sterling was near its (EEC) lower limit against the French franc.

The Japanese yen has remained fairly steady over the past several weeks, about mid-way between its central rate and its upper limit. Japan's continuing large current account surplus is apparently being offset by capital outflows, including repayment of loans from foreign banks, encouraged by official Japanese dollar deposits with Japanese commercial banks. (These deposit transactions initially show up as decreases in Japanese official reserves and as a reduction in the U.S. official settlements deficit.)

In the six-week period since May 3, reserves of 9 major foreign countries have declined by about \$200 million, with Japanese reserve decreases of \$500 million more than offsetting Canadian and French reserve gains, mentioned above. Swiss reserves fell by over \$80 million, with most of this decline accounted for by System swap repayments from the proceeds of Swiss franc purchases in the exchange markets.

The gold market continued to experience large fluctuations in price in recent weeks as speculative demand alternately waxed and waned. A peak of \$66.75 was reached in London on June 8. By June 12, the price had fallen as low as \$59.00, but subsequently has come back to around \$61.00. For the most part, speculation in gold seemed unrelated to any expectation of an increase in the official monetary price of gold, but rather to views about the scarcity of gold as a commodity, in the face of rising industrial and commercial demands and dwindling South African supplies.

In official transactions, the System repaid \$300 million equivalent of Swiss franc and \$20 million equivalent of Belgian franc swap drawings. All of the Belgian francs and \$250 million equivalent of Swiss francs were purchased directly from the respective central banks of issue, while the balance of the Swiss franc payment was made from proceeds of market purchases of that currency. Outstanding System swap obligations now amount to a little over \$2-1/2 billion, down by \$1/2 billion from August 1971.

Euro-dollar market. Near the end of May interest rates for Euro-dollar deposits of one-month and shorter maturities began to rise moderately and have continued to move up through the first half of June. Rates on three-month and longer deposits have not changed substantially since early May.

The recent advances in the shorter-term Euro-dollar rates have somewhat outpaced increases in U.S. interest rates of comparable

maturity over the same period. For example, the overnight Euro-dollar rate, which has been about 4-1/4 percent in recent days (compared to about 3-5/8 percent in mid-May), is presently only about 1/4 percent below the Federal funds rate (versus about 5/8 percent before both rates began to rise toward the end of last month). The table below presents additional details and makes rate differential comparisons after adjustment of Euro-dollar rates to reflect the additional cost to U.S. banks of maintaining borrowings in excess of their reserve-free bases.

SELECTED EURO-DOLLAR AND U.S. MONEY MARKET RATES

Average for month or week ending Wednesday	(1) Over-night Euro-\$ ^{1/}	(2) Federal Funds ^{2/}	(3) Differential (1)-(2) (*)	(4) 1-month Euro-\$ Deposit ^{1/}	(5) 30-59 day CD rate (Adj.) ^{3/}	(6) Differential (4)-(5) (*)
1972 - Jan.	4.58	3.50	1.08 (2.23)	5.02	3.81	1.21 (2.47)
Feb.	4.02	3.29	0.73 (1.74)	4.46	3.43	1.03 (2.15)
Mar.	3.87	3.83	0.04 (1.01)	5.05	3.80	1.25 (2.51)
Apr.	3.92	4.17	-0.25 (0.73)	4.72	4.44	0.28 (1.46)
May	3.79	4.27	-0.48 (0.47)	4.25	4.21	0.04 (1.10)
May 24	3.64	4.24	-0.60 (0.31)	4.14	4.21	-0.07 (0.97)
31	3.81	4.38	-0.57 (0.57)	4.38	4.21	0.17 (1.27)
June 7	4.06	4.48	-0.42 (0.60)	4.52	4.34	0.18 (1.31)
14 ^{p/}	4.15	4.47	-0.32 (0.72)	4.60	4.34	0.26 (1.41)

^{1/} All Euro-dollar rates are noon bid rates in the London market; overnight rate adjusted for technical factors to reflect the effective cost of funds to U.S. banks.

^{2/} Effective rate.

^{3/} Offer rates (median, as of Wednesday) on large denomination CD's by prime banks in New York City; CD rates adjusted for the cost of required reserves.

^{*} Differentials in parentheses are after adjustment of Euro-dollar rates for the 20 percent marginal reserve requirement (relevant to banks with borrowings in excess of their reserve-free bases).

^{p/} Preliminary.

The greater rise in very short Euro-dollar rates relative to U.S. rates may reflect the firmer tone in foreign national money markets that normally tends to develop as the end of the second quarter approaches. In addition, French and Canadian money markets have been tight in recent weeks, independently of seasonal influences. (See discussion beginning on page III - 12). Over the coming quarter-end, Swiss banks are expected to repatriate perhaps as much as \$3/4 billion for balance sheet window dressing. But these temporary reflows will be accommodated by BNS swaps with the banks (under which the BNS will place the dollar proceeds of the swaps in the Euro-dollar market); thus, these repatriations should have little net impact on the Euro-dollar market or the U.S. balance of payments.

U.S. banks' Euro-dollar positions subject to Regulations M and D totaled about \$2.2 billion in the four-week computation period ended May 10, essentially unchanged from the two previous computation periods. U.S. banks raised their Euro-dollar borrowings early in the computation period ended June 7 but reduced these borrowings in the last week of May and the first week of June to avoid incurring required reserves; partial data indicate little change in these borrowings on average in the four-week period ended June 7.

Financial developments in selected industrial countries.

Except in Japan and Italy, it seems that the decline in short-term interest rates abroad has about run its course; indeed, given the outlook for faster expansion in several major countries, an upward movement seems likely. Long-term rates have been rising in recent months in Germany, the United Kingdom, Canada, the Netherlands, and Switzerland.

It seems fairly clear that the active use of monetary policy to stimulate economic recovery, together with the influence of declining rates in the United States, were important factors in bringing down short-term rates abroad. But the continuation of unacceptably high rates of inflation has presumably been a factor in the earlier turn-around of long-term rates.

The following paragraphs set forth the staff view regarding the trend of interest rates in principal countries in the near future, in the light of the prevailing conjunctural situation.

Interest rates in Germany are likely to begin to rise in response to cyclical pressure, even if monetary policy is not overtly tightened. German interest rates have come down considerably further since the Smithsonian meeting and are now back to early 1969 levels. The downward movement of long-term rates began to be reversed in March. A rising budget deficit and stronger economic activity combine to augur for a continuation of the upward movement of recent weeks.

The underlying economic situation has improved a great deal in recent months. Activity, as reflected by industrial output and labor market statistics, has picked up. Order inflows and upward revisions of investment intentions indicate that the recovery is spreading.

The liquidity position of the private sector in Germany is no longer being augmented by large inflows of funds from abroad, and the Bundesbank, in an effort to slow what the authorities think may be too fast a recovery in view of the inflation problem, has moved to neutralize the liquidity effect of the DM 6 billion tax repayments that the government is making from accounts that had been frozen at the Bundesbank. Effective with the repayment, rediscount quotas are being reduced and reserve requirements raised. The announcement of these measures has already produced a stiffening of rates for 30 and 90 day credit, while intermediate rates have moved up even more sharply, indicating that the market anticipates a further tightening of monetary conditions.

Short-term rates have been tending to rise in the United Kingdom since January, though they fell back in March and early April before turning up again. Long-term rates have been rising since March and particularly strongly since early May. Factors that will continue to exert upward pressure on interest rates are the huge public sector borrowing requirement in fiscal year 1972-73 and the current and

forecast upswing in economic activity. The London clearing banks raised their base rates (to which deposit and lending rates are tied) from 4-1/2 to 5% on June 9. The base rate rise reflects the strong demand for loans at a time when the growth of deposits is slowing and the banks' reserve ratios are approaching the new minimum level of 12-1/2 per cent.

Expectations of inflation have clearly been an important factor in keeping long-term interest rates relatively high in the United Kingdom. Indeed, the recent rise in long-term rates might be attributed very largely to price expectations that have been revised upward (a) because of the outlook for wage increases in the wake of the miners' strike, and (b) by the rapid rate of growth of the money supply since the end of 1971 -- 20 per cent at an annual rate, which is lower than in the fourth quarter of 1971 but higher than in the first quarter of last year.

Canadian interest rates have been rising since the beginning of the year and both short- and long-term interest rates will probably continue to rise as the economy proceeds along the upswing of the business cycle. At the same time, the monetary aggregates have been increasing rapidly and the new budget is on balance expansionary. Canadian GNP is projected to grow at 6-6-1/2% in real terms in 1972; the annual rate reached 6.2% in the second half of 1971. Although there is concern about inflationary pressures in Canada, the reduction

of the unemployment rate, which remains unacceptably high, is a major goal of government policy. For this reason, and in order to mitigate upward pressure on the exchange rate, Canadian monetary policy is expected to remain basically accommodating, as exemplified by official pressure on banks that resulted in the lowering of their borrowing rates for large time deposits by as much as one percentage point on June 12.

The already low level of interest rates in France and the prospect of some pick-up in economic activity make a further reduction in French short-term interest rates unlikely.

The French government has recently revised upward its economic forecasts. Real GDP is now expected to grow at a somewhat faster rate in 1972 than in 1971. But the rate of inflation is also expected to be somewhat higher this year than last. The recent increase in the marginal reserve requirements on banks' assets (reserves against assets were first introduced in France in April 1971) was interpreted at the time as a sign of official concern about the implication for prices of the recent rapid rate of monetary expansion; M₂ increased about 20 per cent at an annual rate, seasonally adjusted, in the first quarter of this year.

Short-term interest rates in Switzerland have also risen somewhat following moves by the Swiss National Bank to reduce the banks' liquidity through the imposition of a marginal reserve

requirement on their domestic liabilities and a more restrictive interpretation of the 100 per cent marginal reserve requirement on net foreign liabilities. The main preoccupation of the Swiss authorities is still inflation. Reports of a new acceleration in the rate of rise in aggregate demand in early 1972 have increased their anxiety in this matter.

Interest rates in Japan have generally been declining since November 1970 and are likely to continue to do so in the near future. Such a movement would be appropriate for both domestic and international reasons. Reductions in bank loan and deposit rates have been proposed as part of Japan's seven point yen "defense" program approved by the cabinet on May 23.

Japan's long-awaited economic upswing has apparently begun, though so far only at a relatively modest pace. Industrial production has generally been increasing since last November. Producers' shipments have been rising and inventories of finished goods have been declining. New orders for machinery, however, remain weak.

A higher level of interest rates in Italy is not likely in the foreseeable future. The late-1971 revival in economic activity seems to have halted. Industrial production, which had recovered briskly from August 1971 to January 1972, declined sharply in February and apparently changed little in March. The substantial volume of unutilized plant capacity, together with political uncertainties,

continue to have a depressing effect on investment demand. Although business surveys show industrialists becoming less pessimistic in recent weeks, Governor Carli has recently presented a quite gloomy picture of the economic outlook and the Bank of Italy seems unlikely to act to raise interest rates or to allow market forces to raise them.