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May 15, 1985

RECENT DEVELOPMENTS

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

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SELECTED DOMESTIC NONFINANCIAL DATA
(Seasonally adjusted)

	Latest data			Percent change from		
	Period	Release date	Data	Preceding period	Three periods earlier	Year earlier
				(At annual rates)		
Civilian labor force	Apr.	05-03-85	115.4	-1.5	1.7	1.9
Unemployment rate (%)[1]	Apr.	05-03-85	7.3	7.3	7.4	7.8
Insured unemployment rate (%)[1]	Jan.	04-11-85	2.9	2.8	2.8	3.1
Nonfarm employment, payroll (mil.)	Apr.	05-03-85	96.7	2.7	2.9	3.5
Manufacturing	Apr.	05-03-85	19.7	-2.7	-2.7	.7
Nonmanufacturing	Apr.	05-03-85	77.1	4.1	4.3	4.2
Private nonfarm:						
Average weekly hours (hr.)[1]	Apr.	05-03-85	35.1	35.2	35.2	35.4
Hourly earnings ($)[1]	Apr.	05-03-85	8.57	8.53	8.45	8.31
Manufacturing:						
Average weekly hours (hr.)[1]	Apr.	05-03-85	40.3	40.4	40.6	41.1
Unit labor cost (1967=100)	Mar.	04-30-85	88.6	-4.0	-4.0	-3.3
Industrial production (1967=100)	Apr.	05-15-85	165.4	-2.9	.7	2.0
Consumer goods	Apr.	05-15-85	161.9	-4.4	-.5	.3
Business equipment	Apr.	05-15-85	187.5	-3.8	-3.6	8.1
Defense & space equipment	Apr.	05-15-85	148.8	8.1	8.2	11.7
Materials	Apr.	05-15-85	161.1	-5.2	1.5	-.2
Consumer prices all items (1967=100)	Mar.	04-23-85	319.2	5.7	4.1	3.7
All items, excluding food & energy	Mar.	04-23-85	311.1	4.6	5.3	4.7
Food	Mar.	04-23-85	309.2	-.4	2.6	2.4
Producer prices: (1967=100)						
Finished goods	Apr.	05-10-85	293.6	3.7	1.6	.7
Intermediate materials, nonfood	Apr.	05-10-85	325.4	4.1	-1.1	.2
Crude foodstuffs & feedstuffs	Apr.	05-10-85	236.1	-36.5	-30.4	-10.8
Personal income ($ bil.)[2]	Mar.	04-17-85	3,155.9	6.1	5.7	7.3
				(Not at annual rates)		
Mfgrs. new orders dur. goods ($ bil.)	Mar.	04-30-85	99.7	-3.0	-1.5	-4.5
Capital goods industries	Mar.	04-30-85	33.5	-3.0	-2.3	-12.8
Nondefense	Mar.	04-30-85	27.3	-7.4	1.6	2.1
Defense	Mar.	04-30-85	6.2	22.2	-16.5	-46.9
Inventories to sales ratio:[1]						
Manufacturing and trade, total	Mar.	05-15-85	1.38	1.38	1.36	1.33
Manufacturing	Mar.	04-30-85	1.48	1.49	1.46	1.43
Trade	Mar.	05-15-85	1.29	1.29	1.28	1.25
Ratio: Mfgrs.' durable goods inventories to unfilled orders[1]	Mar.	04-30-85	.555	.549	.553	.522
Retail sales, total ($ bil.)	Apr.	05-14-85	112.2	.9	1.1	4.5
GAF[3]	Apr.	05-14-85	24.9	.6	4.1	7.2
Auto sales, total (mil. units.)[2]	Apr.	05-03-85	11.0	5.4	-1.9	6.2
Domestic models	Apr.	05-03-85	8.6	5.1	1.2	5.4
Foreign models	Apr.	05-03-85	2.3	6.4	-11.6	9.6
Capital Appropriations, Mfg.	1984-Q4	03-11-85	28,984	5.0	—	19.5
Housing starts, private (thous.)[2]	Mar.	04-16-85	1,895	16.2	16.3	11.5
Leading indicators (1967=100)	Mar.	04-30-85	167.1	-.2	1.6	-.1

1. Actual data used in lieu of percent changes for earlier periods.
2. At annual rates.
3. Excludes mail order houses.

Economic activity slowed substantially in recent months from last year's pace. Although domestic spending has been well maintained, much of the rise in demand has been met by increased imports rather than through an expansion of domestic production. Consumer spending, on balance, remained firm through April, and housing activity has shown greater strength recently. However, growth in business fixed investment decelerated sharply in the first quarter, as sluggish spending on new equipment offset some of the continued strength in nonresidential construction. Price inflation has picked up slightly in recent months, in part reflecting temporary pressures in petroleum markets, while wage adjustments have remained moderate on balance.

Employment and Unemployment

Nonfarm payroll employment increased about 215,000 in April, less than the average monthly gain of 285,000 for the previous two quarters. Although the service-producing sector registered less employment growth in April than earlier this year, substantial gains were reported in business and health services, wholesale trade, and finance. Construction hiring was brisk in March and April, reflecting the recent pickup in residential construction and the persistent strength in commercial building. Manufacturing employment, however, fell 45,000 in April, bringing the cumulative job loss since January to 130,000. Most of the recent job declines have occurred in the durable goods industries, with notable cutbacks in electrical equipment and machinery.

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

			1984		1985	1985		
	1983	1984	Q3	Q4	Q1	Feb.	Mar.	Apr.
	-Average monthly changes-							
Nonfarm payroll employment[2]	282	305	224	291	278	116	353	217
Strike adjusted	282	307	216	304	272	114	381	187
Goods-producing	110	88	12	83	23	-103	91	35
Manufacturing	92	55	-4	62	-27	-66	-22	-44
Durable	70	47	15	46	-19	-47	-19	-40
Nondurable	22	8	-19	16	-8	-19	-3	-4
Construction	22	31	10	28	50	-38	114	70
Private service-producing	169	200	140	224	242	205	247	189
Trade	69	87	61	112	87	54	101	47
Finance and services	96	97	63	100	153	136	172	125
Total government	3	16	72	-15	13	14	15	-7
Total employment[3]	331	270	1	293	282	294	434	-174
Nonagricultural	338	266	17	271	290	274	412	-240

1. Average change from final month of preceding period to final month of period indicated.
2. Survey of establishments. Strike-adjusted data noted.
3. Survey of households.

SELECTED UNEMPLOYMENT RATES
(Percent; based on seasonally adjusted data)

			1984		1985	1985		
	1983	1984	Q3	Q4	Q1	Feb.	Mar.	Apr.
Civilian, 16 years and older	9.6	7.5	7.4	7.2	7.3	7.3	7.3	7.3
Teenagers	22.4	18.9	18.6	18.4	18.5	18.4	18.2	17.7
20-24 years old	14.5	11.4	11.4	10.9	11.1	11.2	11.1	11.0
Men, 25 years and older	7.8	5.7	5.5	5.4	5.4	5.4	5.3	5.5
Women, 25 years and older	7.2	6.0	6.0	5.8	6.0	5.9	6.0	6.0
White	8.4	6.5	6.4	6.2	6.3	6.2	6.2	6.3
Black	19.5	15.9	15.8	15.1	15.5	16.3	15.2	15.3
Fulltime workers	9.5	7.2	7.1	7.0	7.0	7.1	6.9	6.9
Memo:								
Total national[1]	9.5	7.4	7.3	7.1	7.2	7.2	7.2	7.2

1. Includes resident Armed Forces as employed.

The civilian unemployment rate held steady at 7.3 percent in April, essentially unchanged since last fall. During the same period, there has been little movement in the unemployment rates for individual categories of civilian workers.

Industrial Production and Capacity Utilization

The index of industrial production declined 0.2 percent in April and, on balance, has been flat since last summer. With the exception of defense and space equipment, most major market sectors shared in the April decline. Auto assemblies were reduced a bit in April to 8.1 million units at an annual rate, and the output of other consumer goods also edged down. Production of business equipment dropped for the fourth consecutive month. Reflecting these widespread declines in output, the capacity utilization rate in total industry dropped 1/2 percentage point in April to about 80-1/2 percent, the lowest level since January 1984.

Personal Income and Consumption

Real personal income continued to rise in the first quarter, although less rapidly than in the second half of last year. Growth in private wages and salaries accounted for most of the first-quarter advance, mainly reflecting higher payrolls in the service-producing sector. However, personal taxes climbed sharply in the first quarter, largely because of delays in processing federal tax refunds. As a result, real disposable income is estimated to have fallen 2 percent at an annual rate. If the processing of refunds had not been delayed, real disposable income would have risen about 2 percent, at an annual rate, compared with an almost 4 percent pace in the second half of last year.

INDUSTRIAL PRODUCTION
(Percentage change from preceding period; based on seasonally adjusted data)

	1984 Q4	1985 Q1	1985 Feb.	Mar.	Apr.
	----Annual rate----		--Monthly rate--		
Total	-2.3	1.8	.1	.3	-.2
Final products	2.6	1.7	-.2	.3	-.2
Consumer goods	-1.2	.2	-.1	.3	-.4
Durable	-3.8	5.2	1.2	1.3	-1.0
Nondurable	-.2	-1.7	-.6	-.1	-.1
Business equipment	4.2	.3	-.4	-.2	-.3
Defense and space equipment	16.2	11.2	.1	1.3	.7
Construction supplies	-6.4	-.5	.4	.2	.1
Materials	-7.7	2.5	.5	.3	-.4
Durable goods	-6.0	-.6	.1	.2	-.7
Nondurable goods	-8.9	-.8	.1	.6	.0
Energy materials	-10.6	18.8	1.9	.4	-.5

CAPACITY UTILIZATION IN INDUSTRY
(Percent of capacity, seasonally adjusted)

	1978-80 High	1982 Low	1967-82 Avg.	1985 Feb.	Mar.	Apr.
Total industry	87.3	69.6	82.4	81.0	81.1	80.6
Manufacturing	87.5	68.8	81.8	80.9	81.0	80.5
Durable	89.4	64.8	80.5	81.7	81.9	81.4
Nondurable	87.2	73.8	83.9	80.0	79.8	79.5
Mining	90.4	69.6	86.5	74.9	75.7	74.5
Utilities[1]	86.8	79.0	88.6	85.6	85.2	85.2
Industrial materials	88.9	66.6	83.3	80.8	80.8	80.2
Metal materials	95.4	46.2	82.2	67.7	68.8	68.4
Paper materials	97.9	86.3	93.4	96.4	95.9	n.a.
Chemical materials	91.3	64.0	85.1	74.7	75.0	n.a.

1. The 1978-80 high is below the 1967-82 average because of the unusually slow growth in demand for electricity.

PERSONAL INCOME AND EXPENDITURES
(Based on seasonally adjusted data)

	1983	1984	1984 Q3	1984 Q4	1985 Q1	1985 Jan.	1985 Feb.	1985 Mar.
	- - Percentage changes at annual rates[1] - -							
Total Personal Income								
Nominal	7.5	9.2	8.7	6.6	6.0	6.6	4.2	6.1
Real[2]	4.3	5.8	4.2	4.1	2.9	-.9	1.5	3.6[e]
Disposable Personal Income								
Nominal	8.5	8.9	8.4	6.0	1.2	7.5	-9.6	-5.9
Real	5.3	5.6	3.9	3.5	-1.8	.3	-12.5	-8.9[e]
Expenditures								
Nominal	9.0	7.5	5.0	6.1	8.0	8.3	11.0	-6.4
Real	5.8	4.2	.7	3.6	4.7	1.0	8.2	-9.7[e]
	- - Changes in billions of dollars[3] - -							
Total personal income	17.0	21.0	20.6	14.5	14.7	17.2	11.0	16.0
Wages and salaries	11.1	11.4	8.3	11.9	10.0	7.6	8.0	14.4
Private	9.5	9.6	6.5	10.5	7.1	2.8	5.6	12.8
Manufacturing	3.3	2.6	1.2	3.3	.6	1.6	-2.0	2.2
Other income	6.8	10.6	12.9	3.3	8.4	19.0	3.5	2.6
Disposable personal income	16.3	17.2	18.2	9.9	-5.9	16.6	-21.4	-13.0
Expenditures	15.7	14.1	11.9	10.6	8.7	16.8	22.3	-13.1
Durables	3.9	2.4	-2.9	6.1	-2.3	-4.7	6.2	-8.3
Nondurables	3.9	4.3	4.0	.2	1.4	3.0	7.1	-5.9
Services	7.9	7.5	10.9	4.4	9.6	18.5	9.1	1.1
Personal saving rate (percent)	5.0	6.1	6.3	6.2	4.6	5.7	4.0	4.0

1. Changes over periods longer than one quarter are measured from final quarter of preceding period to final quarter of period indicated. Changes for quarterly periods are compounded rates of change; monthly changes are not compounded.
2. Total personal income is deflated by the personal consumption expenditure deflator.
3. Average monthly changes are from the final month of the preceding period to the final month of period indicated; monthly figures are changes from the preceding month.
e--FRB estimate.

RETAIL SALES
(Percent change from previous period;
based on seasonally adjusted data)

	1984 Q3	1984 Q4	1985 Q1	1985 Feb.	1985 Mar.	1985 Apr.
Total sales	-.4	2.0	1.4	1.0	-.7	.9
(Real)[1]	-.8	1.5	.9	.8	-.9	n.a.
Total, less automotive, gasoline and nonconsumer stores	.8	1.4	1.0	1.6	-1.0	.7
GAF[2]	.3	3.2	.8	4.1	-.6	.6
Durable	-1.3	4.1	2.3	1.1	-1.2	.6
Automotive group[3]	-3.0	4.2	4.3	1.3	-2.3	1.6
Furniture & appliances	2.3	5.2	1.2	2.9	-.4	-1.2
Nondurable	.2	.8	.9	1.0	-.5	1.0
Apparel	-1.6	2.9	.7	5.5	1.9	.4
Food	1.1	.2	1.2	.0	-.5	1.3
General merchandise[4]	.4	2.5	.7	4.1	-1.7	1.5
Gasoline stations	-3.4	1.1	-.9	-2.9	3.1	1.8

1. BCD series 59. Data are available approximately three weeks following the retail sales release.
2. General merchandise, apparel, furniture and appliance stores.
3. Sales of the automotive group frequently differ from sales of new cars on a unit basis because of broader coverage (for example, parts, used cars, and servicing), seasonal factors, and sampling.
4. General merchandise excludes mail-order nonstores.

AUTO SALES, PRODUCTION & INVENTORIES
(Millions of units; seasonally adjusted annual rates)

	1984 Q3	1984 Q4	1985 Q1	1985 Feb.	1985 Mar.	1985 Apr.	1985 May
Total sales[1]	10.3	10.3	10.9	11.0	10.4	11.0	—
Imports	2.4	2.8	2.4	2.4	2.2	2.3	—
Domestic	7.9	7.5	8.5	8.6	8.2	8.6	8.0[2]
Domestic production	7.5	7.7	8.4	8.2	8.3	8.1	—
Domestic inventories	1.32	1.44	1.49	1.52	1.49	1.53	—
Days' supply[3]	52	58	55	54	56	54	—

1. Components may not add to totals due to rounding.
2. First ten days.
3. Quarterly days' supply are based on end of quarter stocks and average sales for the quarter.

Consumer spending, which had sagged in March, rebounded in April. Sales of domestic cars since the beginning of April have been running at an 8-1/2 million unit annual rate, similar to the strong pace posted in the first quarter. Analysts attribute part of the recent strength to below-market financing provided by the major manufacturers for their smaller cars. Sales of imported cars since February have averaged 2.3 million units, owing to limited supplies of Japanese models.

Excluding outlays for autos, gasoline, and nonconsumer items, nominal retail sales advanced 0.7 percent in April to a level 1/2 percent above the first-quarter average. The rise in sales was widespread, with notable increases in purchases of general merchandise and food. In contrast, spending on furniture and appliances declined in April.

Business Fixed Investment

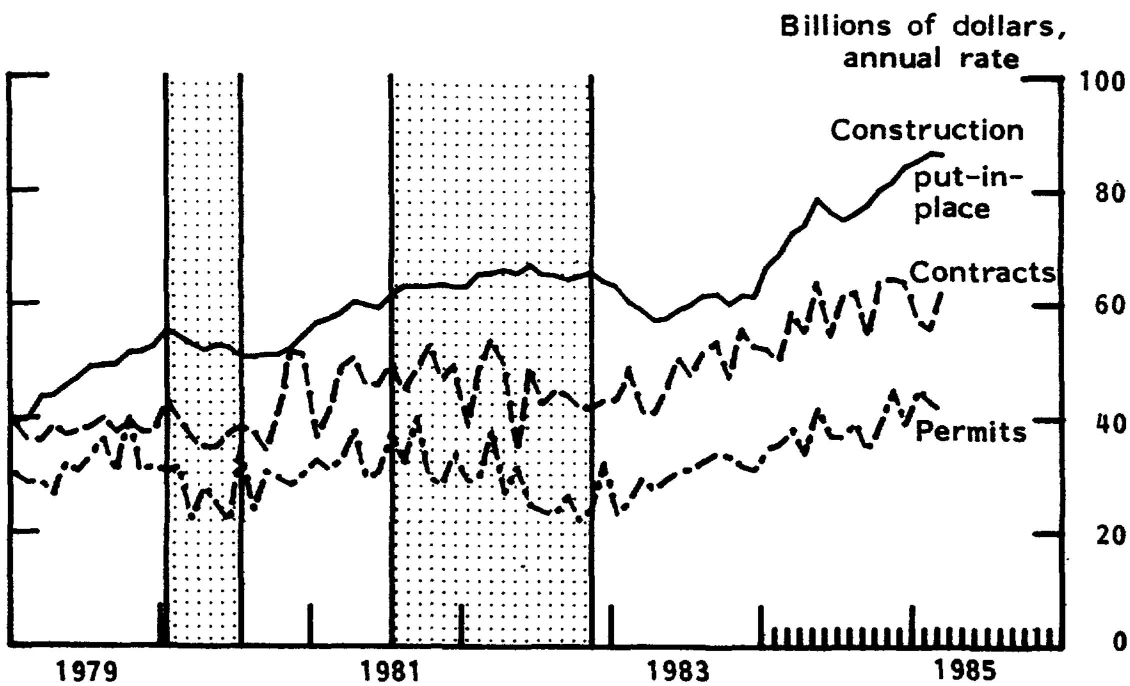
Growth in business fixed investment slowed markedly in the first quarter. While nonresidential construction showed continued strength, real expenditures on producers' durable equipment declined slightly. Moreover, a larger share of the equipment purchased last quarter came from abroad. First-quarter imports of capital goods increased 12 percent in nominal terms, while shipments of nondefense capital goods by domestic producers posted a broadly based decline of 3.2 percent.

The value of nonresidential construction put in place fell 1.4 percent in March, the first monthly drop since July 1984. Nonetheless, for the first quarter as a whole, these expenditures rose 3.7 percent, similar to the average quarterly gain recorded in 1984. The growth in spending over the past year, however, has been confined to office and

BUSINESS CAPITAL SPENDING INDICATORS
(Percentage change from preceding comparable periods;
based on seasonally adjusted data)

	1984		1985	1985		
	Q3	Q4	Q1	Jan.	Feb.	Mar.
Producers' durable equipment						
Nondefense capital goods						
Shipments	2.6	3.2	-3.2	-10.9	4.3	6.4
Orders	-.4	-4.0	1.8	-12.1	24.8	-7.4
Unfilled orders	1.9	-2.3	.6	-1.2	2.4	-.5
Imports of capital goods excluding autos	23.1	-16.0	12.0	16.5	-8.4	4.7
Exports of capital goods excluding autos	1.4	2.2	.0	.1	-7.9	16.5
Sales of heavy-weight trucks (thousands of units, A.R.)	252	316	312	299	316	320
Nonresidential structures						
Nonresidential construction	1.3	3.5	3.7	1.2	1.9	-1.4
Commercial building	1.9	10.7	7.5	3.2	1.1	.8

NONRESIDENTIAL CONSTRUCTION, CONTRACTS, AND PERMITS[1]



1. Source: F.W. Dodge and Census.

other commercial construction; while on balance, the other components of nonresidential construction have been flat. In addition, oil and gas drilling has weakened considerably in recent months.

Indicators of future business investment have been mixed. Following two quarters of decline, new orders for nondefense capital goods received by domestic producers rose a modest 1.8 percent in the first quarter. New orders last quarter would have fallen if not for a 25 percent gain in bookings for office and computing equipment. In the construction area, vacancy rates for office buildings are at record highs, and the value of nonresidential building contracts and permits may be levelling off after substantial increases earlier in the recovery. However, according to capital spending surveys conducted in the past few months, firms still plan to increase nominal plant and equipment outlays 8-1/2 to 11 percent in 1985, consistent with sizable gains in investment spending in the quarters ahead.

Business Inventories

Business inventory accumulation remained moderate in the early part of 1985. After rising at an average annual rate of $33 billion in January and February, the book value of manufacturing and trade inventories fell in March; manufacturers continued modest buildups while retail and wholesale establishments worked to pare their excess stocks. With little net change in shipments and sales in early 1985, the inventory-sales ratio for all manufacturing and trade remained stable throughout the first quarter.

Manufacturers continued to exhibit cautious inventory behavior in the first quarter. The book value of factory stocks rose at an annual rate of $4.7 billion, the same rate as in the fourth quarter. By stage of processing, the first-quarter rise was entirely in stocks of finished and in-process goods.

Inventories at auto dealers rose substantially in the first four months of this year, as car manufacturers stepped up production to alleviate tight supplies for some models. Despite the increase in assemblies, the level of dealers' stocks so far this year has hovered around 54 days of supply, close to the average level during the past year.

Retail trade inventories other than autos fell $11 billion (annual rate) in March and were little changed for the quarter as a whole. This improved the inventory positions of retailers to some extent, especially for general merchandise and apparel stores. Nonetheless, the inventory-sales ratios for these stores in March were still above historical norms, suggesting the possibility of further adjustments.

Housing

Indicators of residential construction activity firmed in the first quarter. Total private housing starts rose 16 percent in March to a 1.9 million unit annual rate. For the first quarter as a whole, housing starts were up 12 percent, following three successive quarters of decline. Newly issued residential building permits also registered a solid gain in the first quarter. The general decline in mortgage credit costs since last summer is the key factor in the recent strengthening of residential construction.

CHANGES IN MANUFACTURING AND TRADE INVENTORIES
(Billions of dollars at annual rates)

	1984		1985	1985		
	Q3	Q4	Q1	Jan.	Feb.[r]	Mar.[p]
Book value basis						
Total	52.2	31.8	18.9	28.4	37.7	-9.4
Manufacturing	29.3	4.7	4.7	.9	4.3	8.8
Wholesale trade	15.5	6.4	2.5	.5	16.6	-9.6
Retail trade	7.5	20.7	4.8	27.0	16.7	8.5
Automotive	.1	11.7	8.9	15.0	9.2	2.5
Ex. auto	7.5	9.0	2.8	12.0	7.5	-11.0
Constant dollar basis						
Total	24.3	11.5	--	16.7	10.7	--
Manufacturing	13.0	-.1	--	3.1	2.7	--
Wholesale trade	8.8	3.5	--	.3	.8	--
Retail trade	2.5	8.1	--	13.3	7.2	--
Automotive	.4	5.0	--	5.7	4.7	--
Ex. auto	2.1	3.1	--	7.6	2.5	--

r--revised estimates.
p--preliminary estimates.

INVENTORIES RELATIVE TO SALES[1]

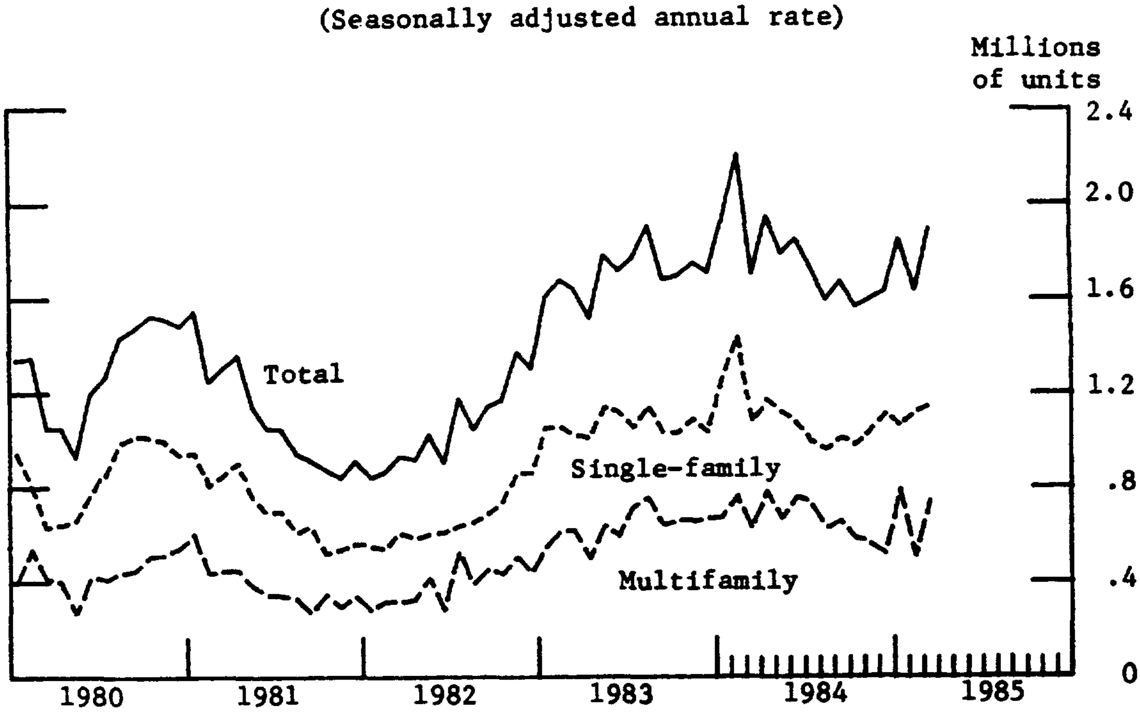
	Cyclical Reference Points[2]		1984		1985	1985		
	1981 Low	1982 High	Q3	Q4	Q1	Jan.	Feb.[r]	Mar.[p]
Book value basis								
Total	1.39	1.53	1.37	1.37	1.38	1.38	1.38	1.38
Manufacturing	1.60	1.77	1.50	1.48	1.49	1.49	1.49	1.48
Wholesale trade	1.06	1.28	1.14	1.16	1.16	1.15	1.17	1.16
Retail trade	1.36	1.43	1.39	1.41	1.42	1.42	1.42	1.42
Automotive	1.59	1.88	1.45	1.51	1.54	1.50	1.52	1.52
Ex. auto	1.29	1.35	1.38	1.39	1.39	1.40	1.39	1.39
Constant dollar basis								
Total	1.62	1.75	1.55	1.55	--	1.54	1.54	--
Manufacturing	1.91	2.11	1.79	1.77	--	1.77	1.78	--
Wholesale trade	1.34	1.52	1.36	1.37	--	1.35	1.35	--
Retail trade	1.34	1.44	1.34	1.36	--	1.36	1.36	--
Automotive	1.49	1.81	1.32	1.40	--	1.39	1.37	--
Ex. auto	1.28	1.37	1.34	1.35	--	1.35	1.35	--

PRIVATE HOUSING ACTIVITY
(Seasonally adjusted annual rates, millions of units)

	1984	1984		1985			
	Annual	Q3	Q4	Q1	Jan.	Feb.	Mar.[1]
All units							
Permits	1.67	1.53	1.56	1.71	1.68	1.64	1.81
Starts	1.75	1.66	1.60	1.79	1.85	1.63	1.90
Single-family units							
Permits	.92	.85	.84	.96	.92	.96	1.01
Starts	1.08	.99	1.05	1.11	1.06	1.12	1.15
Sales							
New homes	.64	.61	.62	.65	.62	.64	.70
Existing homes	2.87	2.76	2.81	2.98	3.00	2.88	3.05
Multifamily units							
Permits	.75	.68	.72	.75	.75	.68	.81
Starts	.67	.67	.55	.68	.79	.51	.75
Mobile home shipments	.30	.30	.29	n.a.	.27	.28	n.a.

1. Preliminary estimates.
n.a.--not available.

PRIVATE HOUSING STARTS
(Seasonally adjusted annual rate)



Single-family starts, which are relatively sensitive to shifts in credit costs, have risen nearly 20 percent above last summer's low point to an annual rate of 1.15 million units in March. The upswing in single-family starts has paralleled an increase in sales volume for both new and existing homes. In fact, sales of existing homes in March reached their highest monthly pace in four and one-half years.

Construction of multifamily units was particularly strong in March. However, starts of such units recently have been quite volatile, falling 18 percent in the fourth quarter of 1984 before rising 23 percent in the first quarter of this year. The recent strength in the multifamily sector has come mainly from construction of rental units located in southern and western states, which have the country's highest rates of rental vacancies. Investors seem to be building rental units in these regions based on long-run economic and tax considerations.

State and Local Sector

Real outlays by state and local governments appear to have picked up in the first quarter, following a slight decline at the end of last year. Construction activity, which had been notably weak in late 1984, rebounded sharply in March. Moreover, the need for further growth in capital spending remains as capital stock of the state and local sector has been shrinking for the past five years. However, new plans, contract awards, and bond sales do point to rising outlays for restoration and modernization.

Federal Government

The NIA federal deficit declined in the first quarter to $161 billion at an annual rate from the $198 billion deficit recorded in the fourth quarter of 1984. Much of the drop can be traced to delays in the disbursement of tax refunds and to irregular patterns in defense procurement. In addition, recent declines in interest rates contributed to slower growth of interest outlays, and individual estimated and final tax payments[1] were substantially above year-earlier levels.

The IRS began processing tax refunds at a much faster rate in April, and the shortfall of refund payments relative to 1984 was eliminated in early May. Nonetheless, net tax receipts remain high relative to 1984 because estimated and final tax payments accelerated more sharply than usual in April and early May. These tax payments have increased this year in part because of provisions in the Tax Reform Act of 1984 that limit income averaging and restrict various tax-sheltering activities.

On the spending side, defense outlays slowed markedly in the first quarter from the strong growth registered in the fourth quarter of last year, reflecting the irregular delivery patterns for large procurement items such as the B-1 bomber. Real defense purchases declined in the first quarter, but they remained almost 6 percent above year-earlier levels.

The administration released revised budget estimates in its April Budget Update on April 15. The FY1985 deficit projection was reduced

1. Individuals are generally required to make estimated tax payments if the current year's tax liability appears likely to exceed tax withholding. Final payments are filed with the tax return and represent the previous year's tax liability minus withholdings and estimated payments.

FEDERAL RECEIPTS AND EXPENDITURES
(NIA; billions of current dollars, SAAR)

	1984 Q1	1984 Q2	1984 Q3	1984 Q4	1985 Q1
Total receipts	686.4	704.3	706.2	721.9	773.8[1]
Total expenditures	847.6	868.0	886.8	919.7	935.0
Defense purchases	213.4	220.8	220.3	231.6	234.5
Real defense purchases(1972 $)	87.1	89.6	89.1	92.7	92.2
Net interest	107.6	110.9	122.0	126.4	126.8
Deficit	161.3	163.7	180.6	197.8	161.3

1. The receipts total is based on staff estimates of corporate profits tax accruals.

INDIVIDUAL ESTIMATED AND FINAL TAX RECEIPTS[1] SINCE JANUARY 1
(Millions of dollars, not at annual rates nor seasonally adjusted)

Cumulative totals through:	Individual refunds 1984	Individual refunds 1985	Estimated and final receipts 1984	Estimated and final receipts 1985	Net estimated and final receipts[2] 1984	Net estimated and final receipts[2] 1985
January 31	128	270	14,110	14,830	13,982	14,560
February 28	2,905	1,341	15,975	16,716	13,070	15,375
March 31	19,547	12,870	19,425	20,529	-122	7,659
April 30	35,080	31,582	55,811	68,780	20,731	37,198
May 10	39,024	42,164	56,591	71,334	17,567	29,170

1. Includes payment of estimated Social Security taxes by self-employed individuals.
2. Estimated and final receipts less refunds.

Source: Daily Treasury Statements.

through minor revisions to economic assumptions that incorporate recent data and through technical reestimates of various tax and nondefense outlay programs. The deficit projections for FY1986 through FY1988 were cut slightly ($2.6 billion in FY1986), and those for FY1989 and FY1990 were increased slightly.

In action on the FY1986 budget, the Senate approved on May 10 a budget resolution that would cut the baseline deficit[1] $56 billion in FY1986, $100 billion in FY1987, and $139 billion in FY1988. The resolution would freeze real defense appropriations in FY1986 and limit real growth to 3 percent per year in FY1987 and FY1988; would freeze for one year the COLAs on Social Security, veterans, military and civilian federal retirement; and would cut numerous nondefense discretionary programs such as trade adjustment assistance, general revenue sharing, the Economic Development Administration and direct loans of the Export-Import Bank. The House Budget Committee is currently marking up its version of a budget resolution.

Exports and Imports

The U.S. merchandise trade deficit in March was close to the sizable rates recorded in January and February. The deficit for the first quarter as a whole--$113 billion at an annual rate--slightly exceeded the record 1984 deficit.

1. Baseline projections are designed to show what the deficit would be in future years if current policies were continued without change. For defense, the Senate used the Administration's February budget proposal as its baseline. The baseline for other spending programs and taxes consists of Congressional Budget Office technical estimates evaluated with the Administration's economic assumptions.

Increased imports largely accounted for the widening trade deficit in the first quarter. There was a broadly based rise in non-oil imports--especially imports of consumer goods, capital goods, and automotive products. The high volume of these imports in the first quarter, as well as the decline in their prices, reflected the past appreciation of the dollar. Oil imports, however, fell substantially during the first quarter; domestic oil consumption edged down and inventories were reduced, at least partly in anticipation of price declines in world markets. The volume of exports in the first quarter fell somewhat from the fourth-quarter level, owing primarily to a drop in exports of agricultural commodities. (Further discussion of international economic developments is included in section IV.)

Prices

The pace of inflation has increased slightly in recent months, but much of the acceleration appears to be temporary. The consumer price index rose 0.5 percent in March, bringing the first-quarter increase to 4.1 percent at an annual rate, 1 percentage point more than in the fourth quarter. This pickup in the CPI resulted from a sharp swing in used car prices, as well as price increases for new cars, cigarettes, and apparel. However, motor vehicle prices at the producer level declined in April reversing the increases posted last quarter.

Consumer energy prices, which had fallen sharply in January and February, increased nearly 2 percent in March. This surge in energy prices reflected what should be a temporary spurt in gasoline prices stemming from reduced inventories. Supplies of crude oil remain abundant

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

	Relative Importance Dec. 1984	1983	1984	1984 Q3	1984 Q4	1985 Q1	1985 Feb.	1985 Mar.
				-Annual rate-			-Monthly rate-	
All items[2]	100.0	3.8	4.0	4.5	3.0	4.1	.3	.5
Food	18.7	2.6	3.8	3.9	3.7	2.6	.5	.0
Energy	11.5	-.5	.2	.1	-.7	-.8	-1.4	1.9
All items less food and energy[3]	69.8	4.9	4.7	5.3	3.5	5.4	.6	.4
Commodities[3]	26.3	5.0	3.1	3.8	.9	6.6	.8	.3
Services[3]	43.5	4.8	5.6	6.2	5.0	5.0	.4	.4
Memorandum:								
CPI-W[4]	100.0	3.3	3.5	7.5	1.6	4.0	.4	.4

1. Changes are from final month of preceding period to final month of period indicated.
2. Official index for all urban consumers, based on a rental equivalence measure for owner-occupied housing after December 1982.
3. Data not strictly comparable. Before 1983, they are based on unofficial series that exclude the major components of homeownership; beginning in 1983, data include a rental equivalence measure of homeowners costs.
4. Index for urban wage earners and clerical workers, based on a rental equivalence measure for owner-occupied housing after December 1984.

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

	Relative Importance Dec. 1984	1983	1984	1984 Q3	1984 Q4	1985 Q1	1985 Mar.	1985 Apr.
				—Annual rate—			—Monthly rate—	
Finished goods	100.0	.6	1.7	.0	1.1	1.0	.2	.3
Consumer foods	24.4	2.3	3.5	4.5	3.3	-2.4	-.2	-1.0
Consumer energy	11.5	-9.2	-4.1	-19.7	5.6	-21.0	-.9	5.8
Other consumer goods	42.4	1.9	2.2	2.5	-.2	6.6	.6	-.2
Capital equipment	21.6	1.9	2.8	2.3	-1.1	6.5	.4	.0
Intermediate materials[2]	95.1	1.4	1.7	-1.1	1.2	-2.5	-.1	.3
Exc. energy	80.1	3.0	2.1	.9	1.5	-1.0	-.1	.0
Crude food materials	53.0	8.0	-1.2	-1.7	10.6	-24.1	-2.8	-3.0
Crude energy	31.7	-4.6	-1.3	.4	-7.6	-12.7	-1.0	.1
Other crude materials	15.4	15.5	-3.4	-15.3	-10.7	-13.4	2.3	2.1

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

worldwide, and spot prices for gasoline have been falling in recent weeks.

Softer food prices have restrained overall price inflation this year. The food component in the March CPI was unchanged, while the PPI for consumer foods declined in March and April. At the farm level, food prices fell during the first four months of this year.

Wages and Labor Costs

Wage data for the first quarter of 1985 give a mixed picture of recent developments. Preliminary data on hourly compensation in the nonfarm business sector, which includes employers' contributions for employee benefits and social insurance programs as well as wages, rose 6 percent at an annual rate—about 2 percentage points more than the increases during 1983 and 1984. Less than half of this recent step-up resulted from legislated changes in social security taxes effective January 1 and higher employers' contributions for unemployment insurance. In contrast, other aggregate wage measures show little if any acceleration. The comprehensive employment cost index (ECI) for wages paid in private industry increased at a 4-1/4 percent annual rate in the first quarter, the same as 1984. Moreover, during the first four months of 1985, the hourly earnings index for production and nonsupervisory workers has increased at an annual rate of 2.5 percent, slightly below the rate posted in 1984.

Despite some divergence in the aggregate measures of wage inflation, certain underlying developments are evident. Throughout the private service-producing sector, wage inflation has continued to decelerate,

SELECTED MEASURES OF LABOR COSTS IN THE NONFARM BUSINESS SECTOR
(Percentage change at annual rates; based on seasonally adjusted data)

	1982	1983	1984	1984 Q3	1984 Q4	1985 to date
						First four months
Hourly earnings index, wages of production workers[1]						
Total private nonfarm	6.1	3.9	3.1	2.7	2.9	2.5
Manufacturing	6.0	2.7	3.3	3.1	3.2	4.7
Contract construction	5.4	1.5	.9	-.7	.3	3.1
Transportation and public utilities	6.1	4.3	3.0	2.7	2.4	1.0
Trade	5.4	4.7	2.6	2.0	3.0	.8
Services	7.0	4.9	4.0	3.9	3.7	1.3
Employment cost index, wages and salaries of all persons[2]						
						First three months
Total	6.3	5.0	4.2	2.7	5.0	4.3
By occupation:						
White collar	6.5	6.0	4.4	2.4	5.2	5.0
Blue collar	5.6	3.8	3.6	2.0	4.9	4.1
Service workers	8.5	4.6	6.2	8.8	6.2	-4.4
Major collective bargaining agreements[3]						
First-year wage adjustments	3.8	2.6	2.4	—	—	2.8
Total effective wage change	6.8	4.0	3.7	—	—	2.8
Labor costs and productivity, all persons[1]						
Compensation per hour	7.2	3.9	4.3	3.6	3.7	6.0
Output per hour	1.4	3.9	2.4	-1.1	2.2	-1.2
Unit labor costs	5.8	.0	1.9	4.7	1.4	7.3

1. Changes are from final quarter of preceding period to final quarter of period indicated. Quarterly and year-to-date changes at compound rates.
2. Seasonally adjusted by the Board staff. Changes are from final month of preceding period to final month of period indicated. Quarterly changes at compound rates.
3. Agreements covering 1,000 or more workers; not seasonally adjusted.

while in manufacturing and construction it has picked up recently from the low rates recorded in 1983 and 1984. All of the recent acceleration in manufacturing wages has occurred among nonunion workers. The union sector, whether within or outside manufacturing, has not been a source of upward wage pressure. New settlements reached during the first quarter call for nearly record-low first-year increases (exclusive of COLAs), and wage adjustments scheduled under earlier contracts have continued to shrink on average.

Productivity in the nonfarm business sector fell at a 1-1/4 percent annual rate in the first quarter, reflecting the sharp slowdown in the preliminary estimate of output growth. Temporary declines in measured productivity often occur when output growth decelerates because firms may continue to base employment decisions on longer-run sales and production expectations. Thus, the data still appear consistent with an underlying trend for productivity growth of 1-1/4 to 1-1/2 percent. Declining productivity, coupled with rising compensation growth, led to a jump in unit labor costs last quarter. However, when viewed over the past year, unit labor costs have risen more moderately--about 3 percent in the nonfarm business sector.

SELECTED FINANCIAL MARKET QUOTATIONS[1]
(Percent)

	1982/1983 Cyclical low	1984 Highs	1985 Previous lows	1985 FOMC Feb. 13	1985 FOMC Mar. 26	1985 May 14	Change from: FOMC Mar. 26
Short-term rates							
Federal funds[2]	8.46	11.63	8.25	8.52	8.57	8.27	-.30
Treasury bills[3]							
3-month	7.08	10.67	7.62	8.24	8.34	7.60	-.74
6-month	7.62	10.77	7.86	8.30	8.80	7.76	-1.04
1-year	7.73	11.13	8.20	8.49	8.98	7.95	-1.03
Commercial paper							
1-month	8.00	11.42	7.86	8.47	8.63	7.98	-.65
3-month	7.97	11.35	7.90	8.56	8.75	8.00	-.75
Large negotiable CDs[3]							
1-month	8.08	11.52	7.95	8.51	8.60	8.00	-.60
3-month	8.12	11.79	8.06	8.70	8.79	8.12	-.67
6-month	8.20	12.30	8.32	9.05	9.35	8.25	-1.10
Eurodollar deposits[4]							
1-month	8.68	11.89	8.09	8.60	8.78	8.24	-.54
3-month	8.71	12.20	8.28	9.04	9.19	8.44	-.75
Bank prime rate	10.50	13.00	10.50	10.50	10.50	10.50	—
Treasury bill futures							
June 1985 contract	10.11	12.82	8.22	8.77	8.86	7.57	-1.29
Dec. 1985 contract	10.86	13.20	9.13	9.64	9.74	8.34	-1.40
rmediate- and long-term rates							
U.S. Treasury (constant maturity)							
3-year	9.33	13.49	10.18	10.44	10.97	9.79	-1.18
10-year	10.12	13.99	11.06	11.39	11.77	10.87	-.90
30-year	10.27	13.94	11.16	11.31	11.72	11.07	-.65
Municipal revenue (Bond Buyer index)	9.21	11.44	9.60	9.96[5]	10.24[5]	9.56[5]	-.68
Corporate--A utility Recently offered	11.64	15.30	12.51	12.65e	13.11e	12.24e	-.87
Home mortgage rates							
S&L fixed-rate	12.55	14.68	12.90	12.90	13.24[6]	13.02[6]	-.22
S&L ARM, 1-yr.	n.a.	12.31	10.59	10.59	10.97[6]	10.61[6]	-.36

	1983 Highs	1984 Lows	1985 Previous Highs	1985 FOMC Feb. 13	1985 FOMC Mar. 26	1985 May 14	% change from: FOMC Mar. 26
Stock prices							
Dow-Jones Industrial	1287.20	1086.57	1297.92	1297.92	1259.72	1273.30	1.1
NYSE Composite	99.63	85.13	106.08	106.08	103.28	106.48	3.1
AMEX Composite	249.03	187.16	231.22	231.22	224.41	227.76	1.5
NASDAQ (OTC)	328.91	225.30	288.35	288.32	276.18	287.72	4.2

1. One-day quotes except as noted.
2. Averages for two-week reserve maintenance period closest to date shown. Last observation is for ntenance period ended May 8, 1985.
Secondary market.
4. Averages for statement week closest to date shown.
5. One-day quotes for preceding Thursday.
6. One-day quotes for preceding Friday.
e--estimated.

Interest rates have fallen substantially in recent weeks, reversing the rise that occurred prior to the March FOMC meeting. Yield declines since late March generally have been in the range of 1/2 to slightly more than a full percentage point, though rates on new home mortgage commitments, which had backed up less, have posted more modest decreases, and the prime rate to date has remained unchanged. The federal funds rate, primarily around 8 to 8-1/4 percent of late, also has declined comparatively moderately, but some market expectation of a further easing of the System's reserve supplying posture or a discount rate cut has been fostered by signs of less buoyant economic activity and slower money growth. In recent days, Senate approval of a deficit-reduction package also has had a constructive effect on market sentiment.

The deceleration of monetary expansion has encompassed all of the aggregates. M1 grew at a little under a 6 percent annual rate in both March and April, half of the average pace during the first two months of the year. And the broader aggregates were essentially flat in April after slowing markedly in March. The moderation in M1 growth appears generally consistent with developments in income and interest rates; however, the sharpness of the slowdown in M2 and M3 appears to have been further accentuated by the effects of swings in bank securities trading positions and government deposits and by less aggressive bidding for deposits by S&Ls in light of sluggish asset expansion.

S&Ls were among the parties likely suffering losses in connection with the failure of two more government securities dealers (Bevill, Bresler, and Schulman, and Parr), and there have been deposit withdrawal incidents reflecting continued public edginess about S&Ls, especially those without federal insurance. Still, there have been no indications of broad effects of recent financial institution problems on the cost or availability of credit. Indeed, credit expansion has slowed only a little from last year's rapid pace. In the business sector, the unabated liquidation of outstanding equity shares through mergers, repurchases, and other transactions has kept corporate borrowing sizable in the face of a moderate underlying financing gap. Firms have tended to favor the bond markets as a source of funds, in light of the lower level of long-term rates. Households apparently have maintained a substantial demand for mortgage credit to finance rising home purchases, and there have been no signs of a slackening in the tremendous growth of consumer credit. State and local government bond offerings have been quite heavy, boosted by an increased volume of refunding issues. And the federal government has continued to borrow large sums, almost entirely in the intermediate- and long-term maturity sectors.

Monetary Aggregates and Bank Credit

M1 growth slowed to a bit below 6 percent at an annual rate in March and April from an 11-1/2 percent pace earlier in the year, leaving the aggregate just above the upper parallel band associated with its 1985 growth range. A deceleration in money expansion was to be expected on the basis of the moderate growth of income and spending and the waning effect of last fall's interest rate declines. Flows related to the April tax date can have significant transitory effects on cash balances, but the net impact of refunds and final payments on the pattern of M1 growth appears to have been small this year.

MONETARY AGGREGATES
(Based on seasonally adjusted data unless otherwise noted)[1]

	1983:Q4 to 1984:Q4	1985 Q1	Jan.	Feb.	Mar.	Apr.pe	Growth from Q4 1984 to Apr. 1985pe
	------- Percentage change at annual rates ------						
1. M1	5.2	10.5	9.0	14.1	5.7	5-1/2	9-1/4
2. M2	7.7	12.1	13.9	11.0	4.1	-1/2	8-1/2
3. M3	10.4	10.7	10.3	8.3	5.6	1	8
							Levels in billions of dollars Mar. 1985
Selected components							
4. Currency	7.2	6.3	5.3	8.3	6.0	4	161.3
5. Demand deposits	1.1	7.0	2.4	12.5	1.0	3	251.9
6. Other checkable deposits	10.5	20.6	23.8	22.6	13.4	13	153.4
7. M2 minus M1[2]	8.5	12.6	15.4	10.1	3.7	-3	1857.1
8. Overnight RPs and Eurodollars, NSA[3]	7.3	64.0	110.4	125.9	-32.8	-147	67.6
9. General purpose and broker/dealer money market mutual fund shares, NSA	17.1	33.1	32.2	22.3	17.1	-7	177.9
10. Commercial banks	8.1	13.6	15.5	9.2	6.5	9	797.0
11. Savings deposits, SA, plus MMDAs, NSA[4]	5.2	29.2	37.9	26.0	10.2	3	414.2
12. Small time deposits	11.1	-1.8	-7.1	-8.4	2.5	15	382.8
13. Thrift institutions	7.2	8.1	7.4	7.8	8.5	4	828.1
14. Savings deposits, SA, plus MMDAs, NSA[4]	-3.6	17.9	24.1	25.9	19.4	1	332.4
15. Small time deposits	15.4	1.9	-3.1	-3.9	1.2	5	495.7
16. M3 minus M2[5]	22.2	5.4	-3.5	-2.1	11.4	7	626.9
17. Large time deposits	26.1	8.8	1.4	6.9	10.9	10	423.5
18. At commercial banks, net[6]	16.0	2.6	-9.5	9.6	22.7	15	269.4
19. At thrift institutions	49.4	19.8	20.5	2.3	-9.3	2	154.1
20. Institution-only money market mutual fund shares, NSA	33.6	31.2	44.0	-51.7	-52.1	2	59.5
21. Term RPs, NSA	45.6	-20.0	-80.9	12.9	53.0	70	68.6
22. Term Eurodollars, NSA	-8.0	3.9	-30.3	11.9	55.6	-53	85.8
	— Average monthly change in billions of dollars —						
MEMORANDA:							
23. Managed liabilities at commercial banks (24+25)	4.7	4.0	-7.4	12.0	7.4	-11	446.4
24. Large time deposits, gross	3.2	1.3	-1.0	0.5	4.5	3	329.8
25. Nondeposit funds	1.5	2.7	-6.4	11.5	2.9	-14	116.6
26. Net due to related foreign institutions, NSA	0.9	0.5	-4.5	3.4	2.5	-6	-30.6
27. Other[7]	0.5	2.2	-1.8	8.0	0.5	-9	147.2
28. U.S. government deposits at commercial banks[8]	0.2	-1.4	-1.4	-1.7	-1.2	3	11.8

1. Quarterly growth rates are computed on a quarterly average basis. Dollar amounts shown under memoranda for quarterly changes are calculated on an end-month-of-quarter basis.
2. Nontransactions M2 is seasonally adjusted as a whole.
3. Overnight and continuing contract RPs issued to the nonbank public by commercial banks plus overnight Eurodollar deposits issued by branches of U.S. banks to U.S. nonbank customers, both net of amounts held by money market mutual funds. Excludes retail RPs, which are in the small time deposit component.
4. Growth rates are for savings deposits, seasonally adjusted, plus money market deposit accounts (MMDAs), not seasonally adjusted. Commercial bank savings deposits excluding MMDAs declined during March and April 1985 at rates of 10.9 and 8 percent respectively. At thrift institutions, savings deposits excluding MMDAs increased in March 1985 at a rate of 3.6 percent and declined during April at a rate of 1 percent.
5. The non-M2 component of M3 is seasonally adjusted as a whole.
6. Net of large-denomination time deposits held by money market mutual funds and thrift institutions.
7. Consists of borrowings from other than commercial banks in the form of federal funds purchased, securities sold under agreements to repurchase, and other liabilities for borrowed money (including borrowings from the Federal Reserve and unaffiliated foreign banks, loan RPs and other minor items). Data are partially estimated.
8. Consists of Treasury demand deposits at commercial banks and Treasury note balances.
pe--preliminary estimate.

M2 growth fell sharply in March to a 4 percent annual rate and then turned slightly negative in April. The weakening in its "nontransactions" component was due in good part to a reversal of earlier increases in overnight repurchase agreements, as an appreciable decline in Treasury securities in bank trading accounts followed a sharp buildup earlier in the year. Moreover, classification of some overnight RPs as term RPs over the Easter weekend temporarily reduced M2 in April.

Growth of MMDAs and money market mutual funds also decelerated, as spreads between market rates and rates on these accounts were wider on average than in February. Growth likely was further damped in April by tax payments from these components, which are not seasonally adjusted. In contrast, small time deposits expanded in March and April for the first time this year, perhaps reflecting the steepening of the offering-rate curve. In April, the sum of savings deposits, MMDAs, and small time deposits apparently grew noticeably more rapidly at banks than at thrifts. While such a pattern could be reflective of investors' concern about the safety of thrift deposits, considerable caution must be exercised in so interpreting these data. Among other things, the sample data for S&Ls used to adjust these deposits for IRA/Keogh accounts are not yet available and could be important in April; there is a considerable month-to-month volatility in the inter-institutional growth differential; and there is evidence through March that S&Ls were bidding less aggressively against banks for deposits.

M3 also slowed in March and April, owing mainly to the deceleration in its M2 components. Growth in large time deposits was substantial in both months as a surge at commercial banks more than offset a decline at thrifts, where reduced credit growth--probably in part related to the new capital requirements imposed by the FHLBB--has eased the need to issue large CDs.

Credit expansion at commercial banks remained strong in March, but fell to a 6-3/4 percent rate in April. Securities holdings were little changed in March and then fell in April when there was a sizable runoff of Treasuries from large bank trading accounts. Real estate and consumer loans continued to grow rapidly in March and April, while business loan growth picked up in March before falling off sharply in April. In March, the increase in business loans at domestic offices partly reflected substantial rebooking of loans to U.S. residents from the foreign branches of U.S. banks as the prime-LIBOR spread narrowed further and a few large New York banks reportedly responded to a clarification of the tax status of these loans by New York state banking authorities.

Business Finance

Commercial paper issuance by nonfinancial firms has been quite variable on a month-to-month basis, offsetting in part movements in bank loans. The sum of bank loans and commercial paper decelerated to 6-3/4 percent in April from a 9 percent rate in March; on average for the first quarter, this measure increased at about a 5 percent annual rate. Growth of finance company credit slowed in March from a considerably stronger pace earlier in the year, and bankers acceptances resumed their earlier downtrend.[1]

The slower growth in loans and open market paper thus far this year is in line with the lower rate of inventory accumulation and the continued

1. The series on bankers acceptances has been revised to focus more clearly on borrowing to finance business activity in the U.S. The appendix discusses the revision and recent developments in the market for bankers acceptances.

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

	1984 Q3	1984 Q4	1985 Q1	1985 Feb.	1985 Mar.	1985 Apr.p	Levels in bil. of dollars Aprilp
	Commercial Bank Credit						
1. Total loans and securities at banks	9.5	9.8	10.2	12.7	11.4	6.7	1768.7
2. Securities	6.6	1.8	5.2	12.2	2.7	-10.4	402.2
3. U.S. government securities	6.8	3.4	10.3	26.3	5.0	-25.2	261.3
4. Other securities	6.3	-5.6	-3.4	-13.5	-17.9	19.0	140.9
5. Total loans	10.5	12.8	11.7	12.8	15.9	11.7	1366.5
6. Business loans	7.5	7.8	10.2	12.8	17.7	0.2	480.5
7. Security loans	2.8	37.5	16.5	-15.3	-7.8	19.5	31.2
8. Real estate loans	11.4	12.1	10.9	13.3	11.6	12.4	389.8
9. Consumer loans	14.2	16.1	17.4	14.6	19.6	15.1	265.2
	Short- and Intermediate-Term Business Credit						
10. Business loans net of bankers acceptances	7.9	7.9	9.3	9.8	17.4	2.8	476.9
11. Loans at foreign branches[2]	8.2	26.0	-45.1	-76.0	-104.3	-31.7	18.4
12. Sum of lines 10 & 11	7.8	8.7	6.9	5.9	12.3	1.7	495.4
13. Commercial paper issued by nonfinancial firms[3]	46.8	51.2	-6.0	37.3	-13.2	41.6	74.6
14. Sums of lines 12 & 13	12.2	13.8	5.1	9.9	9.0	6.8	570.0
15. Bankers acceptances: U.S. trade related[4,5]	-3.2	-6.5	-5.5	0.0	-13.2	n.a.	36.0 (Mar.)
16. Line 14 plus bankers acceptances: U.S. trade related	11.2	12.5	4.4	9.3	7.4	n.a.	606.0 (Mar.)
17. Finance company loans to business[4]	9.8	23.2	21.1	22.0	7.8	n.a.	139.0 (Mar.)
18. Total short- and intermediate-term business credit (sum of lines 16 & 17)	10.9	14.4	7.5	11.8	7.5	n.a.	742.7 (Mar.)

n.a.—not available. p—preliminary.
1. Average of Wednesdays for domestically chartered banks and average of current and preceding ends of months for foreign-related institutions.
2. Loans at foreign branches are loans made to U.S. firms by foreign branches of domestically chartered banks.
3. Average of Wednesdays.
4. Based on average of current and preceding ends of month.
5. Includes acceptances financing U.S. imports, U.S. exports and domestic shipment and storage of goods.

moderate overall gap between capital outlays and internal funds. However, corporate financing needs have reflected as well the run-off of outstanding shares in mergers, buyouts, and share repurchases, which has been at roughly the same pace as in 1984 as a whole. Relatively attractive costs in the bond markets have led to heavier reliance on these markets in recent months.

Corporate borrowing in tax-exempt bond markets has slackened markedly since the year-end rush to beat the application of tighter arbitrage rules and of state-by-state volume limits for industrial development bonds. But issuance of taxable bonds in both domestic and overseas markets by nonfinancial firms has been high so far this year, averaging only a bit less than in the record-breaking fourth quarter. Offerings were particularly strong in March, owing to a $4-1/2 billion exchange of debt for equity by Phillips Petroleum, and in April, reflecting a downward trend in interest rates. The A-rated utility bond index has fallen 7/8 of a percentage point since the last FOMC meeting, narrowing an already low spread against long Treasury bonds. Bond issuance was light in early May but has picked up most recently with the continued decline in yields.

Financial issues totaled more than $5 billion in April, a record even on an inflation-adjusted basis. Finance subsidiaries of automobile manufacturers have been especially heavy borrowers, issuing more than $3-1/2 billion of debt during the intermeeting period; much of the proceeds of these issues has been used to finance new promotional loan programs.

Major stock price averages have remained near their cyclical peaks since the last FOMC; the NYSE has set a new high. The strong market stimulated an increased volume of new equity issues and equity-based bonds in April; even so, in recent months the volume of new stock issues for

GROSS OFFERINGS OF SECURITIES BY U.S. CORPORATIONS
(Monthly rates, not seasonally adjusted, billions of dollars)

	1984			1985		
	Year	Q3	Q4	Q1p	Mar.p	Apr.
Corporate securities - total[1]	9.88	11.00	13.19	12.36	15.31	14.10
Public offerings in U.S.	8.00	8.77	10.40	9.37	14.05	11.30
Stocks--total[2]	1.89	1.64	1.79	2.19	2.30	2.80
Nonfinancial	1.08	.84	1.11	1.18	1.10	1.80
Utility	.22	.17	.20	.48	.40	1.10
Industrial	.86	.66	.90	.70	.70	.70
Financial	.81	.80	.69	1.01	1.20	1.00
Bonds--total[1]	6.11	7.13	8.61	7.18	11.75	3.50
By industry						
Nonfinancial	2.80	3.30	4.48	4.14	7.55	50
Utility	.87	.88	1.51	.79	.90	.20
Industrial	1.93	2.42	2.97	3.35	6.65	2.30
Financial	3.31	3.83	4.13	3.04	4.20	5.00
By quality[3]						
Aaa and Aa	1.85	2.23	3.01	1.23	1.90	2.90
A and Baa	2.11	2.80	2.63	3.96	5.95	3.05
Less than Baa	1.08	1.23	1.71	.86	1.65	1.65
No rating (or unknown)	.26	.27	.28	.39	.75	.35
Memo items:						
Equity based bonds[4]	.50	.61	.82	.44	.58	1.3
Mortgage-backed bonds	.81	.60	.98	.74	1.50	.55
Variable rate notes	.72	1.29	.51	.99	2.55	.75
Bonds sold abroad - total	1.88	2.23	2.79	2.99	1.26	2.80
Nonfinancial	.84	.97	1.08	1.07	.39	1.40
Financial	1.04	1.26	1.71	1.92	.87	1.40

p--preliminary.
1. Securities issued in the private placement market are not included. Total reflects gross proceeds rather than par value of original discount bonds.
2. Includes equity issues associated with debt/equity swaps.
3. Bonds categorized according to Moody's bond ratings. Excludes mortgage-backed bonds.
4. Includes bonds convertible into equity and bonds with warrants attached where the warrants entitle the holder to purchase equity in the future.

nonfinancial firms has been at or below the average of the past 5 years. Stock offerings by public utilities and airlines have been relatively strong, while the volume for other industrials has been low.

U.S. Government Securities Markets

The staff is projecting a combined (on- and off-budget) deficit for the current quarter of about $33 billion. The Treasury is expected to meet its financing requirements for the quarter by net borrowing of about $38 billion from the public, allowing for a small rise in cash balances. The Treasury is raising an even larger-than-usual share of its new money in auctions of marketable coupon issues. The sale of $20.5 billion of securities in May was a record for any mid-quarter financing, but the amount of new funds raised totaled $9.9 billion, less than the all-time high of $11.2 billion in the February 1984 refunding. The mid-quarter financing went well by all of the usual criteria and, in general, the government securities market has continued to function smoothly despite the recent dealer failures. Nonetheless, some small dealers have found it a bit harder to obtain financing.

The Treasury is continuing to expand its STRIPs program, with both the 10- and 30-year securities issued in the mid-quarter financing eligible. The Treasury has announced that the STRIPS program will be modified by assigning "generic CUSIP" numbers to all coupons on securities eligible for STRIPS that are payable on the same date, regardless of the original security from which they were stripped. As a result, they will be interchangeable in trading and at delivery, increasing their liquidity in the secondary market.

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

	1985				
	Q1	Q2[f]	April[p]	May[f]	June[f]
Treasury financing					
Combined surplus/deficit(-)	-58.6	-33.0	8.9	-38.4	-3.5
Means of financing deficit:					
Net cash borrowing from the public	41.8	37.6	17.0	19.9	.7
Marketable borrowings/ repayments(-)	37.0	34.2	16.0	18.0	.2
Bills	5.1	1.9	.4	6.0	-4.5
Coupons	31.9	32.3	15.6	12.0	4.7
Nonmarketable	4.8	3.4	1.0	1.9	.5
Decrease in the cash balance	3.7	-5.6	-26.1	22.3	-1.8
Memo: Cash balance at end of period	13.9	19.5	40.0	17.7	19.5
Other[2]	13.1	1.0	.2	-3.8	4.6
Federally sponsored credit agencies, net cash borrowing[3]	3.6	1.9	0	.7	1.2
FHLB	.2	.1	-.2	.1	.2
FNMA	2.6	2.2	.7	.8	.7
Farm Credit Banks	-1.1	-1.5	-.8	-.7	0
FHLMC	1.4	.5	.2	.2	.1
SLMA	.5	.6	.1	.3	.2

f--staff forecast. p--preliminary.
1. Data reported on a not seasonally adjusted, payment basis.
2. Includes checks issued less checks paid, accrued items and other transactions.
3. Excludes mortgage pass-through securities issued by FNMA and FHLMC.

Borrowing by the sponsored credit agencies was negligible on balance in April after remaining moderate in the first quarter, when net funds raised totaled about $3-1/2 billion. Fannie Mae accounted for most of this borrowing; its mortgage purchases have picked up sharply since the fourth quarter of last year. In addition to its borrowing, Fannie Mae recently issued $100 million of common stock, raising its ratio of stockholders' equity to total assets only slightly to a still low 1.4 percent.

Net issuance of debt was light at the Federal Home Loan Banks and negative at the Farm Credit Banks in the first quarter. The increase in advances by thrift institutions was small, on a not seasonally adjusted basis, and the FHLBs financed them through the deposits of member institutions and by drawing down liquid assets. Borrowing by the Farm Credit Banks has been slack for some time, as increased financial strain among farmers has resulted in a decline in their farm loans outstanding.[1] There is still no evidence that the farm sector problem is affecting the ability of the Farm Credit Banks to sell securities: their most recent issues came at yields very close to those on Treasury securities.

Tax-Exempt Securities Markets

Issuance of all tax-exempt bonds has trended up since early this year; in April, offerings totaled $9.5 billion, and issuance continued near this pace in early May. In the short-term market, offerings of notes had been coming to market at the rate of about $700 million a month, but April's

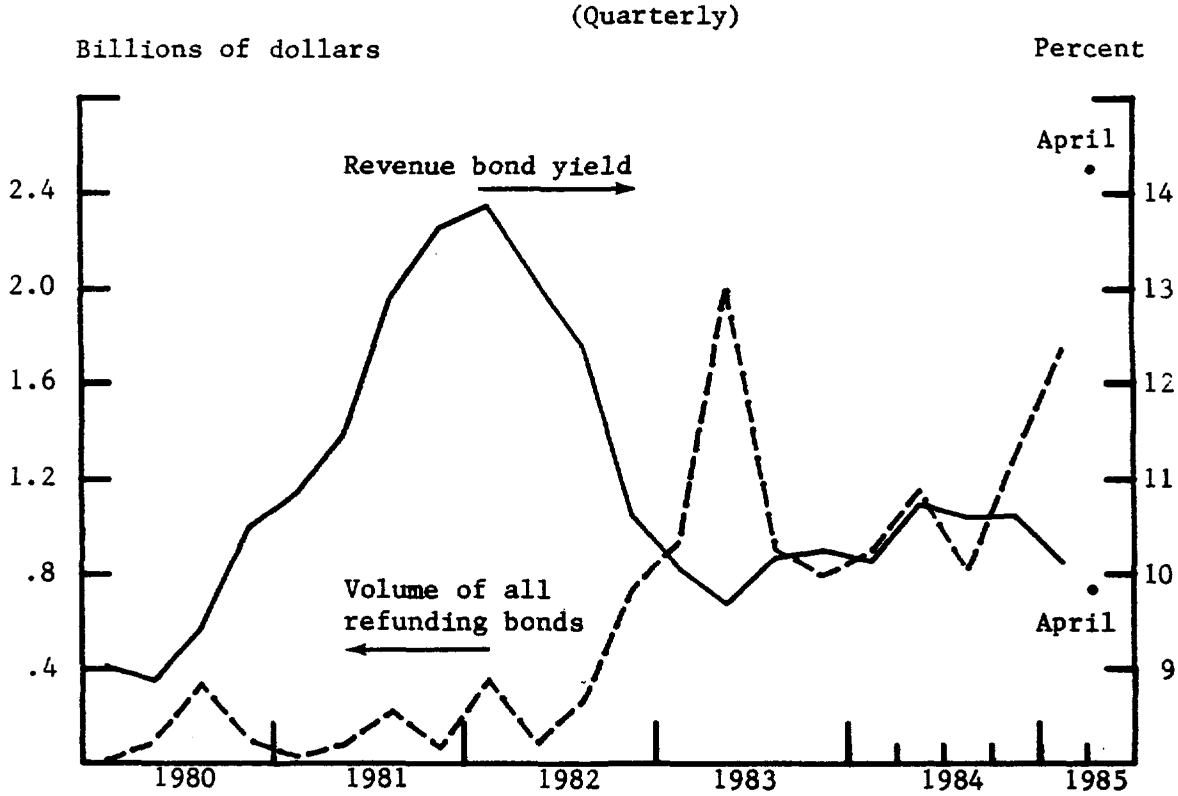
1. In addition, farm loans at commercial banks showed a large decline in the first quarter, following a small increase over 1984. The recent fall in farm credit advanced by private lenders has been partly offset by increased lending at the Farmers Home Administration, particularly under their regular programs rather than the new debt adjustment program.

GROSS OFFERINGS OF TAX-EXEMPT SECURITIES
(Monthly rates, not seasonally adjusted, billions of dollars)

	1984			1985		
	Year	Q3	Q4	Q1p	Mar.p	Apr.p
Total	10.52	11.03	15.45	7.83	8.50	14.70
Short-term[1]	1.70	1.95	1.13	.69	.70	5.20
Long-term	8.82	9.08	14.32	7.14	7.80	9.50
Refundings[2]	1.04	.81	1.30	1.74	1.30	2.50
New Capital	7.78	8.27	13.02	5.40	6.50	7.00
Total Housing	1.57	3.05	2.17	1.23	2.02	1.50
Single-family[3]	.92	2.69	1.25	.56	1.30	1.10

p--preliminary.
1. These figures do not include tax-exempt commercial paper.
2. Includes all refunding bonds, not just advance refundings.
3. Data from the Department of Housing and Urban Development.

TAX-EXEMPT REFUNDING BONDS
(Quarterly)



volume jumped to $5.2 billion, as New York state, in its annual spring financing, issued tax and revenue anticipation notes totaling $4.3 billion.

Offerings of long-term tax-exempt securities have been buoyed this year by a large volume of refunding bonds (see chart), as rates moved below 10 percent in January and again in April. Underwriters report that when market yields are as much as 2 to 3 percentage points below rates on outstanding bonds, the potential cost saving is great enough for state and local units to issue refunding bonds. Offerings of these bonds rose to around $2.5 billion in April and a large amount currently is scheduled again for May.

Municipal bond volume in April also may have been augmented by an expected legislated constraint. Under the Deficit Reduction Act of 1984, bonds that have federal guarantees are ineligible for tax-exemption. A recent court decision suggests that securities backed by letters of credit (LOCs) issued by FDIC-insured banks could be construed as having federal guarantees.[1] The IRS originally had announced that municipal bonds backed by LOCs of federally insured banks could lose their tax-exempt status if issued after May 1, and some financings were moved ahead to beat that deadline. However, in late April, the deadline was postponed to January 1, 1986.

As of mid-May, the Bond Buyer 30-year revenue index had fallen nearly 70 basis points since the last FOMC meeting, somewhat more than the decline in taxable bond yields. At the shorter end of the market, 1-year prime-grade G.O. bonds, at 5.00 percent, were down 50 basis points from their March FOMC level.

1. In December 1984, the U.S. Court of Appeals for the 10th Circuit in Denver ruled that the FDIC had to back up a letter of credit issued by Penn Square Bank, which failed in July 1982.

Mortgage Markets

Costs of home mortgage finance have declined since the last FOMC meeting, nearing the lows of mid-February. Commitments for fixed-rate mortgage loans at selected S&Ls were available at an average contract rate of 13.02 percent for the week ending May 10, 27 basis points below the recent peak in late March. Rates on one-year adjustable-rate mortgages offered by some of these same S&Ls dropped a bit more, and the initial rate advantage on these ARMs widened to 240 basis points, probably reflecting the steepening of the yield curve. Adjustable-rate mortgages accounted for 49 percent of all conventional loans closed in early April--a share that has changed little since last December and is considerably below what was observed in early 1984.

In the market for federally underwritten mortgages, which have accounted for approximately 15 percent of all home loans originated recently, price discounts on GNMA-guaranteed securities issued against pools of FHA and VA mortgages shrank to less than one point in mid-April. In response, on April 19, the Veterans Administration lowered the ceiling rate on its regular VA-guaranteed loans to 12.50 percent, reversing the 50 basis point increase authorized just three weeks earlier.

With continued strong credit demand, total residential mortgage debt growth has remained vigorous in the first quarter, accommodated primarily by strong increases in FNMA portfolio holdings and by heavy issuance of federally-guaranteed mortgage pass-through securities. However, preliminary April data indicate that new issues of these securities dropped off. Mortgage activity at FSLIC-insured thrift institutions generally has been weak so far this year. First-quarter growth in holdings of mortgage-related

MORTGAGE ACTIVITY AT FSLIC-INSURED INSTITUTIONS
(Billions of dollars, seasonally adjusted)

	Mortgage commitments		Net change in mortgage assets[1]		
	New (1)	Outstanding[2] (2)	Total (3)	Mortgage loans (4)	Mortgage-backed securities (5)
1984-May	20.1	70.3	10.9	8.4	2.5
June	18.8	71.3	10.9	8.3	2.6
July	18.1	72.3	8.8	8.2	.6
Aug.	16.6	71.4	9.0	6.6	2.5
Sept.	15.9	70.5	6.4	5.9	.5
Oct.	16.9	69.2	5.5	5.2	.3
Nov.	16.9	69.2	4.5	5.9	-1.4
Dec.	17.5	69.6	3.4	2.8	.6
1985-Jan.	16.9	68.7	3.5	4.3	-.9
Feb.	16.1	68.6	3.2	2.5	.6
Mar.	16.0	67.9	5.1	5.0	.1

1. Data are adjusted to account for structural changes through mergers, acquisitions, liquidations, terminations, or de novo institutions.
2. End of month. Includes loans in process.

NEW ISSUES OF FEDERALLY GUARANTEED MORTGAGE PASS-THROUGH SECURITIES
(Monthly averages, billions of dollars, not seasonally adjusted)

Period	Total	GNMAs	FHLMCs	FNMAs	Memo: FNMA and FHLMC swap issues
1983-Q1	7.1	3.8	2.0	1.3	2.2
Q2	7.4	4.8	1.4	1.2	1.9
Q3	7.6	4.8	1.5	1.2	2.1
Q4	5.7	3.4	1.7	.7	2.0
1984-Q1	4.9	2.7	.9	1.3	1.6
Q2	4.0	2.3	1.1	.5	1.5
Q3	5.1	2.2	1.4	1.5	2.7
Q4	6.1	2.0	2.8	1.3	3.6
1985-Q1	6.3	2.7	2.3	1.3	2.9
Aug.	5.8	2.4	1.6	1.9	3.3
Sept.	4.2	1.9	1.1	1.1	2.1
Oct.	6.2	2.5	2.6	1.1	3.4
Nov.	4.6	1.4	2.0	1.2	2.7
Dec.	7.5	2.1	3.8	1.6	4.7
1985-Jan.	5.5	2.7	2.0	.9	2.3
Feb.	6.9	2.7	2.4	1.8	3.3
Mar.	6.4	2.8	2.5	1.1	3.0
Apr. p	5.3	2.6	1.9	.9	2.3

p--preliminary.

assets by thrift institutions was the slowest since mid-1982, despite a pickup in March, and new commitments to originate or purchase mortgages were off in March, though much less than in the previous two months. As noted earlier, lending by some S&Ls likely is being constrained by the FHLBB net worth regulations that have been in effect since the beginning of the year.

Recently inaugurated purchase programs at FNMA and FHLMC have spurred use of two less common mortgage forms. Mortgages with 15-year maturities accounted for 20 percent of all conventional fixed-rate home loans closed in early March; both agencies have been buying substantial volumes in response to attractive yields and strong investor demand. Another type, known as convertible ARMs, offers the borrower the option of later switching to a fixed-rate payment schedule without incurring many of the usual refinancing fees; this instrument has accounted for approximately half of FNMA's growing (though still limited) ARM purchases in recent months.

Consumer Installment Credit

Partial data suggest that consumer installment credit continued to expand rapidly during April, perhaps matching the 22 percent gain in the first quarter. Growth of consumer credit has been unusually robust during the current expansion; the cumulative growth of total consumer installment credit has increasingly outstripped the average for the five previous business cycle recovery periods. The strength in the current expansion in part reflects vigorous growth in expenditures for autos and other consumer durable goods. Recently, some households may have used consumer credit to finance household expenditures pending the arrival of refund checks.

CONSUMER INSTALLMENT CREDIT

	1983	1984	1984 Q4	1985 Q1	1985 Jan.	1985 Feb.	1985 Mar.
	——— Percent rate of growth, SAAR ———						
Change in outstandings--total	14.6	20.0	17.1	21.8	19.2	23.6	21.4
By type:							
Automobile credit	13.4	20.6	18.8	22.0	20.1	21.9	22.8
Revolving credit	17.7	23.9	20.1	30.0	24.7	31.3	31.8
All other[1]	14.0	17.5	14.0	17.3	15.4	21.2	14.6
	——— Billions of dollars, SAAR ———						
Change in outstandings--total	48.7	76.8	74.1	98.4	86.7	108.5	100.1
By type:							
Automobile credit	16.9	29.5	31.0	37.9	34.6	38.4	40.7
Revolving credit	12.4	19.6	18.2	28.5	23.5	30.3	31.6
All other[1]	19.5	27.8	25.0	32.1	28.6	39.8	27.8
By major holder:							
Commercial banks	19.5	40.4	33.1	54.9	45.6	60.9	58.2
Finance companies	9.3	9.3	9.5	16.6	10.8	14.4	24.6
All other	20.0	27.1	31.6	27.0	30.3	33.2	17.4
	——— Annual percentage rate ———						
Interest rates							
At commercial banks[2]							
New cars, 48 mos.	13.92	13.71	13.91	13.37	n.a.	13.37	n.a.
Personal, 24 mos.	16.68	16.47	16.63	16.21	n.a.	16.21	n.a.
Credit cards	18.78	18.77	18.82	18.85	n.a.	18.85	n.a.
At auto finance companies[3]							
New cars	12.58	14.62	15.22	13.85	15.11	13.78	12.65
Used cars	18.74	17.85	18.28	17.86	17.88	17.91	17.78

1. Includes primarily personal cash loans, home improvement loans, mobile home loans, and sales finance contracts for non-automotive consumer durable goods.
2. Average of "most common" rates charged, on loans of specified type and maturity, during the first week in the middle month of each quarter.
3. Average rate for all loans of each type made during the period, regardless of maturity.
n.a.--not available.

The growth of consumer installment credit has been strong at depository institutions, especially reflecting the attractive margins on various types of consumer loans and unusually favorable delinquency rates.[1] On balance, bankers sampled in the Survey of Senior Loan Officer Opinion in February reported a further increase in willingness to extend consumer credit. Banks have been regaining market share that other lenders, particularly captive finance companies, absorbed between 1979 and 1983. However, during February captive finance companies reduced new-auto loan rates 1-1/4 percentage points, shrinking the rate advantage typically enjoyed by banks. Special interest rate incentives at these finance companies have been extended through May.

Other depository institutions have sought to increase their participation in the consumer credit market. Thrift institutions have continued to respond to the broader lending powers provided by the Depository Institutions Deregulation and Monetary Control Act. In addition, federal credit union lending activity has been boosted by regulatory changes that broadened requirements for membership eligibility.

1. Despite an increase in delinquency rates at captive auto finance companies since mid-1984, these rates remain in a historically low range.

APPENDIX A*

BANKERS ACCEPTANCES IN THE MEASURE OF SHORT- AND INTERMEDIATE-TERM BUSINESS CREDIT

In recent years the analytic focus of the measure of short- and intermediate-term business credit, shown in the table on p. III-6, has been shifting. Formerly, this measure focused on funds raised in U.S. markets for business purposes, regardless of whether the proceeds were used to finance business activity in the United States or abroad. More recently, the measure has focused increasingly on the total volume of funds raised to finance business activity in the United States, regardless of whether the funds were raised in U.S. markets or abroad. Specifically, in the bank loan component of this grouping of business credit, business loans to U.S. residents that are booked at foreign branches of U.S. banks now are included and business loans to foreign residents that are booked at international banking facilities are excluded.

In light of this change in focus, the treatment of bankers acceptances has been revised. Previously, this business credit measure included total outstanding U.S. dollar-denominated bankers acceptances that were payable in the United States, regardless of the nature of the transaction financed by the acceptance. The revised series includes only those acceptances that are related to U.S. trade--that is, those acceptances that finance U.S. imports, U.S. exports, domestic shipment or domestic storage of goods. Excluded are those acceptances that are related to foreign trade--that is, those acceptances that finance shipment of goods between foreign countries or storage of goods in foreign countries.

As shown on the table below, U.S. trade related acceptances grew 6 percent last year, compared with a 1-1/2 percent contraction of total acceptances. Total short- and intermediate-term credit is now estimated to have expanded at an 18 percent annual rate in 1984, up from 16-1/2 percent before the revision. The effect of this revision of the acceptance component is significant for two reasons: first, as indicated on the table, the volume of U.S. trade related acceptances is only about half of all acceptances; and second, total bankers acceptances have not grown on balance since the end of 1982, with particularly pronounced weakness in 1984 in the components related to foreign trade.

The weakness in total bankers acceptances over the past two years has developed despite a significant liberalization of regulations governing the creation of reserve-free acceptances in October 1982. Prior to October 1982, the creation of reserve-free acceptances by member banks was subject to an aggregate limitation of 50 percent of capital and surplus (100 percent with prior Board approval). With the rapid growth of the acceptance market during the 1970s, some major banks reached this limit. Although an increasing share of demands for acceptance financing was met

* Prepared by Patrick Parkinson and Frederick Jensen, Economists, Banking Section, Division of Research and Statistics. Chinhui Juhn and Sukkoo Kim provided valuable research assistance.

by regional banks and by nonmember banks and U.S. agencies and branches of foreign banks, which were not subject to aggregate acceptance limits, the aggregate supply of acceptance financing apparently was significantly constrained by the regulatory ceilings, and spreads on acceptance financing (acceptance commissions) reportedly averaged more than 100 basis points. The Bank Export Services Act of 1982 raised the aggregate ceiling on the creation of reserve-free acceptances to 150 percent of capital and surplus (200 percent with Board approval) and applied the new ceiling uniformly to member banks, nonmember banks, and U.S. agencies and branches of foreign banks. This action effectively removed the constraint on the aggregate supply of acceptance financing since few, if any, institutions have approached the new ceilings.

Growth in Bankers Acceptances and Short- and Intermediate-Term Business Credit
(Seasonally adjusted annual rates)

	Bankers Acceptances		Short- and Intermediate-Term Business Credit[3]	
	U.S. Trade Related (Revised Series)[1]	Total (Old Series)[2]	Revised Series	Old Series
Annual				
1982	13.8	12.9	8.0	8.0
1983	-2.8	-0.7	5.1	4.8
1984	6.1	-1.4	17.9	16.4
Quarterly				
1984-Q1	-4.6	-9.0	19.4	17.5
Q2	39.9	47.6	22.6	24.4
Q3	-3.2	-16.0	10.9	8.6
Q4	-6.5	-24.8	14.4	11.4
1985-Q1	-5.5	2.1	7.5	7.6
Levels in billions of dollars: March 1985	36.1	75.1	742.7	781.7

1. U.S. dollar-denominated eligible acceptances, payable in the U.S., that finance U.S. imports, U.S. exports, domestic shipment or domestic storage of goods.
2. Total U.S. dollar-denominated eligible acceptances, payable in the U.S. In addition to U.S. trade related acceptances, includes acceptances that finance shipment of goods between foreign countries, storage of goods in foreign countries and dollar-exchange acceptances.
3. Short- and Intermediate-Term Business Credit, shown in the table on page III-6, consists of business loans at commercial banks (excluding acceptances), commercial paper of nonfinancial businesses, U.S. trade related bankers acceptances and business loans at finance companies.

Immediately following the removal of the supply constraint, acceptances grew at a 13 percent annual rate in the fourth quarter of 1982. At the same time, acceptance commissions reportedly narrowed. The lack of growth in outstanding acceptances since the end of 1982, combined with reportedly thin acceptance commissions, suggest that demand has stagnated. This conclusion is supported by other evidence, including the views expressed by corporate lending officers in the April 23, 1985 Senior Loan Officer Opinion Survey on Bank Lending Practices (LPS). In addition, banks seem to have become more reluctant to finance this activity at narrow margins.

The demand for acceptance financing is related to the volume of eligible trade transactions and the availability and relative cost of alternative sources of funds. The volume of eligible trade transactions most likely has grown sluggishly, if at all, over the past several years. Worldwide international trade actually contracted in the early 1980s as a result of global recession and the financing difficulties encountered by many developing countries. Moreover, the value of shipments of oil and other commodities, which frequently are financed with acceptances, fell particularly sharply as prices of many of these goods declined. Almost 40 percent of the 60 large banks responding to the April LPS indicated that a reduction in the volume of eligible transactions has contributed to the sharp declines on balance in the volume of acceptance financing since mid-1984.

More importantly, the demand for acceptance financing also has been reduced in recent years by substitution of alternative, less costly forms of financing. Eighty percent of the respondents to the April LPS identified the increased availability of alternative sources of funds as another factor depressing the use of acceptance financing. A large proportion of the acceptances created by domestic banks are essentially interbank loans. Many foreign banks, primarily Japanese and other Asian banks and to a degree Scandinavian banks, have relied on U.S.-chartered banks to refinance their own acceptances.[1] But in recent years Japanese banks apparently have met an increasing share of their financing requirements by substituting Eurodollar CDs and interbank borrowings for acceptance financing. Although

1. After accepting a draft from their own customers, these banks often draw a draft on a U.S. bank for acceptance, thereby creating an acceptance in the U.S. market. The U.S. banks then typically resell these acceptances in the secondary markets and charge the foreign banks a commission, or spread, over and above the rates the U.S. banks pay on their acceptances. Results of the April LPS suggest that roughly 60 percent of the acceptances outstanding at the end of March 1985 were loans to foreign banks for the purpose of refinancing their customers' eligible trade transactions. Acceptance credit extended to U.S. corporate customers accounted for only 17 percent of aggregate acceptance volume at these banks, while foreign customers other than banks accounted for most of the remainder.

the total of acceptances is not affected, Japanese banks also have issued more of their own acceptances directly in the U.S. market rather than refinancing through U.S. banks.[1]

The availability of funding for Japanese banks in the U.S. acceptance market and the Eurodollar CD market in London has increased dramatically in recent years as investors in these markets, primarily U.S. residents, apparently have favorably reassessed the risks associated with claims on Japanese banks. For top rated Japanese banks, the costs of directly issuing acceptances or Eurodollar CDs are generally less than the all-in cost of refinancing acceptances through U.S. banks (the all-in cost is the sum of the acceptance commission and the rate on the U.S. bank's own acceptance). Top tier Japanese acceptances and CDs reportedly now trade at less than 10 basis points above the rates on acceptances issued by prime U.S. banks. Respondents to the April LPS indicated that acceptance commissions on refinancings for prime foreign banks have averaged about 38 basis points recently, implying an all-in cost about 30 basis points higher than the cost to Japanese banks of issuing their own acceptances or Eurodollar CDs to finance eligible transactions. Eurodollar interbank borrowings also have become more attractive relative to refinancings through the acceptance market. Since October 1982 the spread between LIBOR and acceptance rates has fallen from more than 100 basis points to about 30 basis points.

The demand for acceptance financing by U.S. corporations also likely has been restrained in recent years by the spread of attractive financing alternatives. More firms have gained access to the commercial paper market and the volume of outstanding paper has grown considerably. In addition, banks have offered an increasing number of corporations an expanded menu of below-prime pricing options. Loan commitments now frequently offer pricing tied to LIBOR or the effective cost of domestic CDs. To date, however, a bankers acceptance pricing option generally has not been available under loan commitments; 77 percent of the respondents to the April LPS indicated that such an option is offered seldom or is never offered. Consequently, the use of acceptance financing creates an opportunity cost if a corporation pays a fee on the unused portion of a loan commitment.

The growth of the acceptance market also may have been restrained over the last year by a decrease in the willingness of banks to offer acceptance financing. With the decline in acceptance commissions since the liberalization of capital limits, acceptance financing is now regarded as a relatively low-margin business. Under pressure from financial markets and regulatory authorities to reduce leverage, some banks have attempted to reduce the growth of low-margin assets, including acceptance financing. About 37 percent of the respondents to the April LPS reported that attempts to increase commissions or to avoid low-margin activities have led to a decrease in the supply of acceptances in recent months.

1. Since October 1982, Eurodollar CDs outstanding at London branches of Japanese banks increased from $17 to $30 billion. Over the same period, acceptance liabilities of U.S. agencies and branches of Japanese banks have doubled to more than $17 billion.

Foreign Exchange Markets

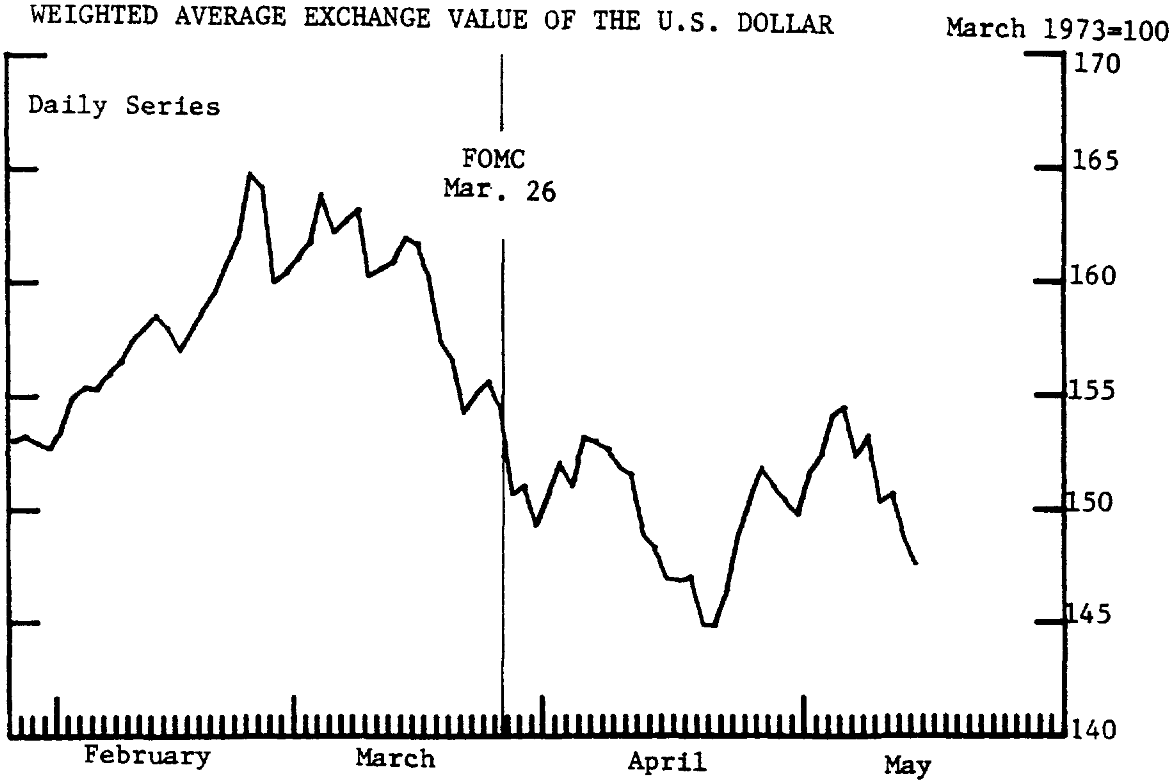
On balance since the last FOMC meeting, the weighted-average foreign exchange value of the dollar, displayed in the top panel of the chart, has depreciated 4-1/2 percent. Shifting perceptions about the strength of economic activity in the United States, about the stability of certain U.S. financial institutions, and about the associated responses of monetary policy and interest rates to these factors appeared to be the primary influences on exchange rate movements over the period.

Over the first four weeks following the last FOMC meeting, the dollar experienced a net depreciation of 7-1/4 percent, bringing the total decline from its late February peak to about 12 percent. The unexpectedly low "flash" estimate of U.S. GNP growth in the first quarter released just before the last meeting, sparked a steep decline in the dollar's value in the first week of the intermeeting period. The dollar rebounded 2-1/2 percent early in April in response to stronger than expected March data for U.S. employment and leading indicators; but downward pressure re-emerged after release of further indications of slowing economic activity and of difficulties at some U.S. financial institutions. In mid-April, the weighted-average value of the dollar reached its lowest level in 5 months following news that first quarter GNP was estimated to have indeed grown only at a 1.3 annual percent rate. By that time, short-term dollar interest rates had fallen about 60 basis points since the last FOMC, while a weighted-average of comparable foreign rates had also eased, but somewhat less. This widening of the interest differential in favor of assets denominated in foreign currencies during the first half of the intermeeting period can be seen in the bottom panel of the chart.

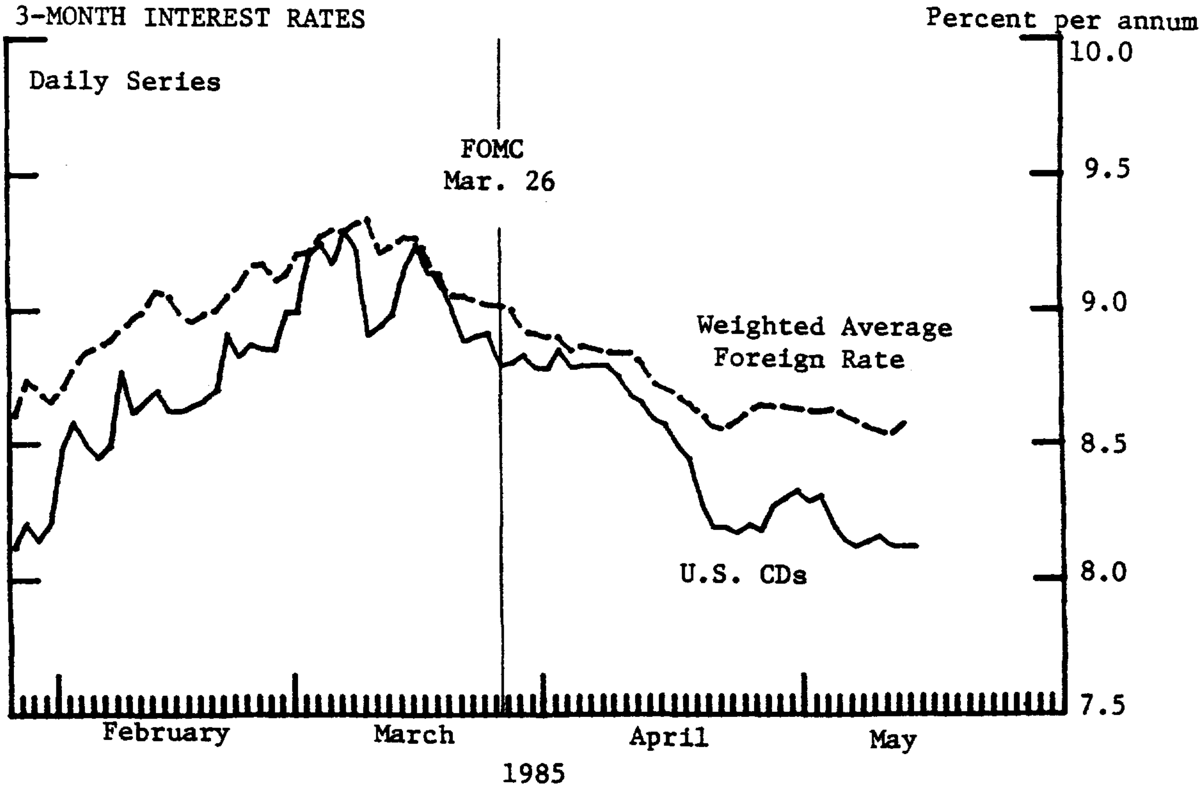
In the ensuing two-week period, the dollar appreciated about 3-1/2 percent, apparently in response largely to predictions by U.S. public officials that U.S. economic growth would pick up over the remainder of 1985. As can also be seen in the bottom panel of the chart, short-term dollar interest rates rose slightly more rapidly than foreign rates during that time. In the final week of the intermeeting period, a series of statements by U.S. public officials about the near-term prospects for U.S. economic growth heightened market uncertainty about the future course of dollar interest rates. The dollar declined while market commentary indicated an increasing expectation that the Federal Reserve would move toward an easing of monetary conditions. Currently, the weighted-average value of the dollar stands 10 percent below its peak in late February.

Sterling has fluctuated over an unusually wide range since the last FOMC meeting, and has appreciated a particularly sharp 7-1/2 percent against the dollar and 4 percent on a weighted-average basis. Indications that growth in sterling M3 continued to exceed its target range appeared to increase expectations that any reduction in sterling interest rates would be delayed, providing support for the pound. On balance over the inter-meeting period, declines in short-term sterling interest rates have kept pace with the fall in comparable dollar rates, but the reductions in sterling interest rates were nonetheless smaller than earlier anticipated. Several reductions in U.K. base lending and money market dealing rates were announced, and the key sterling 3-month interbank rate had fallen nearly 1 percentage point to approximately 12-1/2 percent by the end of the intermeeting period.

WEIGHTED AVERAGE EXCHANGE VALUE OF THE U.S. DOLLAR



3-MONTH INTEREST RATES



External lending by BIS-reporting banks in 1984. Cross-border claims of all BIS-reporting banks increased by $126 billion in 1984, after adjustment to offset the effect of exchange rate changes on the dollar value of the stock of non-dollar claims. This increase, amounting to about six percent, was somewhat greater than in 1983, and followed two years of sharp reductions in total net new bank lending. However, new lending to the non-OPEC developing countries declined for the third successive year, and that to the OPEC countries was almost nil.

In 1984, the only group of countries to which the reporting banks significantly stepped up their lending was that group combining the reporting area countries (most of the industrial countries) and offshore banking centers. These two components were almost fully merged in December 1983 when all banks in most offshore centers became part of the reporting area. (See footnote 3 on table.) The acceleration in lending to these countries was entirely the result of a higher rate of interbank lending between non-U.S. banks. Net new lending to Eastern Europe shifted from negative to positive but the swing was only $3 billion. Net new lending to OPEC countries fell from $10 billion in 1983 to $1 billion last year as claims on these countries either rose more slowly or in some cases (Arabian Gulf States, Nigeria, Venezuela) declined absolutely.

The further drop from $12 billion in 1983 to $9 billion in 1984 in lending to the non-OPEC developing countries was concentrated in Latin America, but lending to the Asian and African countries remained

EXTERNAL CLAIMS OF BIS-REPORTING BANKS
(Billions of dollars)

	Change (no sign = increase)				Outstanding
	1981	1982	1983	1984	12/31/84
Total, all countries	265	180	105	126	2,154
(Memo: unadjusted basis)	(220)	(144)	(62)	(60)	—
Non-OPEC developing countries	40	20	12	9	329
(Latin America)	(30)	(12)	(8)	(4)	(211)
(Others)	(10)	(8)	(4)	(5)	(118)
OPEC Countries	4	8	10	1	106
Eastern Europe	5	-5	-2	1	49
Smaller developed countries[2]	17	16	7	8	90
Reporting area and off-shore banking centers[3]	192	128	73	111	1,547
Miscellaneous	7	13	4	-1	34

1. Adjusted for statistical effect of exchange rate changes.
2. Excluding Finland, Norway and Spain as from December 1983. (See footnote 3.)
3. In December 1983, the reporting area was expanded to include three of the smaller developed countries (Finland, Norway and Spain) as well as banks in six offshore banking centers (Bahamas, Bahrain, Cayman Islands, Hong Kong, Netherlands Antilles, and Singapore). Previously, of the banks in these centers only the U.S. branches in the Bahamas, Cayman Islands, Hong Kong and Singapore were included, along with U.S. bank branches in Panama, which continue to be included.

depressed at around one-half the 1981 rate. The reduced lending to Latin America mainly reflected smaller non-spontaneous lending to Argentina, Chile, Mexico and Peru, partly offset by greater such lending to Brazil. In addition, bank claims on Brazil were reduced by sales of some claims to nonbank foreign investors, mostly multinational corporations.

U.S. INTERNATIONAL FINANCIAL TRANSACTIONS

Data now available on banking, securities and official capital transactions in the first quarter of 1985 account for about sixty percent of the financial counterpart to the large estimated current account deficit over the same period. Sizeable net capital inflows were recorded by banks and through private foreign net purchases of U.S. corporate bonds. Private foreign net purchases of U.S. Treasury obligations accounted for a moderate inflow, though greatly diminished from that recorded in the fourth quarter of 1984. These inflows were somewhat offset by a large recorded net outflow of foreign official reserve assets held in the United States. (See Summary of U.S. International Transactions table.)

Private foreign net purchases of U.S. corporate bonds were strong for the second consecutive quarter, totalling more than $10 billion (see line 2a). This figure mainly reflects a large volume of new issues of U.S. corporate bonds in late 1984 and early 1985. Since there is a lag between the offering date and the payment date on bond issues, the monthly pattern of new issues and the pattern of recorded sales in the balance of payments statistics do not coincide. The pause in underwriting activity in February and March and the buildup of underwriters' inventories, which may have reflected uncertainty over the course of interest rates, will likely be more fully reflected in the second quarter. Unofficial data suggests that more vigorous issuance has resumed in April and the first half of May.

SUMMARY OF U.S. INTERNATIONAL TRANSACTIONS
(Billions of dollars)

	1983 Year	1984 Year	1984 Q1	1984 Q2	1984 Q3	1984 Q4	1985 Q1	1985 Jan.	1985 Feb.	1985 Mar.
Private Capital										
Banks										
1. Change in net foreign positions of banking offices in the U.S. (+ = inflow)	13.4	22.0	12.9	0.7	9.9	-1.6	17.9	9.1	5.1	3.8
Securities										
2. Private securities transactions, net	1.6	8.0	2.2	-0.2	0.3	5.7	7.1	1.7	4.3	1.1
a) foreign net purchases (+) of U.S. corporate bonds	2.2	13.8	0.5	0.6	2.6	10.1	10.6	3.0	4.7	2.9
b) foreign net purchases (+) of U.S. corporate stocks	6.4	-0.8	1.0	-0.1	-1.0	-0.8	-1.1	-0.7	0.1	-0.5
c) U.S. net purchases (-) of foreign securities	-7.0	-5.0	0.7	-0.7	-1.3	-3.6	-2.4	-0.6	-0.5	-1.4
3. Foreign net purchases (+) of U.S. Treasury obligations 1/	8.3	22.5	1.4	6.5	5.1	9.5	2.7	0.9	0.7	1.0
Official Capital										
4. Changes in foreign official reserve assets in U.S. (+ = increase)	5.2	2.7	-3.0	-0.8	-0.5	7.1	-10.9	-3.8	-3.5	-4.0
a) By area										
G-10 countries (incl. Switz.)	6.4	3.1	2.3	-0.7	-0.8	2.2	-5.5	0.1	-2.6	-3.4
OPEC	-8.5	-5.3	-2.8	-2.4	-0.6	0.6	-1.7	-0.5	-1.7	0.6
All other countries	7.3	5.0	-2.6	2.4	0.8	4.3	-3.8	-3.4	0.8	-1.2
b) By type										
U.S. Treasury securities	7.0	4.7	-0.3	-0.3	-0.6	5.8	-7.2	-0.8	-3.4	-3.5
Other 2/	-1.7	-2.0	-2.8	-0.5	**	1.2	-3.7	-3.0	-0.1	-0.6
5. Changes in U.S. official reserve assets (+ = decrease)	-1.2	-2.7	-0.7	-0.6	-0.8	-1.1	-0.2	0.4	-0.4	-0.2
Other transactions (Quarterly data)										
6. U.S. direct investment (-) abroad	-4.9	-6.0	-3.5	2.1	1.9	-6.6	n.a.	n.a.	n.a.	n.a
7. Foreign direct investment (+) in U.S.	11.3	21.2	2.4	8.8	5.3	4.7	n.a.	n.a.	n.a.	n.a
8. Other capital flows (+ = inflow) 3/ 4/	-1.4	3.9	2.0	4.9	-1.4	-1.0	n.a.	n.a.	n.a.	n.a
9. U.S. current account balance 4/	-41.6	-101.6	-19.7	-24.7	-33.6	-23.7	-27.5 e/	n.a.	n.a.	n.a
10. Statistical discrepancy 4/	9.3	30.0	6.0	3.3	13.8	7.0	n.a.	n.a.	n.a.	n.a
MEMO:										
U.S. merchandise trade balance -- part of line 9 (Balance of payments basis, seasonally adjusted)	-61.1	-107.4	-25.2	-25.4	-32.4	-24.4	-28.3	-10.8	-8.0	-9.5

1. Includes U.S. Treasury notes publicly issued to private foreign residents.
2. Includes deposits in banks, commercial paper, acceptances, & borrowing under repurchase agreements.
3. Includes U.S. government assets other than official reserves, transactions by nonbanking concerns, and other banking and official transactions not shown elsewhere.
4. Includes seasonal adjustment for quarterly data.
* Less than $50 million.
e/ Estimated.
NOTE: Details may not add to total because of rounding.

Private net purchases of U.S. Treasury securities totalled less than $3 billion in the first quarter, which is considerably smaller than the net purchases recorded in the previous three quarters. A portion of the diminished foreign demand for Treasury securities may be related to the fact that Japanese Trust Banks are approaching the limit on the proportion of pension fund assets which may be invested in securites denominated in foreign currencies.

In the first quarter foreign official holdings in the United States declined by nearly $11 billion reflecting substantial net intervention sales of dollars during the period. Reductions in the holdings of G-10 countries accounted for nearly one half of the total. Preliminary information indicates that official holdings at the FRBNY are essentially unchanged in April.

There was a massive net inflow from abroad and IBFs into banking offices in the United States in the first quarter. (See the table on the Changes in Net Foreign Positions of Domestic Banking Offices in the United States.[1/] Over one half of this inflow came from banks' own foreign offices and IBFs and reflects the reversal during the quarter of an outflow of similar magnitude which occurred on the final day of 1984. In addition, there were sizeable net inflows from unaffiliated banking offices abroad. The latter consisted mainly of reductions in the category of claims which includes bankers acceptances. There is some evidence that banks have

1. Data shown in the table reporting changes in the Net Foreign Positions of Domestic Banking Offices are not strictly comparable to that shown in the International Banking Table. The former reports the difference between positions on the last day of the month from the Treasury International Capital series whereas the latter shows monthly averages of daily data reported to the Federal Reserve Board.

CHANGES IN NET FOREIGN POSITIONS OF DOMESTIC BANKING OFFICES IN THE UNITED STATES[1]
(Billions of dollars)

	1985 Q1
Through interbank transactions with	
A. Own foreign offices and IBFs	8.9
B. Unaffiliated banking offices in foreign countries	4.4
Through nonbank transactions	
C. Claims on nonbanks in foreign countries (increase = -)	1.7
D. Liabilities to private nonbanks in foreign countries (including custody liabilities)	2.9
Net Change	17.9

1. IBFs are treated as foreign entities. Excludes liabilities to foreign official institutions.

Data is measured as the difference between the values on the last day of March and on the last day of December.

been paring from their balance sheets assets with low profit margins, such as bankers acceptances, in response to pressures to improve their capital adequacy.

In addition, there was an increase of almost $3 billion in liabilities to private nonbanks in the first quarter, mainly from Latin America. Mexicans alone increased their deposits at banks in the United States about $750 million and increased their deposits at IBFs by almost $80 million. These data suggest intensified capital flight, although perhaps one third could reflect accumulating interest on existing balances and part could, in theory, reflect a shift in funds from offshore financial centers.

INTERNATIONAL BANKING DATA
(Billions of dollars)

	1981	1982	1983	1984				1985	
	Dec.	Dec.	Dec.	Mar.	June	Sept.	Dec.	Mar.	Apr.
1. Net Claims of U.S. Banking Offices (excluding IBFs) on Own Foreign Offices	7.8	32.9	39.3	35.3	32.2	30.2	25.4	25.8	28.5
2. Net Claims of U.S. Banking Offices on Own IBFs 1/	11.8	16.2	5.2	4.1	4.4	6.3	7.8	6.1	6.8
3. Sum of lines 1 and 2 of which:	19.6	49.1	44.5	39.4	36.6	36.3	33.3	31.8	35.3
(a) U.S.-chartered banks	22.3	40.0	40.8	36.9	34.7	35.7	32.1	30.4	33.6
(b) Foreign-chartered banks	-2.6	9.1	3.7	2.5	1.9	.6	1.2	1.3	1.7
4. Credit Extended to U.S. Nonbank Residents by Foreign Branches of U.S. Banks	13.2	15.8	18.7	18.5	19.9	20.2	20.7	19.1	19.3
5. Eurodollar Holdings of U.S. Nonbank Residents 2/	95.5	112.6	124.2	126.5	124.3	122.7	117.4	118.8	113.4

1. Corresponds to net claims of international banking facilities (IBFs) on all foreign residents, including all banks whether related or not, and all nonbanks.
2. Include terms and overnight Eurodollars held by money market mutual funds.

Note: These data differ in coverage and timing from the overall banking data incorporated in the international transactions accounts. Line 1 is an estimate constructed as the residual of line 3 minus line 2. Line 2 is data for the last Wednesday of the month for the sample of monthly IBF reporters. Line 3 is an average of daily data reported to the Federal Reserve by U.S. banking offices. Line 4 is an average of daily data. Line 5 is the month-end value for data through September 1983. For dates after September 1983, the overnight portion is an average of daily data and the term portion is an average of Wednesday data.

U.S. Merchandise Trade in 1985-Q1

The merchandise trade deficit in the first quarter of 1985 was larger than in the fourth quarter of last year but smaller than the record third-quarter rate. Most of the changes in the trade deficit in recent quarters have been attributable to swings in imports; the level of exports has been fairly steady.

The strength of nonoil imports in the first quarter was broadly based. The largest increases were in consumer goods (particularly clothing, household appliances and electronic goods), in a wide range of capital goods (industrial machines, construction machinery, business machines, other electronic items, machine tools, and aircraft), and in automotive products (particularly new passenger cars from Europe). There were also increases in many categories of industrial supplies (including steel) and in foods.

U.S. MERCHANDISE TRADE[1/]

	Year	1984			1985		
	1984	Q2-r	Q3-r	Q4-r	Q1	Feb.	Mar.
Value (Bil. $, SAAR)							
Exports	220.3	218.7	222.2	225.4	224.3	226.2	228.3
Agricultural	38.4	37.4	36.9	38.3	34.1	34.8	31.0
Nonagricultural	181.9	181.3	185.4	187.1	190.2	191.5	197.3
Imports	327.8	320.3	351.9	323.0	337.6	322.7	342.1
Oil	57.3	59.6	57.8	56.4	42.3	42.6	36.0
Nonoil	270.5	260.7	294.0	266.6	295.3	280.1	306.1
Trade Balance	-107.4	-101.6	-129.6	-97.6	-113.3	-96.4	-113.8
Volume (Bil 72$, SAAR)							
Exports							
Agricultural	16.3	15.2	15.7	17.3	15.6	15.9	14.3
Nonagricultural	63.0	62.7	64.3	64.7	64.8	65.0	67.0
Imports							
Oil	5.3	5.5	5.4	5.3	4.1	4.1	3.5
Nonoil	103.8	99.9	112.3	101.9	115.7	109.5	120.2

1/ International transactions and GNP basis. Monthly data are estimated.

Compared with the level of imports a year ago, the volume of nonoil imports in the first quarter was up by nearly 15 percent. Much of the increase is in response to the effects of the past appreciation of the dollar and the strength of domestic spending through the first quarter of 1985. Nonetheless, recent quarter-to-quarter changes in the volume of nonoil imports have been very volatile; in the last five quarters, the rates of change have been 13 percent, -1 percent, 12 percent, -9 percent, and 14 percent respectively, at quarterly rates. The unit value price index for nonoil imports changed very little during 1984; in the first quarter of 1985 however, it declined by about 2-1/2 percent, possibly in response to the dollar's appreciation.

The volume of oil imports dropped 23 percent in the first quarter and the average price of imported oil declined by about 75 cents per barrel. Domestic oil consumption declined slightly and inventories were drawn down at a greater-than-seasonal rate, at least partly in anticipation of further price declines in world markets. Spot prices for oil products began to move down in March and continued to decline in April; they had increased in January and February as a consequence of extremely cold weather in Europe, continuation of the coal strike in the United Kingdom (which was settled in March), and a drop in oil production by the USSR and Iran.

OIL IMPORTS

	Year	1984			1985			
	1984	Q2	Q3	Q4	Q1	Jan.	Feb.	Mar.
Volume (mbd, SA)	5.60	5.76	5.66	5.58	4.32	4.87	4.34	3.73
Price ($/BBL)	27.95	28.26	27.91	27.59	26.86	27.18	26.86	26.43
Value (Bil. $, SAAR)	57.31	59.61	57.84	56.38	42.29	48.27	42.57	36.02

Total exports in the first quarter were at about the same level as in the fourth quarter; agricultural exports fell while nonagricultural exports increased somewhat.

The decline in agricultural exports in the first quarter is an indication of the generally weak market for U.S. farm commodities in countries other than the Soviet Union. Most of the reduction in the first quarter was in wheat exports which fell to the lowest level in eight years; U.S. wheat faces intense competition from France, Argentina and Australia as well as from good crops worldwide. Exports of feedgrains (largely corn) declined only marginally as large shipments to the USSR offset the smaller amounts shipped to other countries; traditional U.S. customers such as Japan and Mexico purchased lower-priced feedgrains from China and Thailand. Since last July, the USSR has contracted for a record 22 million metric tons (MMT) of grain from the United States (largely corn); all but 4 MMT of the grain ordered was exported by the end of March.

The volume of nonagricultural exports in the first quarter was about the same as the levels recorded in the previous two quarters. There were increases in machinery (electronic and telecommunications equipment), aircraft, passenger cars to Canada, and coal, that were offset by declines in other items, particularly in industrial supplies. While the current volume of exports is 7 percent above the level of a year ago, most of this increase occurred between the second and third quarters of last year. The average price of nonagricultural exports rose somewhat in the first quarter after being little changed during 1984.

Foreign Economic Developments. In the early months of 1985, the index of industrial production declined in the major foreign industrial countries except the United Kingdom from average monthly levels reached in the final quarter of 1984. Nevertheless, production generally remained above year-earlier levels except in France, where it fell slightly. Unusually severe weather in Europe may have accounted for the fall-off in production, and other indicators of economic activity in Canada and Japan suggest continued growth in the first quarter. Reflecting the overall sluggishness of activity, however, unemployment rates increased in the European countries and were either at post-World War II highs or close to them. The unemployment rate declined slightly in Canada and Japan.

Though inflation in all countries remains relatively low, it appears that further declines may not be imminent. Japan and France continue to show lower inflation, though reductions have been small recently. Canadian inflation, which declined throughout 1984, leveled off in recent months as did inflation in Italy. Meanwhile, inflation in Germany, and the United Kingdom increased slightly in early 1985.

With the exception of Japan and Germany, the external sectors of the foreign industrial countries weakened in early 1985. Japan's current account balance was higher in the first quarter (s.a.a.r.) than in all of 1984, a record year. Germany showed improvement over year-earlier levels in both current account and trade surpluses. Although the Canadian trade balance (s.a.a.r.) remained in surplus early this year, it was lower than 1984's record high. Trade deficits increased in France, Italy, and the United Kingdom.

May 15, 1985

REAL GNP AND INDUSTRIAL PRODUCTION IN MAJOR INDUSTRIAL COUNTRIES
(PERCENTAGE CHANGE FROM PREVIOUS PERIOD, SEASONALLY ADJUSTED)

	Q4/Q4 1983	Q4/Q4 1984	1984 Q2	1984 Q3	1984 Q4	1985 Q1	1984 DEC.	1985 JAN.	1985 FEB.	1985 MAR.	1985 APR.	LATEST 3 MONTHS FROM YEAR AGO+
CANADA												
GNP	7.1	3.7	.8	1.6	.6	N.A.	*	*	*	*	*	3.7
IP	16.1	5.2	1.5	3.2	.3	N.A.	.5	-.8	-.3	N.A.	N.A.	4.7
FRANCE												
GDP	.8	1.9	-.4	.8	.3	N.A.	*	*	*	*	*	1.9
IP	2.4	1.3	-1.3	2.5	-2.0	N.A.	-2.3	-1.6	4.7	N.A.	N.A.	-1.8
GERMANY												
GNP	3.1	2.8	-1.9	2.4	1.4	N.A.	*	*	*	*	*	2.8
IP	6.0	3.6	-4.1	5.7	1.4	-1.5	.4	-1.8	-.2	.1	N.A.	1.3
ITALY												
GDP	1.2	N.A.	.7	1.1	N.A.	N.A.	*	*	*	*	*	3.2
IP	1.7	1.7	.5	1.9	-1.7	N.A.	.5	-4.0	8.2	N.A.	N.A.	2.2
JAPAN												
GNP	3.9	6.4	1.8	.6	2.3	N.A.	*	*	*	*	*	6.4
IP	8.6	10.7	2.8	1.5	2.8	-.7	-.7	-.2	.7	-2.0	N.A.	6.5
UNITED KINGDOM												
GDP	3.8	2.3	-.8	1.0	1.5	N.A.	*	*	*	*	*	2.3
IP	5.3	-.3	-2.1	.4	.8	N.A.	.7	1.5	-.2	N.A.	N.A.	.1
UNITED STATES												
GNP	6.3	5.7	1.7	.4	1.0	.3	*	*	*	*	*	3.5
IP	15.0	5.9	2.1	1.6	-.6	.4	.0	.2	.1	.3	-.2	2.8

* DATA NOT AVAILABLE ON A MONTHLY OR QUARTERLY BASIS.

+ IF QUARTERLY DATA, LATEST QUARTER FROM YEAR AGO.

May 15, 1985

CONSUMER AND WHOLESALE PRICES IN MAJOR INDUSTRIAL COUNTRIES
(PERCENTAGE CHANGE FROM PREVIOUS PERIOD)

	Q4/Q4	Q4/Q4	1983	1984				1985	1985				LATEST 3 MONTHS
	1983	1984	Q4	Q1	Q2	Q3	Q4	Q1	JAN.	FEB.	MAR.	APR.	FROM YEAR AGO
CANADA													
CPI	4.6	3.7	.9	1.2	.9	.9	.7	1.2	.4	.6	.2	N.A.	3.7
WPI	3.5	3.6	.4	1.6	1.2	.5	.3	1.0	.5	.2	.4	N.A.	3.1
FRANCE													
CPI	9.8	6.8	1.9	1.7	1.8	1.7	1.4	1.4	.5	.5	.7	N.A.	6.4
WPI	14.6	10.5	3.6	3.4	2.9	2.2	1.6	N.A.	1.0	.8	N.A.	N.A.	9.0
GERMANY													
CPI	2.7	2.0	.5	.9	.5	.0	.7	1.1	.7	.4	.3	.2	2.5
WPI	.9	1.0	1.2	1.7	.8	-1.4	.0	N.A.	.6	1.3	N.A.	N.A.	.5
ITALY													
CPI	12.8	9.4	3.5	2.9	2.3	1.4	2.4	N.A.	1.1	1.2	N.A.	N.A.	9.3
WPI	9.1	8.8	3.3	3.2	2.2	1.2	1.9	N.A.	1.4	.8	N.A.	N.A.	8.1
JAPAN													
CPI	1.9	2.4	1.4	.9	.6	-.2	1.2	.6	1.0	-.8	.4	.4	1.8
WPI	-3.3	.5	-.6	.1	-.1	.8	-.3	.4	.3	.3	-.3	-.4	.8
UNITED KINGDOM													
CPI	5.1	4.8	1.1	.6	2.0	.9	1.2	1.3	.4	.8	.9	N.A.	5.5
WPI	5.6	6.0	1.3	1.8	2.3	.6	1.3	1.7	.7	.5	.7	1.1	5.7
UNITED STATES													
CPI (SA)	3.2	4.1	1.0	1.3	.9	.9	.9	.8	.2	.3	.5	N.A.	3.6
WPI (SA)	.8	1.7	.3	1.2	.4	.0	.1	.3	.1	-.1	.2	.3	.6

May 15, 1985

TRADE AND CURRENT ACCOUNT BALANCES OF MAJOR INDUSTRIAL COUNTRIES 1/
(BILLIONS OF U.S. DOLLARS; SEASONALLY ADJUSTED)

	1983	1984	1983 Q4	1984 Q1	1984 Q2	1984 Q3	1984 Q4	1985 Q1	1984 DEC.	1985 JAN.	1985 FEB.	1985 MAR.
CANADA												
TRADE	14.4	16.1	3.5	3.5	4.1	4.1	4.4	4.0	1.1	1.1	1.3	1.6
CURRENT ACCOUNT	1.4	1.6	.0	.0	.5	.5	.6	N.A.	*	*	*	*
FRANCE												
TRADE 2/	-5.9	-2.7	-.2	-1.5	-1.2	.4	-.3	-1.1	-.1	-.4	-.6	-.1
CURRENT ACCOUNT 2/	-4.9	-.1	.2	-.7	-.4	.9	.1	N.A.	*	*	*	*
GERMANY												
TRADE	16.4	18.8	3.4	4.3	3.2	5.0	6.3	N.A.	1.9	1.4	1.6	N.A.
CURRENT ACCOUNT (NSA)	4.2	5.8	3.7	.8	-.1	-.9	6.0	1.3	2.2	-.3	.7	.8
ITALY												
TRADE	-7.9	-10.7	-1.0	-2.2	-2.9	-1.4	-4.2	N.A.	-.7	-1.4	-1.0	N.A.
CURRENT ACCOUNT (NSA)	.8	-3.2	.1	-1.7	-1.0	1.3	-1.7	N.A.	*	*	*	*
JAPAN												
TRADE 2/	31.2	44.5	8.2	10.0	11.1	10.1	13.2	11.6	4.0	4.9	3.5	3.2
CURRENT ACCOUNT	21.0	35.0	5.5	7.2	9.2	7.4	11.5	9.4	3.8	4.2	2.7	2.5
UNITED KINGDOM												
TRADE	-.8	-5.7	-.0	-.2	-1.8	-2.1	-1.6	-1.4	-.4	-.1	-.3	-1.0
CURRENT ACCOUNT 2/	4.4	1.3	.9	.6	.9	-.7	.5	.0	.1	.4	.1	-.5
UNITED STATES												
TRADE	-61.1	-107.4	-19.4	-25.2	-25.4	-32.4	-24.4	-28.3	-6.7	-10.8	-8.0	-9.5
CURRENT ACCOUNT	-41.6	-101.6	-17.2	-19.7	-24.7	-33.6	-23.7	N.A.	*	*	*	*

1/ THE CURRENT ACCOUNT INCLUDES GOODS, SERVICES AND PRIVATE AND OFFICIAL TRANSFERS.
2/ QUARTERLY DATA ARE SUBJECT TO REVISION AND ARE NOT CONSISTENT WITH ANNUAL DATA.

* COMPARABLE MONTHLY OR QUARTERLY CURRENT ACCOUNT DATA ARE NOT PUBLISHED.

Individual Country Notes. The pace of economic activity in Japan has apparently slowed. Industrial production declined 2.7 percent (s.a.a.r.) in the first quarter after a sharp rise of 11.6 percent in the final quarter of 1984. Other economic indicators (s.a.) in the first quarter were positive, however, and suggest the expansion is continuing: retail sales rose by 3.3 percent; housing starts increased by 2.6 percent; and new construction orders were up by more than 9 percent, despite a slight decline in March. In addition, the latest monthly assessments by the Economic Planning Agency and the Bank of Japan report that private plant and equipment spending continues to show a healthy expansion.

Inflation remained low in Japan. The wholesale price index in March was less than 1 percent above its year-earlier level. In the year ending April, the Tokyo consumer price index rose 2 percent. The current account surplus in the first quarter was $37-1/2 billion (s.a.a.r.), compared with a surplus of $35 billion in 1984. The first-quarter surplus was, however, below that of the final quarter of 1984, reflecting a slowdown of export growth.

On April 9, Prime Minister Nakasone announced his "New Economic Initiative," consisting of some specific measures and a generalized campaign to persuade the Japanese people to buy more imports. He also stated that he would take "fullest account of" the recommendations of the Advisory Committee on External Economic Issues (headed by Dr. Okita). The Committee's report makes general recommendations on the need to open Japanese markets, and briefly notes the importance of stimulating domestic demand to reduce external surpluses. In mid-

April, Nakasone rejected suggestions from important members of the ruling Liberal Democratic Party (LDP) for a bond-financed increase in the government deficit. Since then his opposition to increased spending is reported to have softened in view of increasing sentiment in the LDP for such a change. However, Finance Minister Takeshita, a possible successor to Nakasone, favors fiscal restraint.

Economic activity in Germany has weakened so far this year. Industrial production has barely changed since January, and on average dropped 1-1/2 percent (s.a.) in the first quarter. The cause for this weakness was lackluster domestic demand, which was only partially offset by strong export activity. The construction sector was particularly weak, as unusually severe winter weather compounded underlying structural problems. Domestic demand for automobiles also added to the weakness, as prospective buyers awaited a government decision about mandatory pollution control equipment. The unemployment rate was 9.3 percent in the first quarter, higher than last year's average and close to the record high reached in the summer of 1983.

Consumer price inflation increased to an annual rate of almost 5.0 percent in the first four months of this year, compared with 3 percent in the final quarter last year. The year-on-year rate in April was 2.5 percent, after having been as low as 1.5 percent late last year. The acceleration of consumer prices can be traced to import prices, which in March were almost 9 percent above their year-earlier level; wholesale and producers prices have also accelerated this year. Both trade and current account surpluses increased in the first quarter compared to the first quarter of 1984.

The Bundesbank announced that foreign banks in Germany will be permitted to lead-manage DM denominated bonds as of May 1. Also lifted were prohibitions against zero coupon bonds, variable rate bonds and swaps.

The industrial production index in France increased by 4.7 percent (s.a.) in February, completely reversing the sharp decline in the index over the previous three months. Production figures for December and January appear to have been distorted owing to unusually severe winter weather. On a year-over-year basis, the January-February average production index was down almost 2 percent. In a further indication of the weakness of French economic activity, it was announced that year-over-year real GDP growth in 1984 had been revised downward to 1.6 percent from the initial figure of 2.0 percent (the revised quarterly pattern is not yet available). After reaching a record high level of 10.7 percent (s.a.) in January, the unemployment rate eased back in March to 10.5 percent to where it was at the end of 1984.

Consumer prices increased by 0.7 percent (n.s.a.) in March, leaving the year-over-year inflation rate unchanged at 6.4 percent. The trade deficit was reduced sharply in March to $60 million (s.a.). For the first quarter as a whole, the trade deficit was $4.4 billion (s.a.a.r.), compared with a trade deficit of $2.6 billion in 1984.

Preliminary indications are that the government's 1986 budget will combine continued tax reductions (including a 3 percent income tax cut) and freezes or reductions in government spending programs (including a 1 percent reduction in civil service employment), designed to leave the government deficit about unchanged at its current level of 3 percent of GDP.

Real gross domestic product (average measure) in the United Kingdom grew 6.2 percent (s.a.a.r.) in the fourth quarter of 1984. About two-thirds of this growth, however, was accounted for by inventory investment as stocks rose following three quarters of decline. For the year as a whole, real GDP grew 2.3 percent (Q4/Q4). More recently the index of industrial production for the two months ending in February was only .7 percent above year-earlier levels. This low growth rate reflects the year-long coalminers' strike which ended on March 4. In the absence of the coal strike, measured industrial production would have been about 3 percentage points higher.

The unemployment rate rose slightly to 13.1 percent (s.a.) in April, a post World War II high, while year-over-year inflation in retail prices increased to 6.1 percent in March. This increase is partly due to rising mortgage interest rates. Although the Bank of England lowered its money market dealing rates by 150 basis points in three steps between March 20 and April 19, it signaled that it is not prepared to sanction a rapid fall in short-term rates.

The trade deficit widened substantially in March to $12.2 billion (s.a.a.r.), from $3.5 billion in February. About one-half of the increase in the trade deficit represented increased imports of fuel oil, thought to reflect a restoration of stocks run down towards the end of the coalminers' strike. The trade deficit for the first quarter of 1985 was $5.6 billion (s.a.a.r.) while the current account was in near balance.

Growth in Canada continued at a moderate pace, following the easing of credit market conditions in the second half of 1984 and into January. Gross domestic product expanded in January and February, pushing the two-month average level 0.7 percent above last year's fourth-quarter pace. Industrial production, which accounts for about 30 percent of total output, declined in January and February leaving the index 1.1 percent below last December's level. Meanwhile, the unemployment rate in April fell to 10.9 percent only slightly below the first quarter's average of 11.1 percent.

Inflation continued to be moderate. Consumer prices were 3.7 percent higher in March than a year earlier. The industry selling price rose only 2.7 percent for the twelve months ending in March, down from February's twelve-month inflation rate of 3.1 percent. Meanwhile Canada's trade surplus increased slightly in March to $1.6 billion, a record high, up from February's surplus of $1.3 billion. The trade surplus for the first quarter was $4.0 billion, below the pace of $4.4 billion achieved in the fourth quarter of 1984.

Economic activity in Italy appears to have slowed in the early part of 1985. Perhaps owing to cold weather in January, industrial production (s.a.) dropped 4 percent, but it rose 8.2 percent (s.a.) in February. The average level of industrial production in January and February was slightly below the average level achieved in 1984, a year of recovery for the Italian economy, and slightly below the monthly average in the fourth quarter. The official February household survey shows a slight decrease in consumer confidence about the general economic situation of the country.

In April, the cost of living index (not shown in table) was 8.8 percent above its year earlier level. No progress has been made in reducing inflation over the last six months. The official goal of a 7 percent rate of inflation, as measured by the cost of living index, by the end of 1985 appears increasingly unrealistic.

The current account deficit increased to $1.7 billion (n.s.a.) in the fourth quarter of 1984 bringing the current account deficit to $3.2 billion for the year as a whole. More recently, the February trade deficit was $1.0 billion (s.a.), a relatively large figure.

The National Bank of Belgium has changed its discount rate policy in early May, seeking a closer alignment with market rates. The discount rate, no longer a discretionary policy instrument, will be fixed every Wednesday to equal the rate on three-month treasury certificates set administratively the previous day. The discount rate will be allowed to fluctuate within a specified range during the following week. To reflect this new policy, the discount rate was reduced within a week from 11 to 9.75 and further to 9.50 percent.

The Central Bank of Sweden raised its discount rate 2 percentage points to 11.5 percent and increased its penalty rate 2.5 percentage points to 16 percent. In addition, the government announced fiscal measures designed to curb consumption and increase savings. These changes are in response to the higher-than-expected current account deficit and measured net capital outflows for the first quarter of 1985. The government's 1985 inflation goal has been jeopardized by excessive wage demands by the civil servants union. In response to these demands and selective strikes the government has imposed a selective lockout on the civil servants.

Economic Situation in Major Developing Countries

Real output in non-OPEC developing countries grew by about 4 percent in 1984, following virtual stagnation in 1982 and 1983. Their aggregate external current account deficit declined by about $35 billion and $10 billion, respectively, in 1983 and 1984 but now appears to be running somewhat higher than in 1984. During the first quarter of 1985, the trade surpluses of Mexico and Brazil dropped by $1.7 billion and $0.5 billion, respectively, from their year-earlier levels.

Among OPEC countries, real output rose by about 1 percent in 1984. GDP of the OPEC countries had declined by over 10 percent from 1979 to 1983, as cartel members cut back their volume of oil production and world market conditions forced the reduction of oil prices.

In March, Mexico and the IMF reached new understandings on the country's 1985 economic policies. Approval of the 1985 program by the IMF Executive Board is expected on June 7. On the strength of these understandings, the signing of the initial agreement under the multi-year debt rescheduling took place on March 29. These developments helped to calm the market for pesos outside Mexico despite continued market skepticism over the slow rate of crawl of the peso in official markets and a weaker trade balance. Economic activity has risen strongly during the past six months, stimulating imports, depressing exports, and bringing the merchandise trade surplus down to $2.6 billion in the first quarter of 1985 from $4.3 billion a year earlier.

Negotiations between Brazil's new government and the IMF regarding a 1985-86 stabilization program are expected to resume in late May and may be protracted. Thus, Brazil is expected to request from commercial banks an extension of at least 90 days in the current agreement to maintain their interbank, trade credit, and redeposit facilities through May 31. Brazil's trade surplus of $2.9 billion through the first four months of 1985 compares with a $3.5 billion surplus during the same period last year. It is likely that Brazil's trade surplus for the full year 1985 will be $2-$3 billion lower than the $13 billion surplus recorded in 1984. After an acceleration of inflation to a 12.7 percent monthly rate in March, inflation dropped to 7.2 percent in April, in large part because of new price controls.

Early in May, Argentina paid $50 million to its bank creditors to eliminate public sector interest arrears for the period November 5-15, 1984, in order to avoid pushing interest arrears in excess of 180 days. Banks have tentatively committed more than 98 percent of the $4.2 billion in new loans that had been agreed as part of the package of new financing and debt rescheduling arranged with the bank advisory committee last November. Argentina and the IMF are continuing negotiations over reduction of the fiscal deficit and other steps needed to put the Argentine stabilization program back on track. Progress so far has been slow. Inflation has been accelerating, reaching about 30 percent in April (2,200 percent at an annual rate). In mid-April, the Argentine government submitted to the Congress 11 bills designed to increase revenues by 0.5 percent of GDP. At the end of the month, the government announced its decision to cut public sector expenditures by 12 percent from the level proposed in an earlier budget and to submit to the Congress three more tax bills, including one that would institute a forced loan from taxpayers. Monetary conditions were also tightened substantially in late April and early May, leading to high real interest rates in the uncontrolled segment of the loan market and a narrowing in the spread between the official and parallel exchange rates from 37 to about 13 percent. A major private bank (which had accounted for about 5 percent of total commercial bank deposits) was closed on May 10, leading to a run on many other private, locally-owned banks in the country.

Venezuela and its bank advisory committee have completed the terms sheet for the multi-year rescheduling agreement negotiated last September. Previous disagreements about provisions for currency switching of dollar denominated debt, the obligation of the public sector to provide foreign exchange to private sector debtors and the organization of a re-lending facility have been resolved. The circulation of the terms sheet to Venezuela's 450 creditor banks will probably begin in early June. Before the final signing of the rescheduling agreement, however, Venezuela must show further progress in the review for registration of some $12 billion in private sector debt. About $10 billion of this private sector debt has been reviewed so far, with about two-thirds having been registered as eligible to obtain foreign exchange at a preferential rate.

Chile's proposed three-year IMF extended arrangement is expected to be approved by the Fund soon after Chile reaches agreement with its major creditors on prospective balance-of-payments financing. The Chileans are negotiating with bank and official creditors to fill a 1985-86 financing gap of nearly $2 billion. On May 4, Chile's bank advisory committee offered $1.05 billion in new money, of which $250 million is proposed to be guaranteed by the World Bank. The banks are continuing to press for Chilean government guarantees to cover commercial risks on the external debt of Chile's private financial sector.

In Peru, the president-elect's public statements suggest that he may stop cooperating with the IMF and may seek to renegotiate the country's foreign debts without an IMF program. Creditors are concerned about the possibility of the new government imposing a unilateral rescheduling. In late 1984 the outgoing government began to implement a series of adjustment measures--an acceleration of daily devaluations, increases in gasoline prices, sales taxes, and interest rates, and a slowdown of public investment projects. However, the announced measures have not been fully implemented. Interest due to foreign commercial banks is more than 180 days in arrears, and such arrears total about \$350 million. Peru made a payment of \$22 million in mid-February. The government announced its intention to make similar payments each month for the remainder of the present administration's term, which ends July 28, 1985, but in March only a \$16 million payment was made, and no payment was made in April.

Colombia appears to have gained acceptance by its bank creditors for an alternative to a formal IMF standby arrangement, consisting of a quantified adjustment program that would be monitored by the Fund but would not involve any Fund resources. Colombia is seeking new loans totalling \$1 billion from the banks over two years; this would represent a \$300 million net increase in bank exposure after amortization payments of \$700 million which would be made on schedule.

At the end of March the Philippines exceeded by 3 percent the IMF ceiling for reserve money (a type of monetary base concept) and breached two other performance targets under the IMF standby arrangement. However, in April the Fund Managing Director approved a revised standby program which the Fund Board will consider on May 31. Under the new program, the Philippines will be eligible to draw SDR 106 million toward the end of June. In late April, the creditor banks finally assembled their commitments to participate in the new, $925 million credit and the $3 billion revolving short-term trade facility negotiated with the Philippine authorities last fall.