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Confidential (FR) Class III FOMC

Part 2

June 26, 1996

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Recent Developments

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

Confidential (FR) Class III FOMC

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RECENT DEVELOPMENTS

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DOMESTIC NONFINANCIAL DEVELOPMENTS

Economic activity apparently advanced at a relatively brisk clip this spring. With the inventory imbalances that held back output earlier in the year largely corrected, industrial production posted large gains in April and May. Furthermore, a healthy underlying trend in income growth lent support to consumer spending. However, some tentative signs have emerged that higher mortgage rates are beginning to damp residential construction and that growth in business capital spending is moderating. Although there is some evidence that wage pressures are mounting, the incoming data indicate that core price inflation has remained in check at both the consumer and producer levels.

Labor markets

The economy has continued to generate an impressive number of jobs. Nonfarm payrolls expanded an average of 222,000 jobs per month over the first five months of the year, driven primarily by growth in the service-producing and construction industries. Employment jumped 348,000 in May, and the gain in April was revised up sharply, to 163,000.

The establishment survey data released last month incorporated annual benchmark revisions and the use of a new seasonal adjustment process.[1] The benchmarking raised the not seasonally adjusted level of employment in March 1995 by 542,000, a large revision by historical standards but in line with the preliminary estimate that the BLS announced last November. In addition, the average monthly change in seasonally adjusted employment between March 1995 and February 1996 was raised about 30,000; revised bias adjustment factors accounted for the bulk of this additional revision since March 1995.

In contrast to the strong gains in employment, growth in aggregate hours of production or nonsupervisory workers has been relatively subdued this spring. Aggregate hours rose 0.1 percent in May after declining 0.2 percent in April. The blizzard effects in

1. Three important features of the annual revisions to the establishment survey are the benchmarking of payroll employment to the March 1995 unemployment insurance tax records; a concomitant revision to the bias adjustment factors for employment after March 1995 (used primarily to account for new establishments not captured by BLS's survey techniques); and the introduction of the new X-12 seasonal adjustment procedure that, among other things, corrects for differences in the length of time between monthly surveys (the so-called four- and five-week effect).

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

	1994	1995	1995 Q3	1995 Q4	1996 Q1	1996 Mar.	1996 Apr.	1996 May
	Average monthly changes							
Nonfarm payroll employment[2]	318	185	174	171	200	158	163	348
Private	295	176	166	164	185	129	158	305
Manufacturing	33	-12	-26	-16	-28	-50	-4	6
Strike-adjusted	35	-13	-25	-20	-27	-47	-7	6
Durable	28	5	-2	6	-15	-36	29	17
Transportation equipment	5	-3	-4	-5	-13	-33	37	11
Nondurable	5	-17	-24	-22	-14	-14	-33	-11
Construction	25	9	16	12	39	-9	11	28
Trade	91	54	41	41	20	22	79	52
Finance, insurance, real estate	-3	4	11	15	15	13	8	20
Services	134	110	113	95	125	133	65	181
Business services	54	33	42	29	32	32	17	67
Total government	23	9	8	7	16	29	5	43
Private nonfarm production workers[2]	267	152	162	128	163	94	119	203
Manufacturing production workers	34	-10	-20	-13	-30	-54	5	-2
Total employment[3]	261	32	157	-18	390	488	-56	367
Nonagricultural	225	51	190	-15	336	521	62	245
Memo:								
Aggregate hours of private production workers (percent change)[2]	.4	.1	.2	.1	.3	.0	-.2	.1
Average workweek (hours)[2]	34.6	34.5	34.4	34.4	34.3	34.5	34.3	34.3
Manufacturing (hours)	41.9	41.6	41.4	41.4	40.9	41.4	41.5	41.7

1. Average change from final month of preceding period to final month of period indicated.
2. Survey of establishments.
3. Survey of households.

SELECTED UNEMPLOYMENT AND LABOR FORCE PARTICIPATION RATES
(Percent; based on seasonally adjusted data)

	1994	1995	1995 Q3	1995 Q4	1996 Q1	1996 Mar.	1996 Apr.	1996 May
Civilian unemployment rate (16 years and older)	6.1	5.6	5.6	5.5	5.6	5.6	5.4	5.6
Teenagers	17.6	17.3	17.7	17.6	17.4	17.5	16.7	16.4
20-24 years old	9.7	9.1	9.5	9.2	9.8	9.6	9.0	9.7
Men, 25 years and older	4.8	4.3	4.3	4.2	4.3	4.4	4.2	4.1
Women, 25 years and older	4.9	4.4	4.4	4.3	4.3	4.3	4.2	4.5
Full-time workers	6.1	5.5	5.5	5.5	5.5	5.5	5.4	5.5
Labor force participation rate	66.6	66.6	66.6	66.4	66.7	66.9	66.6	66.9
Teenagers	52.7	53.5	53.4	52.9	52.6	52.7	52.5	53.5
20-24 years old	77.0	76.6	76.2	76.1	76.9	77.7	77.2	77.5
Men, 25 years and older	76.0	76.0	75.9	75.6	76.0	76.2	76.0	76.0
Women, 25 years and older	58.1	58.3	58.4	58.5	58.4	58.6	58.4	58.6

the first quarter make the usual quarter-to-quarter hours comparisons difficult. Cutting through that difficulty, hours in May were 1.6 percent (annual rate) above the fourth-quarter level--an increase that would be quite reasonably aligned with the close to 3 percent first-half GDP growth anticipated by many forecasters. (Productivity was weak in the fourth quarter of 1995, so an above-trend increase in productivity in the first half would not be surprising.)

In the household survey, the unemployment rate has fluctuated between 5.4 percent and 5.8 percent since late 1994. The rate in May, 5.6 percent, equaled the average for the year to date. Labor force participation averaged 66.7 percent during the first five months of 1996, a slightly higher rate than in 1995. In May, labor force participation jumped 0.3 percentage point, to 66.9 percent, the high end of the recent range of fluctuation. Participation rates rose last month for all demographic groups, but especially teenagers, where variations in the timing of seasonal inflows into the labor force can make participation rates volatile in the spring.

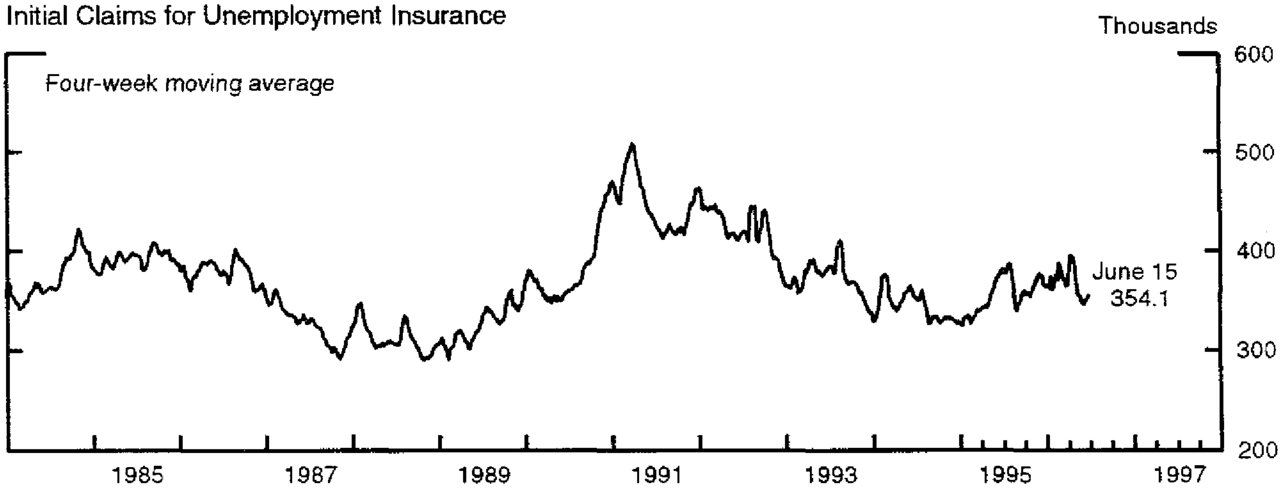
Other indicators also point to a strong labor market. Initial claims for unemployment insurance averaged 358,000 over the four weeks ended June 15, a shade below the average of the first five months of 1996. The adjusted Conference Board help-wanted index (confidential until 10:00 a.m. Thursday, June 27) fell 0.8 point in May, but remained in the narrow range that has prevailed since mid-1994. In the latest Manpower survey, the net percentage of firms planning to boost hiring turned up after having declined fairly steadily over the preceding year. The Conference Board consumer survey readings on perceived job availability have remained in the ranges observed since the end of 1994, although these levels are somewhat less favorable than those during the period in 1988 when the jobless rate also was in the neighborhood of 5-1/2 percent.

Revised estimates of output growth lowered the large jump in nonfarm business sector productivity in the first quarter from 2.6 percent to 2.1 percent (annual rates). First-quarter growth in nonfarm business compensation per hour, at a 3.3 percent annual rate, was unchanged by the revisions. Unit labor costs were revised up some in the first quarter, but the change over the past four quarters was still a moderate 2.4 percent.

In addition to revisions to the national income accounts, the productivity and cost data incorporated the recent revisions to the

Labor Market Indicators

Initial Claims for Unemployment Insurance



Note. State programs, includes EUC adjustment.

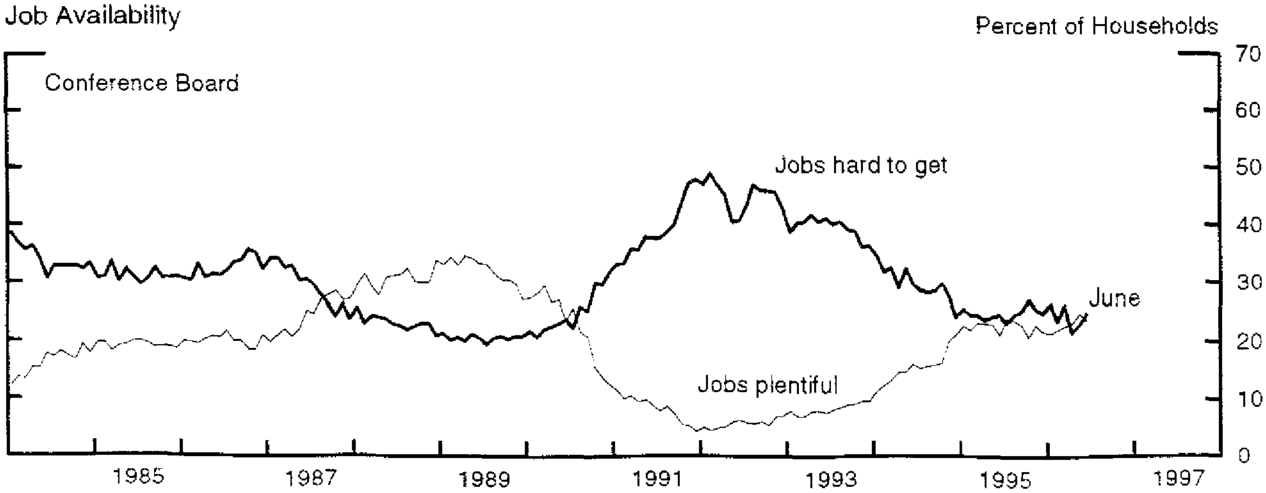
Help Wanted Advertising

Note. Series has been adjusted to take account of various structural and institutional changes, including consolidation of the newspaper industry and a tendency toward increased hiring through personnel supply agencies.

Net Hiring Strength

Note. Percent planning an increase in employment minus percent planning a reduction.

Job Availability

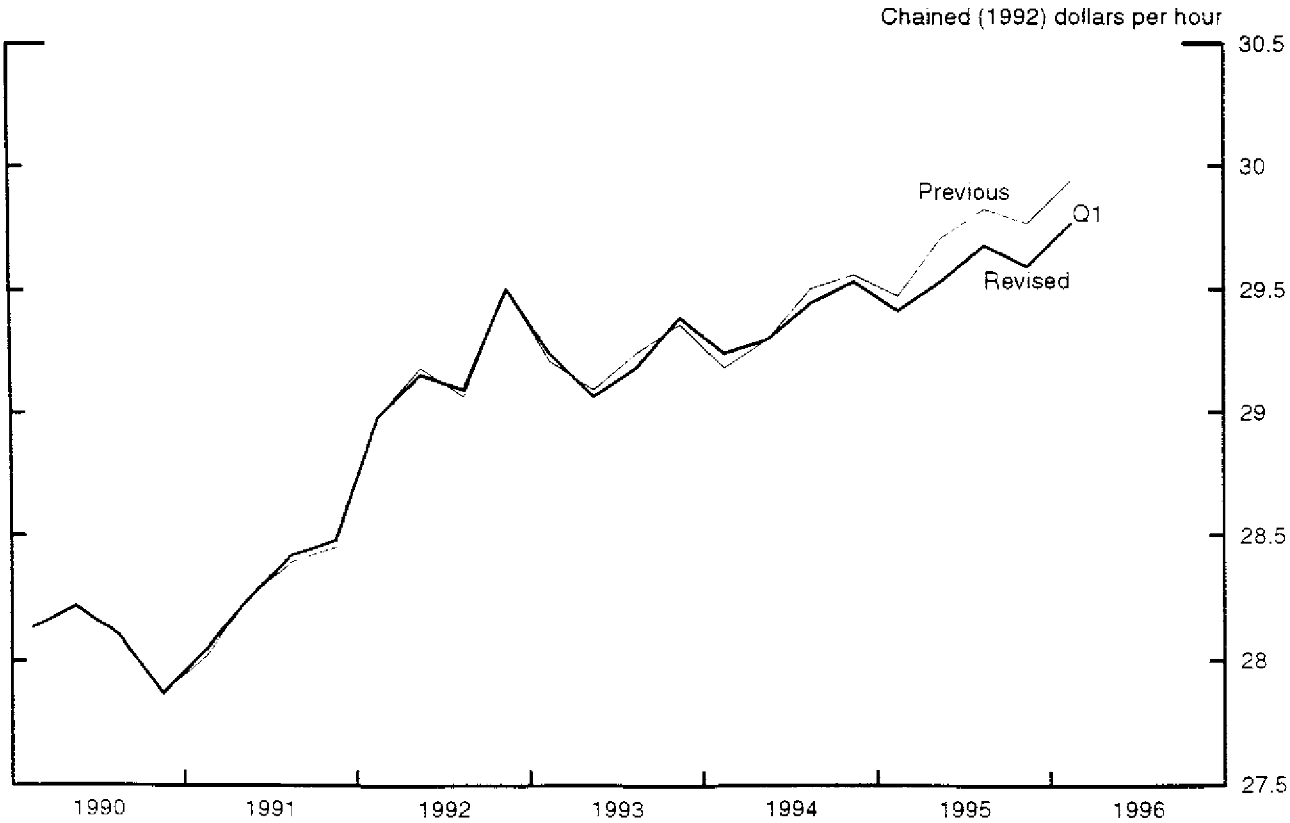


LABOR PRODUCTIVITY AND COSTS
(Percent change from preceding period at compound annual rate; based on seasonally adjusted data)

	1994[1]	1995[1]	1995 Q2	1995 Q3	1995 Q4	1996 Q1	1995:Q1 to 1996:Q1
<u>Output per hour</u>							
Nonfarm business	.5	.3	1.6	1.7	-.8	2.1	1.1
Previous	.7	.7	3.0	1.7	-1.0	2.6	1.6
<u>Compensation per hour</u>							
Nonfarm business	2.3	3.6	4.1	4.1	2.9	3.3	3.6
Previous	2.5	4.1	5.4	4.3	2.8	3.3	4.0
<u>Unit labor costs</u>							
Nonfarm business	1.7	3.4	2.5	2.4	3.7	1.2	2.4
Previous	1.8	3.4	2.3	2.5	3.8	.6	2.3
Memo: ECI compensation per hour	3.0	2.9	2.9	2.6	3.2	2.9	2.9

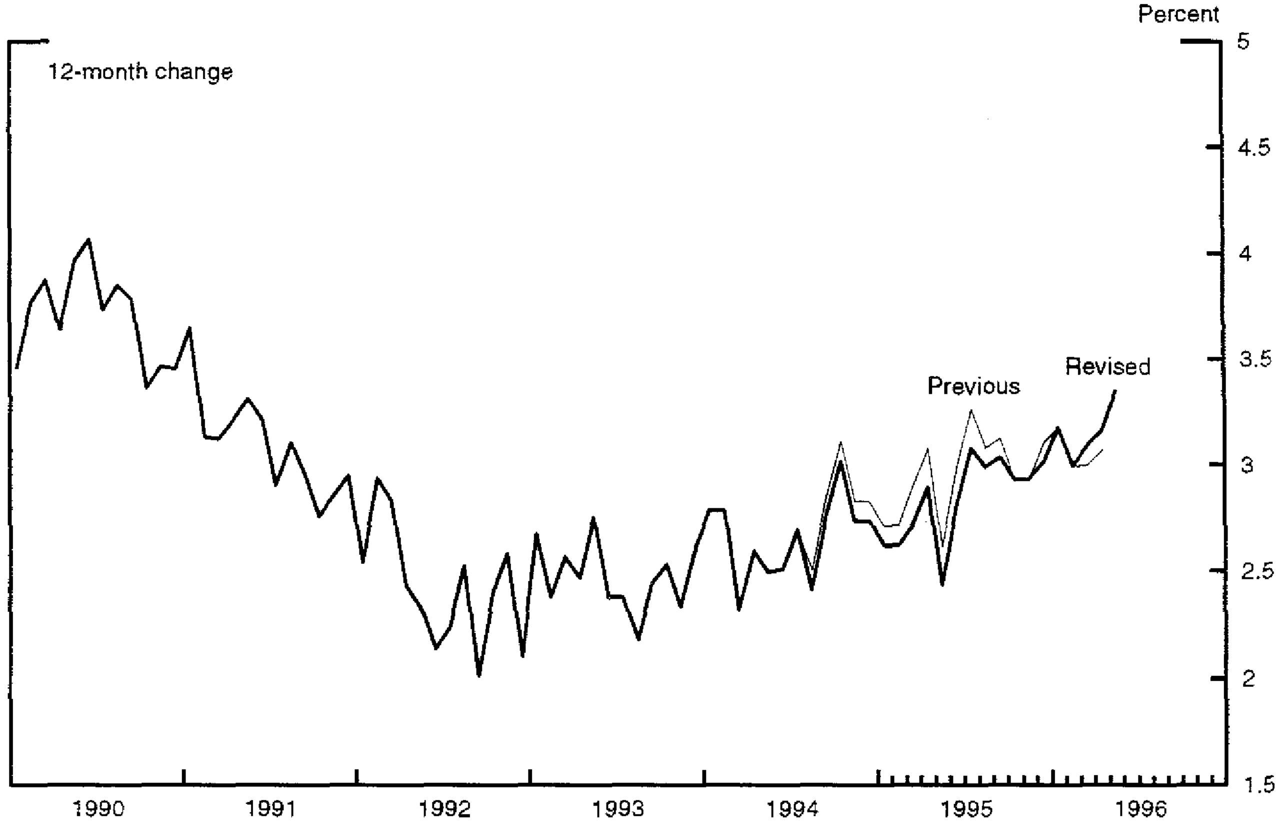
1. Changes are from fourth quarter of preceding year to fourth quarter of year shown.

Nonfarm Business Sector Productivity

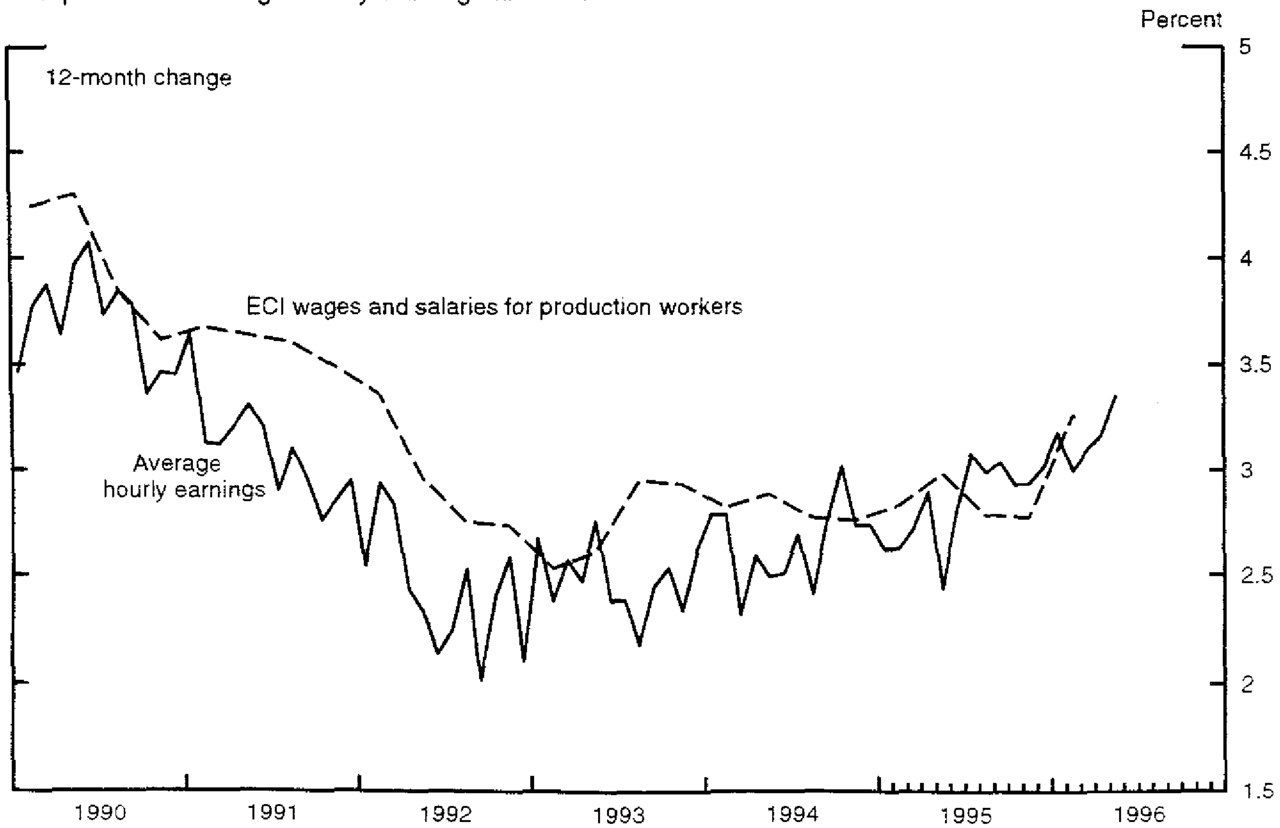


Earnings Measures

Average Hourly Earnings



Comparison of Average Hourly Earnings and ECI



establishment survey as well as technical adjustments to data from the household survey. The four-quarter change in compensation per hour in 1995 was revised down 1/2 percentage point, to 3.6 percent, more in line with the ECI than the previous estimate. Productivity growth in 1995 and early 1996 also was revised down about 1/2 percentage point (annual rate). Over the longer run, however, the underlying trend in the growth of output per hour was little changed; since the business cycle peak in 1990, productivity is now estimated to have increased at an annual rate of 1.05 percent, 0.1 percentage point less than previously estimated.

Only a little information on second-quarter labor costs currently is available, but the data that have come in seem to be providing some statistical confirmation of the many anecdotal reports of rising wage pressures. Average hourly earnings of production and nonsupervisory workers increased 3.3 percent during the year ended this May, up from a 2-3/4 percent pace average during the second quarter of 1995.[2] More comprehensive second-quarter wage and salary data from the ECI will be available in late July; through the first quarter, longer-term movements in ECI wages and salaries were broadly in sync with those in average hourly earnings.

Industrial Production

According to preliminary estimates, industrial production rose 0.7 percent in May, matching the April advance. However, in contrast with April, when much of the increase resulted from the return to work at GM, the gain in May was broader based. A weather-related spurt in electricity generation accounted for about one-third of last month's advance. Much of the remainder of the increase occurred in manufacturing output excluding motor vehicles and parts, which rose 0.5 percent in May after having been unchanged in each of the two preceding months. With the exception of consumer goods, advances were widespread across market groups; the most notable gains were in the production of business equipment and durable goods materials.

Production of motor vehicles remained strong in May. Assemblies were 12.2 million units at an annual rate, the same pace as in April. Brisk sales in April and May, along with some

2. The earnings data were not rebenchmarked, but the average hourly earnings series were recalculated as a result of revisions to payroll employment. Although the revisions do not seem to greatly alter the longer-run pattern of average hourly earnings growth, the new data point to a steeper rise in earnings over the past few months.

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

	Proportion 1995:Q4	1994[1]	1995[1]	1995 Q4	1996 Q1	1996 Mar.	1996 Apr.	1996 May
				-Annual rate-		--Monthly rate---		
Total index	100.0	6.6	1.6	.6	3.0	-.5	.7	.7
Previous		6.6	1.6	.6	2.5	-.5	.9	
Manufacturing	86.5	7.6	1.4	1.4	2.4	-.8	1.1	.5
Motor veh. and parts	5.5	8.6	-2.6	-.5	-20.7	-14.1	19.0	.4
Aircraft and parts	1.7	-7.9	-17.1	-43.2	64.7	1.4	.3	.5
Manufacturing excluding motor vehicles, aircraft, and parts	79.2	8.0	2.2	3.0	3.0	.0	.0	.5
Consumer goods	23.1	4.7	.1	.0	.1	-.1	-.4	.0
Durables	3.7	6.4	-.4	4.0	-5.4	1.1	-.9	.3
Nondurables	19.4	4.4	.2	-.7	1.2	-.3	-.3	.0
Business equipment	13.6	13.1	7.7	8.2	14.2	.3	.6	1.0
Office and computing	3.1	29.6	36.2	45.0	50.6	3.8	3.0	2.2
Industrial	4.3	8.6	3.5	2.6	4.3	-.6	-.3	.4
Other	6.1	8.4	.8	-.5	4.7	-.6	-.2	.0
Defense and space equipment	1.7	-10.5	-7.3	-16.7	-2.3	1.1	-.7	.4
Construction supplies	5.3	8.0	-.4	6.0	.1	1.6	-.6	.3
Materials	28.7	10.5	3.4	4.5	3.7	-.2	.1	.7
Durables	20.3	12.1	6.3	8.0	7.3	-.3	.2	.9
Nondurables	8.2	6.9	-2.8	-2.9	-5.2	.0	.0	.2
Mining	6.0	1.2	-1.8	-7.7	2.0	3.2	-1.3	.0
Utilities	7.5	.2	6.2	-2.1	8.8	1.1	-1.8	3.1
Memo:								
Information-related products[2]	11.2	20.7	21.4	22.7	22.5	1.6	1.2	1.8

1. From the final quarter of the previous period to the final quarter of the period indicated.
2. Includes computer equipment, computer parts, semiconductors, communications equipment, and selected instruments.

CAPACITY UTILIZATION
(Percent of capacity; seasonally adjusted)

	1988-89 High	1967-95 Avg.	1995 Q4	1996 Q1	1996 Mar.	1996 Apr.	1996 May
Total industry	84.9	82.1	82.9	82.8	82.6	82.9	83.2
Manufacturing	85.2	81.4	82.0	81.6	81.3	81.9	82.0
Primary processing	89.0	82.6	86.1	85.2	85.2	85.0	85.2
Advanced processing	83.5	80.7	80.3	80.2	79.6	80.5	80.6

lingering effects of the GM strike, have left inventories of light motor vehicles at relatively lean levels. As a result, automakers set assembly schedules for June at a robust 12.4 million unit pace, and their current plans would hold production at a similar clip in the third quarter.

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

	1996					
	Apr.	May	June	Q1	Q2	Q3
			-sched.-		---sched.--	
U.S. production	12.2	12.2	12.4	11.0	12.2	12.4
Autos	6.3	6.5	6.6	5.5	6.5	6.7
Trucks	5.9	5.7	5.8	5.6	5.8	5.8
Days' supply						
Autos	59.4	50.4	...	...	...	...
Light trucks	71.5	68.8	...	...	...	...

Note: Components may not sum to totals because of rounding.

Apart from motor vehicles, the production of manufactured consumer goods was flat in May. The output of business equipment increased again last month: Information processing equipment made another sizable advance, and, in contrast to the previous two months, industrial equipment also moved up. The gains for industrial equipment are consistent with the pickup in new orders for these items earlier in the year. The output of construction supplies rose 0.3 percent last month, extending the recovery that began last fall. The production of materials surged 0.7 percent in May, reflecting gains in durable goods materials, particularly semiconductors, computer parts, and miscellaneous plastic materials.

Forward-looking indicators of industrial activity suggest moderate growth in the near term. New orders for durable goods, adjusted for inflation and excluding orders that are not closely related to near-term activity, rose 1.0 percent in May following a 1.5 percent advance in April. The orders and production components of the National Purchasing Managers' indexes remained on the positive side for a second consecutive month. Other private surveys also indicate that manufacturers expect moderate growth over the coming three months.[3]

3. The strike at the McDonnell Douglas plant that started on June 5 affects only about 6,700 workers and is expected to have a minor effect on industrial production.

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

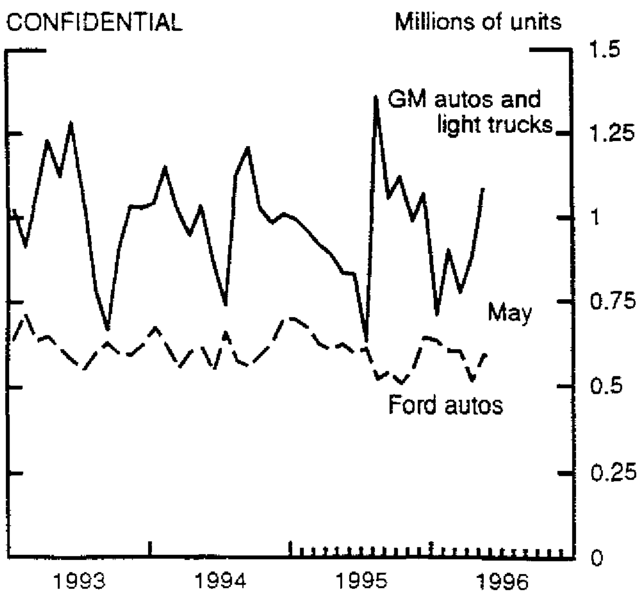
			1995		1996	1996		
	1994	1995	Q3	Q4	Q1	Mar.	Apr.	May
Total	15.05	14.72	15.03	14.91	15.16	15.83	14.45	15.76
Autos	8.99	8.63	8.94	8.65	8.61	9.28	8.26	9.27
Light trucks	6.06	6.09	6.09	6.26	6.54	6.55	6.19	6.49
North American[2]	12.91	12.82	13.18	13.12	13.46	13.93	12.88	13.98
Autos	7.26	7.12	7.46	7.26	7.32	7.83	7.13	7.97
Big Three	5.73	5.43	5.55	5.47	5.41	5.56	5.35	5.92
Transplants	1.52	1.69	1.91	1.79	1.91	2.27	1.79	2.06
Light trucks	5.66	5.69	5.72	5.87	6.15	6.10	5.74	6.01
Foreign produced	2.14	1.90	1.86	1.79	1.69	1.90	1.58	1.78
Autos	1.74	1.51	1.48	1.39	1.30	1.46	1.13	1.30
Light trucks	.40	.39	.37	.39	.40	.44	.45	.48

Note: Data on sales of trucks and imported autos for the most recent month are preliminary and subject to revision.

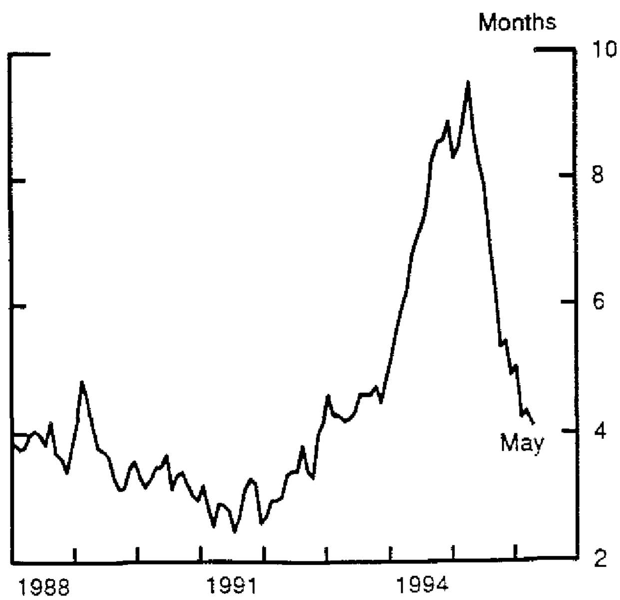
1. Components may not add to totals because of rounding.

2. Excludes some vehicles produced in Canada that are classified as imports by the industry.

GM and Ford Fleet Sales



Medium and Heavy Truck Order Backlog



Unfilled orders divided by shipments of North American product classes 5-8 trucks, seasonally adjusted.

The factory utilization rate rose to 82.0 percent of capacity in May, the same as in the fourth quarter of last year and not much above its 1967-95 average of 81.4 percent. In primary-processing industries, however, the utilization rate continues to be substantially above its long-run average.

Motor Vehicles

Sales of light motor vehicles jumped to 15.8 million units at an annual rate in May, a monthly gain of about 1-1/4 million units. Sales were pushed up about 1/4 million units by an increase in GM fleet sales (confidential), which had been fairly low the previous few months. In addition, Toyota, Honda, and Mazda included about 300,000 units (annual rate) of June sales in their May report.[4] So far in 1996, sales have averaged a 15.1 million unit pace, a little better than the 1994-95 level. Demand for light trucks has remained high, and continued use of incentive packages evidently has helped to maintain favorable views of prevailing car-buying conditions among consumers. Automakers have been a bit surprised by the strength of demand and have upped their sales forecasts for the year by 100,000 to 200,000 units; automakers' forecasts for light motor vehicle sales in 1996 now are a shade above the 15 million unit mark.

The demand for medium and heavy trucks, however, has continued to be soft so far this year. North American orders net of cancellations for truck classes 5 through 8 have averaged about 20,000 units a month, about the same as the 1995 average, but much lower than in 1993 and 1994. Backlogs have fallen from a peak of 9.5 months in April 1995 to 3.4 months in May 1996. This drop in backlogs has begun to show up in production, which has fallen 7-3/4 percent so far in 1996 from its average level in the fourth quarter of 1995. Industry analysts expect further declines in production.

Personal Income and Consumption

Total nominal retail sales rose 0.8 percent in May after slipping slightly in April. Nominal spending in the retail control category, which excludes sales at automotive dealers and at building material and supply stores, moved up 0.2 percent in May following a substantially upward-revised gain of 0.9 percent in April. On balance, the retail sales data, together with the available

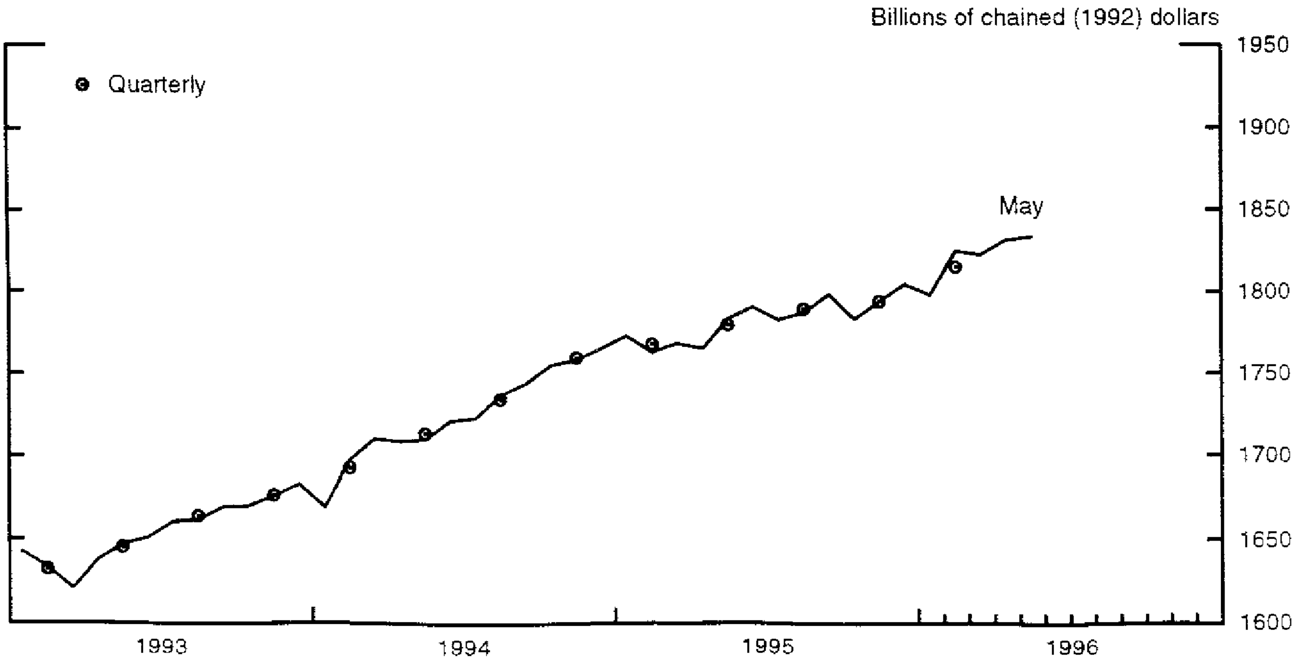
4. We understand that Toyota plans to report some sales from July in June.

Retail Sales
(Percent change; seasonally adjusted)

	1995	1996			
	Q4	Q1	Mar.	Apr.	May
Total sales	.7	2.3	.4	-.1	.8
Previous estimate		2.3	.5	-.3	
Retail control[1]	.4	1.6	.5	.9	.2
Previous estimate		1.7	.5	.5	
Durables	2.0	1.6	2.7	.2	1.2
Furniture and appliances	2.4	-.3	2.0	-.2	1.6
Other durable goods	1.6	3.3	3.3	.6	1.0
Nondurables	.1	1.6	.0	1.0	-.0
General merchandise	-1.1	2.3	-1.2	1.4	1.2
Food	1.2	.9	.4	.8	-.5
Other nondurable goods	-.0	1.8	.3	1.0	-.3

1. Total retail sales excluding building material and supply stores and automotive dealers (but including auto and home supply stores).

PCE Goods Excluding Motor Vehicles



Note. Data for the first quarter, April, and May are staff estimates.

information about prices, suggest that the average level in April and May of real consumer spending on goods excluding motor vehicles was about 0.9 percent above its first-quarter average, not at an annual rate.

Spending on services has advanced moderately, on net, in recent months. Real services expenditures were about flat in April after rising 0.6 percent in March. Expenditures for non-energy services increased modestly in April, with small gains in most major categories. In contrast, spending on energy services declined in April, as temperatures returned to more-normal levels after the unusually cold March. This pattern likely was reversed in May, with spending on electricity probably rising in response to unseasonable temperatures during the month.

Total personal income posted a sizable advance in April; nonetheless, disposable personal income fell 1/2 percent, reflecting a large increase in personal tax payments associated with the third (and final) installment on 1993 tax liabilities incurred by high-income taxpayers under the Omnibus Budget Reconciliation Act of 1993.[5] Despite the April decline, real disposable personal income was almost 2-3/4 percent above the level of a year ago (disposable income also was reduced in April 1995 by OBRA 1993-related payments). The saving rate fell to 3.7 percent in April after averaging 4.6 percent in the first quarter. However, disposable income and the saving rate should rebound in May with tax payments returning to more normal levels.

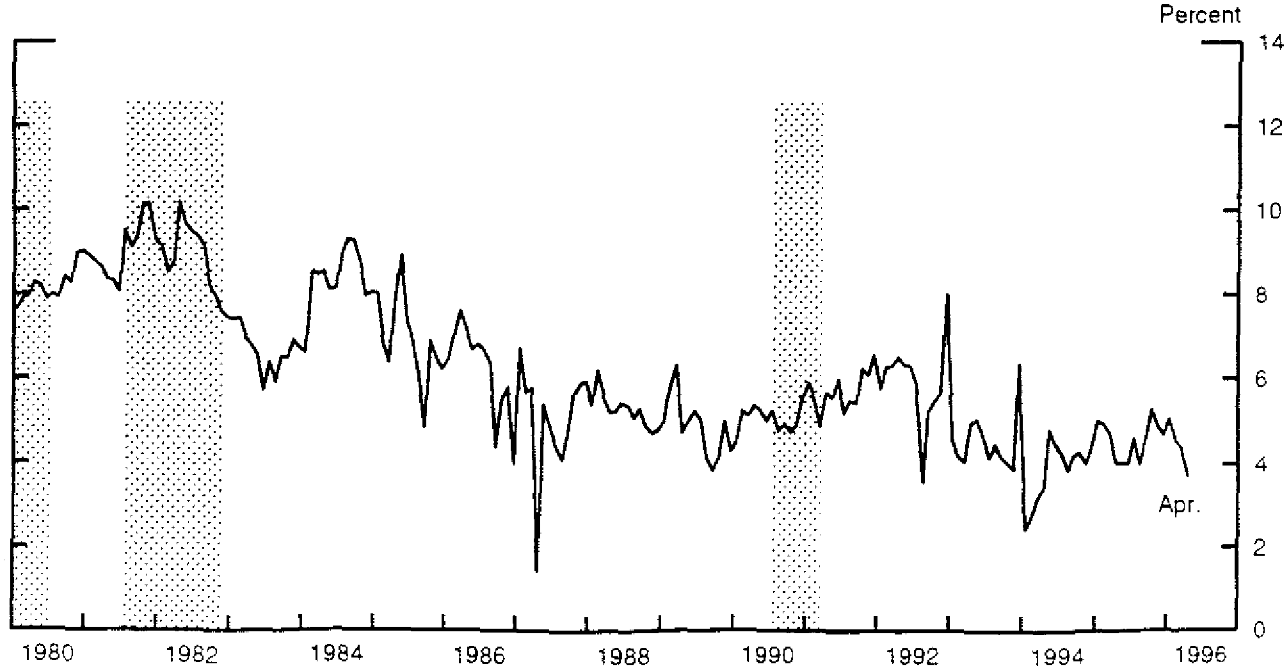
The latest reports on consumer sentiment exhibited divergent readings but continue to indicate positive attitudes among households. According to the preliminary report, the Michigan SRC index of consumer sentiment posted a moderate gain in early June and now stands above the midpoint of the relatively favorable range seen since early 1994. The early June increase reflected substantially more sanguine views of future conditions, which more than offset a

5. BEA generally spreads tax payments equally across the year in the seasonally adjusted NIPA data; however, exceptions are made for payments that it considers unusual. The installment payments on the OBRA 1993 tax liabilities were considered unusual. In contrast, the surprisingly large payments of nonwithheld personal income taxes in the unified budget in April (discussed in the section below on the federal sector) were not considered unusual, and thus they will have little effect on the month-to-month changes in NIPA tax payments for 1996. Indeed, BEA has already started to spread these payments out, raising its estimate of first-quarter nonwithheld taxes by $12 billion between the preliminary and advance GDP estimates.

PERSONAL INCOME
(Average monthly percent change)

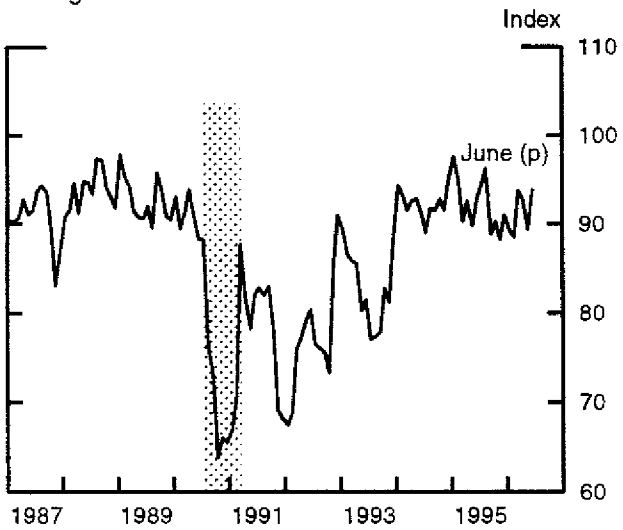
	1994	1995	1995 Q3	1995 Q4	1996 Q1	1996 Mar.	1996 Apr.
Total personal income	.3	.4	.4	.5	.4	.5	.5
Wages and salaries	.1	.4	.5	.4	.5	.5	.5
Private	.0	.4	.5	.4	.5	.5	.6
Other labor income	.4	.5	.3	.3	-.1	.4	.4
Proprietors' income	.7	.3	.4	.5	1.0	1.0	.7
Farm	-1.2	.4	1.7	4.9	6.7	3.6	1.0
Rent	2.8	.6	-.6	2.9	-1.4	-1.3	1.0
Dividend	.7	.6	.7	1.0	.6	.6	.4
Interest	.6	.5	.1	.5	.1	.1	.3
Transfer payments	.4	.6	.4	.4	.7	.6	.4
Less: Personal contributions for social insurance	.5	.4	.4	.3	.3	.4	.4
Less: Personal tax and nontax payments	.3	.6	.5	.3	1.0	1.1	7.0
Equals: Disposable personal income	.3	.4	.4	.5	.4	.4	-.5

Personal Saving Rate

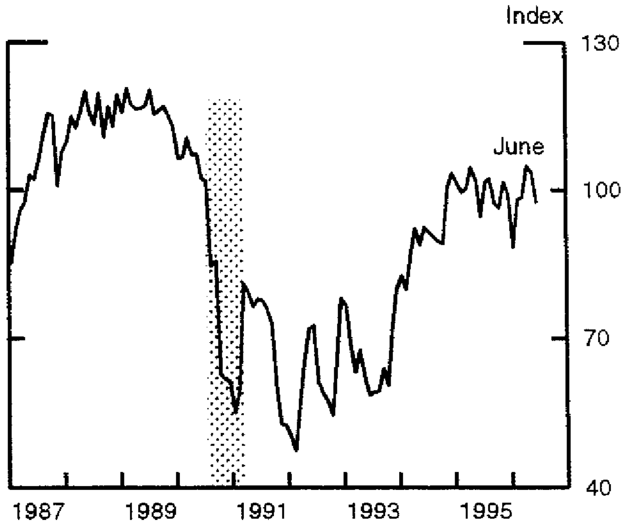


Household Indicators

Michigan Consumer Sentiment

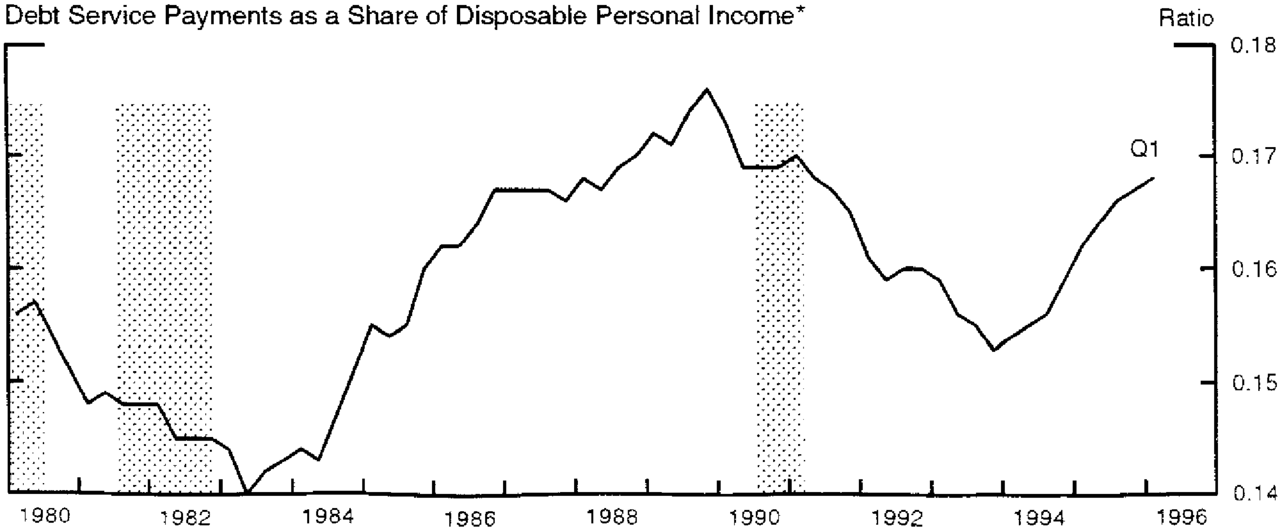


Conference Board Consumer Confidence



Ratio of Net Worth to Disposable Personal Income

Debt Service Payments as a Share of Disposable Personal Income*



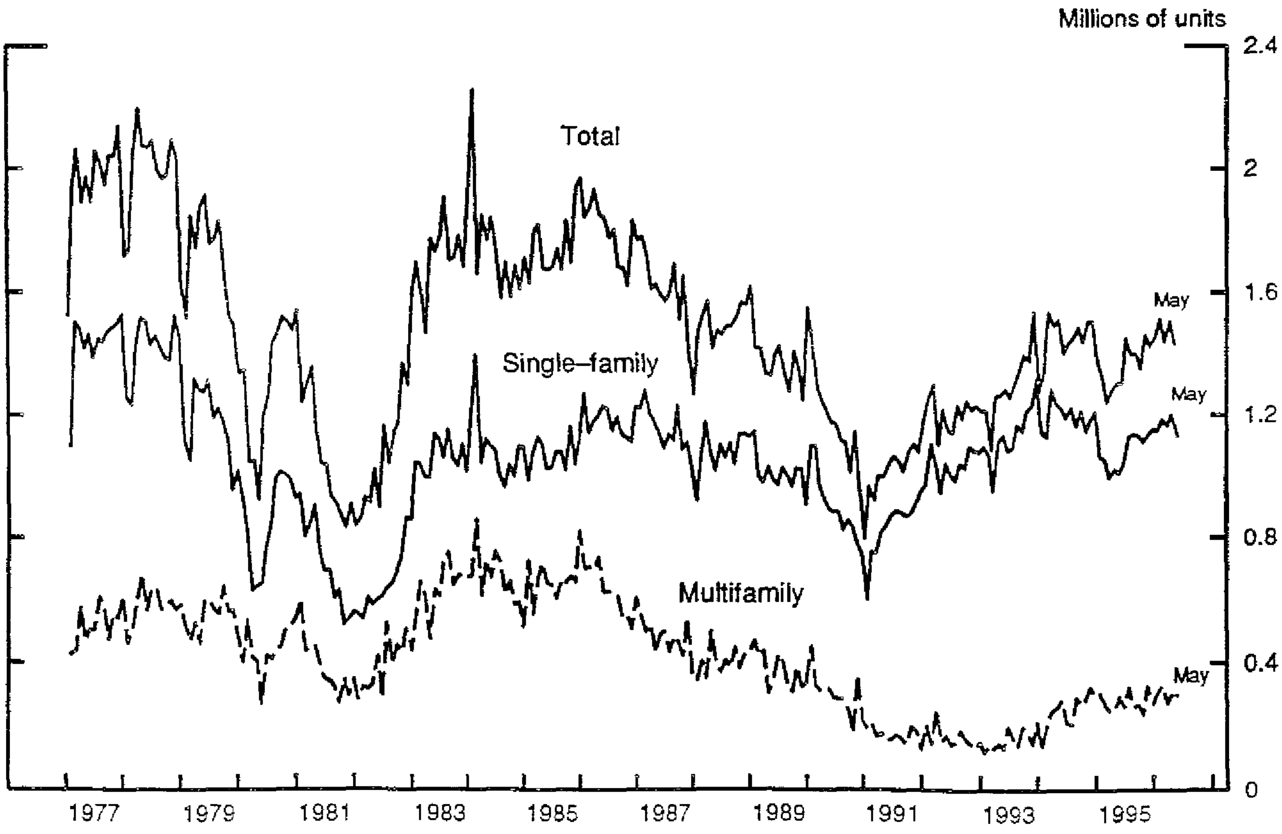
* Debt service payments estimated by Board staff.

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

		1995		1996			
	1995r	Q3r	Q4r	Q1r	Mar.r	Apr.r	Mayp
All units							
Starts	1.35	1.42	1.41	1.47	1.44	1.51	1.43
Permits	1.33	1.39	1.44	1.41	1.42	1.46	1.43
Single-family units							
Starts	1.08	1.13	1.13	1.16	1.16	1.20	1.13
Permits	1.00	1.05	1.08	1.08	1.10	1.12	1.09
New home sales	0.67	0.72	0.68	0.75	0.73	0.78	n.a.
Existing home sales	3.80	4.04	3.98	3.95	4.20	4.20	4.26
Multifamily units							
Starts	0.28	0.29	0.28	0.31	0.28	0.30	0.30
Permits	0.33	0.34	0.36	0.33	0.33	0.34	0.34
Mobile Homes							
Shipments	0.34	0.34	0.35	0.35	0.36	0.38	n.a.

Note. p Preliminary. r Revised. n.a. Not available.

Private Housing Starts
(Seasonally adjusted annual rate)



deterioration in respondents' assessments of current conditions. In contrast, the June Conference Board report shows a considerable decline in the index for consumer sentiment, but it remained in the middle of the favorable range seen over the past couple of years.

Household wealth has been bolstered this year by the further rise in stock prices, and, to a lesser degree, a pickup in the appreciation of house prices. The most recent balance sheet data are for the first quarter; these data indicate that assets increased far more than liabilities and that the ratio of total household net worth to disposable income climbed to 5.1, its highest level in more than two decades. Given the further increase in stock and house prices this spring, household net worth likely has risen further in the second quarter.

Given the solid income growth and the surge in wealth since the beginning of 1995, it is perhaps surprising that consumer spending has grown at an annual rate of only about 2-1/2 percent over this period. One possibility, of course, is that the income or spending data could be revised significantly at some point. But taking current data at face value, it is possible that, in a significant portion of the household sector, financial pressures associated with rising debt-service obligations have tempered spending growth somewhat. Rising delinquency rates for consumer loans suggest that some households have had problems meeting their debt-service payments. However, this rise in delinquencies most likely exaggerates the degree of real financial stress because lenders have made credit available to lower-income or otherwise riskier households that previously were deemed unqualified. Another factor that may have limited the response of household spending to recent wealth gains is an increase in precautionary saving in response to heightened concerns about job security or the adequacy of retirement income.

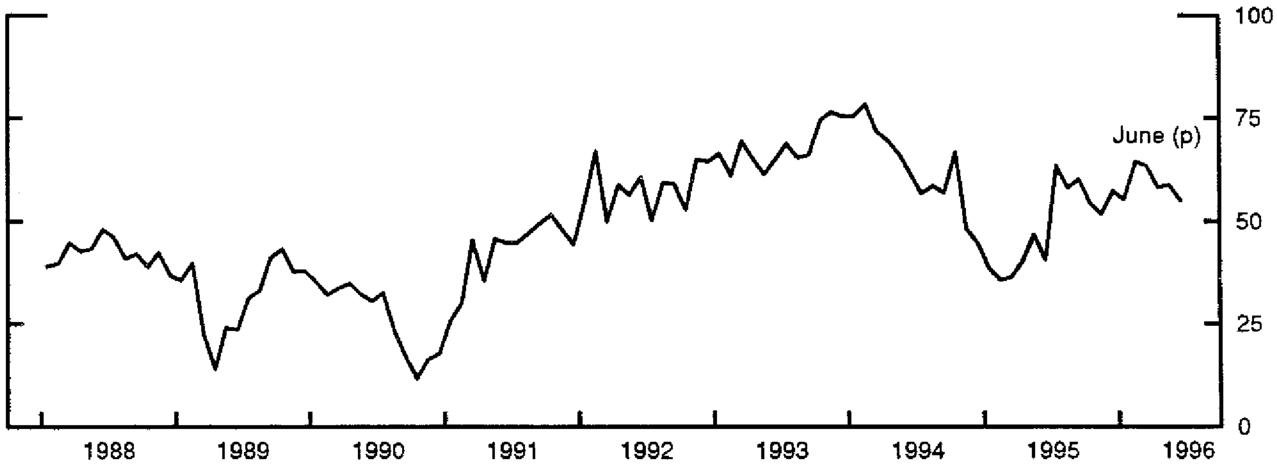
<u>Housing Markets</u>

Housing starts declined in May from the high April level. Single-family starts fell 6 percent, to a 1.13 million unit annual rate, the slowest pace since last November. This decline in starts suggests that the rise in mortgage rates in recent months has begun to damp construction activity. Some confirmation can be found in consumer attitudes toward homebuying, which have turned slightly less favorable since March, mainly reflecting a more widespread perception that mortgage rates are high. In addition, although

Indicators of Housing Demand

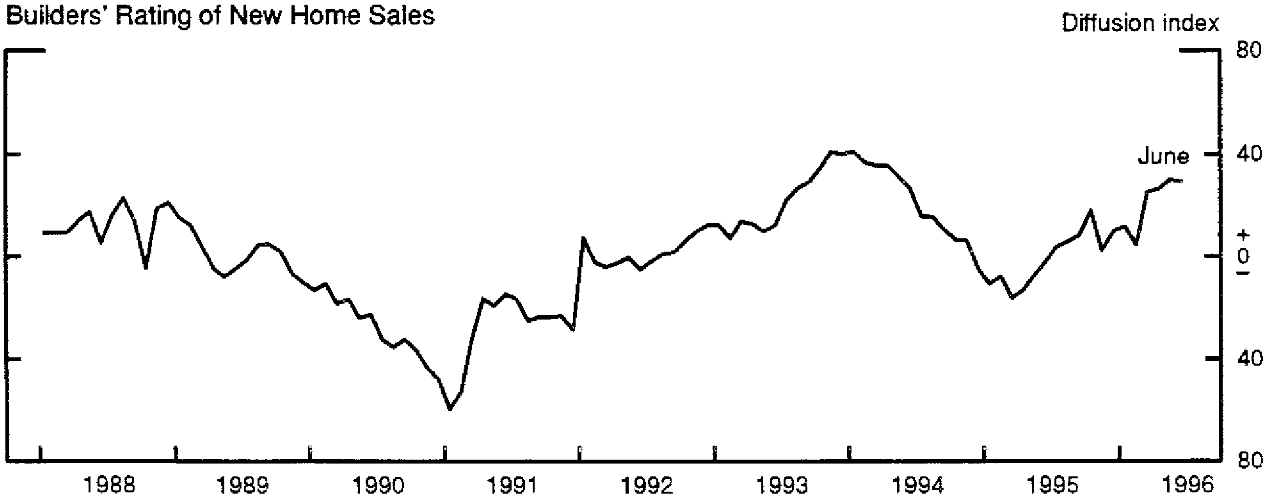
(Seasonally adjusted; FRB seasonals)

Consumer Homebuying Attitudes



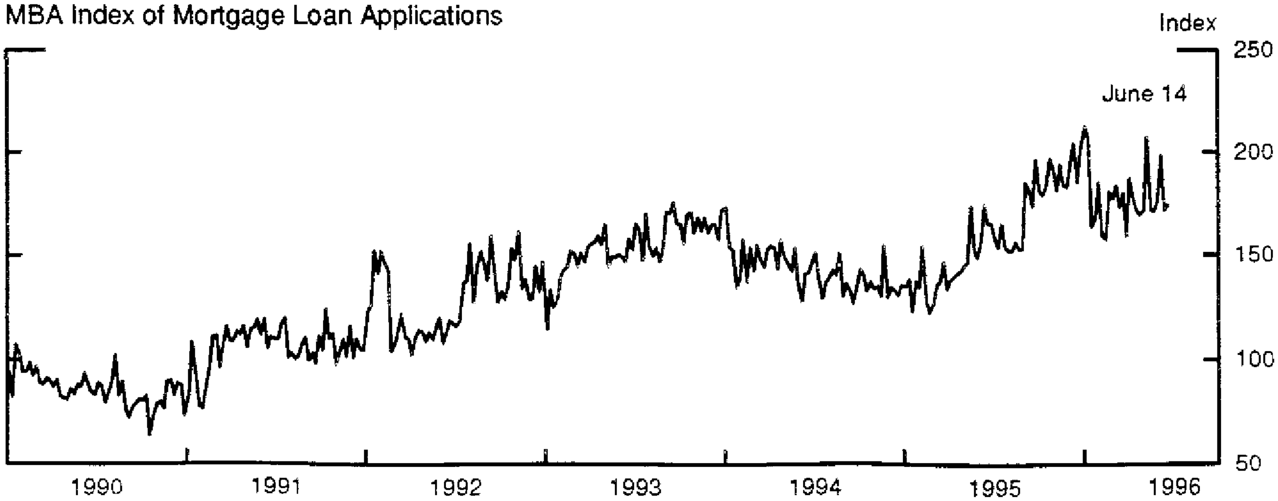
Note. The homebuying attitudes index is calculated from Survey Research Center data as the proportion of respondents rating current conditions as good minus the proportion rating such conditions as bad.

Builders' Rating of New Home Sales



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

MBA Index of Mortgage Loan Applications



Note. MBA index equals 100 on March 16, 1990, for NSA series still relatively low, the proportion of conventional home mortgages with adjustable rate features picked up noticeably in April; a shift toward ARM financing is typical in a market in which households are attempting to lessen the impact of higher mortgage rates on loan qualification and housing affordability.

The starts figures, however, may overstate the magnitude of the drop in building. Permit issuance for single-family units--a statistically more accurate figure than housing starts--also declined in May, but only 2 percent; starts were abnormally low relative to the level of permits. Moreover, sales of existing homes were strong through May. Through early June, home builders' assessments of new home sales and applications for mortgages to finance home purchases also continued to indicate strength in the single-family market.

In the multifamily sector, housing starts were unchanged in May, continuing the flat pattern of the past year and a half. At the national level, construction appears to have outpaced demand. The vacancy rate for multifamily rental housing has risen in the past two quarters (relative to year-earlier levels), and the absorption rate for rental apartments declined in 1995 after having risen in the four preceding years.

Shipments of mobile homes, which grew rapidly between 1991 and 1995, have picked up noticeably again in recent months. In April, shipments reached 378,000 units at an annual rate, a twenty-two year high.

Business Fixed Investment

Growth in business fixed investment appears to be slowing in the current quarter. Earlier this year, such outlays surged, reflecting an explosion in computer expenditures and fairly strong gains in most of the other major categories. However, indicators for the current quarter point to more modest gains in both equipment outlays and nonresidential structures.

New orders for nondefense capital goods excluding aircraft and parts were little changed in May after dropping 3.3 percent in April. However, shipments of these goods retraced half of their April decline. Among the major components, both orders and shipments of computing equipment have been quite volatile in recent months, but they continue to trend upward at a hefty clip--with shipments standing 10 percent above a year earlier in nominal terms. Bookings for communications equipment declined sharply for the

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

	1995		1996	1996		
	Q3	Q4	Q1	Mar.	Apr.	May
Producers' durable equipment						
Shipments of nondefense capital goods	.7	3.6	-.8	.6	-2.1	3.4
Excluding aircraft and parts	1.3	3.6	.7	.2	-2.2	1.3
Office and computing	2.4	5.3	4.7	-3.8	-5.2	3.4
Communications equipment	1.7	8.7	-1.6	3.4	-4.2	2.4
All other categories	.9	1.6	-.2	1.0	-.3	.1
Shipments of complete aircraft[1]	-9.5	-3.9	1.4	27.9	-19.4	n.a.
Sales of heavy trucks	-7.6	6.4	-2.2	-11.3	3.0	10.0
Orders of nondefense capital goods	2.1	7.5	3.4	4.7	-12.6	9.6
Excluding aircraft and parts	-.3	3.3	3.6	-2.0	-3.3	.0
Office and computing	-.7	8.3	2.8	-3.0	-3.5	1.6
Communications equipment	3.5	3.1	7.6	10.0	-11.4	-11.8
All other categories	-1.1	1.5	2.8	-4.8	-.6	2.7
Nonresidential structures						
Construction put-in-place	2.8	-1.7	.6	1.0	1.5	n.a.
Office	5.8	-8.2	-7.2	-1.0	6.6	n.a.
Other commercial	2.1	6.4	2.4	4.0	-.3	n.a.
Institutional	1.0	-3.7	-1.3	1.7	2.9	n.a.
Industrial	-1.6	1.4	-1.9	-1.2	-.4	n.a.
Public utilities	4.3	-12.3	-.8	.4	-.1	n.a.
Lodging and miscellaneous	12.0	17.0	17.8	.3	5.2	n.a.
Rotary drilling rigs in use	-.9	-5.4	6.6	5.8	4.8	3.8
Memo:						
Business fixed investment[2]	5.2	3.1	12.3	n.a.	n.a.	n.a.
Producers' durable equipment[2]	4.9	4.0	13.2	n.a.	n.a.	n.a.
Nonresidential structures[2]	6.2	.9	9.6	n.a.	n.a.	n.a.

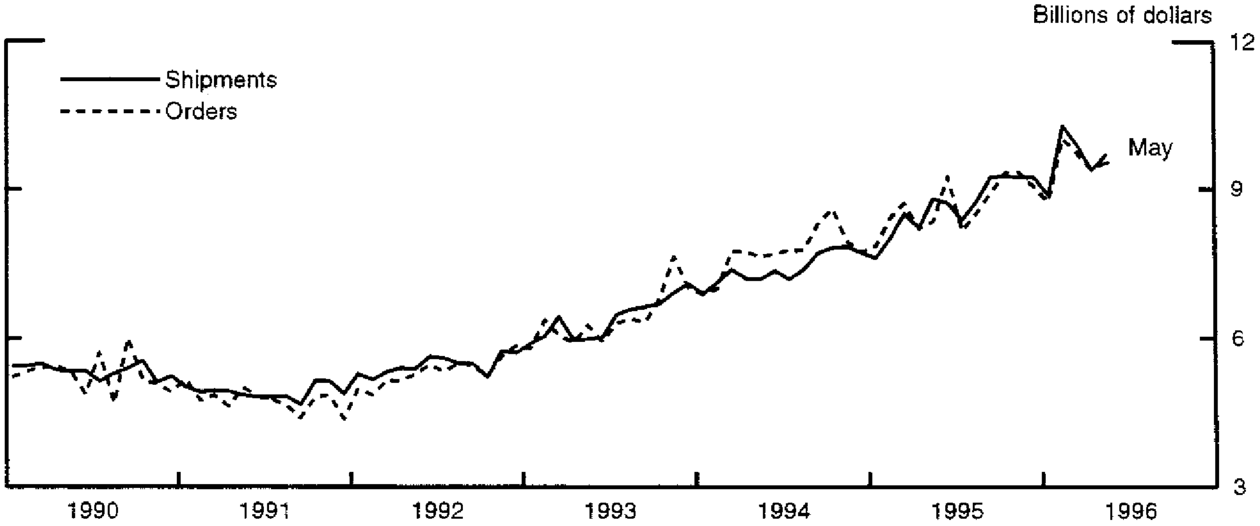
n.a. Not available.

1. From the Current Industrial Report "Civil Aircraft and Aircraft Engines." Monthly data are seasonally adjusted using FRB seasonal factors constrained to BEA quarterly seasonal factors. Quarterly data are seasonally adjusted using BEA seasonal factors.

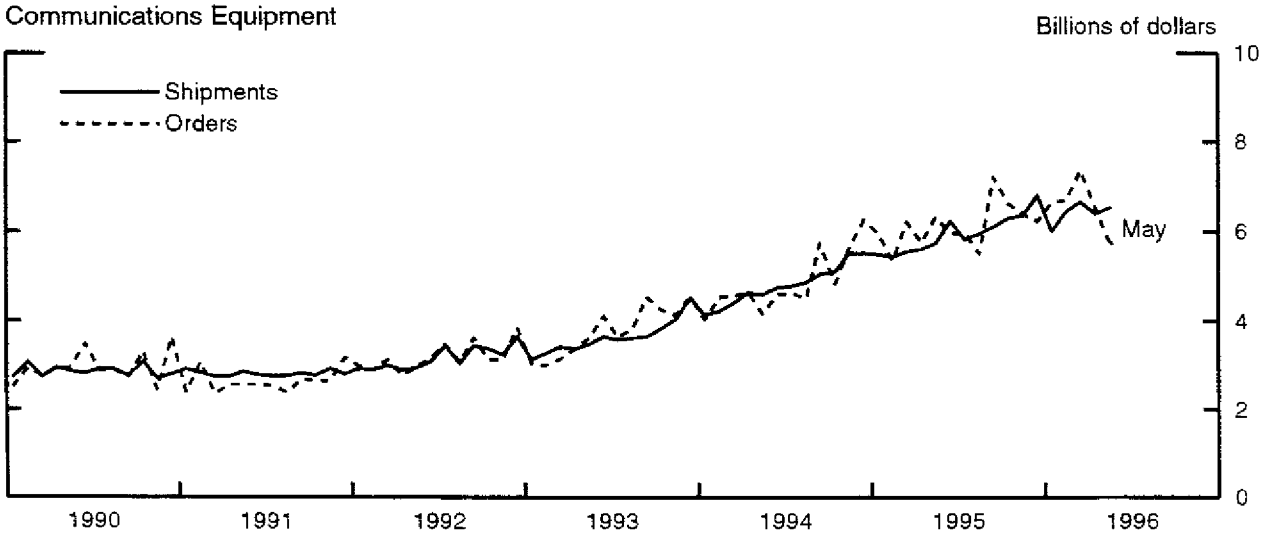
2. Based on 1992 chain-weighted data; percent change, annual rate.

Orders and Shipments of Nondefense Capital Goods

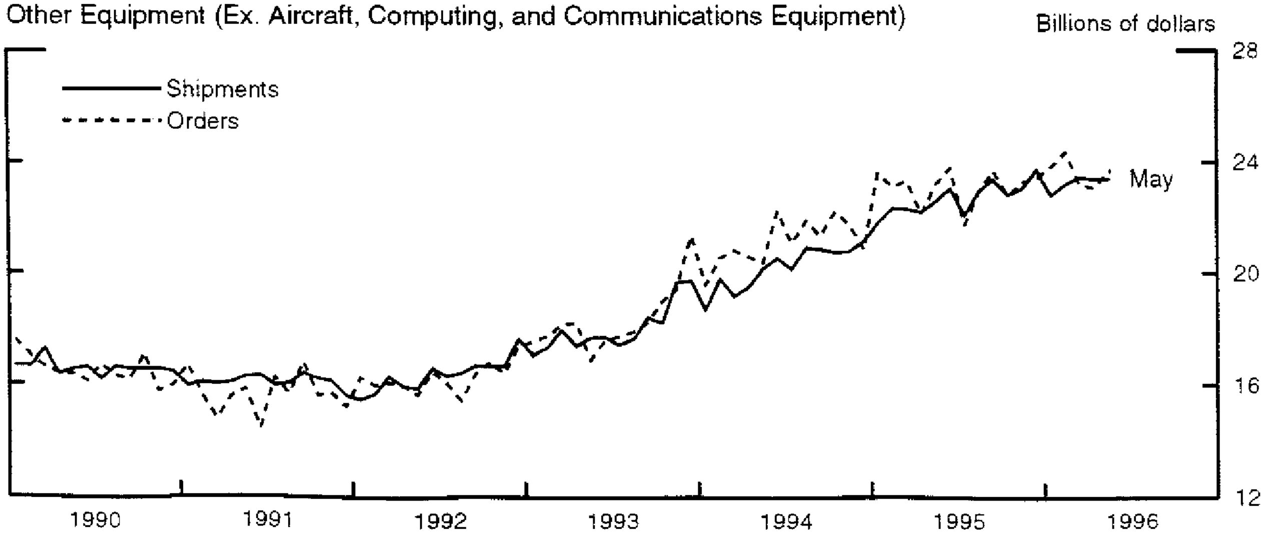
Office and Computing Equipment



Communications Equipment

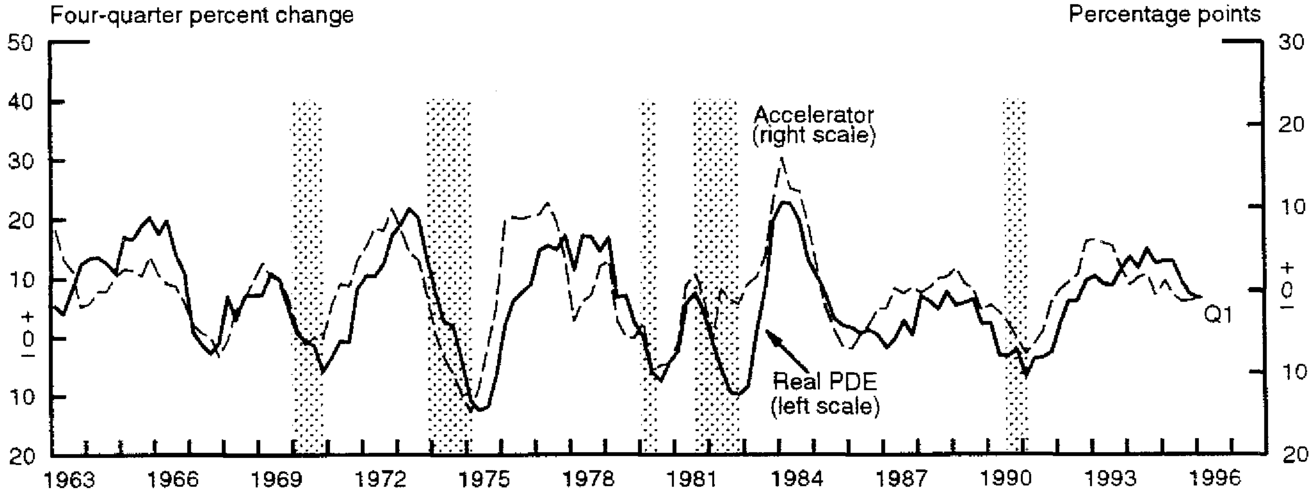


Other Equipment (Ex. Aircraft, Computing, and Communications Equipment)



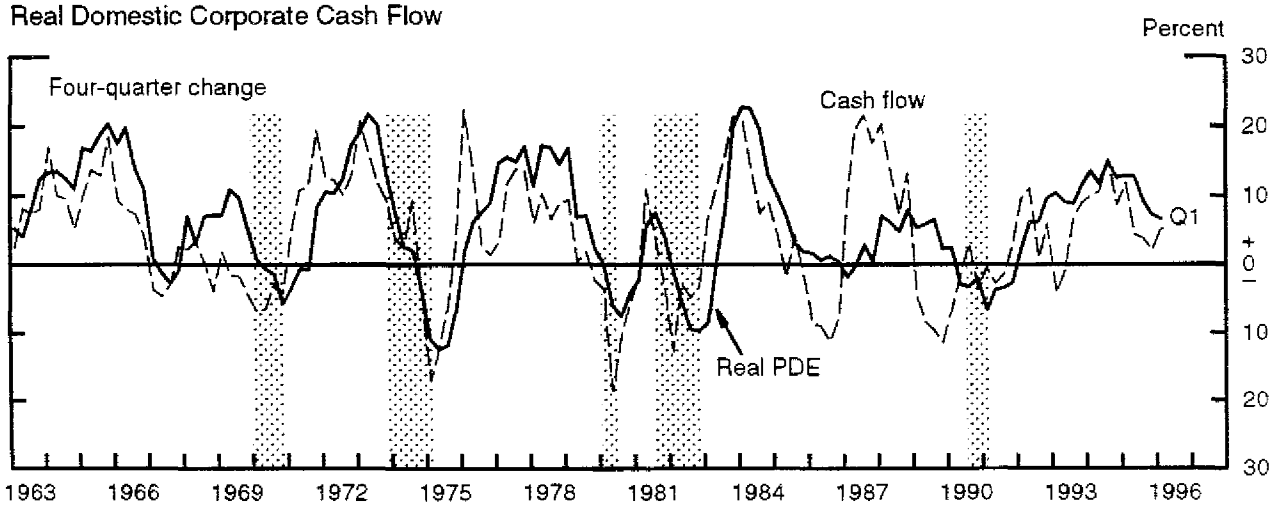
Fundamental Determinants of Equipment Spending

Acceleration of Business Output

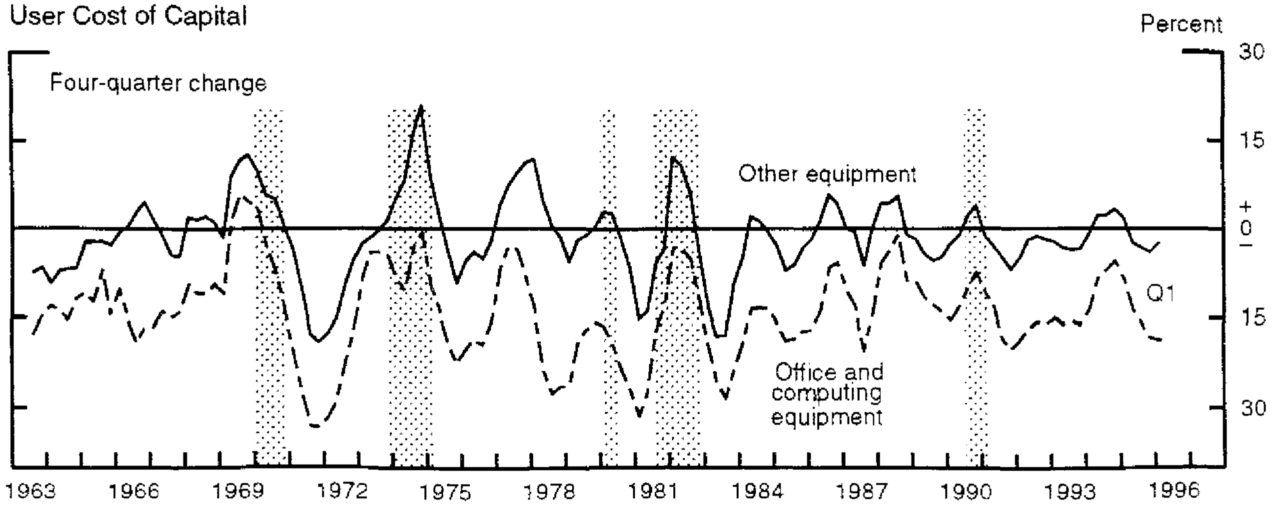


Note. The accelerator is the eight-quarter percent change in business output less the year-earlier eight-quarter percent change.

Real Domestic Corporate Cash Flow



User Cost of Capital



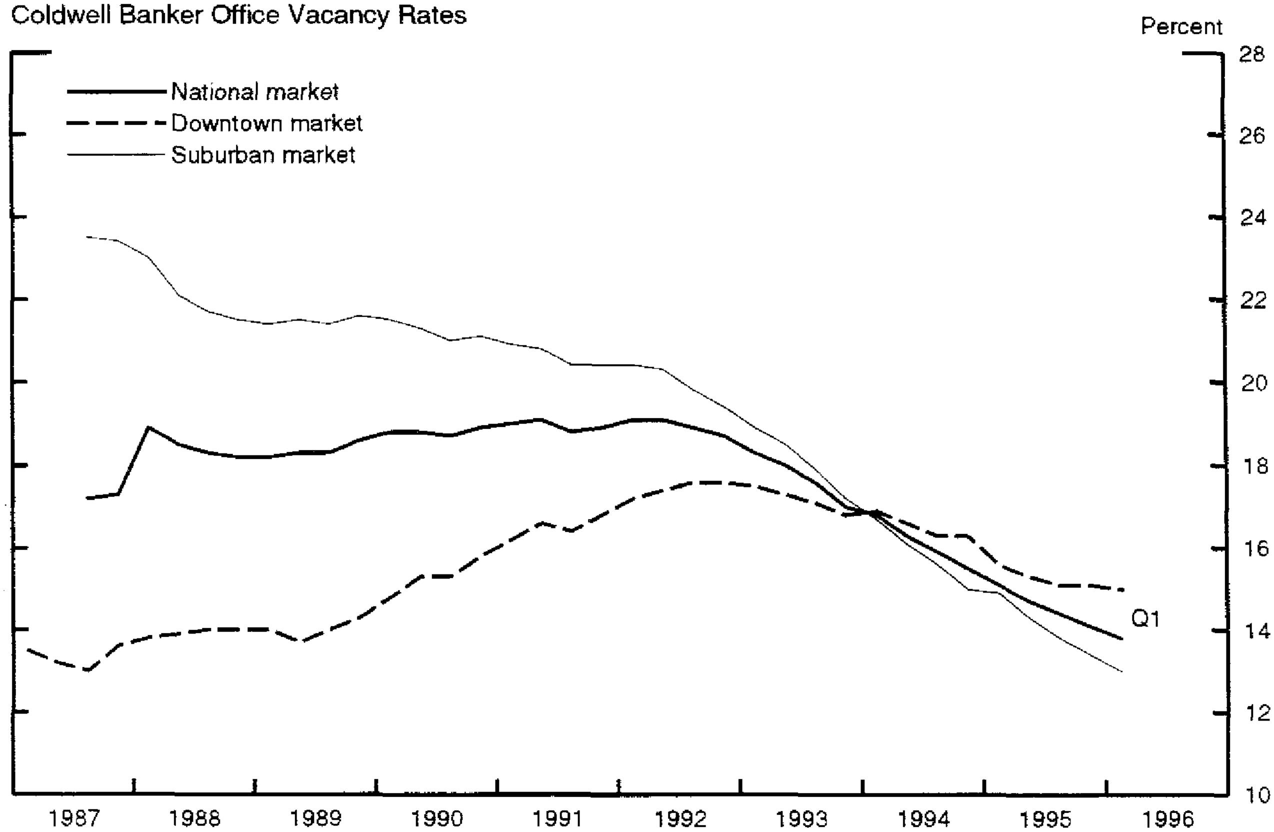
second month in a row. Despite the drop in orders, however, shipments of communications equipment turned up in May; the pickup likely reflects the rise in backlogs that occurred in the first quarter when orders for communications equipment jumped 7-1/2 percent while shipments declined. Orders for other nondefense capital goods (that is, for nondefense capital goods excluding aircraft, computers, and communications equipment) were little changed in May after declining in the previous two months. Shipments of these goods edged up in May.

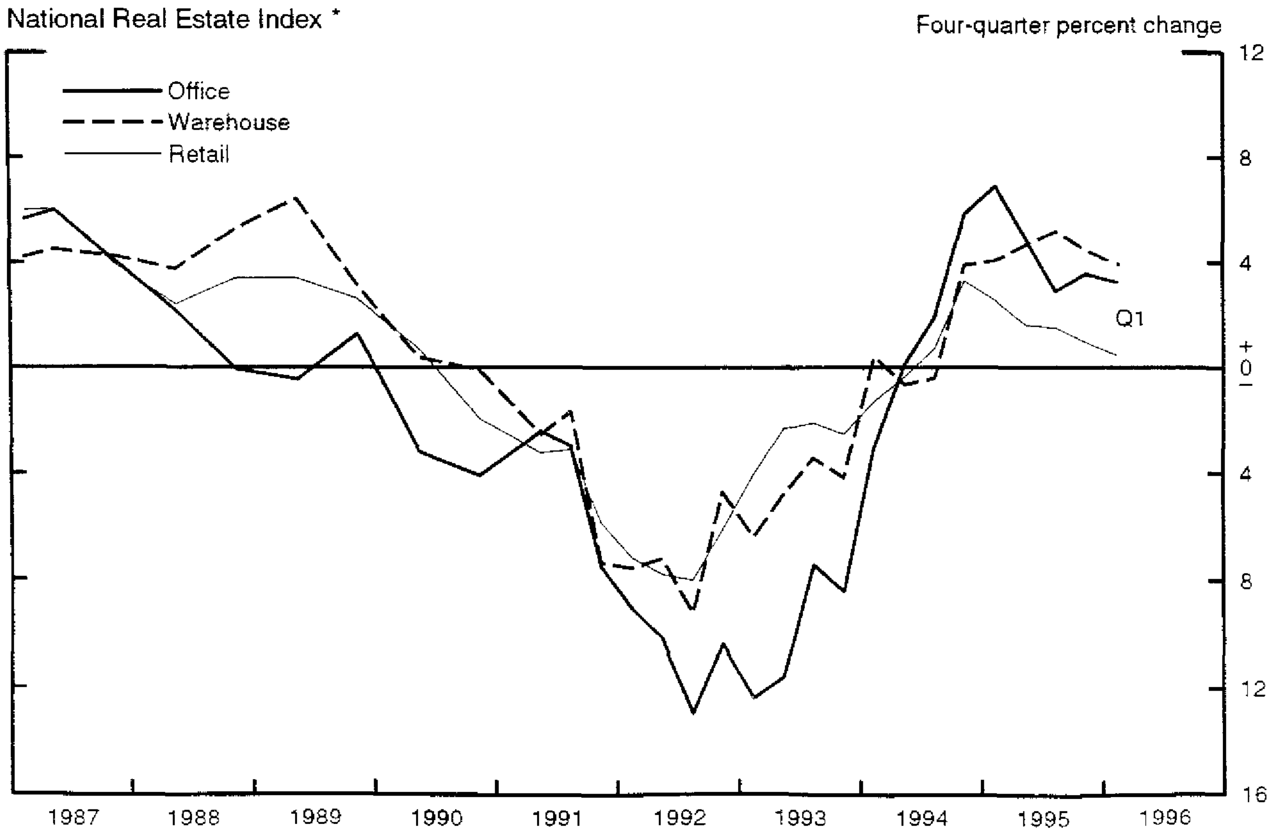
On balance, the fundamental determinants of capital spending are pointing to less-robust gains in equipment outlays in coming quarters. In the current expansion, the accelerator--represented in the chart by the change in the eight-quarter growth rate of business output--peaked in 1993, and has waned since then. Growth in cash flow also has moderated substantially over the past two years. Econometric models that incorporate these factors predicted the 1995 deceleration in PDE and expect yet slower growth in coming quarters. Only the cost of capital is currently sending an upbeat signal; factoring in typical lag relationships, the sharp decline in interest rates last year and the ready availability of equity financing ought to be providing considerable support for investment during the first half of this year. However, the backup in corporate borrowing rates in recent months would be expected to exert a drag on investment late this year and in 1997.

With regard to computers, many industry analysts expect growth in unit shipments of personal computers to cool off in 1996, to a rate somewhere around 15 percent, about 10 percentage points less than the 1995 gain. While this number may seem optimistic given the recent slower growth in computer spending, our contacts are looking for considerable strength in the latter part of this year, in large part because they expect businesses will upgrade their hardware to take full advantage of a new version of Windows NT due out late this summer. Moving upstream, DRAM prices are still quite weak, and given the spurt in capacity during the past nine months or so, a substantial rebound in memory prices is not likely for some time. Disk drive makers also appear to have had overly optimistic demand forecasts and currently are burdened with unsold inventories and excess production capacity.

Spending for real nonresidential structures, after rising 5 percent in 1995, recorded a strong advance in the first quarter of

Nonresidential Construction Indicators

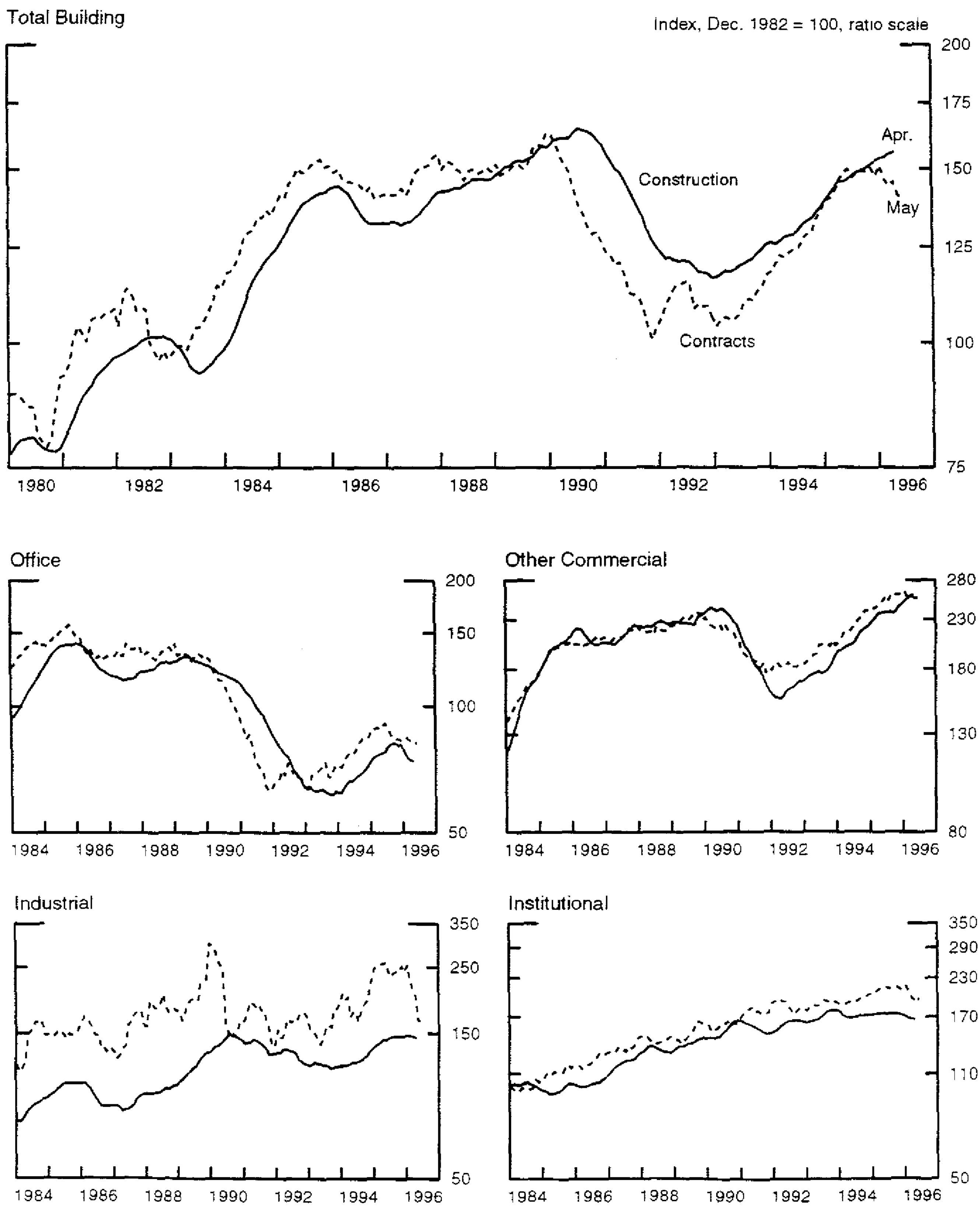




*Data are semiannual from 1986 to 1991, and quarterly from 1992 to present.

Nonresidential Construction and Contracts

(Six-month moving average)



Note. For contracts, total includes private only, while individual sectors include public and private.

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

	1995		1996	1996		
	Q3	Q4	Q1	Feb.	Mar.	Apr.
Book value basis						
Total	52.5	13.7	16.4	7.8	-29.7	52.2
Excluding wholesale and retail motor vehicles	57.0	9.7	24.7	11.8	10.1	50.6
Manufacturing	24.7	9.4	12.0	10.6	-8.2	6.7
Wholesale	16.7	6.0	7.3	-8.3	10.5	41.5
Excluding motor vehicles	19.4	8.4	7.3	-10.3	17.5	33.3
Retail	11.1	-1.7	-2.9	5.4	-32.1	4.0
Automotive	-1.8	6.4	-8.4	-6.0	-32.8	-6.6
Excluding auto dealers	12.9	-8.1	5.5	11.5	.7	10.6
Chained (1992) dollars basis[1]						
Total	31.0	8.0	-9.1	10.4	-65.6	n.a.
Excluding motor vehicles	40.3	10.8	14.6	12.1	-10.3	n.a.
Manufacturing	16.4	11.2	12.4	14.4	-9.2	n.a.
Wholesale	11.6	3.8	-.1	-7.4	-7.3	n.a.
Excluding motor vehicles	14.1	6.6	1.0	-9.9	2.0	n.a.
Retail	3.0	-7.0	-21.4	3.4	-49.0	n.a.
Automotive	-6.2	.4	-24.2	-4.9	-49.2	n.a.
Excluding auto dealers	9.2	-7.4	2.8	8.4	.1	n.a.

1. The March book-value changes have been revised from preliminary figures reported last month; these revisions have not yet been incorporated in the March chained (1992) dollar figures.

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

	1995		1996	1996		
	Q3	Q4	Q1	Feb.	Mar.	Apr.
Book value basis						
Total	1.42	1.41	1.40	1.40	1.39	1.38
Excluding wholesale and retail motor vehicles	1.39	1.37	1.38	1.37	1.37	1.35
Manufacturing	1.39	1.38	1.39	1.39	1.38	1.36
Wholesale	1.35	1.33	1.32	1.32	1.31	1.32
Excluding motor vehicles	1.31	1.30	1.30	1.29	1.29	1.29
Retail	1.55	1.53	1.49	1.50	1.48	1.48
Automotive	1.78	1.79	1.66	1.69	1.64	1.69
Excluding auto dealers	1.47	1.45	1.44	1.43	1.43	1.42
Chained (1992) dollars basis						
Total	1.40	1.39	1.37	1.37	1.37	n.a.
Excluding motor vehicles	1.37	1.35	1.35	1.35	1.35	n.a.
Manufacturing	1.40	1.39	1.39	1.39	1.38	n.a.
Wholesale	1.37	1.34	1.34	1.34	1.34	n.a.
Excluding motor vehicles	1.34	1.32	1.32	1.31	1.32	n.a.
Retail	1.44	1.42	1.37	1.38	1.36	n.a.
Automotive	1.75	1.74	1.50	1.57	1.47	n.a.
Excluding auto dealers	1.35	1.33	1.34	1.33	1.33	n.a.

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

this year. Construction put-in-place for these structures rose 1-1/2 percent in April after a 1 percent gain in March. Upbeat anecdotal reports in the Beige Book are consistent with the recent gains in nonresidential construction. Vacancy rates for office buildings, which have improved markedly in recent years, fell further in the first quarter. The National Real Estate Index indicates that transactions prices for both office buildings and warehouses continued to rise through the first quarter of this year, while prices of retail structures flattened out.

Despite these favorable current conditions, the data on contracts, which are another set of leading indicators of nonresidential construction, have soured in all the major building categories. Declines have been especially pronounced in the office and industrial sectors. The drop in contracts in the industrial sector is not surprising, given that capacity utilization has receded to more normal levels during the past year or so. In addition, contracts for "other commercial" structures (including retail stores) have turned down in recent months; this sector appears to be burdened by excess retail floor space in many parts of the country.

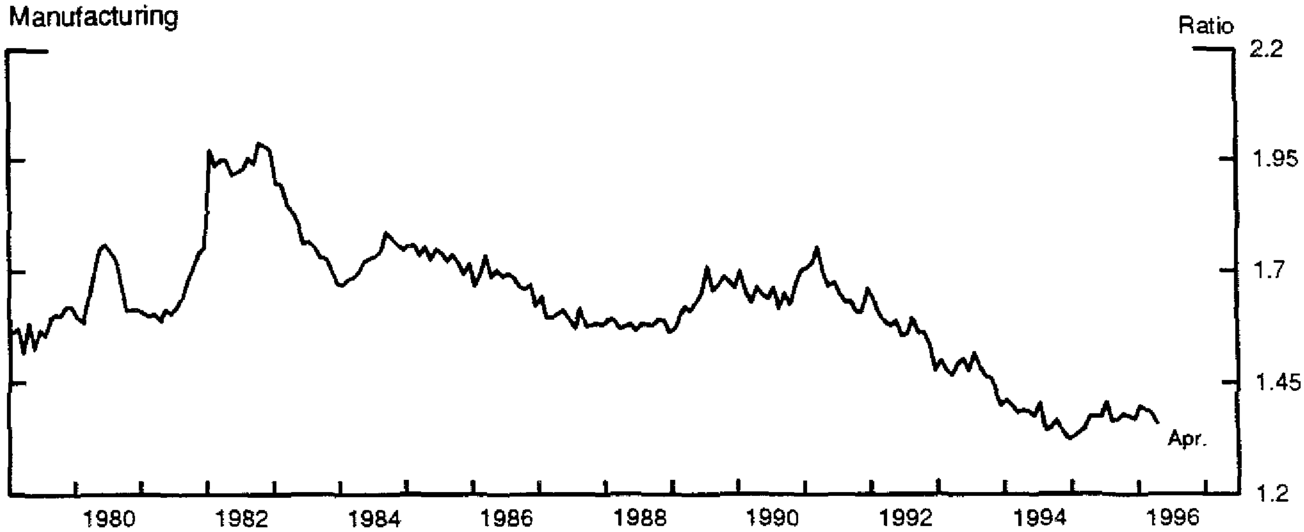
Inventories

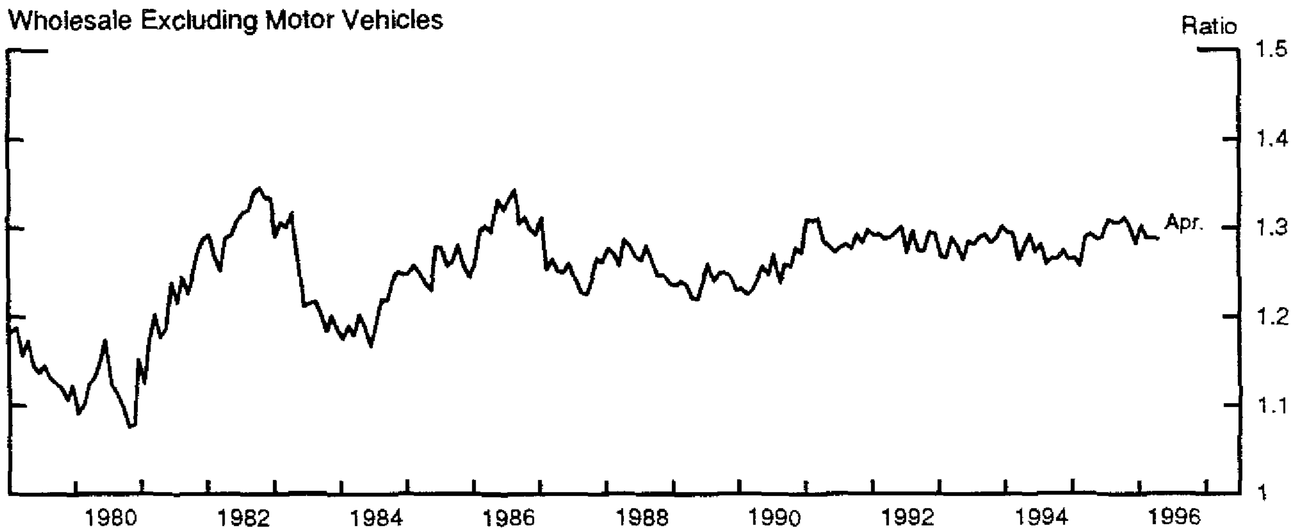
The condition of business inventories improved considerably by April. Manufacturers made significant progress in reducing their stock imbalances, while wholesale and retail trade inventories have remained at satisfactory levels in most areas and even appeared lean in some sectors.

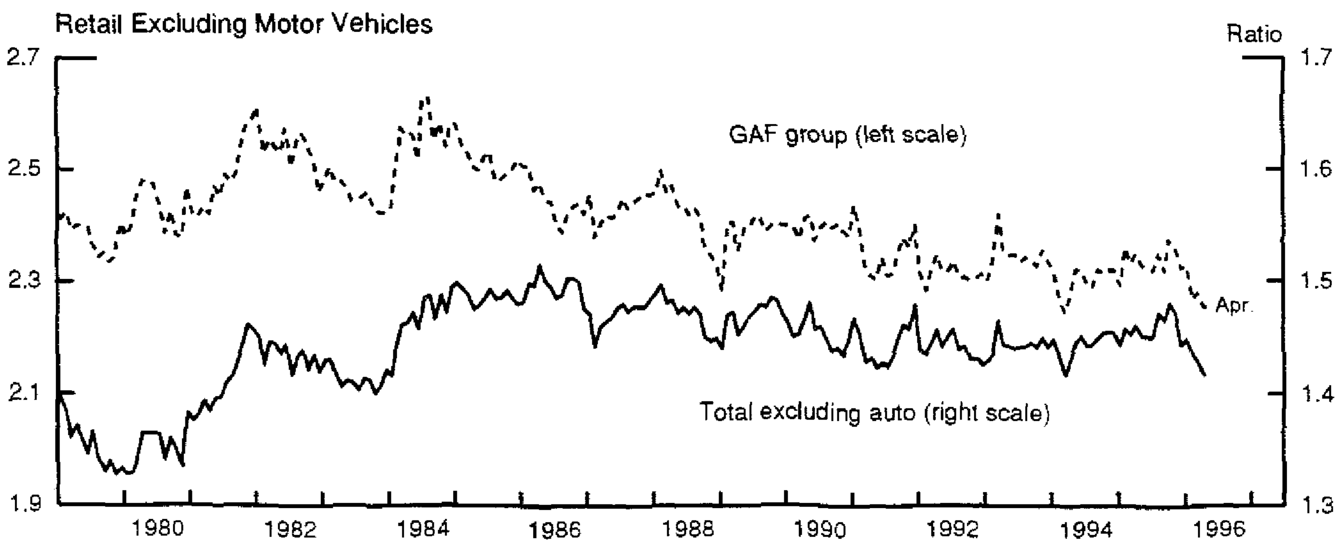
Restrained output during the first quarter and increased shipments in March and April helped to clear away manufacturers' excess stocks. In several industries and market groupings--primary metals, textiles, printing and publishing, and household durables--correction efforts had, by early in the second quarter, returned inventory-shipments ratios to levels well below their recent highs. However, in a few other industries--notably chemicals and paper--inventories remained on the high side in April and may need to be trimmed further. For producers of capital goods, whose orders and shipments have been well maintained over the past year, inventory accumulation resumed in April after a brief interruption in March. The inventory-shipments ratio for capital equipment as a group was relatively low in April, but with orders for these items flattening,

Inventory-Sales Ratio, by Major Sector

(Book value)







inventory investment in this segment of manufacturing could moderate in the months ahead.

SELECTED MANUFACTURERS' INVENTORY-SHIPMENTS RATIOS

	Previous highs		1996			
	1990-91	1995-96	Jan.	Feb.	Mar.	Apr.
Industry grouping						
Primary metals	2.08	1.55	1.52	1.53	1.55	1.50
Textiles	1.72	1.78	1.78	1.72	1.68	1.70
Printing & pub.	.99	.87	.87	.86	.82	.81
Chemicals[1]	1.43	1.19	1.17	1.19	1.19	1.18
Paper[1]	1.31	1.28	1.25	1.27	1.28	1.27
Market grouping						
Household durables	2.16	1.80	1.79	1.76	1.62	1.63
Capital equipment	2.19	1.65	1.61	1.58	1.60	1.56

1. The April inventory-shipments ratio is near its recent peak.

Trade establishments began to make significant progress in gaining control of inventories last year. In wholesale trade, scattered inventory paring occurred as early as November and continued through February. In retail trade, inventories were reduced sharply in December; further liquidations, largely in nondurable stocks, were observed again in March. With but a few exceptions (notably, furniture and appliances in retail trade, and hardware and plumbing in wholesale trade), the inventory-sales ratios for most types of trade establishments in April were at or near the lower range of their recent readings. It is worth noting that retail general merchandise and apparel stores, where serious imbalances often have occurred in the past, have been able to keep their stocks well under control since late last year.

Federal Sector

On a unified basis, the federal government recorded a budget surplus of $19 billion in April and May, compared with a $10 billion surplus a year ago. The adjusted surplus, which corrects for shifts in the timing of certain outlays and excludes net outlays attributable to deposit insurance and spectrum auctions, was up $22 billion from last year.

Outlays in April and May continued to rebound from the low levels seen earlier in the year. For the first six months of the fiscal year ended in March, adjusted outlays had risen 1.7 percent from a year earlier; strong outlays in April and May brought year-over-year growth to 2.8 percent for the first eight months of the

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

	April & May		Fiscal year to date totals			
	1995	1996	1995	1996	Dollar change	Percent change
Outlays	245.6	274.3	1006.7	1047.7	41.0	4.1
Deposit insurance (DI)	-1.9	-1.2	-12.6	-6.6	6.0	-47.6
Spectrum auction (SA)	-.6	.0	-.6	-.2	.4	-.7
Other	247.4	275.5	1019.9	1054.5	34.6	3.4
Receipts	255.8	293.4	870.2	938.6	68.4	7.9
Deficit(+)	-10.2	-19.1	136.5	109.1	-27.4	-20.0
	Adjusted for payment timing shifts[1] and excluding DI and SA					
Outlays	253.7	269.6	1025.5	1054.5	29.0	2.8
National defense	43.0	46.6	179.6	178.7	-.9	-.5
Net interest	40.3	40.8	153.8	161.2	7.4	4.8
Social security	56.0	58.2	219.7	229.4	9.7	4.4
Medicare and health	45.3	54.4	178.7	195.2	16.5	9.3
Income security	41.0	41.0	153.4	162.0	8.6	5.6
Other	28.2	28.6	144.7	128.1	-16.6	-11.4
Receipts	255.8	293.4	870.2	938.6	68.4	7.9
Personal income and social insurance taxes	208.2	246.7	707.8	771.3	63.5	9.0
Corporate	25.7	27.5	82.3	91.7	9.4	11.4
Other	21.9	19.2	80.1	75.6	-4.5	-5.6
Deficit(+)	-2.1	-23.8	155.3	116.0	-39.4	-25.4

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

fiscal year. The April-May surge was concentrated in defense and Medicare and other health outlays, categories that tend to move erratically on a short-term basis.

Unified receipts continue to show strong growth. Increases in profits have pushed corporate profit tax receipts up 11 percent so far this fiscal year relative to last. Individual income taxes also have grown at a strong pace. Indeed, the data received since the May Greenbook confirm a sharp rise in individual tax liabilities in 1995 and early 1996 that appears stronger than can be explained by personal income growth alone. According to Monthly Treasury Statements, personal nonwithheld income taxes--which primarily reflect final payments on 1995 liabilities but also include the first quarterly estimated payments for 1996--were up 30 percent ($22 billion) in April and May from a year earlier. This increase comes on the heels of a 9 percent rise in withheld tax payments last year. This elevated growth in individual tax receipts seems to be explained in part by the run-up in financial asset prices, which may have fueled strong capital gains realizations.

The CBO released The Economic and Budget Outlook: Fiscal Years 1997-2006 in late May. The report included little information that was not contained in preliminary figures released in March and April. At that time, CBO's official deficit estimate for fiscal 1996 was $144 billion. After these estimates were finalized in mid-April, more-recent information concerning final appropriations bills for fiscal 1996 and stronger-than-expected April receipts reportedly has caused CBO to lower its expected deficit for fiscal 1996 to $130 billion.[6]

On June 13, the Congress approved a six-year budget resolution that projects a $5 billion surplus in fiscal 2002. The agreement includes $575 billion in net budget savings from policy changes over the six years--$637 billion in direct spending cuts and $48 billion in debt-service reduction offset in part by $111 billion in tax cuts. About half the reduction in outlays is in mandatory programs, primarily Medicare and other health programs. The resolution also calls for a 9 percent reduction ($297 billion) in discretionary spending. The plan provides for three separate reconciliation bills for mandatory programs and taxes. The first is for welfare and Medicaid, the second is for Medicare, and the third is for taxes.

6. This figure was given by CBO Director June O'Neill in comments reported by the Bureau of National Affairs, Daily Report, May 22, 1996.

Committee work on these bills is targeted for completion in June, July, and September respectively. Welfare and Medicaid reform is already behind schedule, as committee work continues in the House despite a targeted completion date of June 13.

BUDGET RESOLUTION DEFICITS COMPARED WITH CBO BASELINE
(Billions of dollars)

	1997	1998	1999	2000	2001	2002	1997-2002
CBO baseline deficit[1]	171	194	219	244	259	285	1,372
Policy changes[2]	-12	-28	-65	-101	-153	-214	-575
Fiscal dividend[3]	-5	-19	-37	-53	-64	-75	-254
Budget resolution deficit	153	147	117	89	42	-5	543

1. Under current economic policy assumptions. Assumes discretionary spending grows with inflation after 1998.
2. Includes debt-service savings from the direct effects of policy changes on the deficit.
3. Represents the deficit reduction estimated to result from macroeconomic effects of adopting policies to balance the budget in 2002.

According to CBO estimates, the congressional budget resolution would produce essentially the same deficit outcome for fiscal 1997 as would the President's plan, although the congressional proposal contains bigger spending cuts offset by somewhat larger net tax cuts. Over the longer run, the budget resolution contains substantially more deficit reduction than the President's basic plan. However, if the contingent out-year deficit reduction in the President's plan were to be invoked, it too would produce a small surplus by 2002.

State and Local Government Sector

Real spending by state and local governments exhibited strength during the early months of the second quarter; these gains are coming on the heels of a previous rebound in spending from weather-depressed levels earlier in the year. Real construction spending rose 1.3 percent in April. The increase primarily reflects the building of sewer and water supply systems; construction of most other categories declined. Government employment jumped 45,000 in May following a small advance the month before. A little less than half of the May increase reflected temporary hiring of election workers to staff polls in Arkansas, Indiana, Nebraska, North Carolina, West Virginia, and the District of Columbia

With fiscal year 1996 ending on June 30, most states appear to have passed their fiscal 1997 budgets. According to a recent survey by the National Association of State Budget Officers, states are planning to increase general fund spending only 1.8 percent in fiscal 1997, the smallest advance in fourteen years. Several states--most notably New Jersey, New York, and Pennsylvania--are expected to reduce spending. The slowdown in spending appears to reflect both the desire to downsize government and the expectation that federal aid will be reduced.

A number of states--California, Hawaii, New York, Rhode Island, and Vermont--plan to reduce welfare spending in fiscal 1997. In all, thirty-seven states have received federal waivers to adopt limits on the amount of time an individual may receive welfare payments or to impose other restrictions such as stringent work requirements. Most states are relying more heavily on managed care to gain better control of their Medicaid expenditures, but, to date, only a few have undertaken fundamental restructuring of their programs.

Prices

The incoming data on prices have continued to be favorable. The underlying rate of inflation, as measured by the twelve-month change in the CPI excluding food and energy, edged down to 2-3/4 percent in May, and, with the exception of some food and energy commodities, price pressures at earlier stages of processing remain subdued. Increases in broad measures of prices--such as the chain price indexes for GDP and gross domestic purchases--also show a pattern of stability or moderation relative to 1995.

The most recent inflation readings have been dominated by developments in energy and food prices. Energy prices continued to rise rapidly at the retail level in April and May, largely reflecting higher prices for gasoline. Looking ahead, the Lundberg survey of retail gasoline prices, which is not seasonally adjusted, shows that prices fell 1.4 percent in the first three weeks of June, even though gasoline prices typically rise fairly rapidly this time of year. This decline reflects a drop in the price of crude oil in May.

CPI AND PPI INFLATION RATES
(Percent change)

	From twelve months earlier		1995	1996	1996	
	May 1995	May 1996	Q4	Q1	Apr.	May
			-Annual rate-		-Monthly rate-	
CPI						
All items (100.0)[1]	3.2	2.9	2.4	3.2	0.4	0.3
Food (15.8)	3.2	2.6	2.7	2.0	0.3	0.1
Energy (6.7)	3.3	6.2	-3.8	12.9	3.2	1.1
CPI less food and energy (77.5)	3.1	2.7	2.7	2.8	0.1	0.2
Commodities (23.9)	1.5	1.5	1.9	2.2	-0.1	.0
New vehicles (5.0)	2.8	1.6	1.5	1.5	0.1	0.2
Used cars (1.3)	14.4	-0.1	1.5	8.6	-1.3	-0.9
Apparel (5.0)	-2.0	0.2	1.0	1.0	-0.4	.0
Services (53.6)	3.8	3.2	3.0	3.0	0.3	0.3
Owners' equivalent rent (19.7)	3.3	3.3	3.9	3.1	0.3	0.3
Tenants' rent (5.8)	2.5	2.5	2.5	2.9	0.2	0.3
Medical care (6.1)	5.2	3.9	3.9	3.7	0.2	0.3
Auto Finance Charges (0.6)	26.4	-8.6	-4.0	-16.2	0.1	0.2
PPI						
Finished goods (100.0)[2]	2.2	2.3	3.3	3.2	0.4	-0.1
Finished consumer foods (23.4)	1.1	2.6	6.0	0.5	-0.3	.0
Finished energy (13.4)	5.5	5.0	.0	21.6	2.8	-0.6
Finished goods less food and energy (63.2)	2.0	1.6	3.0	0.7	0.1	.0
Consumer goods (38.5)	2.1	1.7	3.2	0.8	.0	0.1
Capital equipment (24.7)	1.8	1.4	3.0	0.4	0.2	-0.1
Intermediate materials (100)[3]	6.9	0.7	-0.3	-0.1	0.3	0.5
Intermediate materials less food and energy (82.6)	7.9	-1.0	-1.8	-3.2	-0.2	0.2
Crude materials (100)[4]	-0.2	12.8	10.3	12.1	5.3	1.3
Crude food materials (44.7)	-9.2	27.9	29.6	-0.7	4.0	6.3
Crude energy (31.4)	-1.4	15.9	13.6	52.7	10.9	-3.8
Crude materials less food and energy (23.9)	19.2	-12.5	-19.7	-9.3	-0.5	-0.3

1. Relative importance weight for CPI, December 1995.
2. Relative importance weight for PPI, December 1995.
3. Relative importance weight for intermediate materials, December 1995.
4. Relative importance weight for crude materials, December 1995.

BROAD MEASURES OF INFLATION
(Four-quarter percent changes)

	1993 Q1	1994 Q1	1995 Q1	1996 Q1
Product prices				
GDP chain price index	2.7	2.3	2.4	2.3
GDP deflator	2.7	2.3	2.5	2.1
Nonfarm business chain price index[1]	2.6	2.1	2.5	1.7
Expenditure prices				
Gross domestic purchase chain price index	2.7	2.1	2.6	2.3
PCE chain price index	2.9	2.2	2.6	2.1
Less food and energy	2.8	2.5	2.6	2.1
PCE deflator	2.9	2.3	2.5	2.0
Less food and energy	3.2	2.5	2.6	1.8
CPI	3.2	2.5	2.8	2.8
Less food and energy	3.5	2.9	2.9	2.9
Median CPI	2.9	2.9	2.8	3.3

1. Excluding housing.

Food prices for consumers inched up 0.1 percent in May after increasing at a faster pace in the previous two months. The run-up in grain prices has had some divergent effects on prices of consumer foods. The index for cereals and bakery products rose 0.6 percent in May despite the first round of highly publicized cuts in breakfast cereal prices, and price increases for both poultry and pork exceeded 1 percent. In contrast, beef prices dropped 1.7 percent, reflecting increased slaughter in response to higher feed prices.

At the commodity level, spot prices for farm crops, while still quite high, have come down since the May Greenbook. Wheat prices have retraced about two-thirds of their run-up earlier this year, as a slight improvement in crop conditions and lower-than-expected pre-harvest usage have combined to take the edge off of the market. Spot prices for corn also have dropped on news of small cutbacks in current usage. By contrast, futures prices for post-harvest contracts of corn have been pushed up slightly by indications that wet weather will prevent some acreage from being planted. Livestock prices remain mixed. Hog prices have weakened appreciably after an earlier run-up, but cattle prices, which were quite weak earlier in the spring, have held fairly steady in spot markets and firmed in futures markets over the past few weeks.

Consumer prices excluding food and energy increased 0.2 percent in May following a 0.1 percent rise in April. The index for commodities other than food and energy was unchanged last month, while prices of non-energy services rose 0.3 percent, the same as the average increase in the first four months of 1996. Over the twelve months ended in May, core consumer prices rose 2.7 percent, compared with 3.1 percent over the year ended in May 1995. Sharp swings in auto finance charges accounted for most of this deceleration; the twelve-month change in core CPI excluding this item edged down from 2.9 percent in May 1995 to 2.8 percent in May 1996.

CPI inflation generally has been higher than the rate of change in PCE prices as measured in the NIPA, particularly over the past year. Between early 1992 and early 1995, the CPI rose roughly 1/4 percentage point faster than the PCE deflator, but over the past year, the gap increased to 3/4 percentage point. Medical services accounted for most of this larger differential. Both PCE and CPI medical services prices rose 4-1/2 percent to 5 percent between 1994:Q1 and 1995:Q1; since then, medical services prices increased about 4 percent in the CPI but rose less than 2 percent in the PCE deflator. The prices of medical services are measured more accurately in the PCE measure than in the CPI. The CPI tends to follow "list" prices and costs out "inputs" into the health care process, such as a one-day stay in a hospital bed. In contrast, the PCE deflator measures actual transactions prices and captures more comprehensive "treatment paths."[7] Medical services have a larger weight in PCE than they do in the CPI: The weights in PCE measure more up-to-date spending patterns and include employer- or government-paid insurance; the CPI weights are based on 1982-84 expenditure patterns and consider only out-of-pocket expenses or household-paid insurance.

7. In January 1997 BLS plans to change the CPI for medical services so that it will measure transactions prices and follow treatment paths. If this move had taken place earlier, the staff estimates that the change in core CPI over the twelve months ended in May 1995 would have been roughly 0.1 percentage point lower, while core inflation over the period ended in May 1996 would have been reduced by about 0.2 percentage point.

At the producer level, the PPI for finished goods excluding food and energy was flat in May and changed little on net over the first five months of 1996. The PPI for intermediate materials excluding food and energy rose 0.2 percent in May, the first monthly increase since August of last year. Despite last month's uptick, the index for core intermediate materials remains 1 percent below its level of a year ago--down sharply from the 7.9 percent increase recorded over the previous twelve-month period. Prices for crude materials other than food and energy fell 0.3 percent in May, bringing the twelve-month drop in core crude materials prices to 12.5 percent. Since mid-May, both the *Journal of Commerce* and KR-CRB price indexes for industrial commodities have declined, as metals prices have fallen considerably. However, a large part of the decline reflects the plunge in copper prices following the revelation of the trading scandal at Sumitomo.

Recent surveys of consumers show that mean inflation expectations dropped back after jumping in May. Mean expected inflation over the next twelve months fell to 4.3 percent in the preliminary June Michigan Survey of Consumers, 1/2 percentage point lower than the previous month. Nevertheless, this survey reading remains 1/4 percentage point higher than its level of a year ago. Median expected inflation, a less volatile series, edged down to 2.9 percent in June, its average over the past year. Longer-term expectations improved more than year-ahead expectations: Mean expected inflation over the next five to ten years was 3.7 percent in the June survey, down more than 1 percentage point from May and 1/2 percentage point from June 1995. Among professional forecasters, the ten-year inflation expectations compiled by the Federal Reserve Bank of Philadelphia was 3 percent in June; this index has been unchanged since last summer.

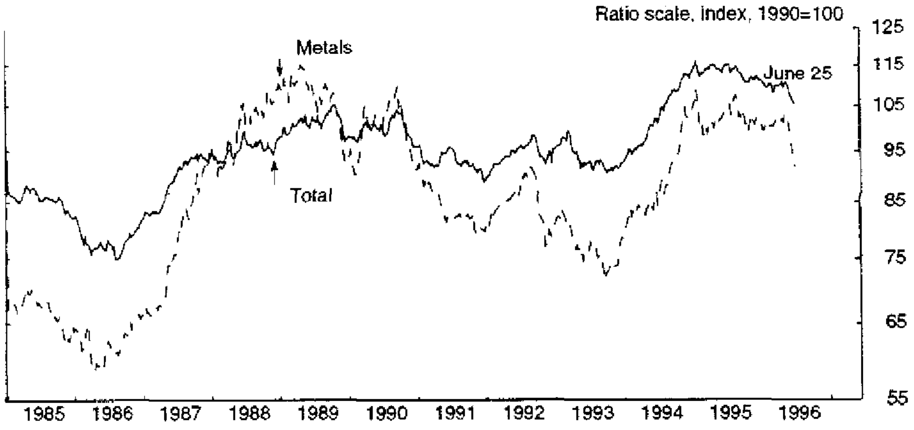
SPOT PRICES OF SELECTED COMMODITIES

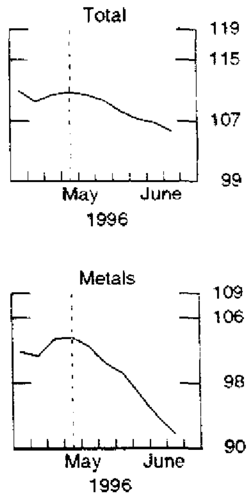
	Current price ($)	Percent change[1]: 1994	1995	Dec. 26 to May 14[2]	May 14[2] to June 25	Memo: Year earlier to date
Metals						
Copper (lb.)	1.040	64.9	-3.5	-.7	-23.0	-29.3
Steel scrap (ton)	138.500	2.9	-6.6	6.3	-2.8	-1.4
Aluminum, London (lb.)	.668	73.5	-12.9	-2.8	-9.1	-16.9
Precious metals						
Gold (oz.)	385.100	-1.7	1.7	.8	-1.4	-1.1
Silver (oz.)	5.160	-5.0	7.2	4.7	-4.0	-3.0
Forest products						
Lumber (m. bdft.)	340.000	-37.1	-14.4	46.8	-7.4	58.9
Plywood (m. sqft.)	296.000	1.5	-6.1	3.9	-8.1	-14.2
Petroleum						
Crude oil (barrel)	18.300	15.6	16.8	6.6	-5.8	8.2
Gasoline (gal.)	.573	32.4	7.7	29.3	-16.2	4.6
Fuel oil (gal.)	.511	12.7	22.6	-1.3	-14.3	8.5
Livestock						
Steers (cwt.)	60.000	-3.4	-5.7	-8.3	-.8	-4.8
Hogs (cwt.)	56.500	-12.9	27.5	31.5	-5.0	22.8
Broilers (lb.)	.597	-4.9	10.7	16.9	-6.0	6.6
U.S. farm crops						
Corn (bu.)	4.755	-23.2	57.4	42.5	-3.8	83.9
Wheat (bu.)	5.935	11.4	24.0	33.8	-18.0	21.1
Soybeans (bu.)	7.660	-19.6	29.0	11.6	-4.7	33.6
Cotton (lb.)	.790	38.5	-8.1	5.0	-4.8	-25.2
Other foodstuffs						
Coffee (lb.)	1.435	153.1	-39.1	37.7	4.7	1.4
Memo:						
JOC Industrials	105.600	22.1	-1.7	-.4	-4.6	-8.4
JOC Metals	91.800	31.9	-1.8	1.9	-11.4	-11.9
KR-CRB Futures	247.710	4.8	3.3	6.6	-4.8	5.6
KR-CRB Spot	330.640	29.1	-3.5	2.6	-2.5	-6.9

1. Changes, if not specified, are from the last week of the preceding year to the last week of the period indicated.
2. Week of the May Greenbook.

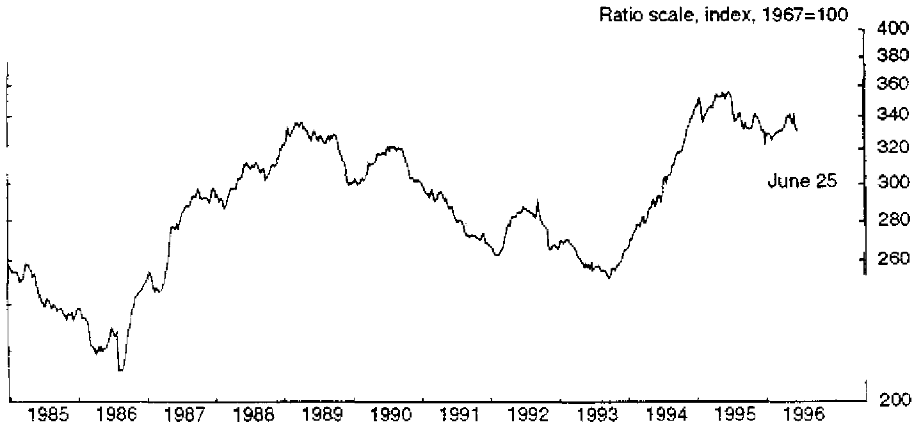
Commodity Price Measures

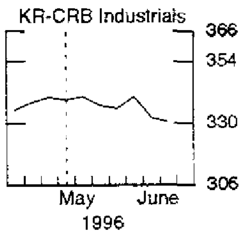
Journal of Commerce Index



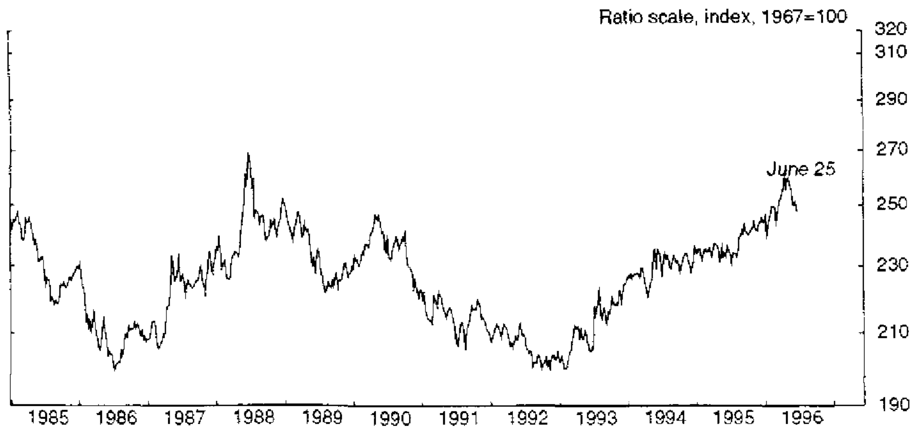


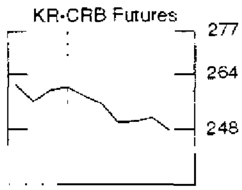
KR-CRB Spot Industrials





KR-CRB Futures





Note. Weekly data, Tuesdays. Vertical lines on small panels indicate week of last Greenbook. The Journal of Commerce index is based almost entirely on industrial commodities, with a small weight given to energy commodities, and the KR-CRB spot price index consists entirely of industrial commodities, excluding energy. The KR-CRB futures index gives about a 60 percent weight to food commodities and splits the remaining weight roughly equally among energy commodities, industrial commodities, and precious metals. Copyright for Journal of Commerce data is held by CIBCR, 1994.

SURVEYS OF (CPI) INFLATION EXPECTATIONS
(Percent)

	Actual inflation[1]	University of Michigan Mean (1-year)[2]	University of Michigan Median (1-year)[3]	Livingston (1-year)[4]	Conference Board (1-year)	Professional forecasters (10-year)[5]	Michigan (5- to 10-year)[6]
1992-Q1	2.9	3.4	2.7		4.6	3.7	4.8
Q2	3.1	3.8	3.1	3.6	4.6	3.9	5.0
Q3	3.1	4.0	3.0		4.5	3.8	4.9
Q4	3.1	3.8	2.9	3.4	4.5	3.6	5.3
1993-Q1	3.2	4.3	3.1		4.6	3.5	5.2
Q2	3.1	4.4	3.3	3.4	4.8	3.7	5.2
Q3	2.7	4.7	3.1		4.6	3.5	4.7
Q4	2.7	3.8	3.2	3.2	4.4	3.5	4.7
1994-Q1	2.5	3.9	2.9		4.3	3.5	5.0
Q2	2.4	4.2	3.0	2.9	4.2	3.5	4.8
Q3	2.9	4.5	3.2		4.3	3.5	5.0
Q4	2.7	4.1	3.1	3.5	4.2	3.5	4.3
1995-Q1	2.8	4.1	3.1		4.2	3.3	4.1
Q2	3.1	4.1	3.1	3.2	4.2	3.4	4.3
Q3	2.6	3.9	2.9		4.0	3.2	4.3
Q4	2.7	3.6	2.8	2.9	3.9	3.0	3.9
1996-Q1	2.7	3.9	2.9		4.1	3.0	4.2
Q2		4.6	3.0		4.3	3.0	4.2
1995-July	2.8	3.8	2.9		4.0		4.3
Aug.	2.6	3.9	2.9		4.0		4.1
Sept.	2.5	4.0	2.8		4.1	3.2	4.4
Oct.	2.8	3.6	2.9		3.6		3.7
Nov.	2.6	3.8	2.8		4.1		4.0
Dec.	2.5	3.3	2.7	2.9	4.0	3.0	3.9
1996-Jan.	2.7	4.0	2.9		4.1		4.2
Feb.	2.7	3.6	2.8		4.0		4.2
Mar.	2.8	4.2	2.9		4.1	3.0	4.3
Apr.	2.9	4.5	3.0		4.2		4.1
May	2.9	4.9	3.0		4.5		4.8
June		4.3	2.9		4.3	3.0	3.7

1. CPI; percent change from the same period in the prior year.
2. Average increase for responses to the question: By about what percent do you expect prices (CPI) to go up, on the average, during the next 12 months?
3. Median increase for responses to the question above.
4. Average 12-month-ahead forecast of the CPI by 'informed' business economists. Constructed by the Federal Reserve Bank of Philadelphia from disaggregated Livingston data; data are for the last month of the period indicated.
5. Compiled by the Federal Reserve Bank of Philadelphia.
6. Average increase for responses to the question: By about what percent per year do you expect prices (CPI) to go up, on the average, during the next 5 to 10 years?

DOMESTIC FINANCIAL DEVELOPMENTS

Selected Financial Market Quotations[1]
(Percent except as noted)

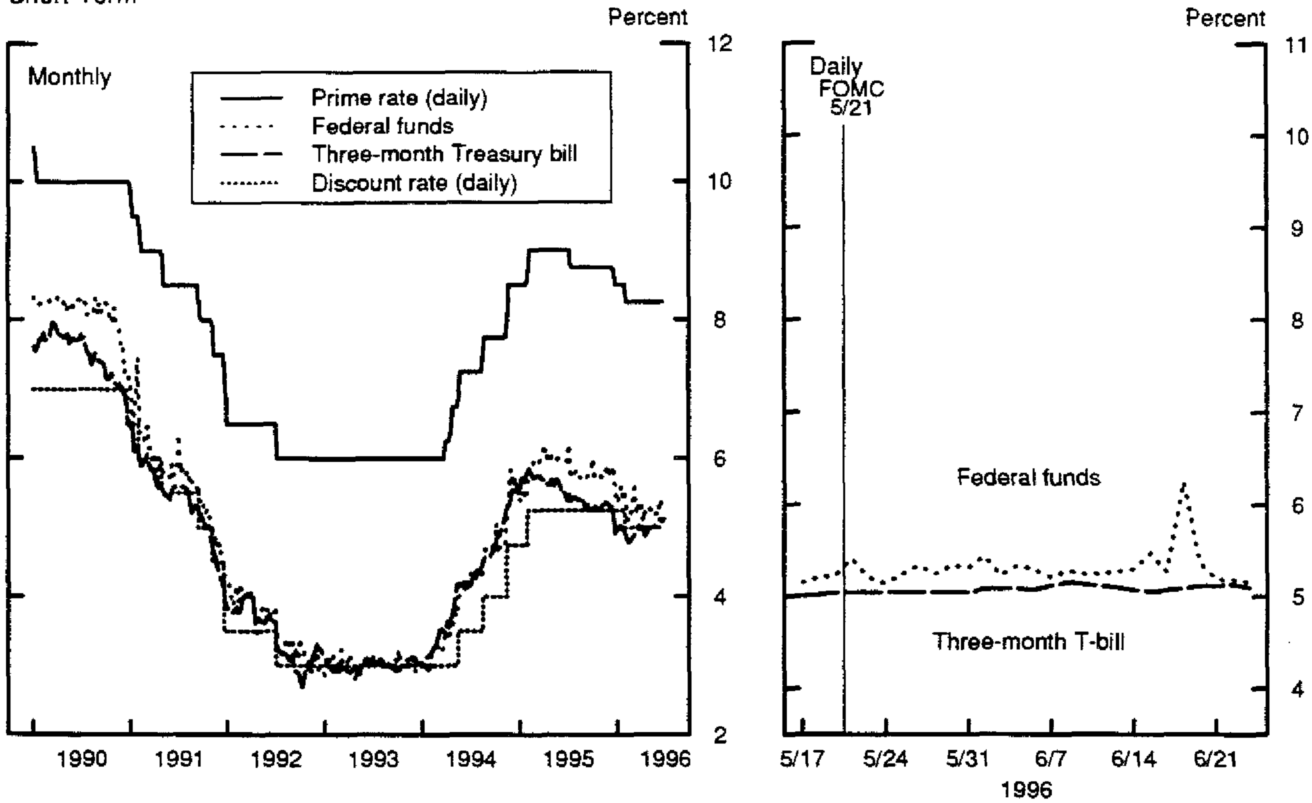
Instrument	1994 high	1996 Feb. low	1996 FOMC, May 21	1996 June 25	Change to June 25, from: 1994 high	Feb. 1996 low	FOMC, May 21
Short-term rates							
Federal funds[2]	5.66	4.92	5.26	5.37	-.29	.45	.11
Treasury bills[3]							
3-month	5.78	4.76	5.02	5.10	-.68	.34	.08
6-month	6.38	4.67	5.12	5.23	-1.15	.56	.11
1-year	6.84	4.55	5.25	5.50	-1.34	.95	.25
Commercial paper							
1-month	6.13	5.27	5.37	5.49	-.64	.22	.12
3-month	6.32	5.12	5.38	5.50	-.82	.38	.12
Large negotiable CDs[3]							
1-month	6.10	5.21	5.31	5.39	-.71	.18	.08
3-month	6.39	5.12	5.35	5.48	-.91	.36	.13
6-month	6.89	4.99	5.44	5.66	-1.23	.67	.22
Eurodollar deposits[4]							
1-month	6.06	5.13	5.28	5.34	-.72	.21	.06
3-month	6.38	5.13	5.34	5.47	-.91	.34	.13
Bank prime rate	8.50	8.25	8.25	8.25	-.25	.00	.00
Intermediate- and Long-term Rates							
U.S. Treasury (constant maturity)							
3-year	7.82	4.98	6.18	6.50	-1.32	1.52	.32
10-year	8.04	5.58	6.62	6.91	-1.13	1.33	.29
30-year	8.16	6.02	6.82	7.06	-1.10	1.04	.24
Municipal revenue (Bond Buyer)[5]	7.37	5.67	6.17	6.27	-1.10	.60	.10
Corporate-A utility, recently offered	9.05	7.18	7.90	8.17	-.88	.99	.27
High-yield corporate[6]	11.43	9.57	10.00	10.19	-1.24	.62	.19
Home mortgages[7]							
FHLMC 30-yr fixed rate	9.25	6.94	8.08	8.30	-.95	1.36	.22
FHLMC 1-yr adjustable rate	6.79	5.19	5.78	5.93	-.86	.74	.15

Stock exchange index	Record high Level	Record high Date	1989 Low, Jan. 3	1996 FOMC, May 21	1996 June 25	Percentage change to June 25, from: Record high	1989 low	FOMC, May 21
Dow-Jones Industrial	5778.00	5/22/96	2144.64	5748.82	5719.27	-1.02	166.68	-.51
NYSE Composite	363.74	5/24/96	154.00	361.09	358.03	-1.57	132.49	-.85
S&P 500 Composite	678.51	5/24/96	275.31	673.15	668.48	-1.48	142.81	-.69
NASDAQ (OTC)	1249.15	6/5/96	378.56	1248.11	1172.58	-6.13	209.75	-6.05
Wilshire	6758.69	5/24/96	2718.59	6719.13	6587.11	-2.54	142.30	-1.96

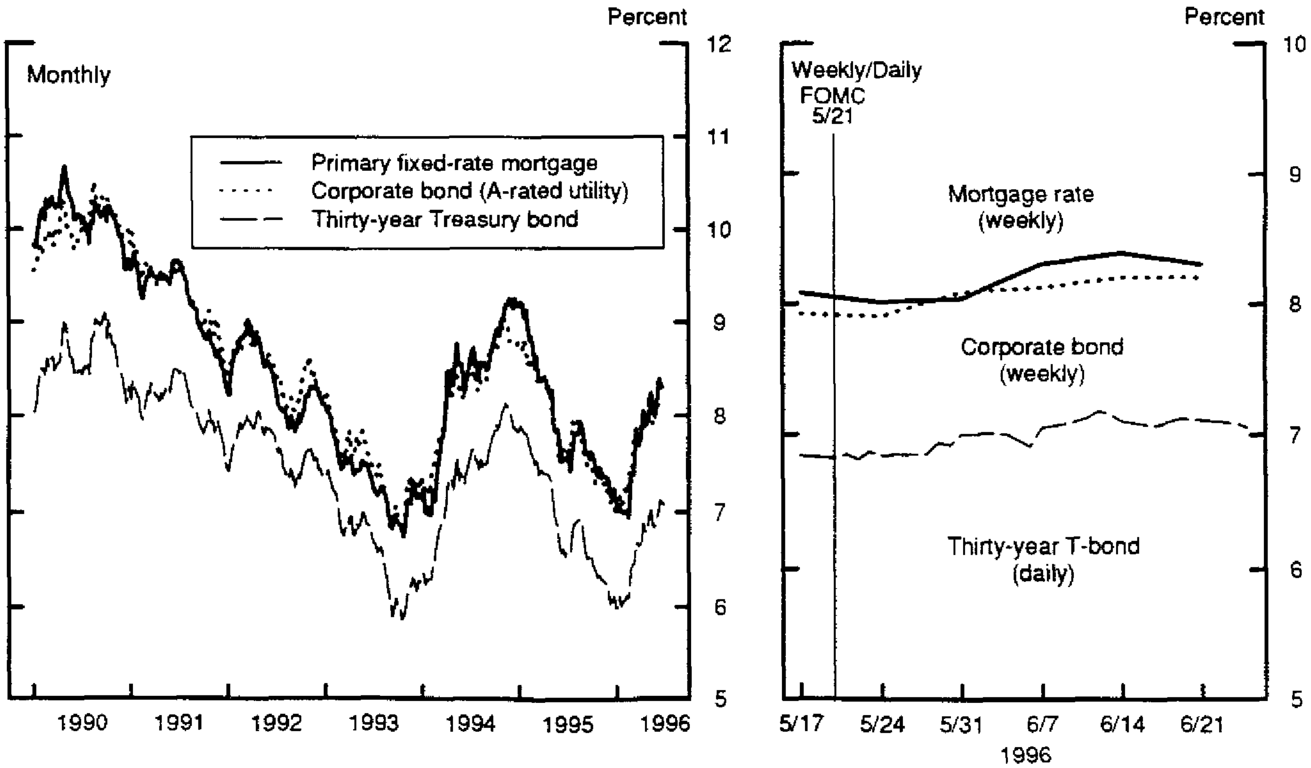
1. One-day quotes except as noted.
2. Average for two-week reserve maintenance period closest to date shown. Last observation is average maintenance period to July 3, 1996.
3. Secondary market.
4. Bid rates for Eurodollar deposits at 11 a.m. London time.
5. Most recent observation based on one-day Thursday quote and futures market index changes.
6. Merrill Lynch Master II high-yield bond index composite.
7. Quotes for week ending Friday previous to date shown.

Selected Interest Rates

Short-Term



Long-Term



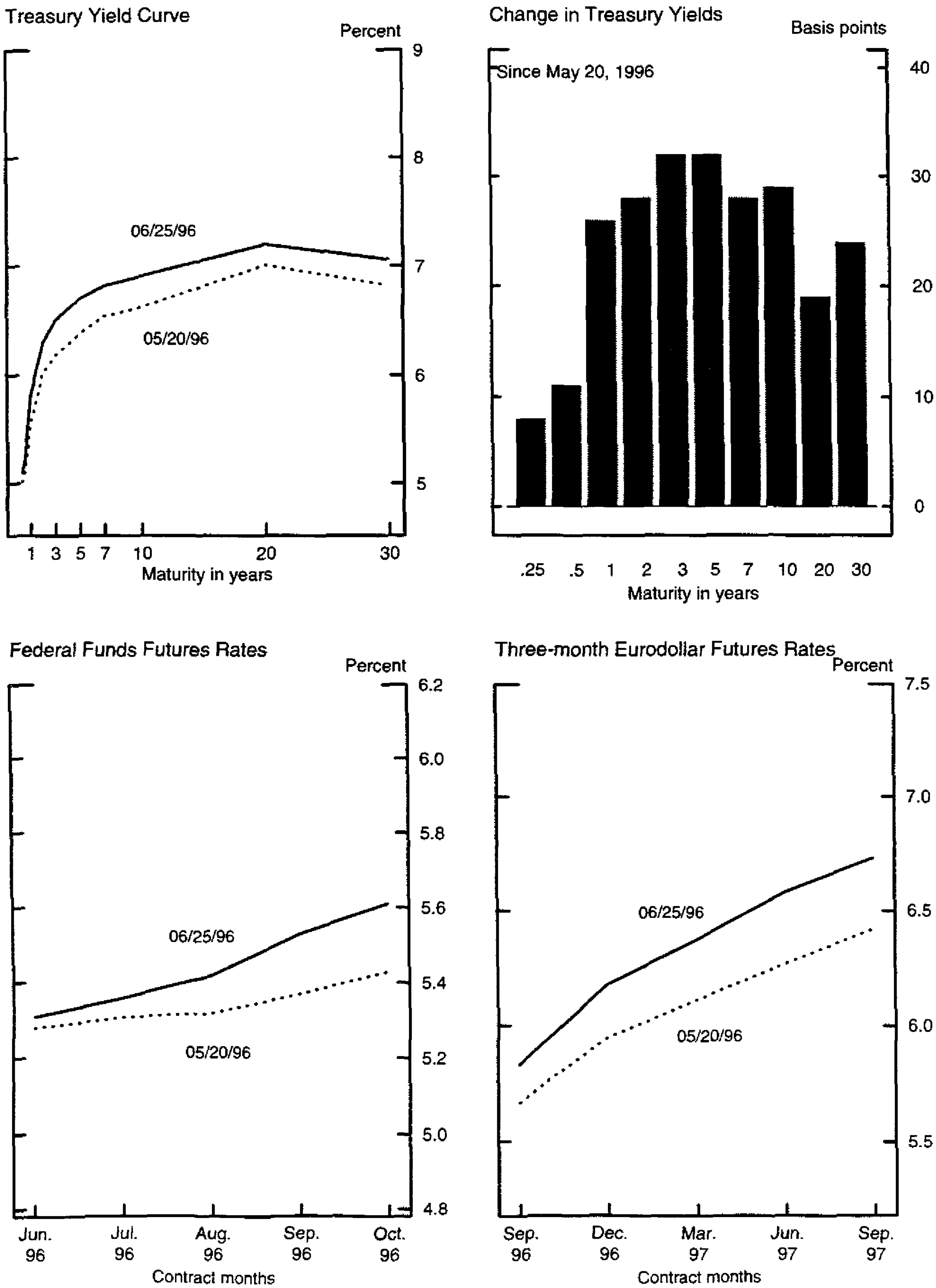
Against a backdrop of unchanged reserve market conditions, intermediate- and long-term interest rates have risen about 30 basis points since the May FOMC meeting, placing the yield on the thirty-year Treasury bond once again above 7 percent. Although there was some good news on price inflation during the intermeeting period, incoming information pointing to an economy growing rather briskly led market participants to raise the odds on a tightening of monetary policy to avoid overheating. Rates on near-term federal funds futures contracts now seem to embody expectations that the federal funds rate will be raised 25 basis points at some point this summer (chart). Yields on private securities generally followed those on Treasuries, preserving the narrow spreads of the past couple of months, and junk bond spreads have shrunk another 10 basis points since the May FOMC meeting.

Equity prices have zigzagged in recent weeks. The Dow and the S&P 500 indexes are off about 1/2 percent on net since the last FOMC meeting. However, the NASDAQ composite index has dropped 6 percent, in part reflecting concerns about the earnings of technology firms. Nonetheless, equity prices remain high in relation to earnings.

The growth of debt of nonfederal sectors has remained moderate in recent months. Business loan growth at banks has held up well, and bond issuance has dipped only a little to date in response to the backup in interest rates. In the household sector, consumer credit growth appears to have slowed a bit further in the current quarter, while mortgage borrowing appears to have been fairly well maintained. State and local government debt outstanding has continued to contract: Although gross issuance has risen a bit, retirements of prerefunded bonds have remained large. Borrowing by the federal government has been weak in the second quarter--indeed, negative on an unadjusted basis--as unusually strong tax receipts produced a surplus in the period.

Market and other indicators suggest that credit generally has been amply available to both business and household borrowers. Rate spreads on corporate debt are quite low, with junk bond spreads at their lowest levels in a decade. In addition, surveys and anecdotal reports indicate that banks remain aggressive in competing for business customers. And although emerging signs of some deterioration in household credit quality have raised caution flags

Selected Market Rates



among banks and other lenders, especially credit card and affordable housing lenders, it appears that any tightening of credit terms and standards to date has been selectively focused.

Money and Bank Credit

The broad monetary aggregates were weak in May: M2 fell at a 1-1/2 percent annual rate and M3 grew at only a 3-1/2 percent rate. However, partial data for June point to a rebound, leaving M2 slightly below and M3 slightly above the upper ends of their respective annual growth ranges.

The weakness in M2 in May likely owed in part to the rise in the opportunity cost of holding deposits in previous months as intermediate- and long-term market interest rates rose. In addition, individuals most likely tapped other checkable deposits (OCDs) and savings deposits to make the unusually large tax payments recorded by the Treasury in the second half of April, as evidenced by the decline in OCDs, even after accounting for sweeps, and the marked slowdown in inflows to savings deposits. Because of the sharp drop in OCDs, M1 fell at a 6-1/2 percent annual rate in May despite a pickup in the growth of currency and demand deposits. Adjusted for retail sweeps, M1 increased at a little more than a 2 percent rate.

Bank credit rose at only a 1-1/2 percent pace in May, well below the 5 percent growth registered on average in late 1995 and early 1996. Asset growth in May was depressed in part by the effects of accounting rules.[1] However, even after adjusting for these accounting effects, bank credit was up at only a 2-1/2 percent annual rate in May, but it appears to have strengthened a bit in June.

Bank loans contracted slightly in May, with all categories weak except business loans. Consumer loans ran off at a 5-3/4 percent pace. However, the reported bank data overstate the weakening in consumer lending because bookings have been bounced around in response to transfers of receivables between a large finance company and its bank affiliate that boosted consumer loans in April but lowered them in May, and because banks continue to remove receivables from their books through securitization. Adjusting for

1. The rules mandate the booking of changes in the market value of bank securities and the booking of the revaluation gains in derivative portfolios in "other securities." The rise in interest rates reduced both the value of securities and the revaluation gains.

MONETARY AGGREGATES
(Based on seasonally adjusted data)

Aggregate or component	1995	1995 Q4	1996 Q1	1996 Mar.	1996 Apr.	1996 May (p)	1995:Q4 to May 96 (p)	Level (bil. $) May 96 (p)
Aggregate	Percentage change (annual rate)[1]							
1. M1	-1.8	-5.1	-2.7	10.0	-3.1	-6.6	-2.0	1117.5
2. M2[2]	4.0	4.1	5.9	11.7	1.9	-1.6	4.6	3732.3
3. M3	6.0	4.6	7.3	11.0	1.7	3.4	6.3	4707.0
Selected components								
4. Currency	5.4	3.8	2.3	6.1	2.2	3.5	2.7	377.0
5. Demand deposits	1.4	-0.4	10.9	29.3	-2.4	10.0	10.8	409.7
6. Other checkable deposits	-11.1	-18.7	-22.7	-8.5	-10.0	-37.9	-20.7	322.1
7. M2 minus M1[3]	6.8	8.4	9.8	12.4	4.1	0.6	7.6	2614.8
8. Savings deposits	-3.3	7.9	15.2	19.1	10.4	4.5	13.2	1197.8
9. Small time deposits	15.1	5.1	0.9	-6.0	-3.1	-2.6	-1.2	929.6
10. Retail money market funds	20.1	16.5	14.7	32.6	2.7	-3.2	11.9	487.4
11. M3 minus M2[4]	14.5	6.3	12.5	8.3	0.9	23.1	13.0	974.7
12. Large time deposits, net[5]	15.4	17.4	8.3	20.7	7.0	14.2	11.1	437.3
13. Institution-only money market mutual funds	23.1	10.2	27.9	21.6	-13.0	-10.3	16.3	243.5
14. RPs	4.6	-16.0	-3.0	-7.8	0.0	98.1	13.9	197.2
15. Eurodollars	12.0	-0.9	10.4	-26.2	3.8	17.8	6.5	95.7
Memo								
16. Monetary base	4.1	2.6	1.6	8.9	-0.8	1.1	1.6	437.0
17. Household M2[6]	4.3	4.5	5.4	9.8	1.7	-2.5	4.0	3323.0
	Average monthly change (billions of dollars)[7]							
Memo								
Selected managed liabilities at commercial banks:								
18. Large time deposits, gross	5.5	4.9	2.9	8.5	4.3	8.2	. . .	464.8
19. Net due to related foreign institutions	3.5	5.8	2.7	-15.1	-7.0	1.4	. . .	255.8
20. U.S. government deposits at commercial banks	-0.1	-1.8	-1.3	5.8	-0.8	-5.6	. . .	11.8

1. For the years shown, fourth quarter-to-fourth quarter percent change. For the quarters shown, based on quarterly averages.
2. Sum of seasonally adjusted M1, retail money market funds, savings deposits, and small time deposits.
3. Sum of retail money funds, savings deposits, and small time deposits, each seasonally adjusted separately.
4. Sum of large time deposits, institutional money funds, RP liabilities of depository institutions, and Eurodollars held by U.S. addressees, each seasonally adjusted separately.
5. Net of holdings of depository institutions, money market mutual funds, U.S. government, and foreign banks and official institutions.
6. M2 less demand deposits
7. For the years shown, "average monthly change" is the fourth quarter-to-fourth quarter dollar change, divided by 12. For the quarters shown, it is the quarter-to-quarter dollar change, divided by 3.
p--Preliminary.

these transactions suggests that the underlying rate of growth of consumer lending at banks averaged about 5 percent at an annual rate over April and May, well below the pace in the first quarter. Real estate loans were flat in May, likely reflecting securitization rather than a lack of originations. Data for the first part of June suggest that the pace of consumer and real estate lending has picked up.

Business loans grew at a 7 percent annual rate in May, off slightly from April though still above the average in the first quarter; partial data for June point to a further slowing. The downtick in May possibly reflected a shift to capital market financing when long-term rates stabilized and then edged lower for a time. The Survey of Terms of Bank Lending for May indicated that banks continued to be accommodative lenders, as spreads on large loans ($1 million and over) remained fairly narrow by historical standards--although a bit wider than in February--and spreads on small loans (less than $100,000) continued to narrow.

Credit performance at commercial banks was still generally quite good at the end of the first quarter (chart), although signs of payment difficulties in consumer loans may have raised some concern. Charge-off and delinquency rates on business and real estate loans remained near the low levels reached in early 1995. In contrast, the delinquency rate on consumer loans remained somewhat elevated, and the charge-off rate on such loans moved close to its 1991 high. More recently, trade reports have highlighted continued deterioration in the quality of credit card loan portfolios in the second quarter and substantial charge-offs or loss provisions at a few large banks, most notably Bank of New York (BONY). However, there has been little impact on the card-backed securities market as such securities have sufficient credit enhancements and market participants apparently feel that they can distinguish between "good" and "bad" portfolios. Although bank stock prices dipped following the BONY announcement on June 20 of a $350 million increase in its loan-loss reserves, these price declines have since been reversed.

Business Finance

Gross issuance of bonds by nonfinancial corporations jumped in May as corporate treasurers took advantage of what they thought

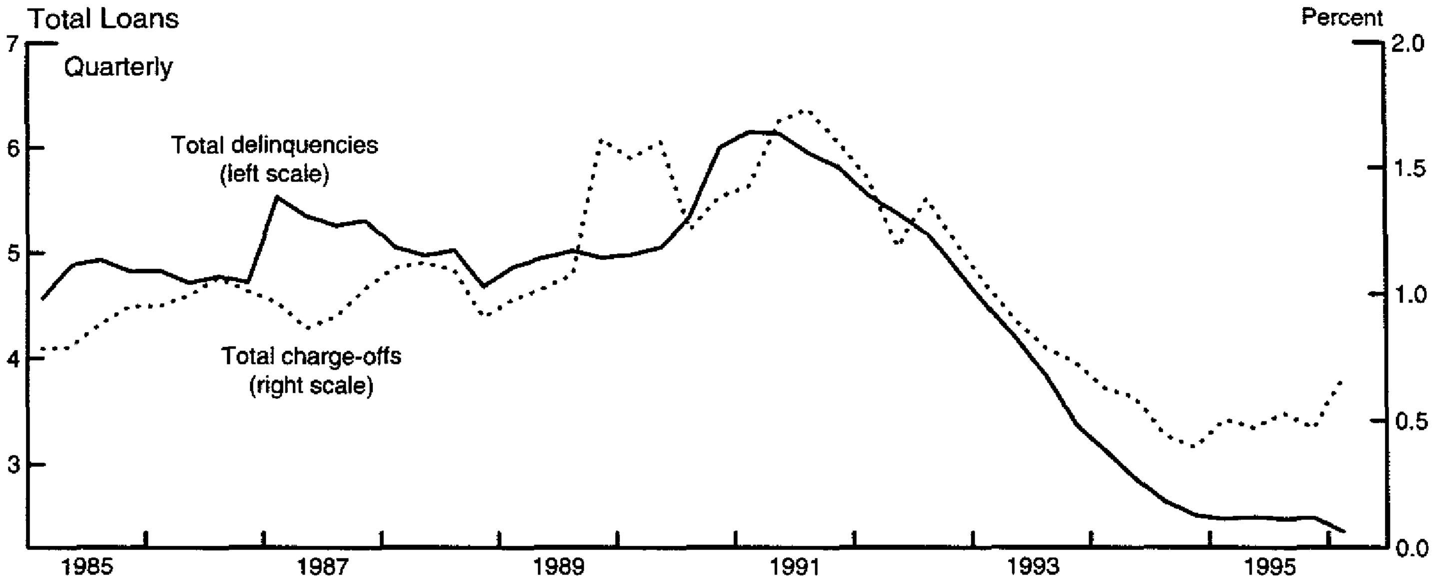
COMMERCIAL BANK CREDIT

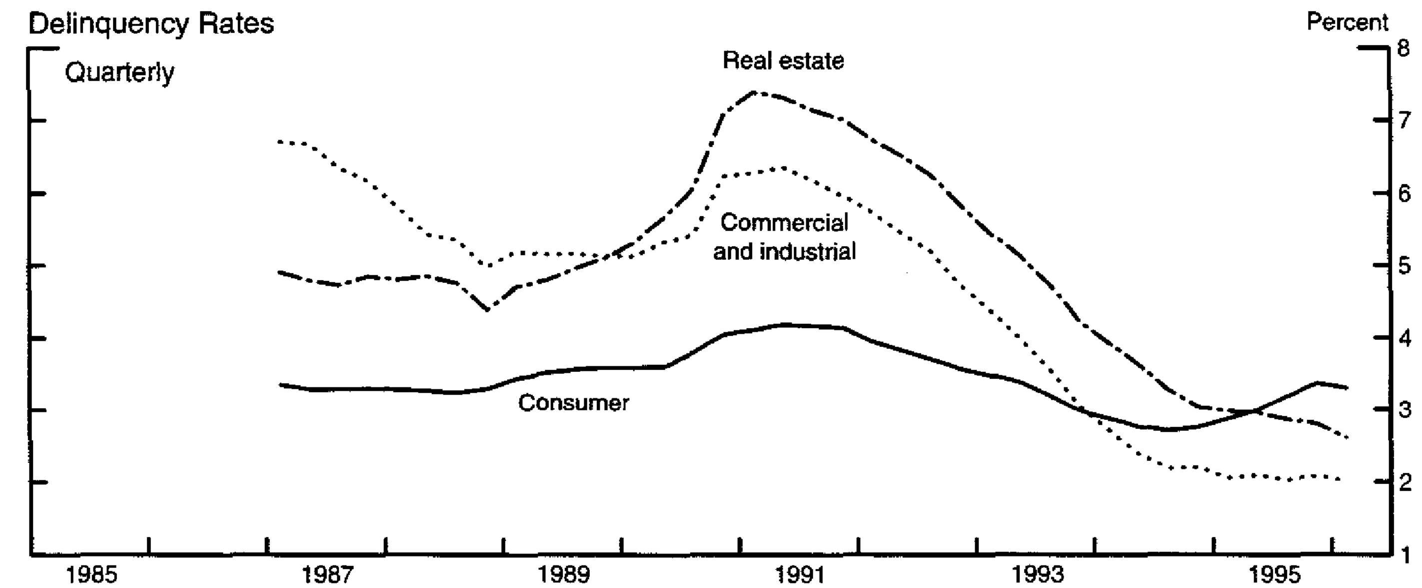
(Percentage change; seasonally adjusted annual rate)[1]

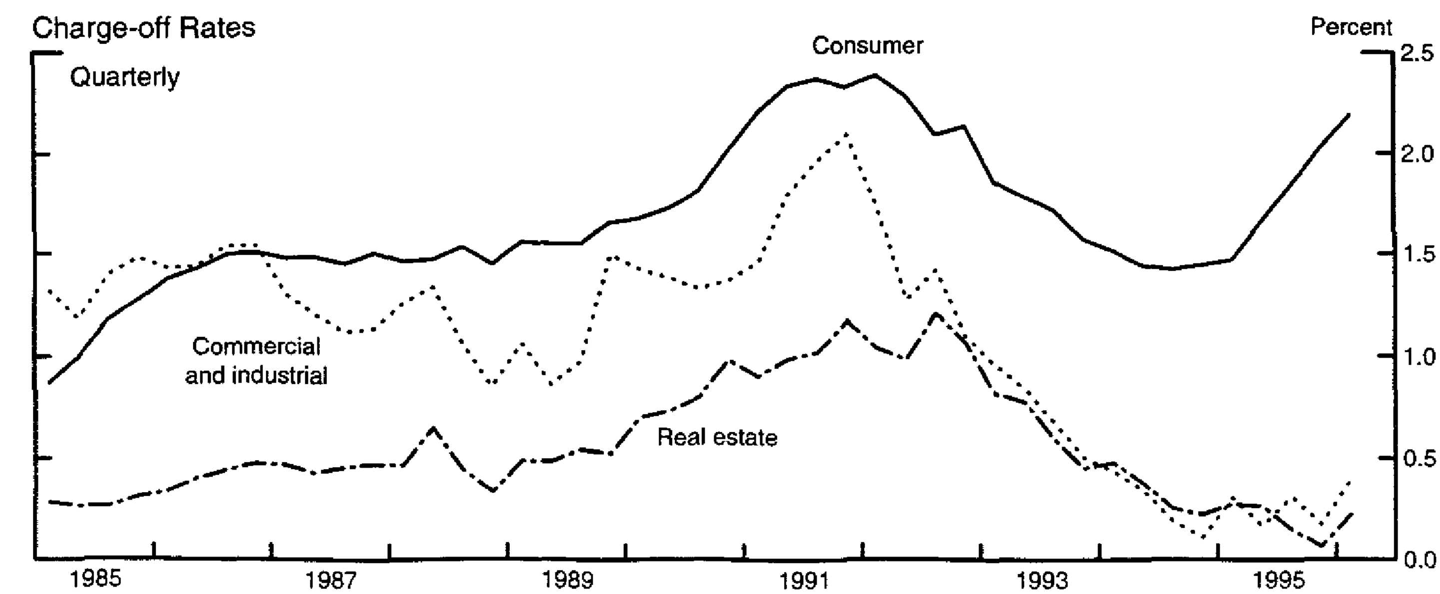
	Type of credit	1995	1995 Q4	1996 Q1	1996 Mar	1996 Apr	1996 May	Level, May 1996 (billions of $)
1.	Total loans and securities	8.6	5.1	4.8	-2.9	5.3	1.4	3,653.8
2.	Securities	3.5	2.8	-.3	-19.4	-1.3	8.5	985.5
3.	U.S. government	-3.1	3.4	-2.7	-17.8	-.5	14.6	713.5
4.	Other[2]	25.4	1.3	6.1	-23.6	-3.5	-7.5	272.0
5.	Loans[3]	10.8	6.1	6.7	3.2	7.7	-1.1	2,668.3
6.	Business	11.5	6.3	5.9	-4.0	9.0	6.9	732.7
7.	Real estate	8.5	3.9	4.5	5.4	1.8	-.1	1,095.7
8.	Home equity	5.2	3.1	5.1	-1.5	3.0	-3.0	79.8
9.	Other	8.8	3.9	4.4	5.8	1.8	.1	1,015.9
10.	Consumer	10.6	6.2	7.1	7.4	6.2	-5.7	503.8
11.	Adjusted[4]	17.6	19.1	13.9	12.2	9.6	1.8	653.0
12.	Security	14.2	-.9	-2.8	-8.4	7.1	-53.3	81.8
13.	Other[5]	18.5	17.8	21.7	10.7	33.4	-2.4	254.2

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

Delinquency and Charge-Off Rates on Loans at Commercial Banks







Source. Call Reports.

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

Type of security	1994	1995	1995 Q4	1996 Q1	1996 Mar.	1996 Apr.[p]	1996 May[p]
All U.S. corporations	41.29	47.64	50.60	56.86	58.85	48.47	63.66
Stocks[2]	5.49	6.10	7.82	7.41	7.91	13.43	14.27
Bonds	35.80	41.54	42.78	49.45	50.94	35.04	49.39
Nonfinancial corporations							
Stocks[2]	3.10	4.39	5.77	5.25	6.78	9.10	10.03
Initial public offerings	1.14	1.70	2.52	2.16	2.57	5.84	3.63
Seasoned offerings	1.96	2.69	3.25	3.09	4.21	3.26	6.40
Bonds	7.99	10.73	11.52	11.66	13.25	8.94	15.59
By rating, bonds sold in U.S.[3]							
Investment grade	4.41	6.45	7.23	5.52	4.42	2.80	7.37
Speculative grade	2.65	3.02	3.09	4.95	6.51	4.76	6.51
Public	2.01	1.95	2.19	2.68	2.93	2.23	3.42
Rule 144A	.63	1.07	.90	2.27	3.59	2.54	3.09
Financial corporations							
Stocks[2]	2.39	1.71	2.05	2.16	1.13	4.33	4.23
Bonds	27.81	30.81	31.26	37.80	37.69	26.10	33.80

Note. Components may not sum to totals because of rounding.

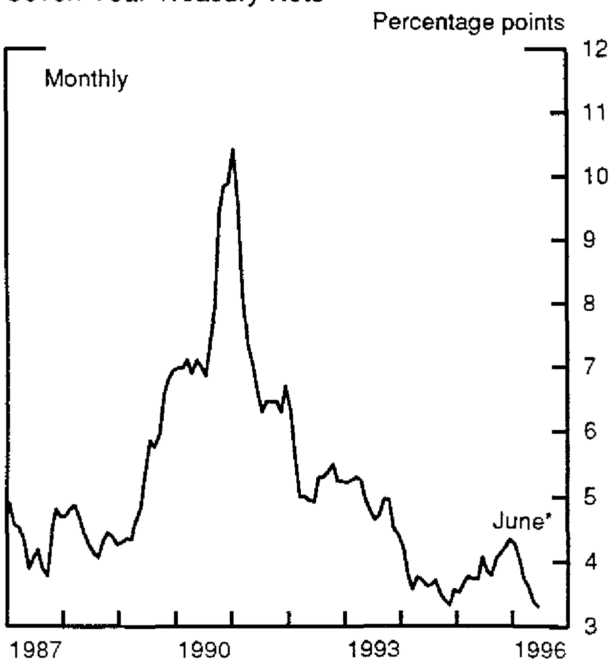
1. These data include speculative-grade bonds issued privately under Rule 144A. All other private placements are excluded. Total reflects gross proceeds rather than par value of original discount bonds.

2. Excludes equity issues associated with equity-for-equity swaps that have occurred in restructurings.

3. Bonds categorized according to Moody's bond ratings, or to Standard & Poor's if unrated by Moody's. Excludes mortgage-backed and asset-backed bonds.

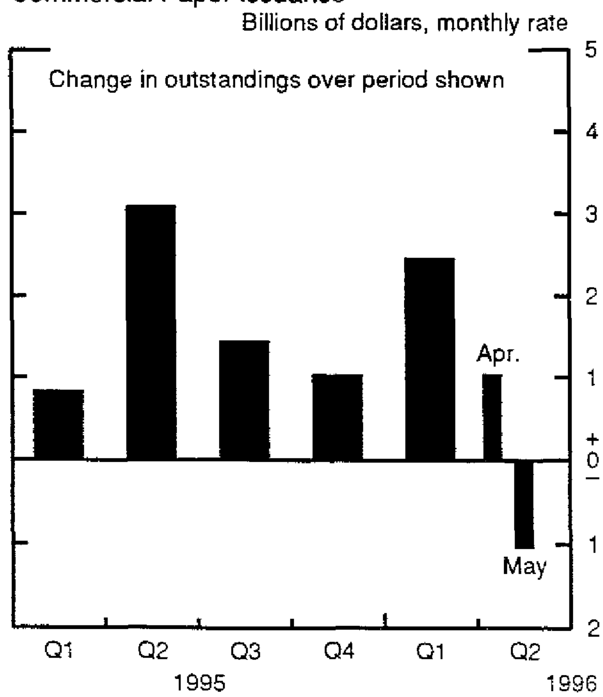
p Preliminary.

Rate on High-Yield Bond Less Seven-Year Treasury Note



* Based on daily data through June 20.

Commercial Paper Issuance*



* Seasonally adjusted.

might be a temporary decline in bond rates (table).[2] In recent weeks, as rates have backed up, issuance by investment-grade firms has remained firm, while junk-grade offerings have slowed. Nonetheless, strong demand for high-yield securities, particularly through mutual funds, continues to entice some issuers into the market and to compress spreads over Treasuries (chart, lower left panel).

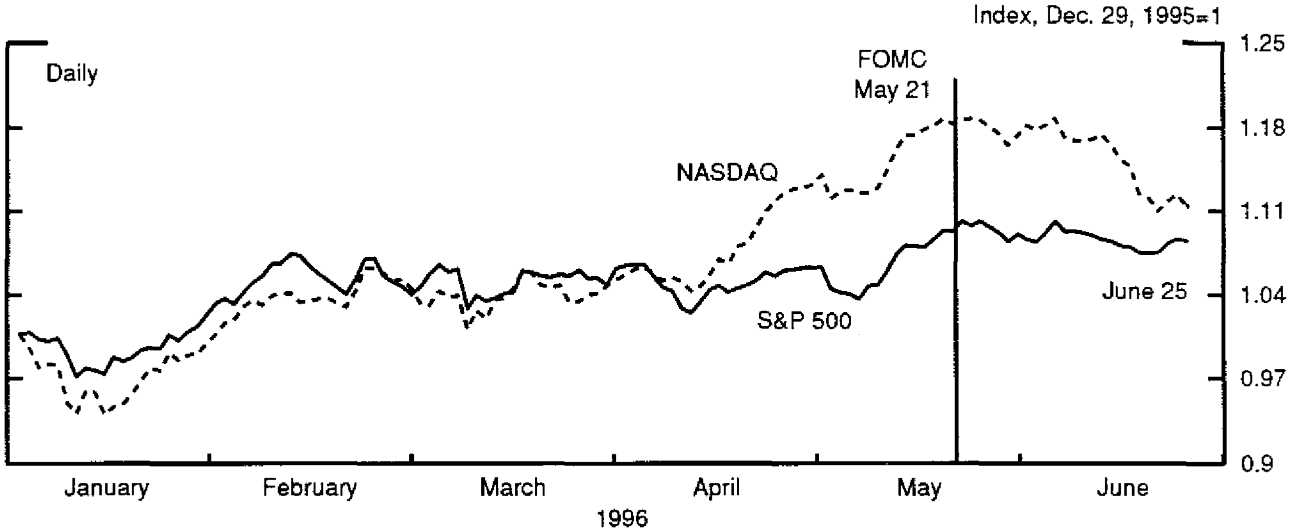
Commercial paper outstanding at nonfinancial firms changed little on net over April and May after rising sharply in the first quarter (chart, lower right panel). The leveling off reflects a slower pace of merger-related issuance as well as paydowns of some previously issued paper. Notably, in May, Lockheed-Martin used the proceeds of a $3.5 billion bond issue--the largest investment-grade bond offering on record--to pay down about $2.2 billion of commercial paper and a smaller amount of bank debt that had been raised to finance its acquisition of Loral.

In addition to narrow spreads of corporate bonds over Treasuries and low delinquency rates on bank loans, other indicators of credit quality of nonfinancial firms have remained favorable on balance. The default rate on junk bonds from year-end 1995 through May was only 0.6 percent (at an annual rate), considerably below last year's rate of 2.8 percent. Business failures over the first five months of this year have been running a little above the 1995 pace, but they remain at the low end of the range observed over the past decade. Recent news on bond ratings has been mixed: According to Moody's, the value of long-term debt downgraded in the second quarter has surpassed that upgraded by about $14 billion, the third consecutive period of small net downgrades after positive ratings changes on net for most of 1995. However, a large portion of the recent downgradings has involved debt of utility firms that appear vulnerable to competitive pressures as deregulation proceeds. Moreover, looking ahead, the dollar value of debt placed on review

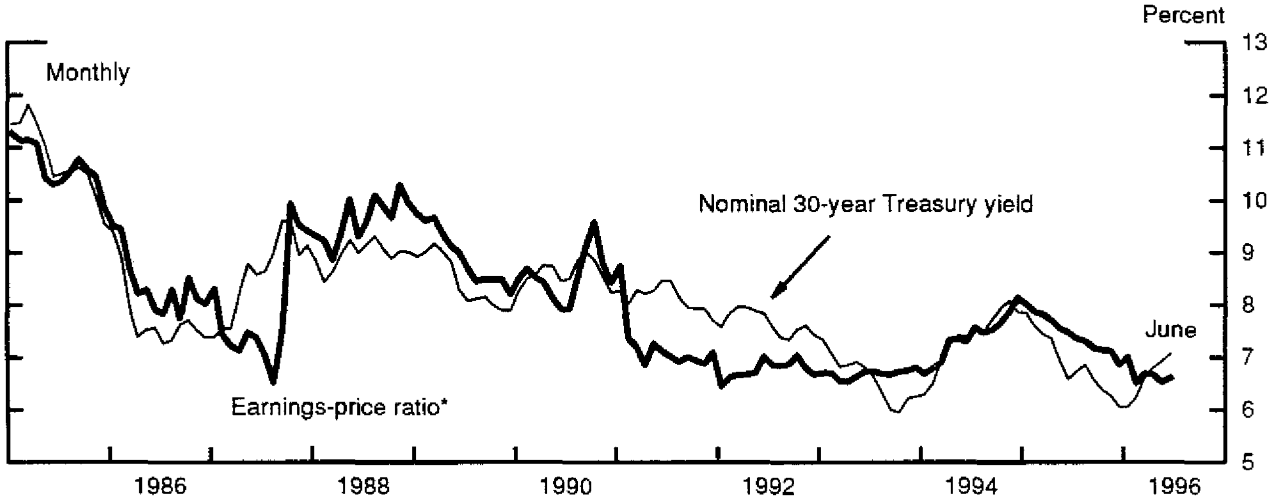
2. The Greenbook table on gross issuance of securities now includes bonds offered privately under SEC Rule 144A, which is designed to facilitate the secondary market trading of private securities among institutions. The market has come to regard 144A bonds as nearly perfect substitutes for public issues of speculative-grade debt. Indeed, most 144A bonds have SEC registration rights, and firms generally convert the bonds to public status shortly after issue. The 144A market attracts firms that need to raise funds more quickly than they can with public issues, which require SEC registration prior to issue.

Stock Market

Selected Stock Indexes

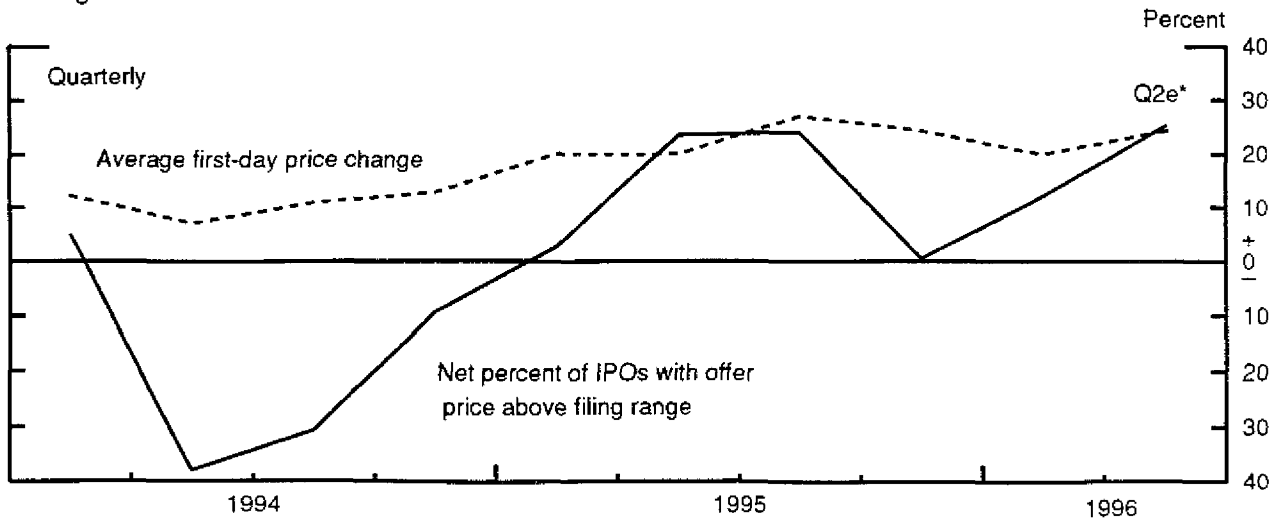


Earnings-Price Ratio for the S&P 500



* 12-month forward earnings as forecast by a consensus of equity analysts at brokerage firms (Source. I/B/E/S.)

Pricing of IPOs



* Based on data through June 21.

for a possible upgrade has risen in the second quarter and exceeds the amount slated for a downgrade by a sizable margin.

Although most major stock price indexes have fallen on net since the last FOMC meeting (chart, upper panel), share prices remain elevated relative to earnings forecasts; indeed, the twelve-month forward S&P 500 earnings-price ratio stands at about 6.5 percent, near its low over the past decade (chart, middle panel).

With these market prices, firms have issued large amounts of stock, lifting gross issuance of equities by nonfinancial firms above estimated retirements in the second quarter for the first time in two and a half years. Gross offerings of equity set successive monthly highs in April and May, and partial data for June suggest that issuance has remained strong. Initial public offerings (IPOs) have continued to be extremely well received by the market (chart, lower panel). An unusually large proportion of IPOs in the second quarter were offered at prices above the range listed in the firm's registration filing; the monthly data indicate that this proportion fell in June from the April-May average but remained relatively high. Even with the buoyant offering prices, IPO issues so far this quarter have recorded an average price increase of about 24 percent on the first day of trading.

Meanwhile, mergers--a significant source of nonfinancial equity retirements over the past two years--have slowed. No previously announced megamerger transactions have been completed since the May FOMC meeting, and the six megamergers that were announced during the intermeeting period will retire a relatively small amount of equity. Nonetheless, the underlying conditions that fueled the recent wave of acquisitions and mergers remain intact: Plentiful financing is available on favorable terms, and strong economic forces exist to drive further consolidation, especially in the health care, defense, and telecommunications industries.

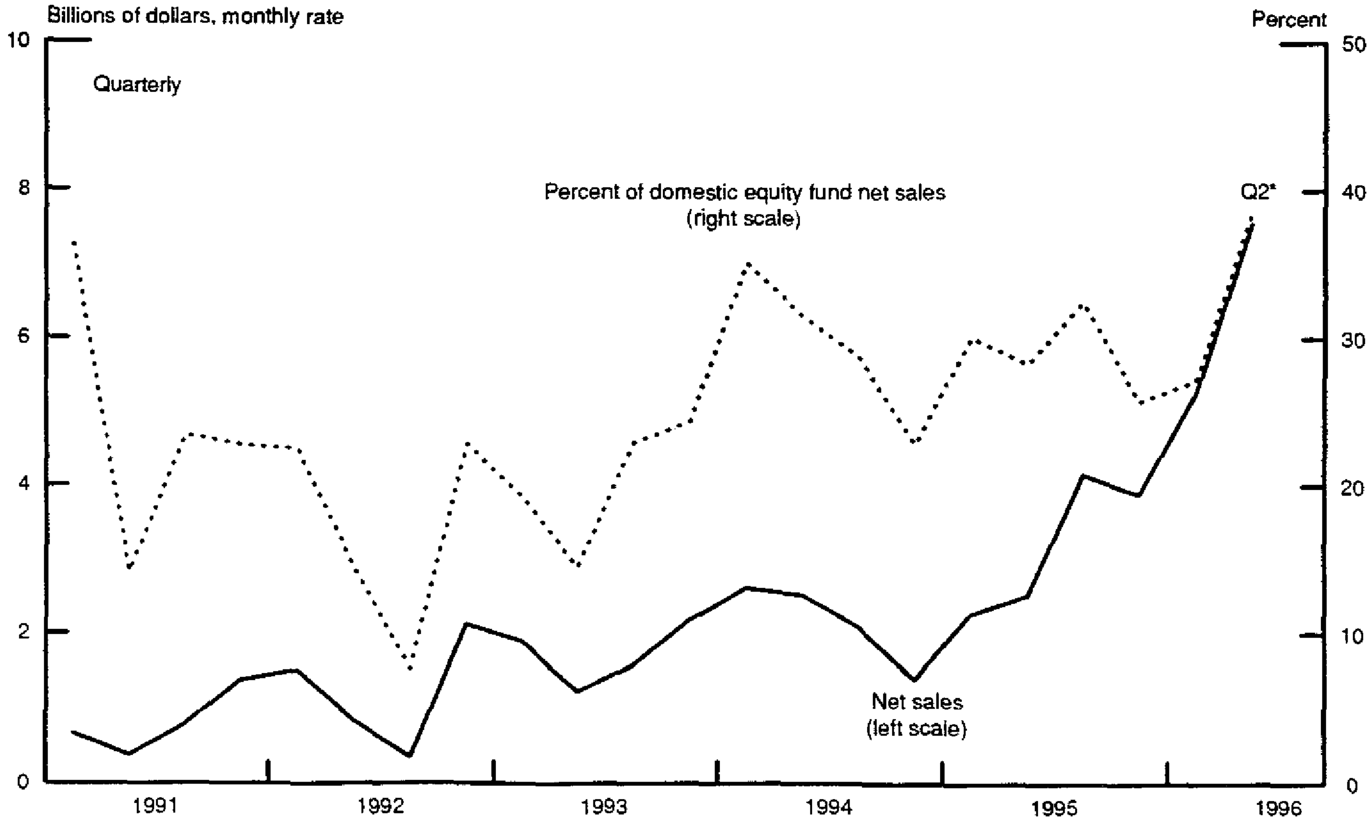
Share repurchases, which accounted for roughly 40 percent of all nonfinancial equity retired in 1995, have picked up from last year's strong pace. About $20 billion in share repurchases is expected to be completed in the second quarter, compared with an average $15 billion per quarter in 1995. Based on recent repurchase announcements, the current large volume of buybacks is likely to continue for some time.

NET SALES OF MUTUAL FUNDS
(Billions of dollars; monthly rate, not seasonally adjusted)

	1995	1996				Memo:
	Q4	Q1	Mar.	Apr.	May[e]	Apr. assets
Total stock	16.8	24.9	23.1	26.9	21.0	1,473.0
International	1.7	5.5	3.9	5.7	3.7	238.0
Domestic	15.1	19.4	19.2	21.2	17.4	1,235.1
Aggressive growth	3.9	5.3	5.1	7.6	7.5	233.5
Total bond	4.3	5.0	4.6	2.7	2.3	819.7
GNMA	-.1	-.1	-.1	-.2	-.2	53.4
Government	-.2	-.2	-.2	-.6	-.8	83.2
High-yield	1.0	.8	.5	1.4	1.4	64.5
Tax-exempt	.3	.1	.1	-.5	.0	244.0
Income	2.8	3.6	3.8	2.5	1.7	307.1
Other	.5	.8	.4	.0	.2	67.5

e Staff estimate.
Source. Investment Company Institute.

Aggressive Growth Equity Mutual Funds



* Through June 19.

Mutual funds continue to be a key acquirer of corporate shares. In May, net sales of equity fund shares exceeded $20 billion for the sixth consecutive month (table). Domestic equity funds have been capturing the bulk of that inflow, with notable strength in aggressive growth funds that invest primarily in IPOs and seasoned small-company shares; in recent months, flows to aggressive growth funds accounted for nearly 40 percent of the total net sales of domestic equity funds (chart).

Household Sector Finance

Household borrowing appears to have moderated somewhat in recent months, mainly reflecting a slowing of consumer credit. In April, consumer credit expansion dropped to a 7 percent annual rate, despite another sizable increase in revolving credit (table), and the relatively slow rise in consumer loans at banks suggests that the more moderate growth continued in May. Information on mortgage lending in the current quarter is mixed. Mortgage securitizations and mortgage applications have remained at relatively high levels, but real estate loan growth at commercial banks has been running well below the first-quarter rate. As long-term interest rates have risen, so has the spread of fixed-rate over adjustable-rate mortgage rates (chart, middle panel). The share of conventional home purchase mortgages closed with adjustable rates increased to 31 percent in May, up from 23 percent in April (chart, middle panel).

Delinquency rates on household debt in the first quarter suggest that repayment problems worsened a bit, although increases on most household debt categories have been moderate and delinquencies remain well below historical peaks. For example, the American Bankers Association's series for closed-end loans has retraced only a third of its decline from the 1991:Q3 high (chart, upper panel), and bank Call Report data show a similar pattern.

Credit card delinquencies tell a less reassuring story. The ABA series for credit card delinquencies reached a new high in the first quarter (chart, middle panel). Other measures of credit card delinquency--from the Call Report and from Moody's--have posted increases that are less sharp but still significant. Hard evidence is lacking, but industry observers believe that many card issuers achieved rapid growth of their credit card receivables in the 1990s by greatly relaxing their lending standards, and as noted above, trade reports have pointed to large increases in loss provisions at

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

Type of credit	1994[r]	1995[r]	1995 Q4[r]	1996 Q1[r]	1996 Mar.[r]	1996 Apr.[p]	Memo: Outstanding April 1996 (billions of dollars)
Total	14.5	14.2	10.6	11.1	10.0	6.9	1140.2
Auto	13.4	10.7	11.7	6.0	5.1	10.8	359.5
Revolving	18.2	22.0	14.4	16.7	15.3	20.2	438.5
Other	11.8	9.1	4.8	9.4	8.6	-13.6	342.2

Note. The consumer credit statistics have been revised to reflect the regular annual benchmarking to Call Reports and other data sources and the recalculation of seasonal factors. In addition, they have been redefined to include noninstallment as well as installment credit, formerly shown as separate items. This change makes the consumer credit statistics in this table conceptually comparable with other series on consumer borrowing contained in the bank credit statistics and the flow of funds accounts. (Noninstallment forms of credit, now included in "other," account for about 6 percent of the total.)

r Revised.

p Preliminary.

INTEREST RATES ON CONSUMER LOANS
(Annual percentage rate)

Type of loan	1994	1995	1995 May	1995 Aug.	1995 Nov.	1996 Feb.	1996 Apr.	1996 May
At commercial banks[1]								
New cars (48 mo.)	8.1	9.6	9.8	9.4	9.4	9.1	n.a.	8.9
Personal (24 mo.)	13.2	13.9	14.0	13.8	13.8	13.6	n.a.	13.5
Credit cards	16.2	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Credit cards[2]								
All accounts	n.a.	16.0	16.2	16.0	15.8	15.8	n.a.	n.a.
Accounts assessed interest	n.a.	15.8	16.2	15.9	15.7	15.4	n.a.	n.a.
At auto finance cos.[3]								
New cars	9.8	9.8	11.4	10.9	10.8	9.9	9.6	9.4
Used cars	13.5	13.5	14.8	14.2	14.0	13.3	13.3	13.5

Note. Annual data are averages of quarterly data for commercial bank rates and of monthly data for auto finance company rates.

1. Average of "most common" rate charged for specified type and maturity during the first week of the middle month of each quarter.

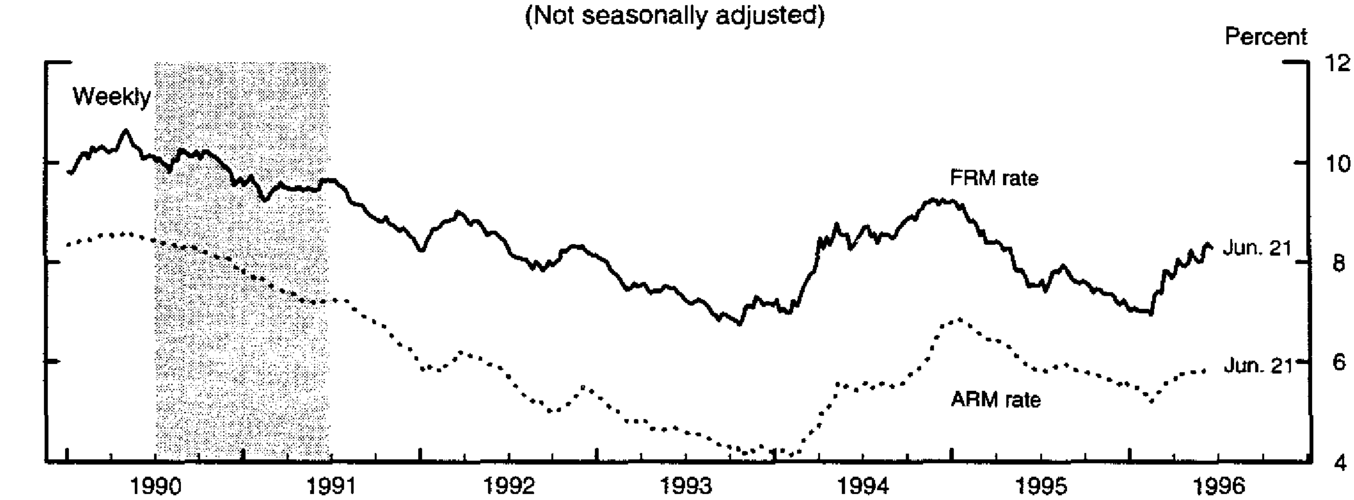
2. The rate for *all accounts* is the stated APR averaged across all credit card accounts at all reporting banks. The rate for *accounts assessed interest* is the annualized ratio of total finance charges at all reporting banks to the total average daily balances against which the finance charges were assessed (excludes accounts for which no finance charges were assessed).

3. For monthly data, rate for all loans of each type made during the month regardless of maturity.

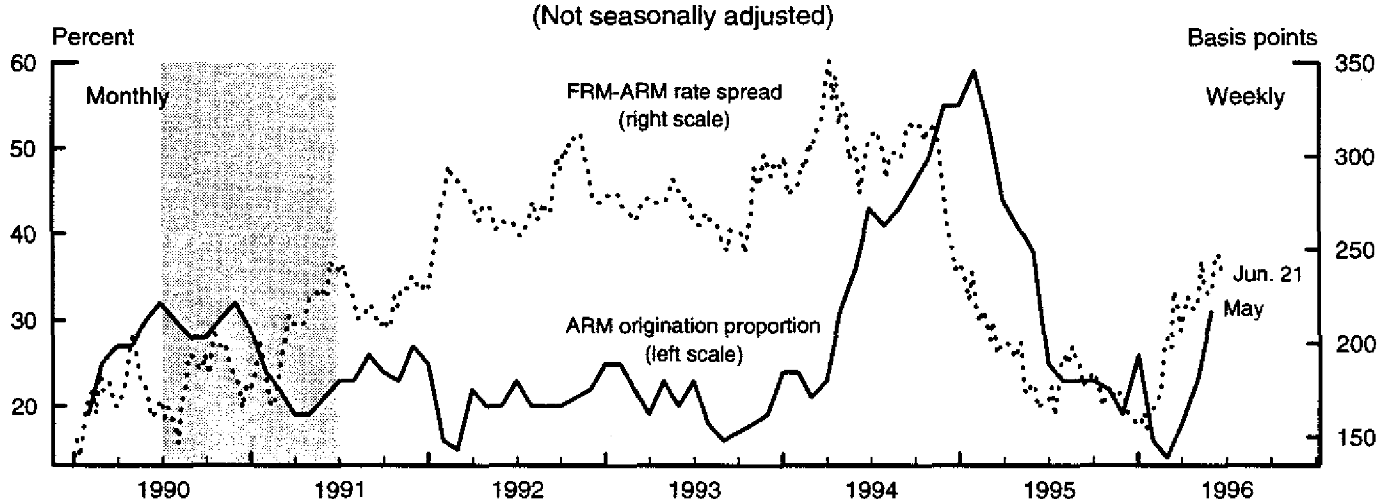
n.a. Not available.

Mortgage Market Indicators

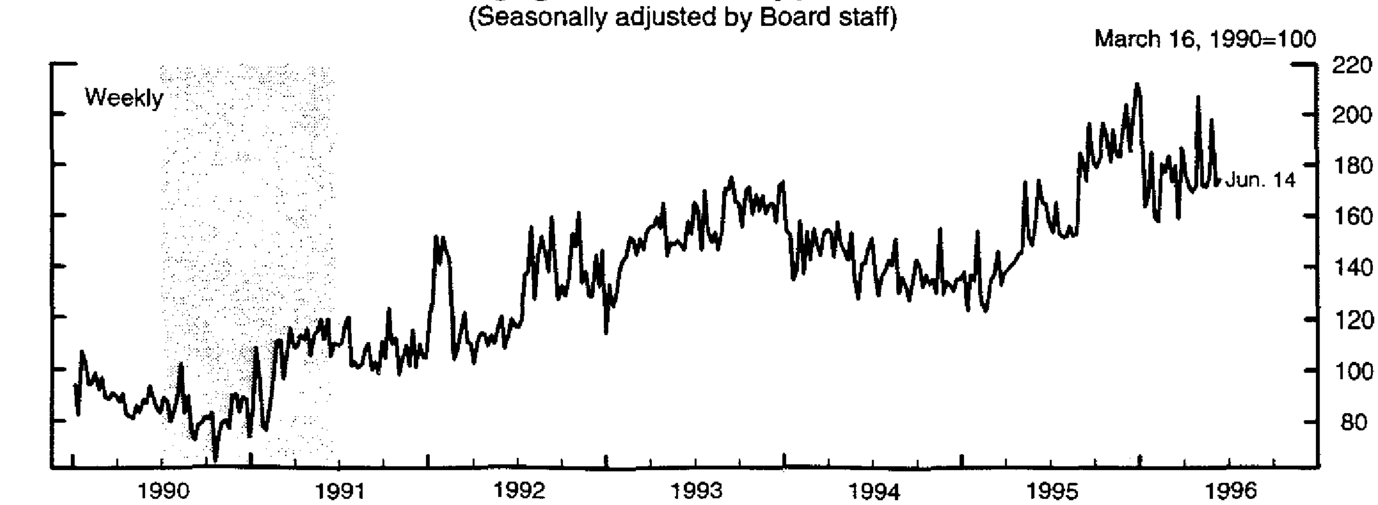
Freddie Mac FRM Rate and ARM Rate
(Not seasonally adjusted)



Freddie Mac FRM-ARM Spread and FHFB ARM Origination Proportion
(Not seasonally adjusted)

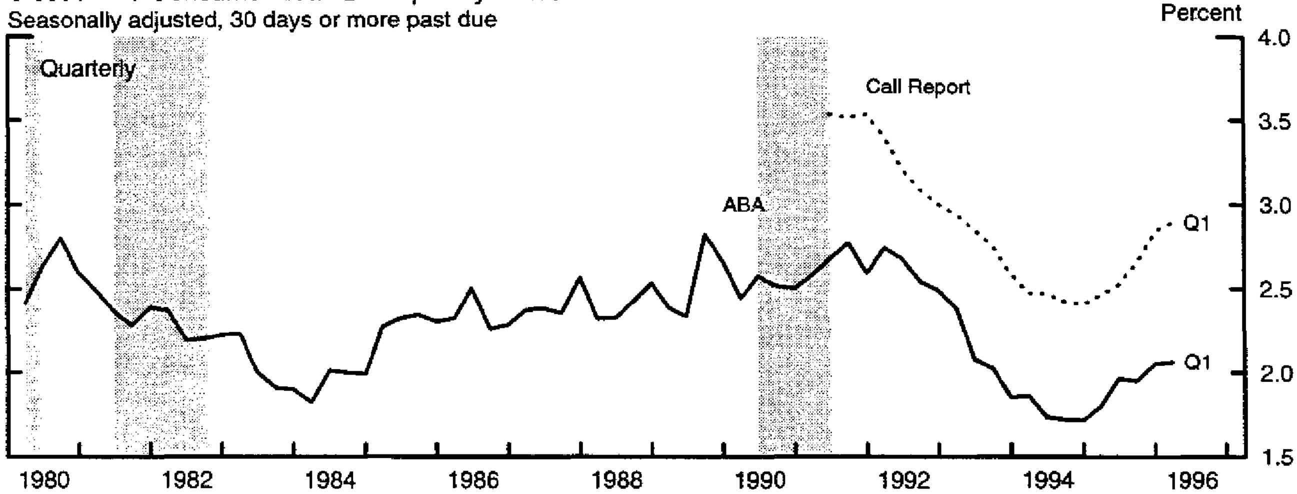


MBA Mortgage Purchase Application Index
(Seasonally adjusted by Board staff)

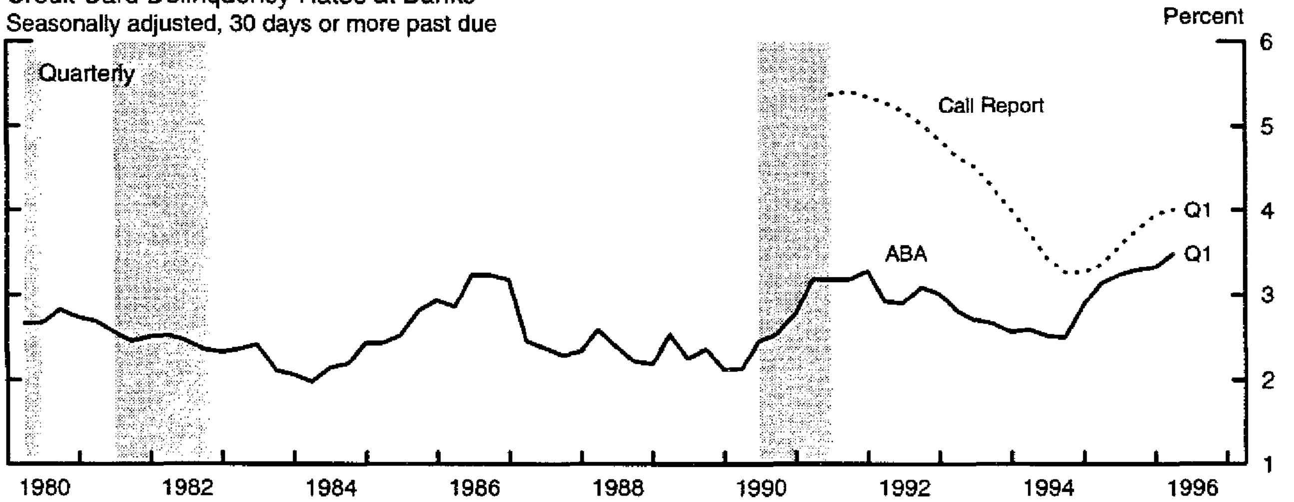


Consumer Credit Quality

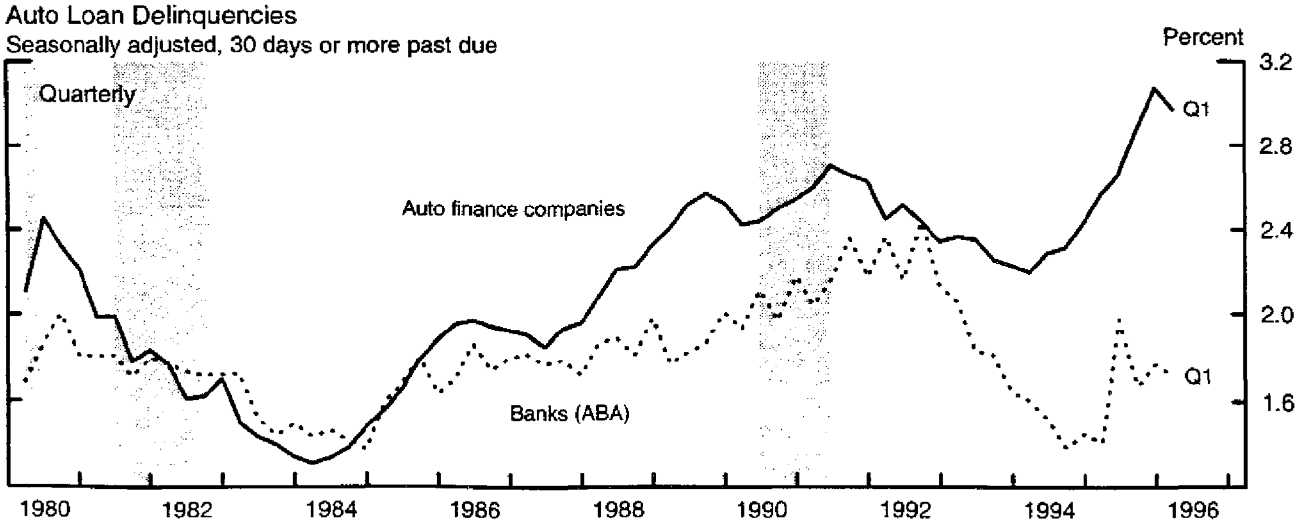
Closed-End Consumer Loan Delinquency Rates at Banks
Seasonally adjusted, 30 days or more past due



Credit Card Delinquency Rates at Banks
Seasonally adjusted, 30 days or more past due



Auto Loan Delinquencies
Seasonally adjusted, 30 days or more past due



some banks in the second quarter. It appears that banks have initiated some steps in recent months to tighten their credit card lending practices, as evident in the May Senior Loan Officer Opinion Survey.

Delinquency rates for auto loans at captive finance companies are on historically high ground (chart, lower panel). According to one finance company credit manager, the rise in delinquencies was, in part, an expected result of an effort to sell cars by liberalizing lending standards. Indeed, in his view, delinquencies have risen less than the company had anticipated. The level of the delinquency rate at captive finance companies has also been boosted a bit by the shift away from loans toward leasing; leases are not included in the loan delinquency data, and lease customers tend to be better credit risks than the average borrower.

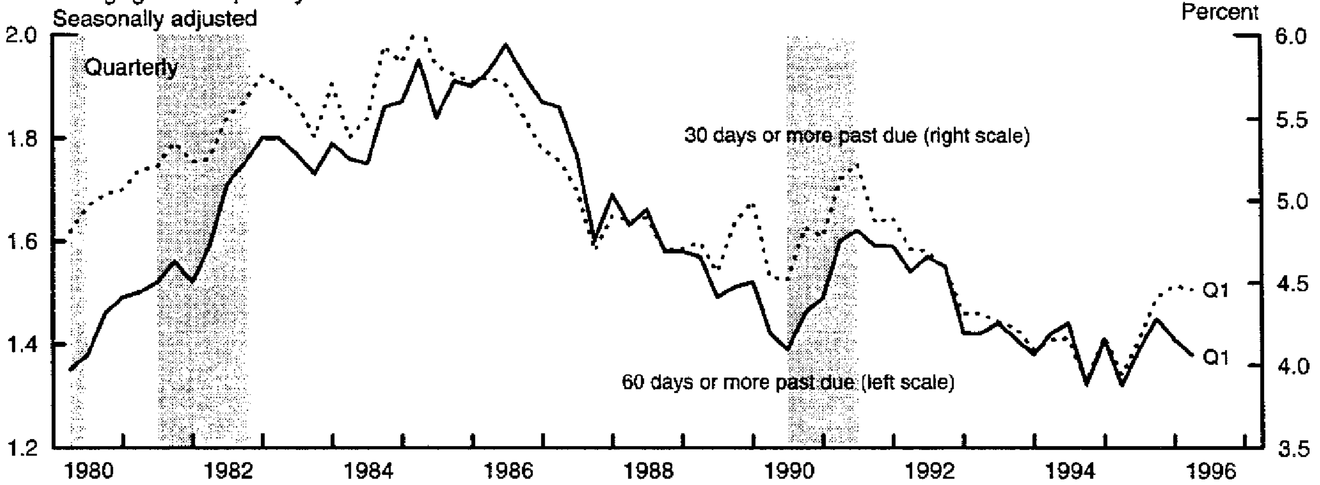
Delinquency rates for mortgages remained on the low side of historical experience. According to Mortgage Bankers Association data, both the delinquency rate for loans thirty days or more past due and for loans sixty days or more past due, a measure of more serious payment problems, edged down (chart, upper panel). Call Report data indicate little change in delinquency rates for home mortgages in total at banks, with the delinquency rate on revolving home equity loans only edged up and delinquency rates on other home mortgage loans unchanged.

With delinquency rates low, mortgage lenders have apparently kept loan terms favorable. Data from the Federal Housing Finance Board's monthly survey of rates and terms on conventional home mortgages indicate that the average loan-to-value ratio at major lenders edged up in April for the third consecutive month to 79.7 percent, the highest level since August 1995 (chart, middle panel).

Finally, another broad measure of household financial distress--the personal bankruptcy rate--has reached a new high (chart, lower panel). While the increase in bankruptcies no doubt reflects the rise in debt payment problems, the dollar amount of assets that can be exempted from liquidation was increased early last year, making bankruptcy a more attractive alternative for troubled debtors. A previous liberalization of bankruptcy law contributed to a threefold surge in filings in the mid- to late-1980s, but not to a commensurate rise in loan losses.

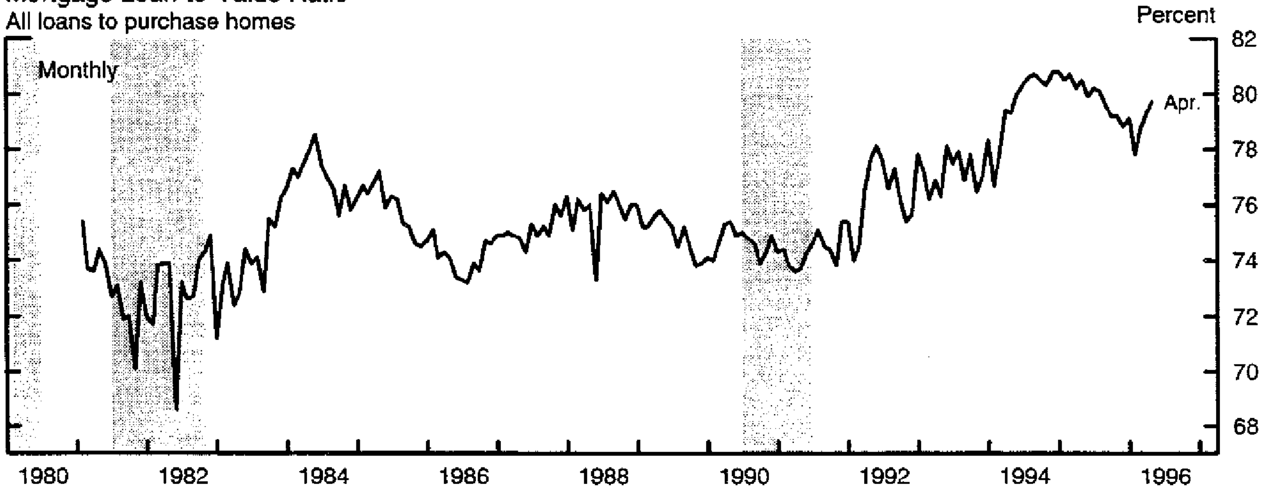
Household Credit Quality

Mortgage Delinquency Rates at All Lenders
Seasonally adjusted



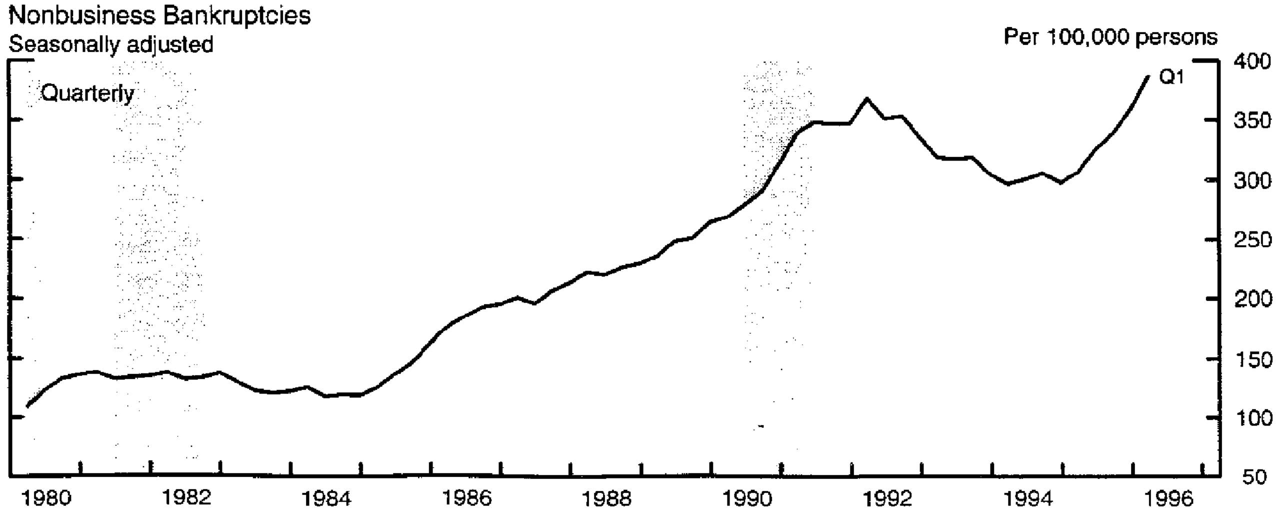
Source. Mortgage Bankers Association

Mortgage Loan-to-Value Ratio
All loans to purchase homes



Source. Federal Housing Finance Board

Nonbusiness Bankruptcies
Seasonally adjusted



Treasury and Agency Financing

The staff projects a second-quarter federal budget surplus of $50 billion (not seasonally adjusted). Together with $13 billion to be raised from coupon issues, this surplus will be used to replenish the Treasury's cash balance and to pay down roughly $42 billion in bills (table).

The Treasury recently increased by $500 million the sizes of its two-, three-, and five-year note auctions. The Treasury appears more willing than previously to vary the size of bill auctions to manage its cash balance. Between May 30 and June 20, bill auction sizes increased from $28 billion to $31 billion, and then fell back to $27 billion.

Following the May announcement that it planned to issue inflation-indexed bonds, the Treasury initiated meetings with dealers and investors and a thirty-day public comment period to develop the precise characteristics of the securities. Decisions on the design of these instruments are expected after the feedback has been evaluated. The Secretary of the Treasury has said that he expects to be issuing such securities in late 1996 or early 1997.

Agency issuance in the primary market has slowed slightly in the second quarter. Spreads between yields on agency debt and Treasuries of comparable maturities have remained steady in the primary market and have widened slightly in the secondary market. The use of foreign markets to fund agency activities continues to expand. In June, Fannie Mae became the first agency to announce that it will issue a yen-denominated security. Since its first foreign issue in June 1994, Fannie has raised nearly $10-1/4 billion in the global bond market, denominated in dollars and deutschemarks.

Municipal Bonds

Gross issuance of long-term municipal debt picked up in May from April's pace, reflecting stronger refunding volume when rates fell temporarily in the latter part of the month (table). Preliminary data for June suggest that issuance has edged off with the backup in rates. Owing to a heavy volume of scheduled bond redemptions in June and July, retirements almost certainly will outpace gross issuance over these two months, keeping outstanding municipal debt on a downward track.

Yields on long-term municipal bonds rose less than those on Treasuries over the intermeeting period, and the long-term tax-exempt to taxable ratio dropped to its lowest level in more than a

TREASURY FINANCING
(Billions of dollars; total for period)

Item	1996 Q1	Q2 p	Apr.	May	Jun. p
Total surplus/deficit (-)	-72.3	50.3	72.4	-53.3	31.2
Means of financing deficit					
Net cash borrowing and repayments (-)	80.5	-26.7	-35.5	20.6	-11.9
Nonmarketable	2.6	2.5	1.1	0.5	0.9
Marketable	77.9	-29.2	-36.5	20.1	-12.8
Bills	51.8	-41.9	-42.9	13.7	-12.8
Coupons	26.1	12.7	6.3	6.4	0.0
Decrease in cash balance	-1.4	-17.5	-26.4	43.8	-34.8
Other[1]	-6.8	-6.1	-10.5	-11.1	15.6
Memo:					
Cash balance, end of period	21.9	39.3	48.3	4.5	39.3

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

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

Agency	1995 Q4	1996 Q1	Mar.	Apr.	May
FHLBs	6.3	-3.9	5.8	3.2	1.0
FHLMC	8.4	4.3	0.5	11.9	5.1
FNMA	22.0	7.6	2.7	-0.5	-1.3
Farm Credit Banks	1.6	2.0	1.9	1.4	n.a
SLMA	-4.1	-1.8	-3.8	n.a	n.a

Note. Excludes mortgage pass-through securities issued by FNMA and FHLMC.
n.a. Not available.

GROSS OFFERINGS OF MUNICIPAL SECURITIES
(Billions of dollars; monthly rates, not seasonally adjusted)

	1993	1994	1995	1995 Q4	1996 Q1	1996 Apr.	1996 May
Total tax-exempt	27.2	16.1	14.9	17.2	14.3	15.7	16.1
Long-term	23.3	12.8	12.1	15.5	12.7	13.0	14.9
Refundings[1]	15.7	4.0	3.6	5.3	4.9	3.5	5.4
New capital	7.6	8.8	8.5	10.2	7.8	9.5	9.6
Short-term	3.9	3.3	2.8	1.7	1.6	2.7	1.2
Total taxable	.7	.7	.7	.3	.5	.5	.3

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

Tax–Exempt to Taxable Yield Ratio
(Bond Buyer municipal revenue yield to thirty–year Treasury yield)

* Based on data through June 21.

year (chart). The yield ratio jumped in mid-1995 and remained elevated at year-end, owing largely to investors' concerns that tax reform would reduce the advantages of municipal debt. As market concerns about tax reform diminished, municipals outperformed comparable Treasuries, reversing a good part of the earlier run-up in the yield ratio.

In explaining movements in the yield ratio over the past year, two other factors are often cited--the shrinking supply of municipal debt and developments in Orange County. However, these factors probably have not been responsible for the rise and the subsequent decline in the yield ratio over the past year. The amount of outstanding municipal debt has been moving lower since 1994, without appreciable variation in the trend. News about Orange County has not had substantial effects on national indexes of municipal security prices, either early when the County's massive investment losses were revealed or more recently when the county emerged from bankruptcy.[3]

3. However, yield spreads for California debt widened somewhat in the wake of Orange County's bankruptcy.

INTERNATIONAL DEVELOPMENTS

U.S. International Trade in Goods and Services

In April, the deficit in U.S. international trade in goods and services widened relative both to the level recorded in March and the average level for the first quarter. Exports in April were 1 percent higher than in March, and imports rose 1-1/2 percent.

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

		Annual rates			Monthly rates		
	1995	1995		1996	1996		
		Q3	Q4	Q1	Feb	Mar	Apr
Real NIPA 1/							
Net exports of G&S	-114.2	-114.3	-96.6	-110.6	...	...	...
Nominal BOP							
Net exports of G&S	-105.1	-97.3	-77.6	-97.4	-6.7	-8.0	-8.6
Goods, net	-173.4	-170.2	-152.1	-171.0	-12.8	-14.5	-14.7
Services, net	68.4	72.8	74.5	73.5	6.1	6.4	6.0

1. In billions of chained (1992) dollars.
Source. U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

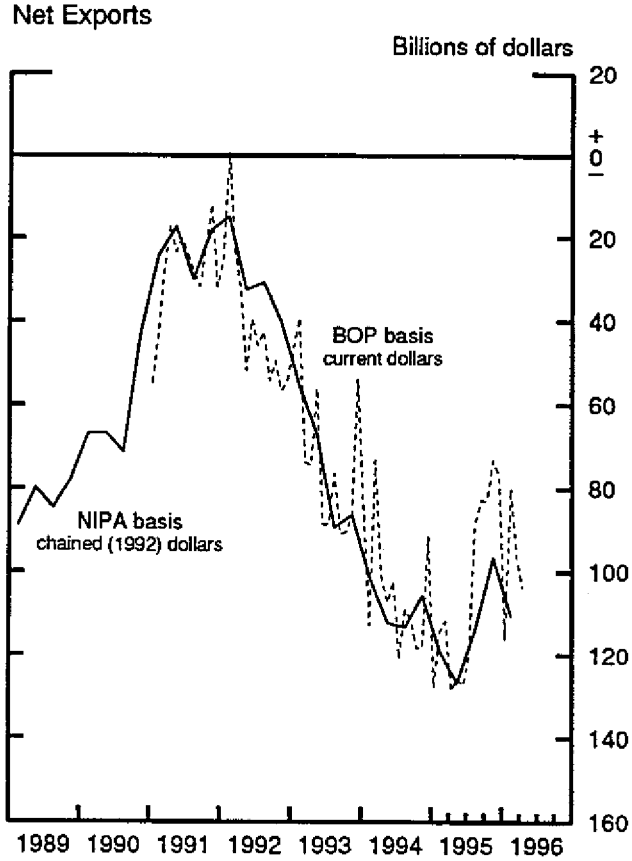
In April, the level of exports rose 2-1/2 percent relative to the first-quarter level. Increases were recorded in most trade categories, but exports of computers, semiconductors, and automotive products remained weak. The level of imports increased almost 3 percent relative to the first quarter. Almost all of the increase was due to higher imports of oil and gold.

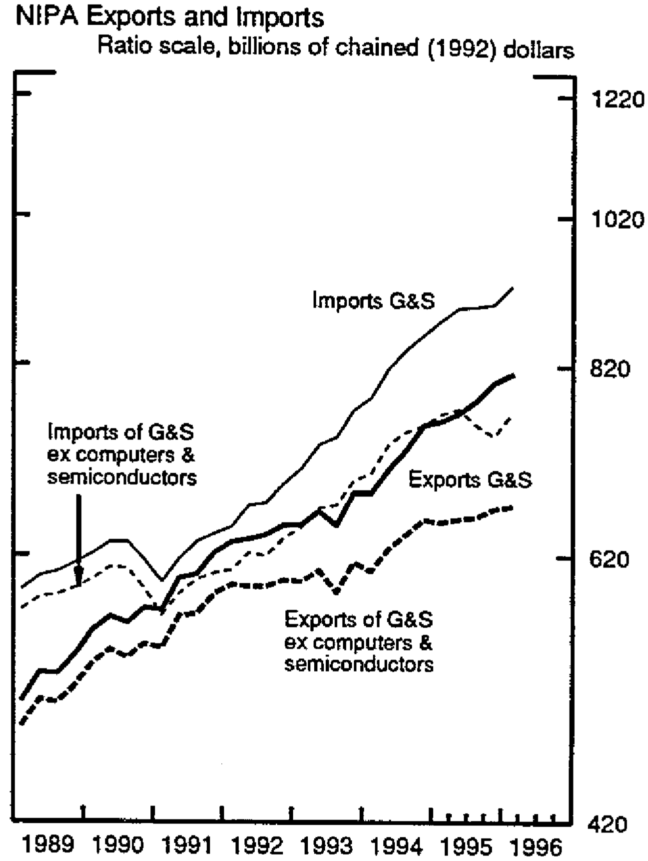
Oil Imports

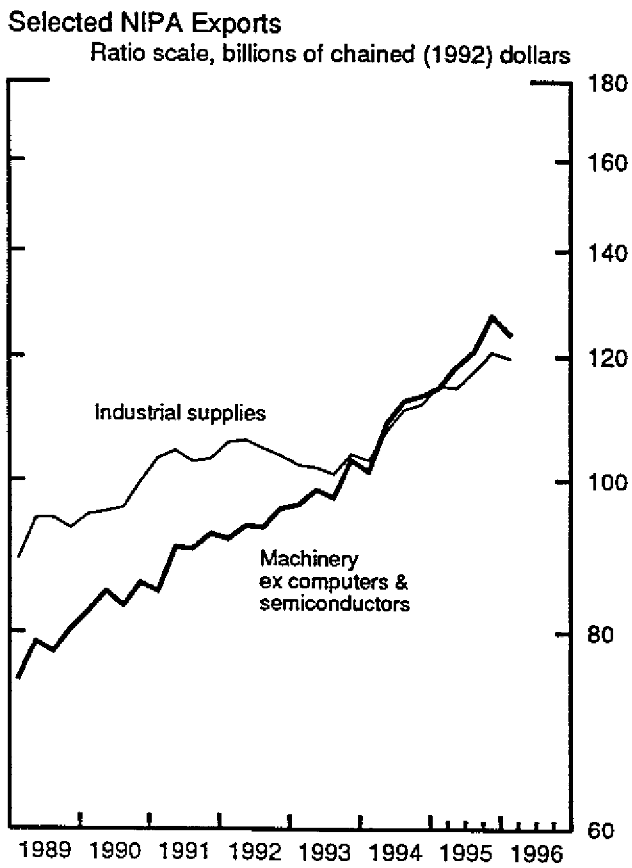
The quantity of oil imported in the first quarter of 1996 increased moderately relative to the fourth quarter, as a strong increase in oil consumption was partially offset by a larger-than-normal seasonal inventory drawdown. April imports were well above first-quarter rates due to an increase in oil inventories. Preliminary Department of Energy statistics indicate that oil imports continued at a brisk pace in May due to a renewed pick-up in consumption and continued rebuilding of oil stocks.

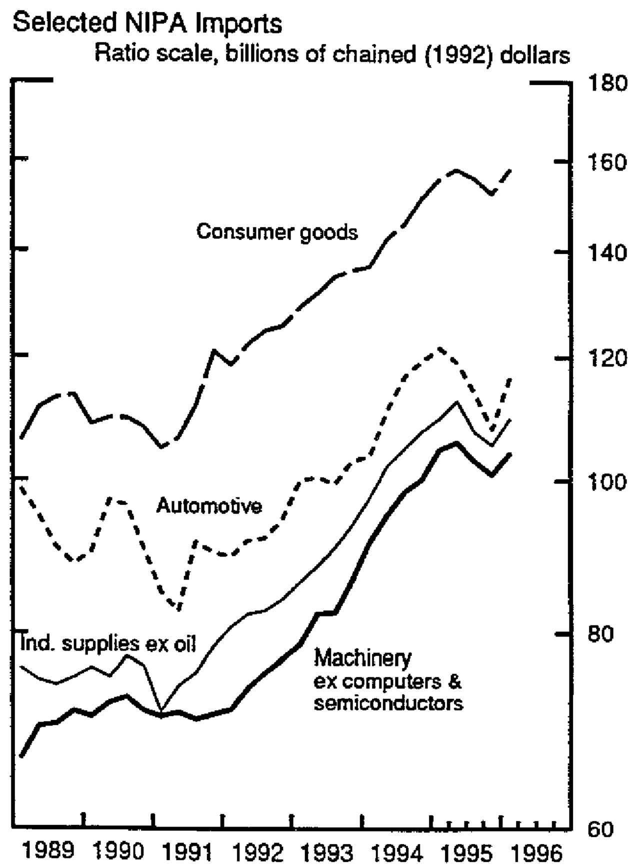
The price of imported oil increased sharply in the first quarter and, again, in April. Unusually cold weather in North America and Japan and weather-related production disruptions in the North Sea and Australia helped drive up oil prices in the first few months of the year. Spot WTI declined more than $2.25 per barrel in

U.S. International Trade in Goods and Services
(Seasonally adjusted annual rate)









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

	Levels				Amount Change 1/			
	1995	1996	1996		1995	1996	1996	
	Q4	Q1	Mar	Apr	Q4	Q1	Mar	Apr
Exports of G&S	814.5	819.7	831.3	839.3	17.6	5.3	1.4	8.0
Goods exports	597.7	600.1	605.9	620.0	17.7	2.4	-4.7	14.2
Agricultural	60.7	63.2	64.5	62.6	1.7	2.6	3.0	-1.9
Gold	3.7	6.3	11.3	15.4	0.4	2.6	7.0	4.1
Computers	43.5	45.4	44.1	44.5	2.2	2.0	-2.6	0.4
Other goods	489.8	485.1	486.0	497.5	13.5	-4.7	-12.1	11.5
Aircraft & pts	25.1	26.5	28.9	33.4	1.6	1.4	-1.1	4.4
Semiconductors	37.7	37.5	37.1	35.3	2.0	-0.2	0.1	-1.8
Other cap gds	142.5	138.4	139.1	142.3	7.5	-4.1	-2.7	3.2
Automotive	62.0	62.0	59.1	60.2	-0.1	0.0	-5.2	1.1
to Canada	34.2	33.1	30.9	33.1	0.9	-1.1	-3.5	2.2
to Mexico	7.0	7.6	8.0	6.5	0.3	0.6	0.1	-1.6
to ROW	20.7	21.3	20.1	20.6	-1.3	0.5	-1.8	0.5
Ind supplies	130.6	128.9	129.2	131.2	-2.2	-1.7	-1.0	1.9
Consumer goods	65.8	67.9	68.6	70.8	1.4	2.1	-0.6	2.2
All other	26.2	23.9	23.9	24.3	3.4	-2.3	-4.6	0.4
Services exports	216.8	219.7	225.4	219.3	-0.1	2.9	6.1	-6.2
Imports of G&S	892.1	917.1	927.5	942.8	-2.1	25.1	17.7	15.4
Goods imports	749.8	771.0	779.3	795.9	-0.3	21.2	15.3	16.6
Petroleum	53.5	55.9	53.6	70.2	-2.4	2.4	0.8	16.6
Gold	3.4	6.8	13.9	18.8	0.9	3.3	10.4	4.9
Computers	61.9	62.2	59.9	62.1	3.4	0.3	-4.1	2.2
Other goods	631.0	646.2	651.8	644.7	-2.2	15.2	8.1	-7.1
Aircraft & pts	10.6	11.0	12.0	10.8	0.2	0.4	1.3	-1.2
Semiconductors	44.6	43.7	44.7	38.7	3.1	-0.9	2.3	-6.0
Other cap gds	114.9	116.7	117.7	114.4	-1.4	1.8	2.2	-3.3
Automotive	119.3	125.0	120.5	126.1	-2.5	5.7	-7.2	5.6
from Canada	45.8	45.7	41.7	47.6	2.8	-0.1	-6.4	5.9
from Mexico	21.1	22.8	22.0	22.9	2.9	1.7	-0.9	0.8
from ROW	52.4	56.4	56.8	55.6	-8.2	4.1	0.2	-1.1
Ind supplies	121.7	124.2	127.6	126.0	-1.1	2.5	5.5	-1.6
Consumer goods	158.6	163.4	164.1	162.2	-2.7	4.8	0.1	-1.9
Foods	32.8	34.2	35.6	36.2	-0.2	1.5	1.8	0.6
All other	28.5	28.0	29.7	30.3	2.3	-0.6	2.2	0.6
Services imports	142.2	146.1	148.2	146.9	-1.8	3.9	2.4	-1.3
Memo:								
Oil qty (mb/d)	9.30	8.74	8.03	9.53	-0.45	-0.56	-0.44	1.50
Oil price ($/bbl)	15.75	17.56	18.29	20.19	0.05	1.80	1.24	1.90

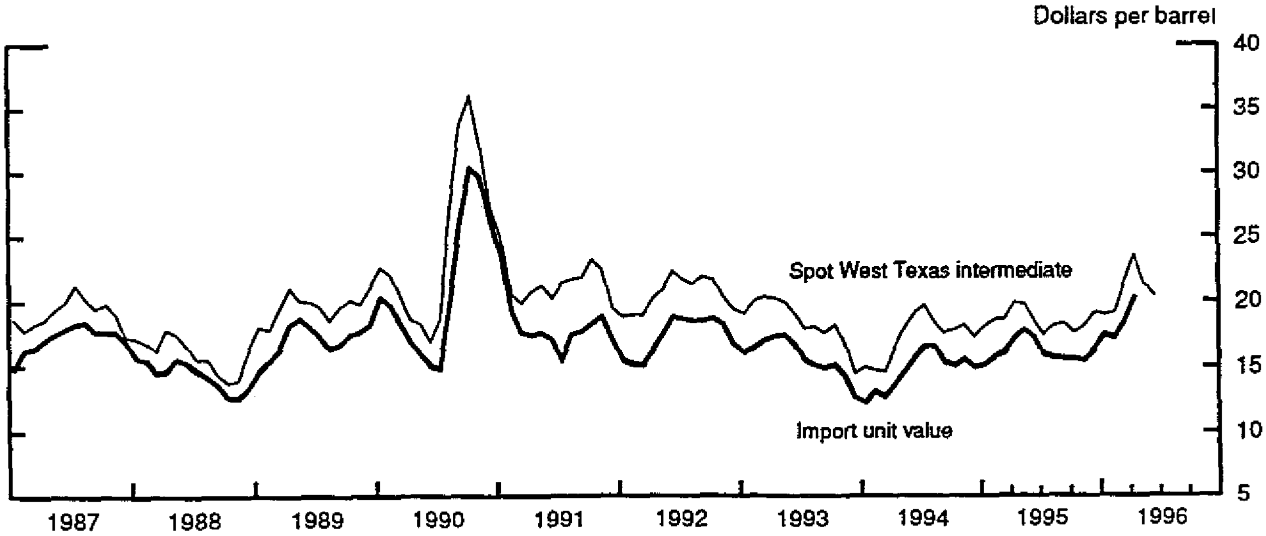
1. Change from previous quarter or month.
Source. U.S. Dept. of Commerce, Bureaus of Economic Analysis and Census.

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

	Annual rates 1995 Q4	1996 Q1	1996 Q2e/	Monthly rates 1996 Mar	Apr	May
	-----------	BLS prices	(1990=100)	-----------		
Merchandise imports	-1.1	2.4	4.0	0.7	0.8	-0.5
Oil	0.4	47.4	60.1	8.5	8.3	-2.2
Non-oil	-1.1	-1.2	-1.3	-0.3	0.0	-0.3
Foods, feeds, bev.	-7.4	-4.5	15.0	-1.4	3.3	0.4
Ind supp ex oil	0.2	-3.1	-4.0	0.3	-0.6	-0.7
Computers	-7.5	-8.1	-12.3	-2.4	-1.0	-0.8
Capital goods ex comp	-2.5	-0.4	-3.5	-0.3	-0.5	-0.2
Automotive products	1.6	-0.8	-0.1	-0.2	0.1	-0.1
Consumer goods	-0.0	1.4	-0.4	-0.1	0.0	-0.1
Merchandise exports	0.0	1.0	2.2	-0.2	0.5	0.4
Agricultural	23.0	13.8	32.6	1.4	4.8	3.1
Nonagricultural	-2.7	-0.9	-1.7	-0.3	-0.1	-0.1
Ind supp ex ag	-11.0	-3.6	-5.1	-0.7	-0.4	-0.2
Computers	-7.4	-9.2	-6.9	-0.3	-1.3	-0.4
Capital goods ex comp	1.8	2.4	1.1	0.0	0.2	0.0
Automotive products	5.0	-0.1	0.1	-0.1	0.0	0.2
Consumer goods	0.4	2.3	0.8	0.1	0.2	-0.3
	---Prices in	the NIPA	accounts	(1992=100)--		
Fixed-weight						
Imports of gds & serv.	-1.6	0.6	n.a.	...	...	...
Non-oil merchandise	-1.7	-0.6	n.a.	...	...	...
Exports of gds & serv.	-0.8	0.5	n.a.	...	...	...
Nonag merchandise	-3.5	-1.7	n.a.	...	...	...

e. Average of two months.

Oil Prices



May, averaging \$21.26 per barrel. Prices have fallen a bit more in June and have been trading in the \$20 per barrel range. The decline in oil prices since April reflects an unwinding of earlier, temporary shocks to the oil market. The announcement of Iraq's agreement with the United Nations to export a limited quantity of oil (estimated to be 800,000 b/d) under U.N. supervision has had little effect on either spot or futures prices.

Prices of Non-oil Imports and Exports

Prices of non-oil imports decreased during April-May combined, at about the same rate as in the two previous quarters. The prices of imported capital goods and industrial supplies continued to fall sharply. These decreases were only partly offset by substantial price increases in a broad array of imported foods (coffee, grains, and vegetables).

Prices of exports increased rapidly in April-May combined, significantly faster than in recent quarters. The pickup is due entirely to a more rapid increase in agricultural prices (especially grains). On balance, prices of non-agricultural exports fell, with continued declines in prices of capital goods and industrial supplies.

U.S. Current Account

The U.S. current account deficit increased \$20.6 billion (SAAR), to \$142.4 billion SAAR, in the first quarter of 1996. The increase in the deficit on trade in goods and services and larger net unilateral transfers more than offset a decrease in net investment income payments. The narrower deficit on investment income owed mostly to larger receipts on U.S. direct investment abroad, while net unilateral transfers were substantially higher partly reflecting U.S. government grant disbursements delayed from the fourth quarter because of the government shutdown.

As is customary each June, estimates of U.S. international transactions are revised to incorporate updated source data and improved methodologies. These revisions increased the current account deficit \$1 to \$2 billion in the years 1986 through 1992 and lowered the deficit \$3 to \$5 billion in 1994 and 1995.

U.S. CURRENT ACCOUNT
(Billions of dollars, seasonally adjusted annual rates)

	Goods & services balance	Investment income, net	Transfers, net	Current acct balance
Years				
1990	-80.3	20.9	-35.2	-94.7
1991	-29.9	15.8	4.5	-9.5
1992	-38.3	11.2	-35.5	-62.6
1993	-72.0	9.7	-37.6	-99.9
1994	-104.4	-4.2	-39.9	-148.4
1995	-105.1	-8.0	-35.1	-148.2
Quarters				
1995-1	-118.1	-3.6	-34.6	-156.2
2	-127.3	-3.4	-33.2	-163.9
3	-97.3	-17.4	-36.0	-150.8
4	-77.6	-7.6	-36.6	-121.7
1996-1	-97.4	-1.6	-43.4	-142.4
Memo:				
$ Change				
Q1-Q4	-19.8	6.0	-6.7	-20.6

Source. U.S. Department of Commerce, Bureau of Economic Analysis.

U.S. International Financial Transactions

Foreign official inflows to the United States slowed markedly in April from the heady pace of the first quarter. (See line 1 of the Summary of U.S. International Transactions table.) Most of the slowing owes to reduced inflows from Japan, which were boosted in the first quarter by large foreign exchange market intervention. Official inflows from non-G-10 countries picked up from their low level in March to resume the robust pace of the first quarter. Partial data for May from FRBNY indicate official inflows of almost $10 billion, primarily by G-10 and OPEC countries. For the first three weeks of June, FRBNY reports a modest outflow attributable to a reduction in Brazil's holdings.

Private foreign net purchases of U.S. securities continued strong in April (line 4), maintaining a pace roughly equal to last year's record. Relative to the first quarter, April's purchases showed a shift toward Treasuries away from corporate and other bonds, reflecting a shift away from federal agency bonds. Private purchases of such bonds fell from more than $14 billion in the first quarter to zero in April.

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

	1994	1995	1995			1996		
			Q2	Q3	Q4	Q1	Mar	Apr
Official capital								
1. Change in foreign official reserve assets in U.S. (increase, +)	38.0	109.7	37.0	39.6	10.6	51.8	12.2	4.2
a. G-10 countries	28.9	32.9	14.3	5.6	-3.8	28.7	10.9	-3.8
b. OPEC countries	-3.3	4.3	-.2	6.2	-2.1	-.8	1.1	2.2
c. All other countries	12.4	72.5	22.9	27.7	16.6	24.0	.3	5.8
2. Change in U.S. official reserve assets (decrease, +)	5.3	-9.7	-2.7	-1.9	.2	*	-.6	*
Private capital								
Banks								
3. Change in net foreign positions of banking offices in the U.S.[1]	102.6	-30.5	-23.4	-7.2	9.6	-25.8	-15.5	8.7
Securities[2]								
4. Foreign net purchases of U.S. securities (+)	92.9	190.1	51.4	69.8	23.1	48.0	15.4	17.3
a. Treasury securities[3]	34.7	99.9	30.5	37.4	1.8	11.9	.4	8.4
b. Corporate and other bonds[4]	53.9	82.1	18.5	27.0	17.3	32.2	14.3	4.9
c. Corporate stocks	4.3	8.1	2.4	5.3	3.9	3.8	.7	4.1
5. U.S. net purchases (-) of foreign securities	-57.3	-97.9	-22.8	-35.4	-32.1	-34.4	-16.5	-6.5
a. Bonds	-9.2	-47.2	-12.5	-13.3	-17.7	-11.9	-6.1	.1
b. Stocks	-48.1	-50.8	-10.2	-22.1	-14.3	-22.5	-10.3	-6.6
Other flows (quarterly data, s.a.)								
6. U.S. direct investment (-) abroad	-54.5	-95.5	-18.2	-38.0	-44.1	-26.8	n.a	n.a
7. Foreign direct investment in U.S.	49.8	60.2	9.7	25.0	14.8	29.5	n.a	n.a
8. Other (inflow, +)[5]	-42.1	-9.7	-23.9	27.3	18.9	.8	n.a	n.a
U.S. current account balance (s.a.)	-148.4	-148.2	-41.0	-37.7	-30.4	-35.6	n.a	n.a
Statistical discrepancy (s.a.)	-13.7	31.5	33.9	-41.5	29.4	-7.5	n.a	n.a

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

1. Changes in dollar-denominated positions of all depository institutions and bank holding companies plus certain transactions between broker-dealers and unaffiliated foreigners (particularly borrowing and lending under repurchase agreements). Includes changes in custody liabilities other than U.S. Treasury bills.

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

3. Includes Treasury bills.

4. Includes U.S. goverment agency bonds.

5. Transactions by nonbanking concerns and other banking and official transactions not shown elsewhere plus amounts resulting from adjustments made by the Department of Commerce and revisions in lines 1 through 5 since publication of the quarterly data in the Survey of Current Business.

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

INTERNATIONAL BANKING DATA[1]
(Billions of dollars)

	1992	1993	1994	1995		1996		
	Dec.	Dec.	Dec.	Sept.	Dec.	Mar.	Apr.	May
1. Net claims of U.S. banking offices (excluding IBFs) on own foreign offices and IBFs	-71.6	-122.1	-224.0	-244.3	-260.0	-260.1	-253.5	-253.3
a. U.S.-chartered banks	-17.0	4.2	-70.1	-86.1	-86.1	-84.1	-82.1	-90.1
b. Foreign-chartered banks	-88.6	-126.3	-153.9	-158.2	-173.9	-176.0	-171.3	-163.2
2. Credit extended to U.S. nonbank residents								
a. By foreign branches of U.S. banks	24.8	21.8	23.1	25.7	26.5	27.3	27.4	27.9
b. By Caribbean offices of foreign-chartered banks	n.a.	90.9	78.4	86.3	86.3	90.0	n.a.	n.a.
3. Eurodollar holdings of U.S. nonbank residents								
a. At all U.S.-chartered banks and foreign- chartered banks in Canada and the United Kingdom	90.0	77.8	85.6	94.6	91.2	95.7	96.0	97.8
b. At the Caribbean offices of foreign-chartered banks	n.a.	79.2	86.0	89.9	92.3	96.6	n.a.	n.a.
MEMO: Data as recorded in the U.S. international transactions accounts								
4. Credit extended to U.S. nonbank residents	188	195	190	215	n.a.	n.a.	n.a.	n.a.
5. Eurodeposits of U.S. nonbank residents	236	231	262	279	n.a.	n.a.	n.a.	n.a.

1. Data on lines 1 through 3 are from Federal Reserve sources and sometimes differ in timing from the banking data incorporated in the U.S. international transactions accounts.

Lines 1a, 1b, and 2a are averages of daily data reported on the FR 2950 and FR2951.

Lines 2b and 3b are end-of-period data reported quarterly on the FFIEC 002s.

Line 3a is an average of daily data (FR 2050) supplemented by the FR 2502 and end-of-quarter data supplied by the Bank of Canada and the Bank of England. There is a break in the series in April 1994.

Lines 4 and 5 are end-of-period data estimated by BEA on the basis of data provided by the BIS, the Bank of England, and the FR 2502 and FFIEC 002s. It includes some foreign-currency denominated deposits and loans. Source: SCB

U.S. purchases of foreign securities slowed considerably in April. Equity purchases throughout Asia slowed, while bond sales in Europe and Canada offset a pickup in purchases of Asian bonds. Banks and securities dealers reported significant inflows in April, reversing about half of the large outflow in March (line 3). Most of April's inflow is attributable to a reduction in non-bank security dealer's liabilities to foreigners. As shown on line 1 of the International Banking Table, U.S. banks increased their net claims on related foreign offices in April.

Direct investment capital inflows surged to almost $30 billion in the first quarter, reflecting a pickup in foreign acquisitions of U.S. firms (line 7 of the Summary Table). In contrast, U.S. direct investment abroad slowed somewhat between the fourth and first quarters, but remained near the pace for all of last year. For the first quarter as a whole, recorded capital inflows exceeded the sum of recorded capital outflows and the current account, leaving a statistical discrepancy of $-7.5 billion.

Foreign Exchange Markets

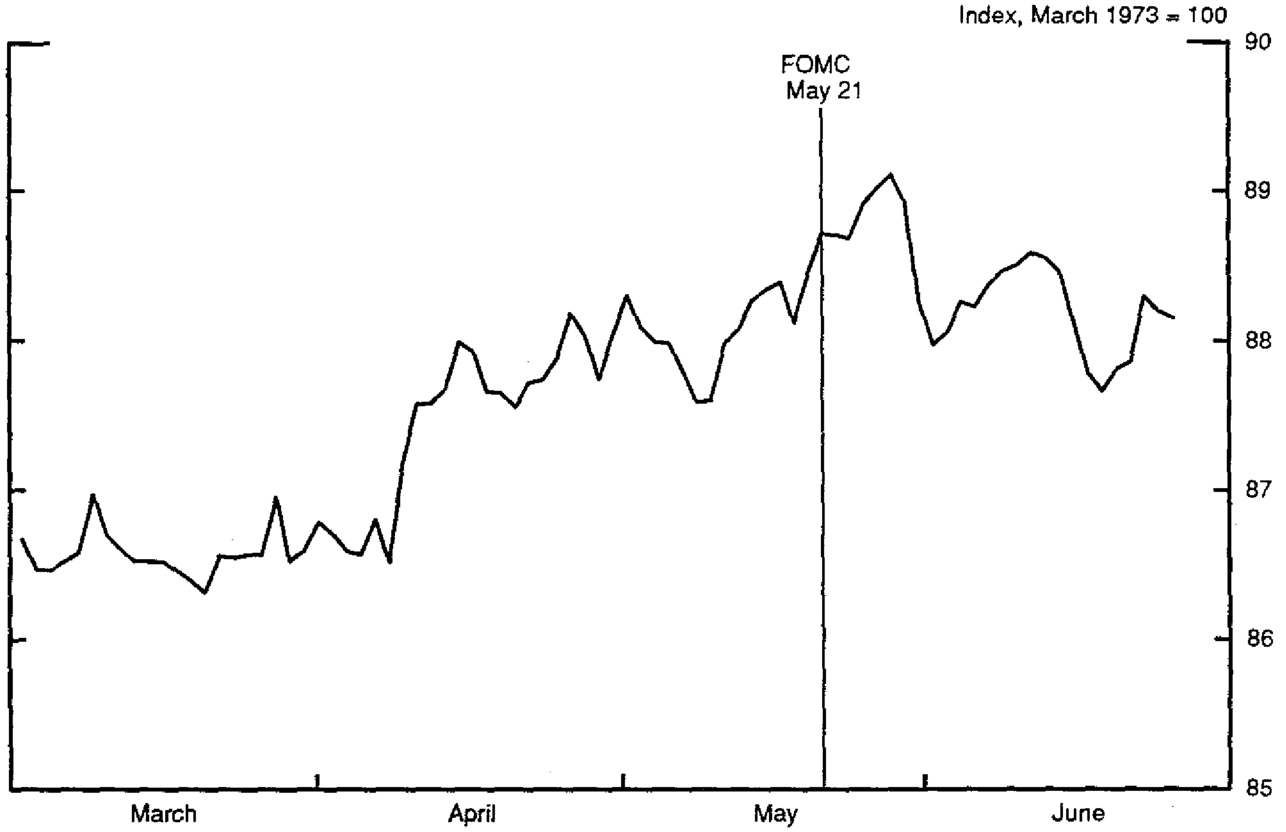
The weighted-average foreign exchange value of the dollar in terms of the other G-10 currencies has declined less than 1 percent since the May 21 FOMC meeting. Over this period, the dollar has depreciated about 1 percent against the mark and most other European currencies, while firming over 2 percent relative to the yen.

The mark's relative strength appears to have reflected mainly a growing sentiment among market participants that the time may have passed for an easing of German monetary policy, and that the next interest rate move by the Bundesbank may well be an increase rather than a decrease. This view has gained credence over the past month as the Bundesbank has kept the repo rate unchanged at the 3.30 percent level maintained since early February, and as incoming data have begun to show some tentative signs of strengthening economic activity in Germany. The continuation of M3 growth well above target--with annualized growth from the fourth-quarter base period easing only to 10.5 percent in May--also was interpreted as lessening the likelihood of any further Bundesbank easing.

In contrast, the relative weakness of the yen recently seems to have been influenced by an apparent reduction of market expectations that the Bank of Japan would move to raise short-term interest

Weighted Average Exchange Value of the Dollar

(Daily data)



Interest Rates in Major Industrial Countries

	Three-month rates			Ten-year bond yields		
	May 21	June 26	Change	May 21	June 26	Change
Germany	3.20	3.30	0.10	6.38	6.58	0.20
Japan	0.60	0.60	0.00	3.25	3.24	-0.01
United Kingdom	6.06	5.72	-0.34	7.96	7.99	0.03
Canada	4.76	4.86	0.10	7.70	7.80	0.10
France	3.80	3.81	0.01	6.43	6.59	0.16
Italy	8.75	8.50	-0.25	9.55	9.46	-0.09
Belgium	3.17	3.20	0.03	6.64	6.80	0.16
Netherlands	2.55	2.90	0.35	6.26	6.50	0.24
Switzerland	2.06	2.63	0.57	4.14	4.34	0.20
Sweden	6.13	5.64	-0.49	8.30	8.19	-0.11
Weighted-average foreign	3.91	3.91	0.00	6.55	6.65	0.10
United States	5.35	5.48[p]	0.13	6.65	6.90[p]	0.25

Note. Change is in percentage points. p. Preliminary rates in the near term. Over the past month, a number of Japanese officials have made statements suggesting that Japanese monetary policy would need to remain accommodative to ensure that the fledgling economic recovery in Japan becomes self-sustaining. The apparent market confidence that there will be no near-term Japanese monetary tightening appears not to have been significantly affected by the announcement on June 18 of very strong real GDP growth in the first quarter.

Short-term interest rates in the major foreign industrial countries have on average been little changed since the May FOMC meeting. The short-term rate in the United Kingdom has declined 35 basis points, reflecting the Bank of England's 1/4 percentage point reduction in its minimum lending rate to 5-3/4 percent announced on June 6. Chancellor of the Exchequer Clarke cited easing cost pressures in the United Kingdom and below-trend growth in support of the move, although some market commentators believed the cut had more of a political motivation. The Bank of France also announced an interest rate reduction on June 6. The Bank's intervention rate--which serves as a lower bound to money market rates in France--was reduced 10 basis points to 3.6 percent. On June 19, the Swedish central bank lowered its official deposit and lending rates by 75 basis points to 5.25 percent and 6.75 percent respectively.

Long-term interest rates in almost all of the G-10 countries have moved higher over the past month, as incoming data have tended on balance to suggest strengthening economic activity in both the United States and many of the major foreign industrial countries. In Germany, the 10-year bellwether bond rate has risen 20 basis points since the May FOMC meeting, 5 basis points less than the rise in the comparable U.S. long-term rate over this period. In contrast, the Japanese long-term rate has recorded almost no net change over the past month.

Since the May FOMC meeting, the Mexican peso has depreciated over 2 percent against the dollar, seemingly influenced mainly by concerns over the impact of higher current and prospective U.S. interest rates, rather than any adverse new information on the Mexican economy. On June 18, the Mexican Finance Ministry announced that it planned to raise a $3 billion five-year loan from a syndicate of commercial banks, and would use the proceeds of this loan, along with an additional $1.7 billion recently raised in international capital markets, to repay $4.7 billion of Mexico's outstanding debt to the U.S. Treasury.

The Desk did not intervene in the foreign exchange market over the intermeeting period.

Developments in Foreign Industrial Countries

Economic activity in the major foreign industrial countries in the first quarter ranged from surprisingly robust to fairly weak. The Japanese economy expanded at a remarkable pace; combined with recent indicators of activity, this suggests that recovery has taken hold. In contrast, the German economy contracted further in the first quarter, but more recent indicators suggest that a rebound might be underway. First-quarter growth in Italy and France was boosted by special factors, while recent data indicate that economic activity is weak. The United Kingdom and Canada extended modest rates of expansion.

Inflationary pressures remain subdued. Recent consumer-price inflation has averaged about 1-1/2 percent in Germany and Canada, and under 3 percent in the United Kingdom and France. Italian inflation, while higher than in the other foreign G-7 countries, has slowed considerably since January. In Japan, prices have risen slightly, reflecting depreciation of the yen, after falling for more than a year.

Individual country notes. The preliminary estimate of first-quarter GDP in **Japan** showed the highest growth rate -- 12.7 percent (SAAR) -- of any quarter since 1973. In addition, fourth-quarter growth last year was revised up. All components of final domestic demand grew strongly in the first quarter, while inventories increased slightly and net exports declined. Four consecutive quarters of significant growth at increasing rates have raised the estimated level of GDP in the first quarter to 5.5 percent above its year-earlier level. The first-quarter figure was much higher than expected in light of other indicators of first-quarter activity even after accounting for a leap-year effect. This raises the likelihood of a downward revision when data on preliminary second-quarter GDP are released in mid-September.

JAPANESE REAL GDP
(Percent change from previous period, SAAR)[1]

	1994	1995	1995 Q2	1995 Q3	1995 Q4	1996 Q1
GDP	0.4	2.5	2.6	2.3	4.8	12.7
Total Domestic Demand	0.4	3.8	2.4	4.6	7.2	14.2
Consumption	1.1	2.6	2.9	4.7	2.5	10.2
Investment	-1.4	6.2	4.7	4.3	19.1	20.8
Government Consumption	0.6	2.8	-4.6	1.0	-1.5	13.9
Inventories (contribution)	0.2	0.1	-0.3	0.3	0.3	0.5
Exports	9.0	3.8	17.9	-6.3	5.1	0.2
Imports	11.3	16.5	18.1	12.6	28.4	11.8
Net Exports (contribution)	-0.0	-1.3	0.3	-2.1	-2.3	-1.4

1. Annual changes are Q4/Q4.

Nonetheless, available indicators for the second quarter, including industrial production, machinery orders, and housing starts, point to continued growth in underlying activity. The Bank of Japan's May survey (Tankan) registered a modest increase in the diffusion index of business sentiment at major manufacturers from its February level. The index for smaller manufacturers also increased modestly in the May survey. However, after declining in March, the unemployment rate returned to its postwar high in April.

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

	1995 Q4	1996 Q1	1996 Q2	1996 Mar	1996 Apr	1996 May	1996 Jun
Industrial Production	2.2	0.4	n.a.	-6.0	3.2	n.a.	n.a.
Housing Starts	11.5	1.6	n.a.	4.7	2.8	n.a.	n.a.
Machinery Orders	4.7	3.4	n.a.	-8.6	13.1	n.a.	n.a.
New Car Registrations	2.7	2.4	n.a.	-4.8	-10.1	11.8	n.a.
Unemployment Rate (%)	3.3	3.3	n.a.	3.1	3.4	n.a.	n.a.
Job Offers Ratio[1]	0.63	0.67	n.a.	0.67	0.67	n.a.	n.a.
Business Sentiment[2]	-14	-12	-3	...	...	...	...
CPI (Tokyo area)[3]	-0.8	-0.3	n.a.	-0.1	0.3	0.2	n.a.
Wholesale Prices[3]	-0.1	0.0	n.a.	0.4	1.3	1.3	n.a.

1. Level of indicator.
2. Percent of manufacturing firms having a favorable view of business conditions minus those with an unfavorable outlook (Tankan survey).
3. Percent change from previous year.

Wholesale and consumer prices have risen slightly in recent months. The increases stem from the effect of yen depreciation on import prices as prices of domestically produced goods have continued to decline.

The May merchandise trade surplus was $4.9 billion (SA) compared with $2.5 billion in April. The April current account surplus was only $3.4 billion (SA) compared with $5.7 billion in March.

German real GDP contracted 1-1/2 percent at an annual rate (adjusted for seasonal and calendar variation) during the first quarter. This followed a decline of more than 1/2 percent (annual rate, revised) in the fourth quarter of last year. In the first quarter, domestic demand rose somewhat, despite a precipitous drop in construction (which fell almost 28 percent at an annual rate) due in large part to the very cold weather, while other elements of domestic spending increased. Exports declined while imports remained unchanged. The composition of GDP growth in the first quarter contrasts with that in the fourth quarter, when a significant decline in domestic demand (due largely to a drawdown in inventories) was offset by a strong external sector.

GERMAN REAL GDP
(Percent change from previous period, SAAR)[1]

	1994	1995	1995			1996
			Q2	Q3	Q4	Q1
GDP	3.7	1.0	3.7	0.1	-0.6	-1.5
Total Domestic Demand	4.0	0.0	4.0	-0.5	-2.7	0.3
Consumption	0.3	3.0	3.6	-1.1	1.9	2.0
Investment	8.8	-2.0	1.9	-1.9	-5.1	-17.5
Government Consumption	1.4	3.4	4.4	0.8	3.2	4.9
Inventories (contribution)	1.6	-1.2	0.7	0.4	-3.2	2.4
Exports	8.8	5.5	9.3	2.3	12.6	-6.7
Imports	9.9	1.2	10.8	0.0	4.0	-0.2
Net Exports (contribution)	-0.3	1.1	-0.4	0.6	2.1	-1.7

1. Annual changes are Q4/Q4.

Growth appears to have bounced back in the second quarter, perhaps quite significantly, largely due to a pick-up in construction activity. Stronger construction output helped industrial production in April rise 1.7 percent to stand 1.3 percent above the first-quarter average. April orders, particularly from domestic firms, picked up strongly as well. The IFO business climate measure, which combines surveys of current and expected conditions, showed some improvement in April and May from a very low level in March. Price pressures remain modest, with producer prices down on a 12-month basis. Data released on June 26 show that the 12-month change in the CPI slowed to 1.2 percent in June.

The mediators in the public sector pay dispute reached an agreement that would increase wages of public sector workers about 1/2 to 3/4 percent in 1996 and 1997. As part of a package of fiscal measures announced in late April, the government had sought to hold public sector wages unchanged and reduce the payments for sick leave. The issue of sick pay was not addressed in the new wage agreement.

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

	1995	1996					
	Q4	Q1	Q2	Mar	Apr	May	Jun
Industrial Production	-1.5	-1.5	n.a.	0.9	1.7	n.a.	n.a.
Orders	-3.0	-0.5	n.a.	1.8	2.2	n.a.	n.a.
Unemployment Rate (%)	9.7	10.3	n.a.	10.4	10.3	10.3	n.a.
Western Germany	8.5	8.9	n.a.	9.0	8.9	9.0	n.a.
Eastern Germany	14.7	16.2	n.a.	16.4	15.8	15.5	n.a.
Capacity Utilization[1]	84.4	83.0	n.a.	...	...	...	...
Business Climate[1,2]	-10.3	-15.3	n.a.	-19.0	-15.0	-14.0	n.a.
Retail Sales[3]	-2.3	-2.0	n.a.	-3.0	2.0	n.a.	n.a.
Consumer Prices[1,3]	1.5	1.4	1.3	1.4	1.3	1.5	1.2

1. Western Germany.
2. Percent of firms (in manufacturing, construction, wholesale, and retail) citing an improvement in business conditions (current and expected over the next six months) less those citing a deterioration in conditions. May figure is estimate.
3. Percent change from previous year.

In **France**, first-quarter GDP grew 4.9 percent (SAAR) after having contracted 1.6 percent in the fourth quarter of 1995.

However, underlying economic activity is estimated to have been considerably weaker than this GDP figure would suggest. Over half of the rise in GDP last quarter can be attributed to a rebound from the strikes last November and December and to a leap-year effect. Total domestic demand turned around owing to a sharp rise in private consumption (due to higher energy consumption and a catch-up after the strikes), but investment remained soft and inventories continued to be a drag on growth. Surprisingly strong export growth underpinned a positive contribution from net exports.

FRENCH REAL GDP
(Percent change from previous period, SAAR) [1]

	1994	1995	1995			1996
			Q2	Q3	Q4	Q1
GDP	4.1	0.5	0.4	0.4	-1.6	4.9
Total Domestic Demand	4.8	0.5	0.6	3.2	-3.4	3.1
Consumption	1.6	1.1	6.1	0.0	-1.2	10.0
Investment	4.7	0.3	-9.6	4.9	0.4	0.4
Government Consumption	0.6	1.1	0.8	1.6	1.6	2.8
Inventories (contribution)	2.7	-0.6	-1.2	2.0	-3.4	-3.4
Exports	7.6	0.5	0.0	-3.9	-5.1	13.9
Imports	10.2	0.5	0.8	5.7	-11.2	7.4
Net Exports (contribution)	-0.7	0.0	-0.2	-2.8	1.9	1.7

1. Annual changes are Q4/Q4.

Monthly indicators for the second quarter suggest that underlying economic activity has remained weak. Industrial production in April fell, suggesting that the first-quarter rise reflected a strike rebound. Business surveys by INSEE throughout the second quarter point to weak output, above normal inventories, and a deterioration in business confidence. Real consumption of manufactured products fell in May for the fourth straight month putting the April-May average below the first-quarter average (which reflects the sharp rise in January associated with a strike-rebound effect). Consumer confidence in May fell to the low registered last December. Annual revisions to the unemployment data reveal a sharper rise in the unemployment rate since last year. A slight acceleration in consumer prices this year continues to reflect higher food and energy prices and the increase in the VAT last August.

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

	1995		1996				
	Q3	Q4	Q1	Feb	Mar	Apr	May
Industrial Production	0.0	-1.6	1.3	0.3	0.5	-1.3	n.a.
Capacity Utilization	84.2	83.6	83.3	...	...	...	...
Unemployment Rate (%)	11.6	11.9	12.2	12.2	12.3	12.3	n.a.
Consumption of Manufactured Products	-1.0	-2.0	4.9	-0.5	-1.3	-1.5	-0.1
Consumer Prices[1]	1.8	1.9	2.1	2.0	2.3	2.4	2.4

1. Percent change from previous year. Includes the increase in the VAT on August 1, 1995

In the **United Kingdom**, real GDP rose 1.6 percent (SAAR) in the first quarter, slightly below the pace seen during the previous several quarters. Stronger total domestic demand underpinned first-quarter growth. While investment slowed somewhat from its sharp rise in the fourth quarter of 1995, robust consumption growth boosted total domestic demand.

UNITED KINGDOM REAL GDP
(Percent change from previous period, SAAR)[1]

	1994	1995	1995			1996
			Q2	Q3	Q4	Q1
GDP	4.1	1.9	2.0	2.0	2.0	1.6
Total Domestic Demand	3.0	1.0	4.6	2.1	0.7	2.5
Consumption	2.2	2.2	2.7	2.1	2.2	3.1
Investment	2.0	-0.6	-3.3	-3.2	4.2	2.8
Government Consumption	1.5	0.9	2.7	0.2	0.8	1.4
Inventories (contribution)	1.0	-0.5	2.9	1.3	-1.5	-0.2
Exports	10.2	2.6	-1.6	9.6	-3.3	n.a.
Imports	6.1	-0.2	8.3	10.2	-7.5	n.a.
Net Exports (contribution)	0.9	0.8	-2.7	-0.2	1.3	n.a.
Non-oil GDP	3.9	1.8	2.3	1.6	2.0	1.6

1. Annual changes are Q4/Q4.

Available second-quarter data for the consumer and manufacturing sectors are mixed. According to the Halifax house-price index, house prices rose in May for the tenth consecutive month helped by falling mortgage interest rates. Consumer credit rose sharply in April. However, retail sales declined in May due to unseasonably cold weather. April industrial output fell from its upwardly revised March level, and the May purchasing managers' index showed a further decline in both output and orders.

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

	1995		1996				
	Q3	Q4	Q1	Feb	Mar	Apr	May
Industrial Production	0.8	-0.1	0.2	0.5	0.7	-0.8	n.a.
Retail Sales	0.1	0.7	0.4	0.8	0.2	0.1	-0.1
Unemployment Rate (%)	8.2	8.0	7.9	7.9	7.8	7.8	7.7
Consumer Prices[1]	2.9	2.9	2.9	2.9	2.9	2.9	2.8
Producer Input Prices[2]	8.4	5.8	3.1	2.8	2.7	2.4	1.0
Average Earnings[2]	3.3	3.3	3.7	3.8	3.8	3.8	n.a.

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

Targeted inflation, measured as the change from a year earlier in retail prices excluding mortgage interest payments, has been little changed (at about 2.9 percent) for the past year. Headline inflation fell to 2.2 percent in May from the first-quarter average of 2.8 percent due to declining housing costs. A large fall in oil prices lowered May producer input prices noticeably.

In **Italy**, the advance GDP release stated that real economic activity rose 0.8 percent (SAAR) in the first quarter, owing in part to a leap-year effect. [No further details will be available until final first-quarter GDP is released on July 5.] GDP had declined 3.6 percent (SAAR) in the fourth quarter largely due to a sharp drop in exports and reduced government expenditure. The slowdown in real economic activity that began in the fourth quarter of last year appears to have continued into the second quarter. Industrial production in April fell sharply. At the same time, while picking up from the fourth-quarter low, business sentiment remained significantly below levels registered in mid-1995.

On balance, news on Italian inflation continues to be encouraging. The 12-month CPI inflation rate, which had declined in three successive months before plateauing in April, slowed further through June (preliminary) reflecting the slowing of the economy as well as lira appreciation. Although the wholesale price index ticked up slightly in April, 12-month rates of increase in wholesale prices and wages continued to recede.

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

	1995	1996					
	Q4	Q1	Q2	Mar	Apr	May	Jun
Industrial Production	-0.9	-2.0	n.a.	0.6	-3.0	n.a.	n.a.
Cap. Utilization (%)	78.5	75.9	n.a.	...	...	...	...
Unemployment Rate (%)	11.9	12.0	n.a.	...	...	...	...
Consumer Confidence[1]	110.0	107.7	113.8	106.1	108.8	114.8	117.9
Bus. Sentiment[2] (%)	11.3	15.7	n.a.	10.0	16.0	n.a.	n.a.
Consumer Prices[3]	5.9	5.0	4.2	4.5	4.5	4.3	3.9
Wholesale Prices[3]	10.5	7.7	n.a.	5.6	6.0	n.a.	n.a.

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

After being sworn in on May 18, the Prodi government gained full powers on May 31 upon winning the second of two confidence votes in parliament. Prodi's cabinet includes former technocrats as well as nine members of the PDS, the largest party in the center-left bloc. Former prime minister and previous Bank of Italy governor Ciampi is in charge of a portfolio that combines the treasury and budget ministries. Prodi's predecessor Dini has joined the new cabinet as foreign minister.

On June 19, the government approved a $10.5 billion supplementary budget for 1996. The supplementary budget, which is designed to enable the government to maintain its deficit target for this year, aims to raise about $3 billion from increased revenues and $7.5 billion from planned spending cuts.

Economic activity in **Canada** expanded 1.2 percent (SAAR) in the first quarter of 1996, following growth of 0.9 percent in the fourth quarter of last year. Total domestic demand expanded at a robust pace, but was partially offset by a decrease in the contribution from net exports. Both exports and imports were affected by the General Motors strike in March, while a decline in exports of crude materials contributed further to the drop in total exports.

CANADIAN REAL GDP
(Percent change from previous period, SAAR)[1]

	1994	1995	1995			1996
			Q2	Q3	Q4	Q1
GDP	4.9	0.7	-1.0	1.2	0.9	1.2
Total Domestic Demand	2.5	-0.1	0.9	-1.5	-0.5	5.5
Consumption	3.1	0.9	1.9	2.5	0.0	3.7
Investment	4.9	-1.8	-1.1	-5.2	6.6	11.1
Government Consumption	-1.5	-1.4	-0.5	-4.7	-1.1	-1.3
Inventories (contribution)	-0.1	0.1	0.2	-1.0	-1.6	1.2
Exports	20.9	5.0	-11.1	10.7	12.3	-6.1
Imports	14.0	4.0	-4.8	4.5	9.5	3.1
Net Exports (contribution)	2.2	0.4	-2.8	2.4	1.1	-4.0

1. Annual changes are Q4/Q4.

Data for the second quarter are limited. Retail sales in April were flat for the third consecutive month. Although employment declined slightly in May, the April-May average remained 0.3 percent above the first-quarter average. The unemployment rate has been slow to improve, however, as job growth has led to increased labor-force participation. Housing starts rebounded in May, bringing the April-May average to 5.5 percent above the first-quarter average.

Consumer-price inflation remains subdued, despite recent increases in gasoline prices that have contributed to higher monthly consumer-price inflation since March. In May, the 12-month change in consumer prices was 1.5 percent, still in the lower half of the Bank of Canada's target band of 1 to 3 percent.

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

	1995		1996				
	Q3	Q4	Q1	Feb	Mar	Apr	May
Industrial Production	0.3	-0.4	0.6	-0.4	-0.4	n.a.	n.a.
Manufacturing Survey:							
Shipments	1.1	-0.2	-0.8	-1.4	-1.2	n.a.	n.a.
New Orders	1.2	-0.2	-0.2	-1.6	-3.1	n.a.	n.a.
Retail Sales	1.0	-0.7	1.0	0.1	0.0	0.0	n.a.
Housing Starts	-2.4	5.8	2.1	8.6	13.3	-16.4	26.9
Employment	0.1	0.3	0.7	0.3	-0.1	0.3	-0.1
Unemployment Rate (%)	9.5	9.4	9.5	9.6	9.3	9.4	9.4
Consumer Prices[1]	2.4	2.1	1.4	1.3	1.4	1.4	1.5

1. Percent change from year earlier.

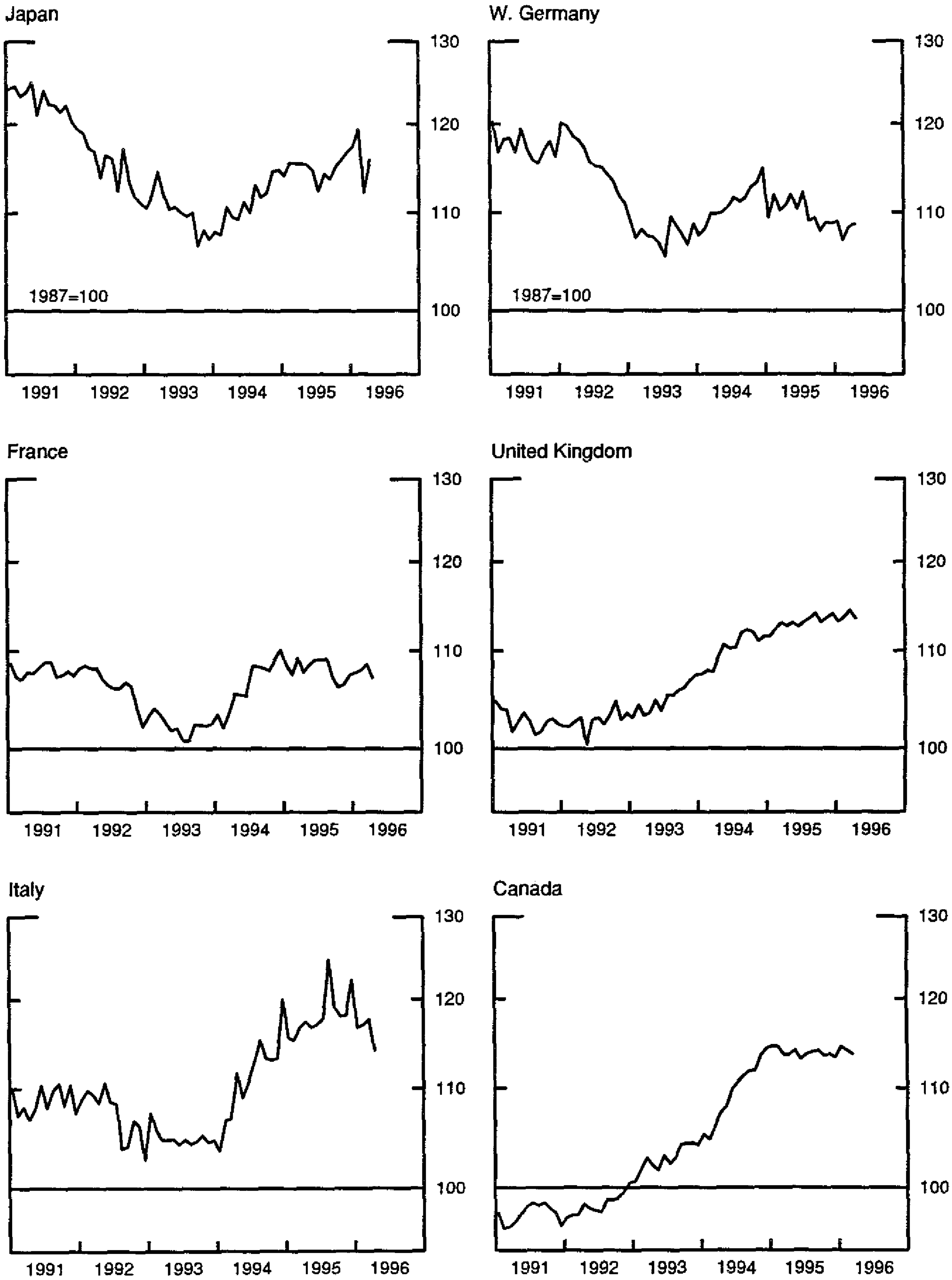
EXTERNAL BALANCES
(Billions of U.S. dollars, seasonally adjusted)

	1995	1995		1996				
		Q3	Q4	Q1	Feb	Mar	Apr	May
Japan: trade	106.6	25.5	22.5	16.6	4.6	7.0	2.5	4.9
current account	110.6	28.5	23.5	15.5	4.1	5.7	3.4	n.a.
Germany: trade[1]	63.6	14.9	17.8	13.8	6.0	4.2	n.a.	n.a.
current account[1]	-17.4	-8.7	-5.3	-3.1	0.5	-0.9	n.a.	n.a.
France: trade	20.6	4.2	5.6	6.1	2.1	2.4	n.a.	n.a.
current account	16.7	0.6	3.0	7.1	2.2	2.0	n.a.	n.a.
U.K.: trade	-18.3	-5.5	-5.0	-5.4.	-2.0	-1.2	n.a.	n.a.
current account	-10.6	-3.3	-3.6	n.a.	...	...	...	...
Italy: trade	27.6	7.6	6.9	n.a.	n.a.	n.a.	n.a.	n.a.
current account[1]	27.4	9.0	7.4	n.a.	3.3	n.a.	n.a.	n.a.
Canada: trade	20.7	5.5	6.2	5.4	1.4	1.9	1.9	n.a.
current account	-8.1	-1.7	-0.2	-1.4	...	...	...	...

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

Industrial Production in Selected Industrial Countries

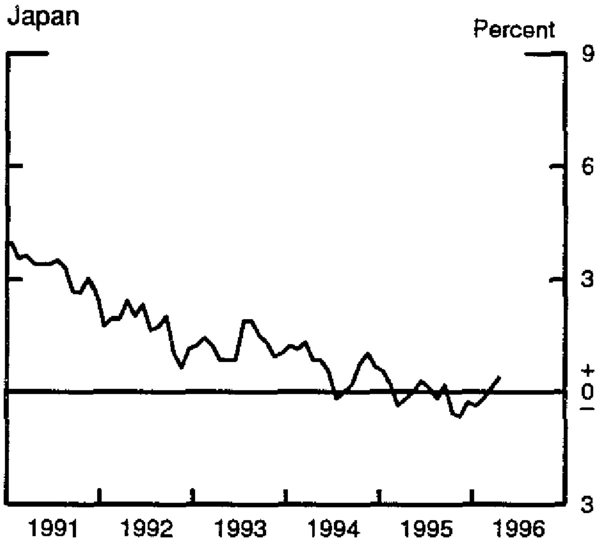
(Monthly data; seasonally adjusted; ratio scale, index)



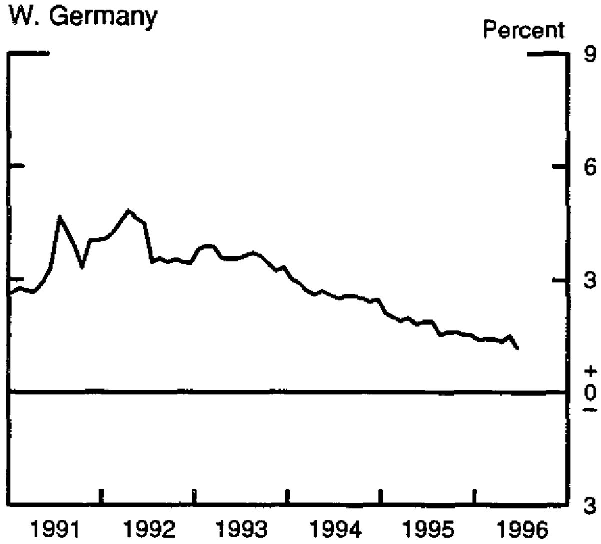
Consumer Price Inflation in Selected Industrial Countries

(12-month change)

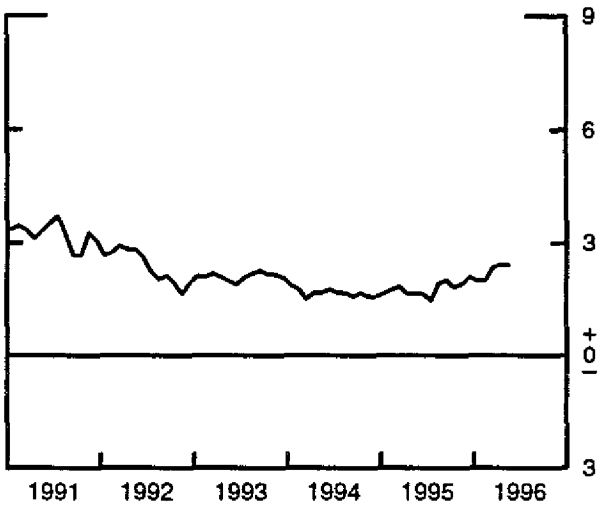
Japan



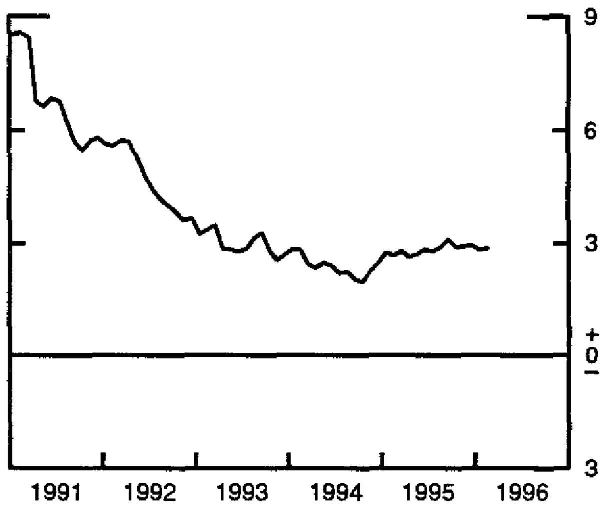
W. Germany



France

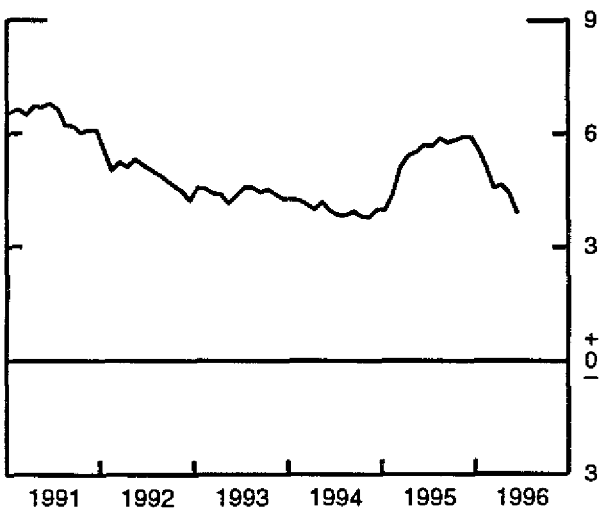


United Kingdom

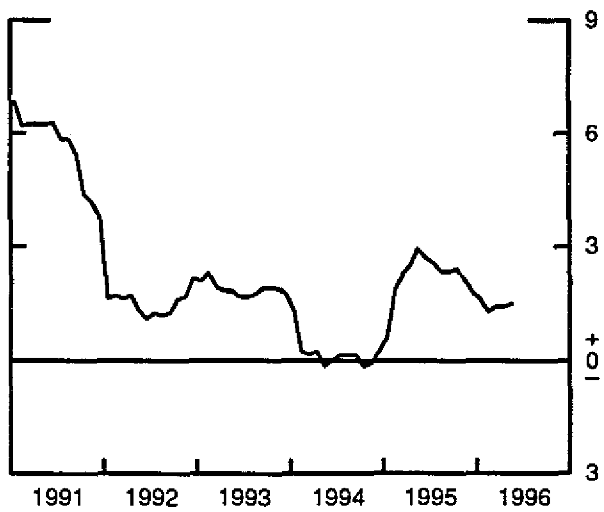


Note: Excludes mortgage interest payments.

Italy



Canada



Economic Situation in Other Countries

In recent months, real GDP in Mexico and Argentina has rebounded from lows experienced during 1995, but measures of economic activity in Brazil are mixed. Economic growth in major Asian developing economies appears to have moderated to more sustainable rates, while Russian real GDP has continued to contract. During May, monthly inflation declined in Mexico but increased sharply in Venezuela and slightly in Brazil. Twelve-month inflation in Argentina, as well as the major Asian economies, has been fairly stable and well below 10 percent. In recent months, Mexico has continued to register trade surpluses, and Argentina's trade surplus has widened. China experienced a small trade deficit during the first five months of 1996, while Taiwan's trade surplus in May was the largest in almost a decade.

Individual country notes. In **Mexico**, real GDP in the first quarter of 1996 was only 1 percent below its year-earlier level, compared with a year-over-year 5.8 percent decline in the fourth quarter of 1995 and a year-over-year 8.1 percent decline in the third quarter. The comparatively strong performance during the first quarter of 1996 partially reflects the fact that economic activity was already depressed during the first quarter of 1995. On a seasonally adjusted basis, GDP is estimated to have increased about 2 percent (not at an annual rate) in the first quarter after rising 3 percent in the fourth quarter of 1995. Rapid growth in the first quarter of this year, as in the fourth quarter of 1995, was largely due to a recovery of domestic demand. By contrast, net export growth, which moderated the decline in GDP during the first two quarters of 1995, has weakened somewhat in the most recent three quarters.

Movements in monthly indicators suggest continued recovery in the second quarter. The urban unemployment rate (n.s.a.) declined from an average of 6.2 percent in the first quarter to 5.4 percent in May. Imports grew substantially in April and May, also pointing toward a recovery of demand. Because export growth also has been substantial, however, Mexico has continued to register trade surpluses.

Consumer price inflation ticked up to 2.8 percent in April, as a result of scheduled increases in the minimum wage and public sector prices, but declined to 1.8 percent in May. Inflation during the first half of June was just below 0.9 percent, suggesting that inflationary pressures remain subdued.

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

	1994	1995	1995 Q4	1996 Q1	1996 Apr	1996 May
Real GDP	4.5	-6.2	-5.8	-1.0	...	...
Industrial Production (SA)	3.9	-7.5	-6.9	2.2	n.a.	n.a.
Unemployment Rate (%)	3.2	6.3	6.0	6.2	5.9	5.4
Consumer Prices[1]	7.1	52.1	8.0	8.3	2.8	1.8
Trade Balance[2]	-18.5	7.4	1.7	1.8	0.8	0.5
Imports[2]	79.4	72.5	19.4	19.9	7.1	7.5
Exports[2]	60.8	79.9	21.0	21.8	7.9	8.0
Current Account[2]	-29.5	-0.7	-0.5	-0.5	...	...

1. Percentage change from previous period.
2. Billions of U.S. dollars, NSA

In **Brazil**, real GDP fell in the first quarter of 1996 from its level a year earlier (partially reflecting strong performance during the first quarter of 1995), but was above its level in the other three quarters of 1995. Industrial production in April was higher than in March but was down 2.5 percent from a year earlier. Inflation picked up recently due to seasonal factors, but remains low by Brazilian standards. In mid-June, the Central Bank adjusted the limits of the exchange rate band from 0.999-1.004 *reais* per dollar to 1.002-1.007 *reais* per dollar. International reserves at end-May 1996 totalled $59 billion (liquidity concept), up considerably from $34 billion a year ago, and the trade surplus increased slightly in May.

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

	1994	1995	1995 Q4	1996 Q1	1996 Apr	1996 May
Real GDP	5.7	4.1	0.2	-2.1	...	...
Industrial Production (SA)[1]	7.8	2.0	1.7	-2.4	2.6	n.a.
Open Unemployment Rate (%)	3.4	4.4	4.4	6.4	6.0	n.a.
Consumer Prices[1]	929.0	22.0	4.7	2.5	0.9	1.3
Trade Balance[2]	10.4	-3.6	0.3	-0.1	0.2	0.3
Current Account[2]	-1.5	-17.8	-4.0	-3.4	...	...

1. Percentage change from previous period.
2. Billions of U.S. dollars, NSA

In a move designed to stimulate growth and boost exports, the Brazilian government announced two measures on June 20. The first is a $500 million package of credit for small companies that will be administered by the National Development Bank. The second is a $1 billion credit line to exporters over the next 12 months.

Brazil's lower house of Congress voted on a series of amendments to the government's pension reform bill. The government, however, failed to defeat an opposition amendment that maintains special conditions for pension funds of state-owned firms.

Brazil's privatization program is progressing, despite the announced resignation of privatization director Elena Landau. A Brazilian senate panel has approved a bill that would allow the government to privatize state mining giant Vale do Rio Doce without upper house approval. The bill must now be approved by the full senate.

In **Argentina**, real GDP contracted by 3.2 percent in the first quarter of 1996 from a year earlier. However, compared with the fourth quarter of 1995, real GDP grew by about 3 percent (AR), suggesting that a recovery is now taking hold. Inflation remained subdued, with consumer prices declining by 0.3 percent in May compared with a year earlier. International reserves less gold totaled $14 billion at end-May, compared with $14.3 billion at the end of both 1994 and 1995. The trade surplus in April continued to expand.

A $754 million budget deficit in May has renewed fears that Argentina may not satisfy the fiscal targets in its IMF program, which calls for a 1996 fiscal deficit (excluding privatization revenue) of $2.5 billion. Many analysts believe that the 1996 deficit could be as high as $5 billion, forcing Argentina to renegotiate its IMF program. In an effort to reduce expenditures, President Menem signed a decree on June 25 to streamline the government by cutting the number of departments by a third.

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

	1994	1995	1995 Q4	1996 Q1	1996 Apr	1996 May
Real GDP	7.4	-4.4	-7.7	-3.2	...	...
Industrial Production (SA)	3.1	-11.5	-11.5	-8.5	5.3	1.5
Unemployment Rate (%)[2]	11.7	17.4	16.4	...	...	n.a.
Consumer Prices[1]	3.9	1.5	0.0	-0.5	0.0	-0.1
Trade Balance[3]	-4.0	3.0	0.2	0.2	0.4	n.a.
Current Account[3]	-9.9	-3.2	...	...	...	...

1. Percentage change from previous period.
2. Unemployment figures available only in May and October of each year. The annual figure is the average of the two surveys.
3. Billions of U.S. dollars, NSA

In **Venezuela**, monthly consumer price inflation surged during May, due to the liberalization of exchange controls and the depreciation of the bolivar. Following the announcement of the new macroeconomic stabilization program in April, Venezuela reached preliminary agreement with the IMF for a $1.4 billion equivalent 12-month stand-by arrangement. In recent weeks, Venezuela has approved two measures, which should help facilitate the IMF program. First, on June 19, the Venezuelan Congress approved an increase in the wholesale tax rate, a major step toward reducing the fiscal deficit. Second, the government recently allocated an extra $152 million to meet foreign debt payments, mostly to Paris Club creditors. (Venezuela, however, remains over $400 million in arrears on its foreign debt payments.) The IMF Executive Board is expected to consider the program for Venezuela on July 12.

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

	1994	1995	1995 Q4	1996 Q1	1996 Apr	1996 May
Real GDP	-2.8	2.2	...	...	...	...
Unemployment Rate (%)	8.8	10.8	10.2	...	...	...
Consumer Prices[1]	71.0	56.6	17.1	24.0	8.5	12.6
Trade Balance[2]	-3.6	-6.0	-1.5	-0.9	n.a.	n.a.
Current Account[2]	2.5	2.7	...	...	...	...

1. Percentage change from previous period.
2. Billions of U.S. dollars, NSA, non-oil trade balance.

Venezuelan interest rates have fallen sharply in the last month, due to excess liquidity. Average deposit rates have fallen about 20 percentage points to around 27 percent and average loan rates have fallen about 30 percentage points to around 43 percent.

In **China**, inflation has remained relatively steady in recent months. China ran small trade surpluses in April and May. Over the first five months of the year, however, China's trade deficit registered $0.5 billion, compared with a surplus of $10 billion in the year-earlier period. The value of exports in the first five months fell 7 percent from a year earlier, while the value of imports rose 15 percent. The decline in exports appears to reflect a cut in China's export tax rebate. Foreign exchange reserves reached $85 billion at the end of May, up $11 billion from the end of 1995.

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

	1994	1995	1995	1996	1996	
			Q4	Q1	Apr	May
Real GDP[1]	11.8	10.2	10.2	10.2	...	...
Industrial Production	22.0	15.8	15.9	16.4	15.8	n.a.
Consumer Prices	25.5	10.1	10.1	9.9	8.7	8.9
Trade Balance[2]	5.2	17.2	0.3	-1.2	0.5	0.2

1. Cumulative from the beginning of the year
2. Billions of U.S. dollars, NSA

In mid-June, China announced plans to make its currency convertible for current account transactions by the end of 1996. While the currency is already convertible for most trade-related purposes, the new measures will relax restrictions on transactions for services and the repatriation of profits.

In **Taiwan**, real GDP in the first quarter was up 5.3 percent from a year earlier. Industrial production, however, has been relatively flat in 1996. Taiwan's monthly trade surplus of $1.9 billion in May was its highest level in nine years, primarily reflecting an 18 percent fall in imports from their year-earlier level. Taiwan's trade surplus reached $5.3 billion during the first five months of 1996, compared with a $2.3 billion surplus a year earlier. The value of exports was up 5 percent, while the value of imports was down 2 percent.

In early June, Morgan Stanley announced that it would include Taiwanese stocks in its emerging market equity index. The move has contributed to a surge in Taiwan's stock exchange in recent months.

As of June 26, the stock market was up 23 percent for the year, and up nearly 40 percent from its low following Chinese missile tests in mid-March.

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

	1994	1995	1995 Q4	1996 Q1	1996 Apr	1996 May
Real GDP	6.5	6.1	4.9	5.3	...	...
Industrial Production	6.6	4.2	-1.1	0.1	0.3	n.a.
Consumer Prices	2.6	4.6	4.6	3.0	2.8	2.8
Trade Balance[1]	12.0	8.3	4.1	2.5	0.9	1.9
Current Account[1]	6.0	5.0	3.6	1.5	...	...

1. Billions of U.S. dollars, NSA

In **Korea**, economic growth appears to have slowed to a more sustainable rate since the second half of 1995. Despite a high level of capacity utilization, inflation has remained low by historical standards. Import growth has weakened considerably since the middle of last year, in part because of a dramatic deceleration in imports of capital goods. However, falling export prices and weak demand for Korea's exports from industrial countries led to a noticeable widening of Korea's current account deficit from its year-earlier level during the first four months of the year.

Korea recently announced several financial liberalization measures intended to strengthen its bid to become a member of the OECD. These measures include allowing foreign banks to operate wholly owned subsidiaries in Korea by the end of 1998 and further relaxing the limit on foreign ownership of Korean equity. It is unclear whether these moves will be sufficient to satisfy requirements for OECD membership.

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

	1994	1995	1995 Q4	1996 Q1	1996 Apr	1996 May
Real GDP	8.4	9.0	6.8	7.9	...	...
Industrial Production	10.7	11.7	7.1	8.7	8.3	n.a.
Consumer Prices	5.6	4.7	4.5	4.9	4.6	5.1
Trade Balance[1]	-3.1	-4.5	0.4	-2.2	-1.5	n.a.
Current Account[1]	-4.7	-8.8	-0.5	-4.1	-2.2	n.a.

1. Billions of U.S. dollars, NSA

In **Russia's** June 16 Presidential election, Boris Yeltsin finished in first place, capturing 35 percent of the vote. Communist Gennady Zyuganov was second with 32 percent. Since no candidate won a majority, Yeltsin and Zyuganov will compete in a July 3 run-off. In an effort to solidify his position, Yeltsin appointed third-place finisher Alexander Lebed as Secretary of the government's Security Council and National Security Advisor. Yeltsin's strength in the first-round election and his rapprochement with Lebed did much to calm anxiety about the political situation in Russia's financial markets.

Russian real GDP during the first five months of 1996 declined by 3 percent from its year-earlier level, and industrial production fell by 4 percent. Russian officials have linked the decline in economic activity during the first half to "under investment," due to political uncertainty in the run-up to the election. Monthly inflation during May remained at 2 percent. The ruble depreciated at a monthly rate of 1.5 percent during May and the first three weeks of June.

Russia has completed one quarterly review and two monthly reviews under its IMF Extended Fund Facility (EFF). A severe shortfall in fiscal revenues, however, threatens the viability of the program; revenues during the first quarter were only 89 percent of levels anticipated in the EFF. During April, net international reserves declined from $8.7 billion to $6.7 billion, but remained above the program's $4.8 billion floor.

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

	1994	1995	1995	1996	1996	
			Q4	Q1	Apr	May
Real GDP	-15	-4	-4	-3	-1	-7
Industrial Production	-21	-3	-5	-4	0	-6
Consumer Prices[1]	10	7	4	3	2	2
Ruble Depreciation[1]	9	2	1	2	2	2
Trade Balance[2]	14.3	18.1	3.9	5.6	...	...
Current Account[2]	3.2	5.3	1.2	2.6	...	...

1.Monthly Rate.
2.Billions of U.S. dollars.