FEDERAL RESERVE

press release

For immediate release December 9, 1968

The Board of Governors of the Federal Reserve System and the Federal Open Market Committee today released the attached record of policy actions taken by the Federal Open Market Committee at its meeting on September 10, 1968. Such records are made available approximately 90 days after the date of each meeting of the Committee and will be found in the Federal Reserve Bulletin and the Board's Annual Report.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on September 10, 1968

Authority to effect transactions in System Account.

Consumer expenditures had been expanding vigorously this summer, according to reports at this meeting. Staff projections suggested, however, that the rate of business inventory accumulation was declining markedly in the third quarter--largely because of a shift from accumulation to liquidation of steel stocks--and that growth in over-all activity was slowing as a consequence.

Steel production had been cut back sharply following the wage settlement in the steel industry at the end of July, and as a result the industrial production index was tentatively estimated to have declined in August. Although nonfarm payroll employment increased fairly sharply in August, manufacturing employment was unchanged for the second consecutive month. Total civilian employment declined in August, but the labor force declined somewhat more and the unemployment rate fell to 3.5 per cent from 3.7 per cent in July.

Growth in Federal outlays appeared to be slowing in the third quarter, but total final sales were now estimated to be rising at a rapid rate. Retail sales, which had increased sharply in July, remained at a high level in August according to available weekly figures. The sizable advance in consumer spending apparently was associated with a decline in the saving rate; the new income tax surcharge affected paychecks beginning in mid-July, and disposable income was estimated to be advancing less rapidly in the third quarter than earlier in the year. Housing starts also rose considerably in July, and it appeared that residential construction outlays would be somewhat higher in the third quarter than in the second. A new Commerce-SEC survey, taken in August, indicated that business outlays on plant and equipment would be somewhat lower in 1968 as a whole than estimated earlier, but that businesses planned to increase their outlays moderately from the second quarter to the third.

Staff projections for the fourth quarter suggested that the rate of inventory accumulation would be reduced somewhat further as liquidation of steel stocks continued and that the expansion in final sales would slow. It was expected that the increase in Federal expenditures would be quite small and that the rise in consumer spending would slacken as a result of continuing slow growth of disposable income. Little change was anticipated in residential construction expenditures, and the recent Commerce-SEC survey suggested that business outlays for plant and equipment would be maintained at about the third-quarter rate.

Average prices of industrial commodities, according to preliminary estimates, were unchanged in August after rising only slightly in July. It was expected, however, that the industrial average for September would be affected by advances already announced in prices of steel mill products. Prices of farm products and foods, which had increased considerably in July, declined in August, and the over-all wholesale price index moved down to its June level. The consumer price index rose substantially in July for the second month in a row; as in June, a large part of the advance reflected higher costs of consumer services, including mortgage interest charges.

In foreign exchange markets, rumors in late August that a revaluation of the German mark was imminent led to large-scale inflows of funds into Germany and to sharply increased pressures on the French franc and sterling. On September 4 the French Government unexpectedly removed the foreign exchange controls it had imposed on May 31. Following the announcement of this action and the simultaneous publication of preliminary estimates of the French budget for 1969, the position of the franc improved; but pressures subsequently resumed. The sterling exchange rate strengthened appreciably after the announcement on September 9 that final agreement had been reached by the Bank of England and 12 other central banks on new arrangements to offset fluctuations in overseas sterling balances. The price of gold in the private London market had risen by about $1 per ounce since mid-August and currently was fluctuating narrowly around $40.

U.S. exports increased slightly and imports fell sharply in July--resulting in a small surplus in the foreign trade balance after 2 months of deficit. Despite a foreign trade deficit in the May-July period as a whole, the payments balance on the liquidity basis, apart from special official transactions, had improved considerably. However, tentative estimates for August suggested that a large deficit had re-emerged. The balance on the official settlements basis apparently was in surplus in August, as liabilities of U.S. banks to their foreign branches rose to a new high after declining during the last 3 weeks of July.

In domestic financial markets, prior to the reductions in Federal Reserve Bank discount rates from 5-1/2 to 5-1/4 per cent--the first of which was announced on August 15--interest rates on various types of market securities had been rising from the lows they had reached early in the month. Market reactions to the discount rate cuts were varied; some observers interpreted the action as a confirmation of earlier expectations of some relaxation in monetary restraint, while others--who had expected more vigorous action--thought it indicated that a marked easing of policy was not likely in the near future.

On balance, interest rates on new corporate bonds and on Treasury securities changed little during the latter half of August. However, yields on municipal bonds remained under upward pressure in the face of continuing heavy flotations of new issues by State and local governments. In early September yields on new corporate bonds and on Treasury securities also advanced, as corporate underwriters released unsold new offerings from syndicate and some Government securities dealers acted to lighten their heavy inventories. The market rate on 3-month Treasury bills was 5.24 per cent on the day before this meeting, 13 basis points above its level following the mid-August announcement of discount rate action. Rates on longer-term Treasury bills had risen only slightly during the interval and currently were close to or below the rate on 3-month bills.

Growth in commercial bank time and savings deposits, which had stepped up sharply in July, accelerated further in August. Expansion in large-denomination CD's outstanding was substantial but less than the very large rise of July, when interest rates on competing market instruments had been declining. The average level of U.S. Government deposits increased considerably in August as a result of Treasury cash financings, and expansion in private demand deposits and the money supply slowed appreciably--the money supply to an annual rate of about 5 per cent from nearly 15 per cent in July.

In August, as in July, banks were heavy buyers in the large offerings of securities undertaken by Federal, State, and local governments. Growth in bank loans to businesses was maintained at about the recent average pace, and loans to brokers and dealers to finance holdings of securities increased moderately further. Total bank credit, as measured by the bank credit proxy--daily-average member bank deposits--expanded at the unusually high annual rate of 21 per cent, after rising at a 9 per cent rate in July. Allowance for changes in the daily average of U.S. bank liabilities to foreign branches would have served to increase the growth rate by about 1/2 of a percentage point in August and 1-1/2 percentage points in July.

System open market operations in the period since the Committee's August 19 meeting had been directed mainly at facilitating orderly adjustments in money market conditions to the reduction in Federal Reserve Bank discount rates. As the period progressed less emphasis was placed on the supplementary objective of moderating upward pressures on Treasury bill rates, in light of accumulating evidence that bank credit was growing at a higher rate than that projected at the time of the Committee's previous meeting. The effective rate on Federal funds, which had been mostly in a 6 to 6-1/4 per cent range prior to the discount rate cuts, subsequently fluctuated in a 5-3/4 to 6 per cent range and was at the upper end of that range at the close of the period. Net borrowed reserves and member bank borrowings averaged about $185 million and $480 million, respectively, in the 3 weeks ending September 4, down from averages of about $290 million and $640 million in the previous 3 weeks.

Growth in bank credit was expected to moderate from the high August rate in September and October. The Treasury was not expected to engage in another major cash financing until the latter part of October; and prospects favored some reduction from the current high level of outstanding loans to finance holdings of securities and also a slower growth in business loans, particularly after the mid-September tax date. New staff projections suggested that the bank credit proxy would expand at an annual rate of 7 to 10 per cent in September if prevailing conditions in money and short-term credit markets were maintained. Growth in about the same range was foreseen for October, on the assumption that the Treasury would raise about $3 billion of new cash in the latter part of the month. The projections suggested that expansion in time and savings deposits would moderate in September, and that on the average Government deposits would change little over September and October and the money supply would rise only slightly.

The Committee decided that no change in monetary policy was warranted at this time. On the one hand, a relaxation of monetary restraint was not deemed appropriate in light of the current strength of final demands and the persistence of inflationary pressures; on the other hand, greater restraint was not considered desirable in view of the outlook for slowing in over-all economic activity, although it was noted that firm evidence was lacking thus far on the amount of slowing in prospect. However, a number of members--while not advocating a firming of policy--expressed concern about the rapid rates of bank credit expansion in recent months, and some thought that expansion in September and October at a rate near the upper end of the projected range would be higher than desirable in the current economic environment.

At the same time, it was noted that Treasury bill rates might well come under temporary upward pressure as a result of credit demands associated with the September tax date and the large-scale sales of bills by the System that were expected to be required in the next week or so to absorb reserves supplied by market factors. A number of members expressed the view that such pressures should be moderated if they proved to be unduly marked or prolonged, in light of the risk that persistent large increases in bill rates might precipitate a change in market expectations that would result in a new general uptrend in market interest rates.

The Committee concluded that it would be desirable at present for open market operations to be directed at maintaining about the prevailing conditions in the money and short-term credit markets, on the understanding that increases in Treasury bill rates in the near term, if moderate, would not be considered inconsistent with this objective. The proviso was added that operations should be modified if bank credit appeared to be deviating significantly from current projections.

The following current economic policy directive was issued to the Federal Reserve Bank of New York:

> The information reviewed at this meeting suggests that, although consumer demands have been strong this summer, reduced rates of inventory accumulation and tapering growth of Government expenditures are being reflected in a slowing of expansion in over-all activity. Industrial prices have been increasing less rapidly in recent months, but consumer prices have continued to rise substantially and wage pressures remain strong. Most market interest rates have changed little on balance following reductions in Federal Reserve Bank discount rates. Growth in bank credit and time and savings deposits has been rapid this summer; growth in the money supply slowed in August as U.S. Government deposits were built up following an extended decline. The earlier improvement in the U.S. balance of payments was not maintained in August, according to preliminary indications, and the foreign trade balance and underlying payments position continue to be matters of serious concern. In this situation, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to sustainable economic growth, continued resistance to inflationary pressures, and attainment of reasonable equilibrium in the country's balance of payments.
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> System open market operations until the next meeting of the Committee shall be conducted with a view to maintaining about the prevailing conditions in money and short-term credit markets; provided, however, that operations shall be modified if bank credit appears to be deviating significantly from current projections.

Votes for this action: Messrs. Martin, Hayes, Brimmer, Daane, Galusha, Hickman, Kimbrel, Maisel, Mitchell, Morris, Robertson, and Sherrill. Votes against this action: None.