FEDERAL RESERVE

press release

For immediate release February 19, 1974

The Board of Governors of the Federal Reserve System and the Federal Open Market Committee today released the attached records of policy actions taken by the Federal Open Market Committee at its meetings on November 19-20 and December 17-18, 1973. As in the past, the record for the December meeting of the Committee has been released along with the record for the November meeting rather than in accordance with the usual schedule of approximately 90 days after the meeting in order to complete the published record for the year in advance of the Chairman's testimony at the Congressional hearings on the Economic Report of the President and the Annual Report of the Council of Economic Advisers.

These records will be published in the Board's Annual Report for 1973 and in the Federal Reserve Bulletin. The summary descriptions of economic and financial conditions they contain are based on the information that was available to the Committee at the time of the meetings, rather than on data as they may have been revised since then.

Attachments

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on November 19-20, 1973[1/]

Domestic policy directive

The information reviewed at this meeting suggested that growth in real output of goods and services--which had risen to an annual rate of about 3.5 per cent in the third quarter from about 2.5 per cent in the second quarter--would remain moderate in the current quarter. Staff projections continued to suggest that, in the absence of an oil crisis, growth of real output would slacken in the first half of 1974 and that the rise in prices would remain rapid. It was also suggested that continuation of the embargo on the flow of Arab oil to the United States--announced in the latter part of October--could have significantly adverse effects on the U.S. economy.

In October industrial production continued to grow at a substantial pace, reflecting advances in output of business equipment and consumer goods; output of materials, which was pressing against the limits of capacity in some industries, changed little. Employment expanded in manufacturing, after a 3-month period of little change, and total nonfarm payroll employment increased appreciably. The unemployment rate

1/ This meeting was held over a 2-day period beginning on the afternoon of November 19, 1973, in order to provide more time for the staff presentation concerning the economic situation and outlook and the Committee's discussion thereof.

dropped from 4.8 to 4.5 per cent, the lowest rate in 3-1/2 years. And advance reports indicated that retail sales rose substantially during the month, although sales of new automobiles declined significantly.

The index of average hourly earnings of production workers on nonfarm payrolls continued to advance at a relatively fast pace in October. During the third quarter compensation per manhour in the private nonfarm sector of the economy increased substantially more than output per manhour, and unit labor costs rose sharply further.

The uptrend in wholesale prices of industrial commodities accelerated in October, reflecting a large rise in prices of petroleum products and other fuels and widespread increases among other commodities. Wholesale prices of farm and food products fell substantially for the second consecutive month, as a result of marked decreases for livestock, meats, poultry, and soybeans; however, the index remained well above the pre-freeze level of early June. In September the rate of advance of the consumer price index slowed as retail prices of foods declined slightly after having risen sharply in August.

Staff projections for the first half of 1974 suggested that business fixed investment would rise considerably further, that State and local government purchases of goods and services would continue to grow at a substantial rate, and that consumption expenditures would expand at about the moderate pace of the second half of 1973. However, it was also anticipated that the decline in residential construction outlays would persist and that business inventory investment would level off.

U.S. merchandise exports rose sharply further in September--reflecting for the most part considerable increases in exports of capital equipment and industrial materials--while imports declined. As a result, the trade balance moved into substantial surplus. For the third quarter as a whole, the trade surplus was sizable for the first time in 3 years. The over-all balance of payments on an official settlements basis also was in substantial surplus in the third quarter, and it remained so in October.

Following the announcement in late October of the large U.S. trade surplus, demand for dollars rose considerably, and exchange rates for the dollar appreciated against major foreign currencies. The dollar registered a further sizable appreciation after the development of the oil crisis, which was interpreted in the markets as creating particularly severe problems for the economies of Western Europe and Japan.

Outstanding business loans of U.S. commercial banks, which had increased little in September, were unchanged in October. Business borrowers continued to shift to the commercial paper market as market interest rates declined further relative to effective rates on bank loans--even though most banks lowered the prime rate applicable to large corporations from 10 to 9-3/4 per cent during the month and a few reduced the rate to 9-1/2 per cent. Expansion in most other types of loans slowed in October, and banks continued to liquidate substantial amounts of their holdings of Government securities. Bank holdings of other securities--primarily Federal agency issues--rose appreciably, but the increase in total bank credit remained moderate.

The narrowly defined money stock (M_1)2/ rose moderately in October, following 2 months of declines. Preliminary calculations based on new benchmark data indicated that the level of the money stock in recent months would be adjusted upward and that monetary growth over the year ending in October had been somewhat faster than the rate of 5.1 per cent suggested by the currently published data.3/ Inflows of time and savings deposits other than large-denomination CD's picked up sharply, and the more broadly defined money stock (M_2)4/ grew at a rapid pace. The outstanding volume of large-denomination CD's declined substantially further as banks continued to reduce the rates paid on such CD's, in response to the further weakening in business loan demand at

2/ Private demand deposits plus currency in circulation.

3/ The measure of the money stock has been revised annually to incorporate new seasonal adjustment factors and, among other things, benchmark adjustments for deposits at nonmember banks on the basis of data reported for 2 days a year, the last day of June and the last day of December; for member banks, deposits are averages of daily figures. The growth rate cited is calculated on the basis of the daily-average level in October 1973 relative to that in October 1972.

4/ M_1 plus commercial bank time and savings deposits other than large-denomination CD's.

banks, to the large inflows of consumer-type time deposits, and to the effect on the cost of such funds of the recent increase in marginal reserve requirements against large-denomination CD's. As a result, the bank credit proxy[5/] increased relatively little.

Net deposit inflows at nonbank thrift institutions improved somewhat further in October, and the measure of the money stock that includes such deposits (M_3)[6/] rose appreciably after having grown at a slow pace over the third quarter. Contract interest rates on conventional mortgages and yields in the secondary market for Federally insured mortgages declined.

On October 24 the Treasury announced that on October 30 and 31 it would auction up to $1.5 billion of 25-1/2 month notes, up to $2.0 billion of 6-year notes, and up to $300 million of 19-3/4 year, 7-1/2 per cent bonds to refund $3.6 billion of publicly held bonds maturing on November 15; on October 29 the Treasury set coupon rates of 7 per cent for both of the note issues. In the auctions the Treasury sold $1.5 billion of the 25-1/2 month note at an average price to yield 6.91 per cent, $2 billion of the 6-year note at an average price to yield 6.82 per cent, and $300 million of the bond at a price to yield 7.35 per cent to maturity. In addition, the Treasury raised $1.2 billion of new cash by auctioning bills on November 9 and 12; the funds were raised to meet cash needs generated by redemptions of special Treasury securities by some foreign monetary authorities,

5/ Daily-average member bank deposits adjusted to include funds from nondeposit sources.

6/ M_2 plus time and savings deposits at mutual savings banks and at savings and loan associations.

which in turn resulted from the surplus in the U.S. balance of payments, and also to increase Treasury cash balances because the authority to borrow directly from Federal Reserve Banks had expired on October 31.

Short-term market interest rates in general declined further in the first week after the Committee's meeting on October 16, in large part because of continued market expectations that the weakness of recent months in the behavior of the monetary aggregates would lead to more aggressive System efforts to supply reserves and, consequently, to an easing in money market conditions. Later, however, when the aggregates strengthened and money market conditions remained relatively stable, market expectations changed and interest rates turned up. After the Treasury's early November announcement of the sale of bills to raise new cash, short-term rates--especially those on Treasury bills--rose further to or above their levels of mid-October. Just before this meeting the market rate on 3-month Treasury bills was 7.50 per cent, up from a recent low of 7.02 per cent on October 24 and 7.19 per cent on the day before the October meeting.

In long-term markets interest rates advanced somewhat in the inter-meeting period in association with the rise in short-term rates and with the expansion of demands for funds in the capital markets. The volume of new public offerings of corporate bonds rose sharply in October, and a further increase was in prospect for November. The volume of new State and local government bonds also expanded substantially in October, but the volume appeared likely to fall off in November.

Soon after the October meeting, available data suggested that in the October-November period the monetary aggregates would grow at rates within acceptable ranges but that reserves available to support private nonbank deposits (RPD's) would grow at a rate below the range that the Committee had specified because an anticipated upturn in the outstanding volume of large-denomination CD's had not developed. Data becoming available later, however, suggested that the monetary aggregates would grow at rates in excess of acceptable ranges. System action to limit such monetary expansion was tempered by the Treasury refunding that was in process and by the unsettled conditions that developed in the Government securities market for a time after the early November announcement of Treasury sales of bills to raise new cash. The Federal funds rate, which had been about 10 per cent at the time of the October meeting, was at or above 10 per cent in the days preceding this meeting. In the 5 weeks ending November 14, member bank borrowings averaged about $1,446 million, down from an average of $1,690 million in the preceding 4 weeks.

The Committee agreed that the economic situation and prospects continued to call for moderate growth in monetary aggregates over the months ahead. A staff analysis suggested that in the near term the demand for money would expand in response to the sizable increase in nominal GNP estimated for the fourth quarter and to the uncertainties generated by the oil shortage. The analysis also suggested that growth of consumer-type time and savings deposits at banks would moderate from the high rates of recent months. While the outstanding volume of large-denomination CD's was expected to expand toward the end of the year in response to a renewal of growth in business loans at banks, it was anticipated that required reserves against such CD's would drop further in the November-December period. Consequently, negative growth in RPD's in that period--at an annual rate within a range of -1 to -3 per cent--was thought likely to be consistent with moderate growth in both the narrowly and the more broadly defined money stock over the months ahead. It was expected that such a change in RPD's would be associated with little change in money market conditions.

The Committee decided that operations should be directed at fostering growth in RPD's during the November-December period at an annual rate within a range of -1 to -3 per cent, while avoiding unduly sharp changes in money market conditions. The members also agreed that, in the conduct of operations, account should be taken of international and domestic financial market developments, of the forthcoming Treasury financing, and of deviations in monetary growth from an acceptable range. It was understood that the Chairman might call upon the Committee to consider the need for supplementary instructions before the next scheduled meeting if significant inconsistencies appeared to be developing among the Committee's various objectives and constraints.

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

> The information reviewed at this meeting suggests that growth in economic activity in the fourth quarter is likely to remain at about the moderate rate of the third quarter, but curtailment of oil supplies from abroad has generated considerable uncertainty about subsequent prospects. In October total nonfarm employment expanded substantially further, and the unemployment rate dropped from 4.8 to 4.5 per cent. The advance in wage rates has remained relatively rapid, and unit labor costs have been increasing at a fast pace. Wholesale prices of industrial commodities rose sharply in October, reflecting in part large increases for petroleum products; although farm and food prices declined considerably further, they remained well above the pre-freeze level of early June. In foreign exchange markets, the dollar appreciated against major foreign currencies following announcement in late October of a large surplus in the U.S. merchandise trade balance, and the dollar strengthened markedly further in early November as expectations grew that the developing oil crisis would create particularly severe problems for Western Europe and Japan. In the third quarter and in October, the balance of payments on an official settlements basis was in substantial surplus.
>
> The narrowly defined money stock, which had declined in August and September, rose moderately in October. The

more broadly defined money stock expanded sharply as a result of large net inflows at banks of consumer-type time deposits. Net deposit inflows at nonbank thrift institutions improved somewhat further. Bank credit expansion remained moderate in October, reflecting in part a lack of growth in business loans as borrowers shifted to the commercial paper market. The outstanding volume of large-denomination CD's, which had begun to decline in late September, fell substantially further. Short-term market interest rates, while fluctuating widely, rose on balance from mid-October to mid-November. Rates on most types of long-term market securities also advanced somewhat.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to abatement of inflationary pressures, a sustainable rate of advance in economic activity, and equilibrium in the country's balance of payments.

To implement this policy, while taking account of international and domestic financial market developments, the Committee seeks to achieve bank reserve and money market conditions consistent with moderate growth in monetary aggregates over the months ahead.

Votes for this action: Messrs. Burns, Hayes, Balles, Brimmer, Bucher, Daane, Francis, Holland, Mayo, Mitchell, and Sheehan. Vote against this action: Mr. Morris.

Mr. Morris dissented from this action because he felt that in view of the marked deterioration in the economic outlook that had occurred over the past few weeks, stemming from the energy crisis, a modest move in the direction of a more stimulative monetary policy was appropriate.

Subsequent to the meeting it appeared that in the November-December period growth in the monetary aggregates might exceed acceptable ranges. In view of that behavior, the System, under ordinary circumstances, would have become somewhat more restrictive in its reserve-supplying operations, expecting that money market conditions would tighten somewhat. On November 30, however, the available members concurred in a recommendation by the Chairman that, in light of current uncertainties regarding the economic outlook and the sensitive state of financial market psychology, the System aim to maintain current money market conditions for the time being.