FEDERAL RESERVE press release

For Use at 4:10 p.m. May 23, 1980

The Federal Reserve Board 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 April 22, 1980. This record also includes policy actions taken during the period between the meeting on April 22, and the next regularly scheduled meeting held on May 20.

Such records for each meeting of the Committee are made available a few days after the next regularly scheduled meeting and are published in the Federal Reserve Bulletin and the Board's Annual Report. The summary descriptions of economic and financial conditions they contain are based solely on the information that was available to the Committee at the time of the meeting.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on April 22, 1980

Domestic policy directive

The information reviewed at this meeting suggested that economic activity turned down in the latter part of the first quarter of 1980. For the quarter as a whole, however, real gross national product grew at an annual rate of about 1 percent, according to preliminary estimates of the Commerce Department, compared with a rate of 2 percent in the fourth quarter of 1979.

Retail sales on a constant-dollar basis fell sharply in February and March, after having increased in January, and were estimated to have declined over the first quarter as a whole. Unit sales of new automobiles slowed in both February and March from a brisk pace in January and apparently remained weak in early April.

Private housing starts fell considerably in January and February and dropped sharply further in March to an annual rate of just over one million units, about 40 percent less than in the second and third quarters of 1979 and the lowest rate since April 1975. Building permits for new units also declined substantially further in March. In February sales of single-family homes fell for the fifth consecutive month.

The index of industrial production fell 0.8 percent in March, after changing little on balance in other recent months. The March decline reflected widespread cutbacks in output of final products and materials. The rate of capacity utilization in manufacturing fell nearly 1 percentage point in March to 83 percent, about 4 percentage points below its recent high in March 1979.

Nonfarm payroll employment declined appreciably in March following a substantial rise earlier in the year, and the rate of unemployment rose 0.2 percentage point to 6.2 percent. Employment in manufacturing fell somewhat in March after changing little in January and February, and the length of the average workweek was reduced for the second consecutive month.

The rise in average prices, as measured by the fixed-weight price index for gross domestic business product, accelerated to an annual rate of about 12 percent in the first quarter from a rate of about 10 percent during 1979. Producer prices of finished goods and consumer prices rose at annual rates of about 19 percent and 18 percent respectively during the first quarter. The advances reflected a continuing surge in prices of energy-related items and substantial increases in prices of numerous other items. The index of average hourly earnings of private nonfarm production workers rose at an annual rate of 9-1/2 percent during the first quarter, compared with a rise of about 8-1/2 percent during 1979.

In foreign exchange markets the strong demand for dollars that emerged in mid-February persisted through early April, but some selling pressure developed in the second week of April, in large measure because accumulating signs of a recession in the United States led many market participants to conclude that U.S. interest rates had peaked. Despite the recent weakening of the dollar, its trade-weighted value against major foreign currencies was currently about 5 percent above its level of early February.

The U.S. foreign trade deficit rose further in February following a sharp increase in January. The marked increase over the first two months of 1980 reflected a surge in imports, associated in large part with rising prices, that was only partly offset by a moderate expansion in exports.

At its meeting on March 18, the Committee had agreed that open market operations in the period until this meeting should be directed toward expansion of reserve aggregates consistent with growth over the first half of 1980 at annual rates of 4-1/2 percent for M-1A and 5 percent for M-1B, or somewhat less, provided that in the intermeeting period the weekly average federal funds rate remained within a range of 13 to 20 percent. In the Committee's view, this short-run policy should be consistent with growth in M-2 at an annual rate of about 7-3/4 percent over the first half of the year.

During the first part of the intermeeting period, demands for bank reserves continued strong in relation to the supply being made available through open market operations, and the federal funds rate rose from an average of 16-1/4 percent in the statement week ending March 19 to about 19-3/8 percent in the week ending

April 2. Subsequently, the demand for bank reserves eased, and the funds rate dropped to an average of about 18-3/8 percent in the week ending April 16. Member bank borrowings averaged around $2-1/4 billion in the three statement weeks ending April 16, down from an average of about $3-1/4 billion in the preceding two weeks.

The monetary aggregates weakened substantially in March after growing at accelerated rates in February. M-1A and M-1B, which had expanded at annual rates of around 12 percent in February, declined at annual rates of 3-1/2 and 2 percent respectively in March, and available data suggested further contraction in early April. Growth in M-2 slowed from an annual rate of 10-3/4 percent in February to 3-1/2 percent in March, reflecting mainly the contraction in the narrow measures of the money stock. Growth in money market mutual funds slowed markedly on a monthly average basis, but the impact on M-2 was offset by greater strength in small-denomination time deposits, principally reflecting rapid growth in money market certificates. From December to March, M-1A and M-1B grew at annual rates of about 4 percent and 4-1/2 percent respectively, and M-2 expanded at a rate of 7 percent.

Expansion of total credit outstanding at U.S. commercial banks slowed substantially in March after accelerating earlier in the year. The slowdown was especially pronounced for business loans, but growth in real estate loans also moderated appreciably. Overall expansion in short-term business credit remained relatively strong as nonfinancial corporations continued to issue large amounts of commercial paper.

Most market interest rates declined considerably on balance during the intermeeting period. Following the Committee's meeting on March 18, interest rates extended earlier advances and reached new highs in late March or early April. Subsequently, most interest rates turned down, with the federal funds rate falling moderately and other rates declining sharply as market participants reacted to accumulating signs of a slowdown in economic activity and to weakening in the monetary aggregates. During the period commercial banks initially raised their loan rate to prime business borrowers from 18-1/2 percent to 20 percent and then lowered it to 19-1/2 percent. In primary markets for home mortgages, average rates on new commitments leveled out at around 16-1/2 percent.

Staff projections prepared for this meeting suggested that real GNP would decline in the current quarter and continue to move lower for a number of quarters. The contraction in activity was projected to be somewhat larger than had been anticipated a month earlier and to be accompanied by a substantial increase in unemployment. The rise in average prices was projected to remain rapid, although some moderation was expected after the current quarter.

In the Committee's discussion of the economic situation, the judgment was broadly shared that a decline in overall activity had probably begun, especially in light of new evidence that had accumulated since the Committee's meeting in March. It was emphasized, however, that uncertainties concerning the outlook persisted and that, in any case, forecasting the severity and duration of a recession was always difficult.

The degree of prospective weakness in consumer spending was viewed as a major source of uncertainty. The anti-inflationary measures announced on March 14 appeared to have curbed considerably spending in anticipation of price increases. It was noted in this connection that a rise in the saving rate from the abnormally low levels of the most recent two quarters to a more normal rate would imply a marked cutback in consumer spending. Such a development would also tend to depress business investment in inventories and plant and equipment. However, it would be premature to conclude that inflationary attitudes and behavior had been fundamentally altered, especially in view of the prospect that the rapid rise in the consumer price index would persist for a number of months.

At its meeting on February 4-5, 1980, the Committee had agreed that from the fourth quarter of 1979 to the fourth quarter of 1980 average rates of growth in the monetary aggregates within the following ranges appeared to be consistent with broad economic aims: M-1A, 3-1/2 to 6 percent; M-1B, 4 to 6-1/2 percent; M-2, 6 to 9 percent; and M-3, 6-1/2 to 9-1/2 percent. The associated range for the rate of growth in commercial bank credit was 6 to 9 percent. It had also been agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be reconsidered in July or at any other time that conditions might warrant, and also that short-run factors might cause considerable variation in annual rates of growth from one month to the next and from one quarter to the next.

In contemplating policy for the period immediately ahead, the Committee took note of a staff analysis indicating that M-1A and M-1B were likely to decline further on the average in April and, consequently, that growth over the first four months of the year would fall considerably short of the objectives for the first half of the year established by the Committee at its meeting in March. Thus, realization of those objectives would require substantial expansion in M-1A and M-1B over May and June. A significant rebound in their growth was likely over the two-month period, given the staff projection of a fairly sizable expansion in nominal GNP in the current quarter and the associated increase in the transactions demand for money, but efforts to realize the first-half objectives for growth established in March could require System open market operations that would put further downward pressure on the federal funds rate. The staff analysis also suggested that growth of M-2 over the half year was likely to be lower in relation to growth of the narrower monetary aggregates than had been thought a month earlier, owing to a scaling down of expected expansion in money market mutual funds.

In the Committee's discussion of policy for the period immediately ahead, most members favored reaffirming the monetary growth objectives for the first half of 1980 that had been established at the previous meeting, but some sentiment was also expressed for lower rates of monetary growth. The members generally accepted the view that retention of the earlier objectives for monetary growth was likely to be associated with further downward pressure on interest rates.

Several members noted their concern that if a large decline in interest rates were to occur over the next few weeks, it was likely to be perceived by some market participants--depending upon which variables they thought important--as an easing of monetary policy and could have very undesirable repercussions on inflationary psychology and on the dollar in foreign exchange markets. Such a decline in interest rates could ultimately prove especially troublesome and unsettling to financial markets if after a short interval a stronger-than-expected resurgence in monetary and credit expansion led to its reversal. The view was also expressed that the course of economic activity would not be adversely affected if any decline in interest rates were gradual rather than precipitous.

Other members, however, stressed the risk that a continued shortfall in monetary growth and persistence of relatively high interest rates could exacerbate recessionary forces in the economy. It was observed that a significant decline in interest rates, if that were to occur in coming weeks, should be regarded as a consequence of the Committee's continuing emphasis on its announced objectives for achieving limited monetary growth and not as a shift toward a stimulative policy. The Committee's monetary objectives should be perceived as fully consistent with a moderation of inflationary forces over time as well as with resistance to recessionary tendencies in the short run. With respect to foreign exchange markets, the view was expressed that the possibility of downward pressure on the dollar in association with a relative decline in U.S. interest rates would have to be faced sooner or later. On the other hand, some decline in U.S. interest rates might already have been discounted, and exchange markets should in any event be reassured by the general thrust of monetary policy and the prospect for improvement over time in the performance of the current account. It was also noted that U.S. interest rates remained higher than key interest rates abroad.

In light of the outlook for a somewhat lower federal funds rate in the weeks immediately ahead, most members believed it would be appropriate to reduce the upper limit of the current range, and several members suggested 19 percent for the new upper limit. Most members expressed a preference for retaining the current lower limit of 13 percent.

At the conclusion of the discussion, the Committee agreed that open market operations in the period until the next meeting should continue to be directed toward expansion of reserve aggregates consistent with growth over the first half of 1980 at annual rates of 4-1/2 percent for M-1A and 5 percent for M-1B, or somewhat less, provided that in the intermeeting period the weekly average federal funds rate remained within a range of 13 to 19 percent. Consistent with this short-run policy, in the Committee's view, M-2 should grow at an annual rate of about 6-3/4 percent over the first half, and expansion of bank credit should slow in the months ahead to a pace compatible with growth over the year as a whole within the range of 6 to 9 percent agreed upon. It was generally recognized that conditions could arise that might make desirable a review of the situation in advance of the next regular meeting scheduled for May 20. In any case, if it appeared that the constraint on the federal funds rate was inconsistent with the objective for the expansion of reserves, the Manager for Domestic Operations was promptly to notify the Chairman who would then decide whether the situation called for supplementary instructions from the Committee.

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

> The information reviewed at this meeting suggests that economic activity turned down in the latter part of the first quarter of 1980, although for the quarter as a whole real GNP expanded somewhat further and the rise in prices accelerated. Retail sales in real terms declined sharply in February and March, after having increased in January. In March industrial production and nonfarm payroll employment declined, and the unemployment rate edged up to 6.2 percent. Private housing starts declined throughout the first quarter, to a rate in March about two-fifths below that in the third quarter of last year. The rise in producer prices of finished goods and in consumer prices was considerably more rapid during the first three months of 1980 than in 1979. Over the first quarter, the rise in the index of average hourly earnings was somewhat above the rapid pace recorded in 1979.
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> The strong demand for the dollar in exchange markets that began in mid-February persisted through early April. Some selling pressure developed in the second week of April as market participants reacted to indications that U.S. interest rates might have peaked, but the trade-weighted value of the dollar against major foreign currencies remained well above its level of early February. The U.S. foreign trade deficit rose further in February.

M-1A and M-1B, which had expanded sharply in February, contracted in March and early April; M-2 increased relatively little in March. From December to March, M-1A and M-1B grew at annual rates of about 4 percent and 4-1/2 percent respectively, and M-2 grew at a rate of 7 percent. Expansion of commercial bank credit slowed substantially in March from the accelerated pace earlier in the year. Since mid-March, most market interest rates on balance have declined considerably.

Taking account of past and prospective economic developments, the Federal Open Market Committee seeks to foster monetary and financial conditions that will resist inflationary pressures while encouraging moderate economic expansion and contributing to a sustainable pattern of international transactions. At its meeting on February 4-5, 1980, the Committee agreed that these objectives would be furthered by growth of M-1A, M-1B, M-2, and M-3 from the fourth quarter of 1979 to the fourth quarter of 1980 within ranges of 3-1/2 to 6, 4 to 6-1/2, 6 to 9, and 6-1/2 to 9-1/2 percent respectively. The associated range for bank credit was 6 to 9 percent.

In the short run, the Committee seeks expansion of reserve aggregates consistent with growth over the first half of 1980 at an annual rate of 4-1/2 percent for M-1A and 5 percent for M-1B, or somewhat less, provided that in the period before the next regular meeting the weekly average federal funds rate remains within a range of 13 to 19 percent. The Committee believes that, to be consistent with this short-run policy, M-2 should grow at an annual rate of about 6-3/4 percent over the first half and that bank credit should grow in the months ahead at a pace compatible with growth over the year as a whole within the range agreed upon.

If it appears during the period before the next meeting that the constraint on the federal funds rate is inconsistent with the objective for the expansion of reserves, the Manager for Domestic Operations is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

Votes for this action: Messrs. Volcker, Guffey, Morris, Partee, Rice, Roos, Schultz, Solomon, Mrs. Teeters, and Mr. Winn. Vote against this action: Mr. Wallich.

Mr. Wallich dissented from this action because he believed that it represented a premature and excessive relaxation of restraint. He favored a policy for the period until the next meeting directed toward lower rates of monetary growth over the first half of the year, accompanied by an intermeeting range for the federal funds rate that would allow for considerably less decline.

On May 6 the Committee held a telephone conference to review the situation and to consider whether supplementary instructions were needed. Available data suggested that the demand for money and hence the demand for reserves had remained weak, and the federal funds rate most recently had fallen below the 13 percent lower limit of the intermeeting range of 13 to 19 percent. The Committee voted to reduce the lower limit of the intermeeting range for the funds rate to 10-1/2 percent.

> On May 6 the Committee modified the domestic policy directive adopted at its meeting on April 22, 1980, to reduce the lower limit of the range for the federal funds rate to 10-1/2 percent.
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> > Votes for this action: Messrs. Volcker, Morris, Rice, Roos, Schultz, Mrs. Teeters, and Mr. Winn. Votes against this action: Messrs. Guffey, Solomon, and Wallich. Absent: Mr. Partee.

Messrs. Guffey and Solomon voted against this action because they preferred smaller reductions in the lower limit of the federal funds rate and Mr. Wallich voted against it because he preferred to maintain the lower limit at 13 percent.