TRANSCRIPT

FEDERAL OPEN MARKET COMMITTEE CONFERENCE CALL

April 27, 1979

Prefatory Note

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FEDERAL OPEN MARKET COMMITTEE
CONFERENCE CALL
April 27, 1979

PRESENT: Mr. Miller, Chairman
Mr. Volcker, Vice Chairman
Mr. Black
Mr. Coldwell
Mr. Mayo
Mr. Partee
Ms. Teeters
Mr. Wallich

Messrs. Guffey, Morris, Roos, and Winn, Alternate Members of the Federal Open Market Committee

Messrs. Baughman, and Eastburn, Presidents of the Federal Reserve Banks of Dallas and Philadelphia respectively

Mr. Altmann, Secretary
Mr. Bernard, Assistant Secretary
Mr. Petersen, General Counsel
Mr. Mannion, Assistant General Counsel
Mr. Axilrod, Economist

Messrs. R. Davis, Ettin, Henry, Parthemos, Keir, Keran, Kichline, Scheld, and Truman, Associate Economists

Mr. Sternlight, Deputy Manager for Domestic Operations, System Open Market Account

Mr. Coyne, Assistant to the Board, Office of Board Members, Board of Governors
Mr. Kalchbrenner, Associate Director, Division of Research and Statistics, Board of Governors
Ms. Farar, Economist, Open Market Secretariat, Board of Governors
Mrs. Deck, Staff Assistant, Open Market Secretariat, Board of Governors

Messrs. Fossom, Gainor, McIntosh, and Williams, First Vice Presidents, Federal Reserve Banks of Atlanta, Minneapolis, Boston, and San Francisco respectively

Messrs. Balbach, Boehne, Burns, Eisenmenger, J. Davis, Senior Vice Presidents, Federal Reserve Bank of St. Louis, Philadelphia, Dallas, Boston, and Cleveland, respectively

Messrs. Cox, Davenport, and T. Davis, Vice Presidents, Federal Reserve Banks of Atlanta, Minneapolis, and Kansas City respectively

Transcript of Federal Open Market Committee Conference Call of
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MR. ALTMANN. Good morning. This is Murray Altmann in the Board Room. [Secretary's note: Mr. Altmann called the roll to determine whether all Reserve Banks were connected and the attendance at each Bank.]

CHAIRMAN MILLER. All right, you are all on. This is the process of consultation following [our practice] in recent months when we've had variations in the growth of the money aggregates from expectations. Our consultations in the past have involved circumstances where money growth was weaker than expected and we have wanted to be sure that we had an accord in the Committee before deciding on the continuing instructions to the Desk. This time the money aggregates are growing more strongly than had been anticipated, so we also would like to get your sense of how we should proceed. Let us start off first by looking briefly at what is happening in the economy to see what new data or updated data we have that would guide us. Jim Kichline is here to give us a brief review.

MR. KICHLINE. Since the last Committee meeting the Commerce Department has published its first preliminary estimate of GNP, which shows real GNP growth of about 3/4 percent at an annual rate in the first quarter. The rate of increase in the gross business product deflator was estimated at about 9-3/4 percent at an annual rate. Both numbers were about a half percentage point less than the staff had estimated. They still are subject to considerable revision, and various hints of what may happen [to individual components] suggest some upward and some downward revisions. Overall at this point we don't have additional new information that would suggest to us the direction ultimately of a significant change.

We have received a couple of pieces of new information that seem significant. One is the new orders figures for March, which showed that total durable goods orders in March declined appreciably, although for the quarter as a whole they remained considerably above, on average, the level that prevailed in the fourth quarter of 1978. Nondefense capital goods orders declined 4.3 percent, which is a large decline; a good deal of it was attributable to the volatile aircraft sector. However, machinery orders, which seem to be a reasonable indicator of the underlying trend in capital goods orders, were down in both March and in the preceding month. We believe these numbers are consistent with the staff's forecast, and at this point they would suggest some slowing in the rate of increase in business investment later in the year.

The consumer price index was released yesterday and showed a rate of increase of 1 percent for the month of March. Once again food and energy prices were quite high, but the increases were widespread throughout all sectors. The one possible helpful hint there is that the rate of increase of food prices was down from the very high pace in February. Other information also suggests that we may get some relief later this year from the sizable increases in food prices.

One other final piece of information would be on new auto sales. For the first 20 days of April they were running at 8-3/4 million units, which is about 1/2 million below the very high level in March. On average we would judge that the auto market remains quite strong. That's all I have, Mr. Chairman.

CHAIRMAN MILLER. Thank you very much, Jim. Let's continue with the briefings before we come back to any questions. I would ask Steve Axilrod to comment on the aggregates numbers themselves.

MR. AXILROD. Thank you Mr. Chairman. The Committee had a target rate of growth for M1 for the two-month April-May period of 4 to 8 percent, and for M2 a 4 to 8-1/2 percent target rate. We are currently estimating for the April-May period for M1 a growth rate of 8-3/4 percent, which would be 3/4 of a point above the upper end of the range. That [reflects] an April growth rate of around 17-1/2 percent because of the recent sharp rates of growth in the weeks of April 11th and April 18th that we just published and the preliminary unpublished data for April 25th that show a further increase of $1.2 billion. That's after the $4 billion rise in the April 18th week and we have assumed a fairly noticeable decline in subsequent weeks. So on the assumption that the level of M1 at the end of May will be about $2 billion lower than it is at the end of April, we would have a zero rate of growth in May. We believe that there are special factors in the April figure that make it reasonable to assume a decline in the level of M1 following this late April [period]. There seems to be evidence that the Treasury is accelerating refunds because of some laggardness earlier and also accelerating them so rapidly that it may be getting [funds] out that would ordinarily have gone out in May. Secondly, there is evidence that the Treasury had delayed collecting checks that had been sent in by people to pay income taxes. That, of course, would have left more money in private demand deposits waiting for collection by the Treasury as the days have been going by in late April. Our staff has estimated the effect of these special factors to be on the order of, say, 7 to 9 percentage points in April. The ATS shift, by the way, was worth about 2.8 percentage points at an annual rate in April. So if you added that to the 17.4 percent, growth [in M1] would be at a 20.2 percent rate for that month. Time deposits as well are running relatively strong and for M2 we're estimating growth for the two-month April-May period at 8-1/2 percent--the top of the Committee's range--with April estimated at 13-1/4 percent and May estimated at 3-1/2 percent.

Very quickly, Mr. Chairman, I think there are two other points that ought to be brought to the Committee's attention. The bank credit figures have been revised--it's a benchmark revision--by the staff. They've been revised upward for the last half of '78 and the first quarter of '79. Formerly, in the first quarter of 1979, bank credit rose 11.2 percent; on the revised basis it's 12.8 percent. Business loans had been up 17.6 percent; on the revised basis it's19.5 percent, though still showing the pattern of a high January, low February, and an even lower March. Data for April suggest a very strong rebound in bank credit. But this too, like the [behavior of] M1, is related to some extent to the high tax payments that are occurring.

Then finally, Mr. Chairman, on the market, short-term rates have dropped since the Committee meeting because the market had been expecting a tightening and with the funds rate remaining unchanged short rates dropped. Also, there was the unwinding of the Treasury's large cash management bill offering in early April. While short rates were dropping--though they did rise this morning because of the large M1 figure that was published for the week ending April 18th--long rates rose. [That occurred] in part because the Treasury has announced a $4-1/4 billion refunding, with half of that going into the 30-year bond area and in part also because the corporate market was adversely affected by the bad publicity on public utilities and there were fairly large public utility offerings this week. In addition, rates have risen in the mortgage market, partly reflecting these corporate bond yields but also reflecting the weakening of inflows into thrift institutions. The [growth of] April inflows to S&Ls has been reduced to around 7 percent and the data for early April suggest a further weakening of inflows relative to what had happened in previous Aprils, and April '78 was a weak period. So the evidence on the mortgage market is for fairly constricted growth in credit availability there. That's all I have, Mr. Chairman.

CHAIRMAN MILLER. Peter Sternlight, are you on the line?

MR. STERNLIGHT. Yes I am, Mr. Chairman.

CHAIRMAN MILLER. Before we turn to Committee members I'd just like to ask you for your comments on the market situation as you see it and any comments you would have on the directive as it now stands if we were not to give you new instructions. The directive now reads --as we all recall it was a money market directive--that with equal weight given to M1 and M2 if the rates of growth appeared to be close to or beyond the upper or lower limits of the indicated ranges, the objective for the funds rate was to be raised or lowered in an orderly fashion within its range. So, Peter, could you just give us your comments on how you see market conditions now and how you would interpret this directive unless we give you any additional [instructions]?

MR. STERNLIGHT. As for market conditions, I don't think I'd have anything significant to add to what Steve has given. I'd perhaps just note one thing--that, as he said, the longer end of the market has been heavy and I would think that's in part also because inflation expectations are continuing quite strong. Also, and this is very hard to quantify, I think there is a bit of disappointment in the market that there wasn't a firming after the last meeting that participants in the long market could have interpreted as a strengthening of System intentions to get a grip on inflation. But, as I say, I don't know how much to make of that factor. As for the federal funds rate, in the last full week that has averaged 10.09 percent; in the previous couple of weeks it was just a shade under 10 percent. We have, of course, been continuing to aim in the 10 to 10-1/8 percent range. On your question about what the Desk would be aiming for in the absence of new instructions, it seems to me that the strength in the aggregates is such as to call for a response from the Desk. And it appears to me that something on the order of a 10-1/4 percent funds rate would be about what I would be recommending in light of the performance of the aggregates.

The other factor I want to call to the Committee's attention is the delicate timing that we face now because of the Treasury funding that Steve also referred to. The Treasury announced the 10-year and 30-year auctions that are coming up on next Tuesday and Wednesday. If there were to be any adjustment to our funds rate objective, I think it would be important to make that intention clear to the market today if possible and Monday so that market participants could bid in [those auctions with] some reasonable knowledge of where policy is now.

CHAIRMAN MILLER. Thank you, Peter. I'm going to suggest that at this time I go down the roll--first of the voting members of the Committee and then the other Presidents or their representatives--and ask for your views, in light of these circumstances, on what our posture should be. If you have any specific questions on the information provided by the staff we would welcome those, but I hope the situation is clear enough that we can just get your advice on what you personally would recommend at this time. Let's start alphabetically with Bob Black.

MR. BLACK. Mr. Chairman, this looks like another case where the aggregates have gone through their usual April acrobatics and I don't think we really ought to be so surprised by it. These deposit shifts that have been incident to the tax payments and refunds seem to defy all our efforts to get a statistically reliable seasonal factor. So I don't think we ought to attach a great deal of weight to these April figures, particularly in view of the 7 to 9 points that Steve mentioned a while ago was the extra [estimated effect]. I'd be inclined to wait to see if we get some unwinding in early May. And even if we didn't, we still wouldn't have gotten above the 1-1/2 percent growth target we set. So I think we're okay at this point and I would hold off.

CHAIRMAN MILLER. Thank you, Bob. Phil Coldwell. I hope you're on.

MR. COLDWELL. I am, Mr. Chairman.

CHAIRMAN MILLER. I'm sorry you missed part of the discussion earlier but I think you know the facts and the background in any case.

MR. COLDWELL. I knew all of the background. I didn't miss much anyway. I have one comment. As I understand it, Steve, you're talking 17.5 percent M1 growth for April and last year as I recall we knocked 6 percentage points off in our seasonal adjustment revision.

MR. AXILROD. Yes.

MR. COLDWELL. So if this were last year we'd be looking at 23 percent.

MR. AXILROD. Well, we'd be looking at 26 percent with the ATS effect.

MR. COLDWELL. Either one is exceptionally high. I must admit that this is another April package but on general grounds, and more particularly the continuing high rate of

inflation, I would permit the directive to be exercised as it is written, raising the fed funds rate to 10-1/4 percent.

CHAIRMAN MILLER. Thank you, Phil. Bob Mayo.

MR. MAYO. I'd leave it the way it is, Mr. Chairman. The economic prospects seem, if anything, a little more sluggish to me than they were when we met in April and I consider that more important than what Bob Black has called the April acrobatics. I have no faith in so short term a movement; if it continues for 3 or 4 weeks like that, I'll eat those words but not for now.

CHAIRMAN MILLER. Thank you, Bob. Chuck Partee.

MR. PARTEE. Well, we have been looking at the figure moving up for the last three weeks, Bob, and it is pretty high.

MR. MAYO. I need three more weeks.

MR. PARTEE. As I look at the M1 number, it appears that we are going to have a two-month average here that's very high. It seems to me that the staff estimate for May is making full allowance for the oddities of the April figure and, therefore, we will have an 8 percent or thereabouts increase for the two months and it could be considerably more. I'm also impressed by the strength of the bank credit numbers--both the revision and the April bank loan numbers at the large banks--which seem to me to put us back more on the track [prevailing] early in the year than in March. And finally, I'm impressed by Peter's argument on the Treasury financing. These are long-term issues and I think if there is a prospect of [our] moving, that we ought to signal it before those auctions because it's not just a standard financing in my view when they're going to be selling a 30-year bond. So I guess I would proceed to follow along the directive as written and do what Peter suggested--raise the funds rate to 10-1/4 percent with the idea that if the strength holds up we'll move up further in the range in a couple of weeks.

CHAIRMAN MILLER. Thank you, Chuck. Nancy.

MS. TEETERS. Mr. Chairman, I would agree with Bob Mayo and Bob Black. I think that we have a great deal of difficulty with our money supply numbers in April. And I, too, am impressed by the weakness that's been showing up in the first-quarter numbers. We're considerably below where we thought we were when the FOMC [last] met. If I'm wrong and [the strong money growth] continues, I can change my mind later. But I don't think we should change from the funds rate of approximately 10-1/8 percent at the present time.

CHAIRMAN MILLER. Thank you, Nancy. Paul Volcker.

MR. VOLCKER. Let me just say, so far as the aggregates are concerned, Mr. Chairman, that while apparently the staff up here doesn't depart from the general outline of what

Steve reported, they do have substantially higher numbers for May than the zero that Steve has for M1 growth. In other words, they [estimate growth will be] down but not down that far, which would give us a two-month figure somewhere above Steve's projections. I don't know how much this is worth but [our staff's estimates] are all off in that direction. And, of course, we've got these other numbers like the NOWs and ATS accounts and money market mutual funds continuing to rise. So I think we do have a pretty big bulge here, despite the complications of the tax date. In general, as you know, I thought we should have been a little tighter before so I'm not disinclined to following the directive. That seems to be a minimal [step]; I would associate myself with Mr. Coldwell and Mr. Partee in that regard.

CHAIRMAN MILLER. Thank you very much, Paul. Henry Wallich.

MR. WALLICH. Well, I would not give a great deal of weight to these aggregates; they are only marginally above our ranges. On the other hand, as I look at the economy I see inflation expectations clearly worsening in the face of some straws on the down side in the real sector. I'm impressed by the evidence on the inflation expectations in the rise in long rates and the declines simultaneously in short rates, which both are in the wrong direction. I've been in favor of a higher funds rate previously and I would think that the minimum we ought to do now is to go to 10-1/4 percent. But my preference would be for [going] somewhat higher [on the funds rate] and if that could be done later, I would regard that as right.

CHAIRMAN MILLER. Thank you, Henry. At least that's a sign of consistency; you weren't paying attention to the aggregates before and you're still not. I think that's a good move. At least it shows [consistency].

MR. WALLICH. Even with conditions changed.

CHAIRMAN MILLER. I realize that and I commend you for sticking with your guns because that's the point you made at the last meeting, as I recall. Now we have Roger Guffey, who is the alternate for John Balles, as I understand it.

MR. GUFFEY. Thank you, Mr. Chairman. I would be inclined to join Bob Black and Bob Mayo, particularly in view of the fact that we have experienced six months of very slow [economic] growth. In fact, [given] the experience in April of the last few years, I'd like to wait and get some additional information on [the aggregates]. As a result I would like to stay where we are for at least two more weeks and perhaps take a look at it [then]. The aggregates are obviously a matter of concern but they jump around so much that I'm not prepared to recommend going up [on the funds rate].

CHAIRMAN MILLER. Thank you, Roger. Next we have Larry Roos who is the alternate for Monroe Kimbrel.

MR. ROOS. Thank you, Mr. Chairman. I have always previously paid attention to the aggregates and still do.

CHAIRMAN MILLER. Another consistent one!

MR. ROOS. As you recall, prior to this surge in the aggregates, I spoke out at the last meeting for some ease because of my concern about the undershooting of the [M1] range. I do think that we should take it seriously, even though we don't know whether the present surge is temporary or not. There is some historical perspective. Last year at this time of the year the aggregates did surge upward and they then remained at a fairly level but higher [rate of growth] for a period of time, so I don't think we can ignore this. I would recommend that the Desk be authorized to use the full 9-3/4 to 10-1/2 percent range for the fed funds target and be prepared to permit the fed funds rate to move upward toward 10-1/2 percent in an orderly fashion. If this surge in the aggregates is temporary, then we can permit it once again to fall toward 10 [or even] 9-3/4 percent. So I think we ought to broaden the fed funds [movement] and use the full range and be flexible as we see how permanent the present surge turns out to be.

CHAIRMAN MILLER. Larry, I commend you for also being consistent in watching the aggregates. But I'm not sure I understood what you thought the instructions should be to the Desk or what the interpretation should be today as distinguished from over the period.

MR. ROOS. Well, ideally, I would like to see us say to the Desk that it should move [the funds rate] up to 10-1/2 percent if on the basis of its judgment it sees fit to do so. Realistically, I would say that to proceed in an orderly way we should move to 10-1/4 percent as quickly as possible and [subsequently] move it higher. And if the fed funds rate does continue to move upward, Mr. Chairman, I think some consideration should be given to an increase in the discount rate.

CHAIRMAN MILLER. Let me go on. I hope Ernie Baughman is now on the line.

MR. BAUGHMAN. I have just come on, Mr. Chairman, so I am not privy to very much of the preceding discussion. My inclination would be that in the circumstances the federal funds rate should be edged up and the record when it becomes public should show that we were resisting at least to some extent a surge in the growth rate of the monetary aggregates.

CHAIRMAN MILLER. Thank you very much, Ernie. Willis Winn.

MR. WINN. Mr. Chairman, I think I would join with the group that would like to see a little more [evidence] in the behavior [of the aggregates] before we move. I would be inclined if we want to indicate concern in this area to do it through the discount rate rather than the federal funds rate at this time. We resisted [making a move] when [the deviation from our target was] was on the down side and it seems to me that we don't have enough evidence yet on the up side to make a change in our operations.

CHAIRMAN MILLER. Thank you, Willis. Frank Morris.

MR. MORRIS. Mr. Chairman, I still believe that the economy is in a peaking process and I believe that the aggregates have to be viewed in the light of what has been going on in the past six months. Even with this bulge, M2 has only grown at a 4 percent rate in the past six months, so at the moment I would not make any change. If this strength should be sustained into May then I think we would have to move against it. But at the moment I would do nothing.

CHAIRMAN MILLER. Thank you, Frank. Dave Eastburn. I hope Philadelphia is still with us.

MR. EASTBURN. Yes, I'm on. I would hold where we are at the present time. Judging by last year's experience, as Larry pointed out, following an April surge May and June were still relatively high. If that happens again, I think perhaps we should take action. But I think we need to watch that and I wouldn't take the action right away.

CHAIRMAN MILLER. Thank you very much, Dave. We have Kyle Fossum on for Monroe Kimbrel. So, Kyle, we'll hear from you.

MR. FOSSUM. It's a close call for us but we come down on the side of holding where we are and viewing [developments] for another week or so before we would suggest changing. I would report, though, that in a conference call with our Bank's executive committee this morning the discount rate was discussed and there was some inclination to snug it up a bit.

CHAIRMAN MILLER. Thank you, Kyle. We have Tom Gainor on for Mark Willes.

MR. GAINOR. Mr. Chairman, we would favor no change. We'd like to see two or three more weeks to test whether the April figures are significant.

CHAIRMAN MILLER. Thank you, Tom. John Williams for John Balles.

MR. WILLIAMS. We would agree with Frank Morris. We'd be strongly opposed at this time to any [increase] in the federal funds rate. We think that April is not the month that we want to respond to, particularly if the data are on the high side--April being not a typical month and also a very unreliable month. So until we get further confirmation of this upsurge in the aggregates, we think it would be very premature to move. We would recommend waiting until the May data come in.

CHAIRMAN MILLER. Well, thank you all very much. It shows you that I was right at the last meeting when I said it would take a month before we get to be unanimous. We haven't reached [unanimity] yet. It's a very interesting situation. Without my vote we have five of

the voting members who would prefer moving up to 10-1/4 percent and four who would like to stand pat. Of the nonvoting members we have six who would like to stand pat and one who would edge [the funds rate] up. It's an amazing dispersion and leaves us with a circumstance that is not very appealing. After listening, and recognizing all of the risks and difficulties, on balance I think I would tend to encourage the Desk to follow the directive that we have and therefore to tighten up a bit. I would like to suggest, because with this dispersion I don't think an official vote does us all much good, that we merely view this consultation as a consultation involving advice and [guidance] on how the Desk should act. I hope that will be agreeable to everyone because this is a close one to call. I think everyone had a persuasive argument on both sides [but] the differences in terms of what really will be done are fairly narrow. And that being so, my tendency would be to follow the directive as we've written it, which the Desk would interpret as meaning they should be moving [the funds rate] up to 10-1/4 percent. Let me just run through [my list] quickly to see if anyone objects to that procedure or that conclusion. Bob Black.

MR. BLACK. It's fine with me, Mr. Chairman.

CHAIRMAN MILLER. Phil Coldwell.

MR. COLDWELL. Fine.

CHAIRMAN MILLER. Bob Mayo.

MR. MAYO. Fine.

CHAIRMAN MILLER. Chuck Partee.

MR. PARTEE. It's fine.

CHAIRMAN MILLER. Nancy Teeters.

MS. TEETERS. It's all right

CHAIRMAN MILLER. Paul Volcker.

MR. VOLCKER. Seems to me highly appropriate.

CHAIRMAN MILLER. Henry Wallich.

MR. WALLICH. Seems fine to me but we should look again as the data evolve.

CHAIRMAN MILLER. Of course. Roger Guffey.

MR. GUFFEY. Fine.

CHAIRMAN MILLER. Larry Roos.

MR. ROOS. Fine.

CHAIRMAN MILLER. Ernie Baughman.

MR. BAUGHMAN. I agree.

CHAIRMAN MILLER. Willis Winn.

MR. WINN. Yes.

CHAIMAN MILLER. Frank Morris.

MR. MORRIS. Okay.

CHAIRMAN MILLER. Dave Eastburn.

MR. EASTBURN. I guess it's all right.

CHAIRMAN MILLER. Kyle Fossum.

MR. FOSSUM. Fine with us.

CHAIRMAN MILLER. Tom Gainor.

MR. GAINOR. Fine.

CHAIRMAN MILLER. John Williams.

MR. WILLIAMS. Okay.

CHAIRMAN MILLER. Thank you all. You've been patient and very, very helpful. I appreciate it and I hope we'll get our [phone] system working a little better. It was so perfect before. We'll put our technicians to work so we can try to get our equipment functioning better. I really think this opportunity to consult is valuable, so I hope we can do it from time to time. Thank you. We'll close now.

END OF SESSION