FEDERAL RESERVE

press release

For immediate release July 29, 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 April 30, 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 April 30, 1968

1. Authority to effect transactions in System Account.

Over-all economic activity had expanded at a very rapid pace thus far in 1968 and prices had risen substantially. The outlook was for continued rapid expansion in activity and persisting inflationary pressures.

In the first quarter, according to preliminary Department of Commerce estimates, real GNP advanced at a 6 per cent annual rate and average prices--as measured by the GNP deflator--at a 4 per cent annual rate. Defense spending and business capital outlays expanded considerably, and outlays on residential construction increased moderately. Most of the advance in GNP, however, reflected a sharp rise in consumer expenditures; personal income increased at an unusually rapid rate in the quarter, and the percentage of income saved fell below the unusually high figure of the preceding quarter. Partly because of the large increase in consumer expenditures, the rate of business inventory accumulation declined markedly.

In March nonfarm employment rose substantially further, and the unemployment rate edged down to 3.6 per cent from 3.7 per cent in February. Industrial production increased moderately, and retail sales continued to advance rapidly. In early April, however, retail sales apparently were adversely affected by civil disorders in many cities.

The consumer price index rose considerably further in March to a level about 4 per cent above a year earlier. With the cost of living advancing at a rapid pace, settlements in recent wage negotiations had provided for increases in wages and fringe benefits of 6 per cent or more per year. The rise in average prices of industrial commodities moderated in both March and April, mainly because of large declines for a few major industrial materials. Average prices of farm products changed relatively little in the 2 months.

It appeared likely that in the second quarter real GNP would advance as fast as or faster than in the first quarter and that average prices would continue upward at about the first-quarter pace. In prospect were further large rises in consumer income and spending and another substantial increase in defense outlays. It was expected that business capital spending and outlays on residential construction would level off, but that business inventory accumulation would rebound from its low first-quarter rate.

Since the establishment of the two-market system for gold on March 17, the price of gold in the private market had for the most part ranged between $37 and $40 per ounce. The volume of foreign official gold purchases from the U.S. Treasury had increased considerably in recent weeks.

The deficit in the U.S. balance of payments in the first quarter now appeared to have been smaller than estimated earlier and considerably smaller than in the fourth quarter of 1967. The surplus on merchandise trade was reduced further in the first quarter from the low level to which it had fallen in late 1967; in March, when exports declined largely because of a longshoremen's strike in New York, U.S. foreign trade was in deficit. The deterioration in the trade account, however, was more than offset by a marked improvement in capital transactions, reflecting in part a net reflow of U.S. bank credits during the quarter that was about as large as the foreign credit restraint program was intended to achieve over the full year. The outlook was for some recovery in the trade account but for substantial deterioration in the capital account--especially in view of the likelihood that the reflow of bank credit and certain other favorable first-quarter capital movements would not be sustained.

System open market operations had been directed toward achieving slightly firmer conditions in the money market following the meeting of the Committee on April 2. After the increase in Federal Reserve Bank discount rates from 5 to 5-1/2 per cent effective April 19 and the meeting of the Committee on that day, operations had been directed at achieving still firmer money market conditions while facilitating orderly market adjustments to the higher discount rate. In the first part of April the effective rate on Federal funds moved up to a range of 5-1/2 to 5-7/8 per cent, and subsequently it rose to a range around 6 per cent. Net borrowed reserves of member banks averaged $335 million in the 4 weeks ending April 24, compared with an average of about $310 million in

March; and average borrowings of member banks increased to about $690 million in the latest 4 weeks from about $650 million in the earlier period.

Interest rates on most types of short- and intermediate-term market securities rose substantially over the course of April, in part as a result of the increase in discount rates and the firming of money market conditions. The market rate on 3-month Treasury bills, at 5.48 per cent on the day before this meeting, was 14 basis points above its level on April 18 and 35 basis points higher than on April 1. Yield changes were more irregular in capital markets, where investor sentiment was influenced by fluctuating prospects for fiscal action and for Vietnam peace negotiations, but since mid-April long-term yields in general had also been rising. Several large additions to the April and May calendar of public offerings of corporate bonds and the continuation of a relatively large volume of new issues of municipal bonds contributed to upward pressures on yields of such securities.

The Treasury was expected, on the day following this meeting, to announce the terms on which it would refund securities maturing in mid-May, of which about $4 billion were held by the public. Estimates suggested that the Treasury would have to raise a substantial amount of new cash before the end of the fiscal year. It was thought likely that some of this would be raised in connection with the May refunding, although the amount was uncertain, and that further cash financing would be undertaken in June.

Interest rates on new-home mortgages, which had changed little in February, edged up in March to postwar highs. Net inflows of funds to nonbank depositary institutions had improved somewhat in February and March, but in the 4 months through March they were at an annual rate about one-third less than in the preceding 7 months. Although withdrawals during the interest- and dividend-crediting period in late March and early April were smaller than many observers had anticipated, net inflows in the period shortly thereafter apparently were not as large as usual.

Commercial bank credit, as measured by the bank credit proxy--daily-average member bank deposits--was estimated to have declined at an annual rate of 3.5 per cent in April. Business loans outstanding, which had begun to expand more rapidly after mid-March, increased substantially in April. However, banks continued to liquidate their holdings of U.S. Government securities. They also reduced the pace at which they acquired other securities, notably municipal obligations. Following the April 19 increase in the discount rate, commercial banks raised their prime lending rate from 6 to 6-1/2 per cent.

The money supply increased in April at a pace considerably above that of earlier months of the year. Private demand deposits rose sharply as U.S. Government deposits declined, and currency holdings of the public continued to expand at a higher-than-normal rate. Total time and savings deposits of banks were estimated to have increased relatively little in April; with short-term interest rates rising, inflows of consumer-type time and savings deposits slackened and the volume of large-denomination CD's outstanding contracted substantially. The CD run-off was concentrated in the first half of the month, before offering rates were increased under the higher ceilings that became effective on April 19. By the month-end offering rates were at the new maximum levels for shorter-term CD's but were somewhat below the ceilings for longer-term certificates.

In the 5 months through April the bank credit proxy had grown at an annual rate of 3.7 per cent, about one-third of the rate for the preceding 7 months. In the same period commercial bank time and savings deposits had expanded at a rate of 5.5 per cent, less than two-fifths of the earlier pace; and the money supply had grown at a 5.6 per cent rate, about two-thirds of that prevailing earlier.

Changes in bank credit in May and June were expected to depend in part on the pattern of Treasury financing operations. On the assumptions that prevailing money market conditions would be maintained and that the Treasury would raise only a moderate amount of new cash in connection with the May refunding--meeting the bulk of its residual needs for the fiscal year 1968 in June--the annual rate of change in the bank credit proxy was projected in a range of -2 to +2 per cent in May and in a range of +4 to +6 per cent in June. On the same assumptions, U.S. Government deposits were projected to decline substantially further in May and private demand deposits and the money supply to increase rapidly, although not so rapidly as in April. It was expected that banks would expand their outstanding CD's somewhat, but that consumer-type time and savings deposits would continue to grow at a relatively slow pace.

The Committee agreed that the Treasury's forthcoming refunding operation precluded a change in monetary policy at this time. Although members expressed concern about persisting inflationary pressures and the recent worsening in the U.S. foreign trade balance, a number indicated that they would have favored no change in policy at present even if Treasury financing were not in prospect. Among the reasons they advanced were the considerable degree of restraint already achieved by recent monetary policy actions, the effects of which were still in train; and the view that prospects for restrictive fiscal action had improved. At the same time, the desirability was noted of avoiding any tendency toward relaxation in the degree of money market firmness.

The Committee concluded that the firmer conditions now prevailing in the money market should be maintained, with the proviso that operations should be modified, insofar as permitted by the Treasury financing, if bank credit appeared to be deviating significantly from the projection. It was understood that allowance would be made in interpreting this proviso for any substantial difference between the amount of new cash the Treasury actually raised in connection with the May refunding and the amount assumed in the projection.

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

> The information reviewed at this meeting indicates that over-all economic activity has expanded at a very rapid pace thus far in 1968, with prices rising substantially, and that prospects are for a continuing rapid advance in activity and persisting inflationary pressures in the period ahead. Since late fall, growth rates of bank credit, the money supply, and time and savings accounts at financial institutions have on balance moderated considerably. Market interest rates have risen in recent weeks, partly in reaction to the firming of monetary policy including the further increase in Federal Reserve discount rates. The U.S. foreign trade balance has worsened further, and the international payments position of the United States continues to be a matter of serious concern. In this situation, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to resistance of inflationary pressures and attainment of reasonable equilibrium in the country's balance of payments.
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> To implement this policy, while taking account of Treasury financing activity, System open market operations until the next meeting of the Committee shall be conducted with a view to maintaining the firmer conditions prevailing in the money market; provided, however, that operations shall be modified, to the extent permitted by Treasury financing, if bank credit appears to be deviating significantly from current projections.

Votes for this action: Messrs. Martin, Hayes, Brimmer, Daane, Ellis, Galusha, Kimbrel, Maisel, Robertson, and Sherrill. Vote against this action: Mr. Hickman.
Absent and not voting: Mr. Mitchell.

In dissenting from this action, Mr. Hickman expressed the view that the recent upward adjustment of interest rates had been less than contemplated under the policy directive the Committee had issued at its April 19 meeting, and less than was desirable in view of the inflationary pressures in the economy. He agreed that the prospective Treasury financing precluded substantial firming of money market conditions before the Committee's next meeting. Nevertheless, he thought that firmer conditions should be sought, if and when feasible after the Treasury financing had been completed, on the understanding that the stance of monetary policy would be reexamined should fiscal action be taken.

2. Amendment to authorization for System foreign currency operations.

The Committee amended paragraph 1B(3) of the authorization for System foreign currency operations to increase, from $200 million to $250 million, the limit on authorized System Account holdings of sterling purchased on a covered or guaranteed basis. With this amendment, the first paragraph of the authorization read as follows:

> 1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, for System Open Market Account, to the extent necessary to carry out the Committee's foreign currency directive:
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> A. To purchase and sell the following foreign currencies in the form of cable transfers through spot or forward transactions on the open market at home and abroad, including transactions with the U.S. Stabilization Fund established by Section 10 of the Gold Reserve Act of 1934, with foreign monetary authorities, and with the Bank for International Settlements:

Austrian schillings
Belgian francs
Canadian dollars
Danish kroner
Pounds sterling
French francs
German marks
Italian lire
Japanese yen
Mexican pesos
Netherlands guilders
Norwegian kroner
Swedish kronor
Swiss francs

B. To hold foreign currencies listed in paragraph A above, up to the following limits:

(1) Currencies held spot or purchased forward, up to the amounts necessary to fulfill outstanding forward commitments;

(2) Additional currencies held spot or purchased forward, up to the amount necessary for System operations to exert a market influence but not exceeding $150 million equivalent; and

(3) Sterling purchased on a covered or guaranteed basis in terms of the dollar, under agreement with the Bank of England, up to $250 million equivalent.

C. To have outstanding forward commitments undertaken under paragraph A above to deliver foreign currencies, up to the following limits:

(1) Commitments to deliver foreign currencies to the Stabilization Fund, up to $350 million equivalent;

(2) Commitments to deliver Italian lire, under special arrangements with the Bank of Italy, up to $500 million equivalent; and

(3) Other forward commitments to deliver foreign currencies, up to $550 million equivalent.

D. To draw foreign currencies and to permit foreign banks to draw dollars under the reciprocal currency arrangements listed in paragraph 2 below, provided that drawings by either party to any such arrangement shall be fully liquidated within 12 months after any amount outstanding at that time was first drawn, unless the Committee, because of exceptional circumstances, specifically authorizes a delay.

Votes for this action: Messrs. Martin, Hayes, Hickman, Brimmer, Daane, Ellis, Galusha, Kimbrel, Maisel, Robertson, and Sherrill. Votes against this action: None. Absent and not voting: Mr. Mitchell.

This action was taken on grounds that it would be helpful in connection with discussions of specific arrangements, including a drawing by Britain on its $1.4 billion standby facility with the International Monetary Fund, for repayment by the Bank of England of outstanding drawings under its swap line with the Federal Reserve. It was understood that initial use of the enlarged authority would be subject to the approval of Chairman Martin in light of developments in those discussions.