



FEDERAL RESERVE

press release

For immediate release

May 15, 1972

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 February 15, 1972.

Such records are made available approximately 90 days after the date of each meeting of the Committee 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 on the information that was available to the Committee at the time of the meeting, rather than on data as they may have been revised since then.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on February 15, 1972

1. Current Economic Policy Directive.

The information reviewed at this meeting indicated that in the fourth quarter of 1971 real GNP had grown at an annual rate of about 6 per cent, compared with (downward revised) growth rates of about 3.5 and 2.5 per cent in the second and third quarters, and that prices had risen relatively little in reflection of the 90-day freeze imposed in mid-August. Staff projections suggested that the faster pace of growth in real GNP would be sustained through the first half of 1972, and that prices were likely to rise sharply for a time in the post-freeze period.

In January industrial production and manufacturing employment increased somewhat, although the average workweek in manufacturing declined after having risen for several months. Total nonfarm payroll employment advanced substantially further, and the unemployment rate edged down to 5.9 from 6.0 per cent in December. Weekly data suggested that retail sales increased a little in January, following a substantial decline in December.

The wholesale and consumer price indexes rose sharply from November to December, reflecting in part the mid-November termination of the 90-day freeze. About half the rise in both indexes was accounted for by increases in foodstuffs, which are

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largely uncontrolled, and in imported goods and other items exempt from the controls. Wage rates also rose substantially in December when, under the post-freeze program, some increases--both previously scheduled and newly negotiated--were allowed to go into effect. However, the advance in wage rates slowed in January.

The staff's projection of growth in real GNP in the first half of 1972 was about unchanged from 5 weeks earlier, although expectations for some major categories of expenditure were altered. Thus, the projected expansion in Federal purchases of goods and services--which had been raised 5 weeks earlier to reflect the Government pay increase effective in early January--was raised further to reflect a concentration of outlays in the second quarter of the year, roughly in line with the administration's late-January estimates of the Federal budget for the 1972 fiscal year. On the other hand, the prospective gains in consumer spending were scaled down moderately, in large part reflecting the recent lack of strength in retail sales and evidence that new withholding schedules were resulting in substantial over-withholding of personal income taxes. As in the previous projection, it was anticipated that business capital outlays, residential construction, and State and local government expenditures would continue to grow at substantial rates and that business inventory investment would increase further.

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In foreign exchange markets, rates for most major currencies appreciated against the dollar in January and early February, rising to or above their new central values. Over the whole period from the time of the Smithsonian agreement on December 18 through early February, there was a small surplus in the U.S. balance of payments on the official settlements basis, as reflows of funds to the United States after the agreement were somewhat in excess of the deficit on current account and normal capital transactions.

The Treasury announced on January 26 that in its mid-February financing it would offer at par a 51-month, 5-3/4 per cent note and a 10-year, 6-3/8 per cent bond in exchange for issues maturing in February 1972 and in February and May 1974. This combination of a refunding and a pre-refunding was well received. About \$1.2 billion or 32 per cent of the \$3.8 billion of the publicly held issues maturing this February were redeemed for cash, and the Treasury met the cash requirement by reducing its balance from a relatively high level.

Interest rates on long-term securities generally had risen in recent weeks, largely in reaction to the new estimates of a larger Federal deficit in fiscal 1972 than had been anticipated and to numerous announcements of prospective new corporate security issues. However, some corporate borrowers indicated that the exact timing of their offerings would depend on market conditions, and others postponed prospective issues in reaction to rising interest rates. In the month of January the volume of new corporate issues rose somewhat more than seasonally while that of State and local government issues declined.

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Most short-term interest rates had declined since the last meeting of the Committee in response to strong private domestic and foreign official demands for short-term securities as well as to further easing in money market conditions. Treasury bill rates had risen early in the period, reflecting expectations of heavy Treasury financing in the short-term area, but after that they fell back. At 3.00 per cent on the day before this meeting, the market rate on 3-month bills was about the same as 5 weeks earlier.

Contract interest rates on conventional new-home mortgages and yields in the secondary market for Federally insured mortgages continued to decline in January. Inflows of savings funds to nonbank thrift institutions rose sharply further--approaching the record high rates of early 1971--in part because of the continuing decline in yields available on short-term market securities relative to the rates paid on savings shares and deposits.

Business loans at commercial banks increased somewhat in January, but business loan demand apparently remained relatively weak, and major banks again lowered their prime rates. Real estate and consumer loans continued to expand rapidly, and banks further increased their holdings of securities other than Treasury issues.

Following the January 11 meeting of the Committee, System open market operations had been directed at fostering substantial growth in total member bank reserves in January, while continuing

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to take appropriate account of conditions in the money market. After late January, System operations gave primary emphasis to maintaining steady conditions in the money market while the Treasury was engaged in its refunding operation. Total reserves were indicated to have grown from December to January at an annual rate of 23 per cent on the basis of earlier seasonal adjustment factors, and at about a 21 per cent rate on the basis of the factors emerging from the annual revision of seasonal adjustments, completed shortly before this meeting. In late January and the first half of February the Federal funds rate fluctuated around 3-1/4 per cent, down from 3-5/8 per cent at the time of the Committee's meeting on January 11. In the 5 weeks ending February 9, member bank borrowings averaged about \$20 million compared with \$110 million in the preceding 4 weeks.

Growth in the narrowly defined money stock (private demand deposits plus currency in circulation, or M_1), remained relatively slow in January. However, money more broadly defined (M_1 plus commercial bank time deposits other than large-denomination CD's, or M_2) grew at a fast pace as inflows of savings to commercial banks--like those to nonbank thrift institutions--rose sharply further. Growth was also rapid in the adjusted bank credit proxy--daily-average member bank deposits, adjusted to include funds from nondeposit sources--although the average volume of outstanding large-denomination CD's declined moderately and Government deposits changed little.

In continuation of a discussion begun at a meeting on the previous day, the Committee considered the relative merits of money market conditions and various measures of member bank reserves as "operating targets"--that is, as variables for guiding day-to-day

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open market operations in the effort to achieve its intermediate monetary objectives and, in the process, contribute to the Nation's basic economic goals. Some arguments were advanced in favor of placing about the same degree of emphasis on money market conditions as had been customary prior to the meeting on January 11. However, the Committee concluded that in the present environment it was desirable to increase somewhat the relative emphasis placed on reserves while continuing to take appropriate account of money market conditions. Committee members believed that doing so would enhance their ability to achieve desired intermediate monetary objectives. These include the performance of various measures of money stock and bank credit that are supported by reserves as well as interest rates and over-all liquidity and credit conditions. At the same time, the members believed that reserve-supplying operations should be conducted so as to avoid disturbing effects in money and credit markets.

At this meeting the Committee decided to express its reserve objectives in terms of reserves available to support private nonbank deposits--defined specifically as total member bank reserves less those required to support Government and interbank deposits. This measure was considered preferable to total reserves because short-run fluctuations in Government and interbank deposits are sometimes large and difficult to predict and usually are not of major significance for policy. It was deemed appropriate for System open market operations normally to accommodate such changes in Government and interbank deposits.

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The Committee agreed that the economic situation and outlook at this time called for growth in the monetary aggregates at moderate rates. It took note of a staff analysis suggesting that, over the months of February and March combined, such growth was likely to be associated with expansion in the reserve measure employed at about an 8 per cent annual rate, and possibly with some firming of money market conditions. The members decided that it would be desirable to seek growth in the reserve measure in the February-March period at an annual rate in a range of 6 to 10 per cent, while avoiding both sharp short-run fluctuations and undesirably large cumulative changes in money market conditions in either direction in the period between meetings. They also decided that some allowance should be made in the conduct of operations for any significant deviations that might develop between the actual rates of growth in the monetary aggregates and the moderate growth rates expected.

The members also agreed that account should continue to be taken of international developments, and that to the extent feasible the Government securities purchased in reserve-supplying operations should include intermediate- and longer-term issues as well as Treasury bills.

Finally, it was understood that the Chairman might call upon the Committee to consider the need for supplementary instructions if it appeared during the period before the next scheduled meeting that the Committee's several objectives and constraints were not being met satisfactorily.

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

The information reviewed at this meeting indicates that real output of goods and services increased more rapidly in the fourth quarter than it had in the third quarter, but the unemployment rate remained high. For the current quarter, growth is projected at a rate close to that of the fourth quarter. Prices increased sharply in December, in part reflecting termination of the 90-day freeze. Wage rates also rose substantially in December when some increases that had been deferred under the freeze were allowed to go into effect, but the rise slowed in January. The narrowly defined money stock, which had not grown on balance from August to November, rose somewhat in December and January. Inflows of time and savings funds at bank and nonbank thrift institutions increased sharply in January, and both the broadly defined money stock and the bank credit proxy expanded rapidly. Some short-term interest rates have declined further in recent weeks while yields on long-term securities generally have increased from the lows reached around mid-January. Exchange rates for most major foreign currencies against the dollar have appreciated to levels near or above their new central values. Since the Smithsonian meeting, capital reflows to the United States have somewhat exceeded the underlying U.S. balance of payments deficit. In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to sustainable real economic growth and increased employment, abatement of inflationary pressures, and attainment of reasonable equilibrium in the country's balance of payments.

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

Votes for this action: Messrs.
Burns, Brimmer, Clay, Daane, Kimbrel,
Maisel, Mayo, Mitchell, Morris,
Robertson, and Sheehan. Vote against
this action: Mr. Hayes.

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Mr. Hayes dissented from this action for essentially the same reasons he had dissented from the directive adopted at the previous meeting. First, he did not favor placing as much emphasis as contemplated on reserves as an operating target; he preferred to place main emphasis on money market conditions for that purpose. Second, he thought the policy agreed upon could result in an easing of money market conditions to a degree that in his judgment would entail substantial risks both domestically and internationally.

2. Continuing authority directive.

On January 26, 1972, a majority of Committee members had voted to suspend, until close of business on February 15, 1972, the lower limit (set forth in paragraph 1(c) of the continuing authority directive with respect to domestic open market operations) on interest rates on repurchase agreements arranged by the Federal Reserve Bank of New York with nonbank dealers. The provision in question, which also had been suspended for the period from December 23, 1971, through January 11, 1972, specified that such repurchase agreements were to be made "at rates not less than (1) the discount rate of the Federal Reserve Bank of New York at the time such agreement is entered into, or (2) the average issuing rate on the most recent issue of 3-month Treasury bills, whichever is the lower."

Votes for this action: Messrs.
Burns, Hayes, Brimmer, Clay, Daane,
Kimbrel, Maisel, Mayo, Mitchell, Morris,
and Sheehan. Vote against this action:
Mr. Robertson.

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This action was taken on recommendation of the System Account Manager, to provide against the contingency that under existing rate limitations it might not prove feasible to enter into repurchase agreements during coming weeks in the volume likely to be found desirable to meet the Committee's objectives for member bank reserves. It was understood that rates below 3-1/4 per cent would not be used without prior notification to the Committee.

The action of January 26 was ratified at today's meeting. Mr. Robertson dissented from the ratification as well as from the original action for reasons similar to those underlying his dissent from the similar action taken in December. He preferred to have needed reserves injected into the banking system by means of outright purchases of Treasury securities in the open market rather than through repurchase agreements with Government securities dealers. In his judgment such agreements actually constituted subsidized loans to dealers, and he saw no justification for increasing the subsidy by making them at lower and lower rates of interest.

3. Revision of guideline for operations in agency issues.

On August 24, 1971, when the Committee had first authorized outright operations in securities issued by Federal agencies, it had approved certain initial guidelines for the conduct of such operations with the understanding that they would be subject to review and revision as experience was gained. At this meeting the Committee revised guideline No. 5, under which purchases were limited to issues outstanding in amounts of \$300 million or over in cases where the obligations have a maturity of 5 years or less at the time of purchase, and to issues outstanding in amounts of \$200 million or over in cases where the securities have a maturity of more than 5 years at the time of purchase. As revised, the guideline specified that the maturity of the obligation should be taken as of the time of issuance, rather than as of the time of purchase, in determining whether it was eligible for purchase.

Votes for this action: Messrs.
Burns, Hayes, Brimmer, Clay, Daane,
Kimbrel, Maisel, Mayo, Mitchell,
Morris, Robertson, and Sheehan.
Votes against this action: None.

This action was taken on recommendation of the System Account Manager, on the grounds that from a practical standpoint it was undesirable for an obligation initially eligible for purchase and perhaps already held in the System Account to become ineligible merely because its maturity had shortened with the passage of time.