FEDERAL RESERVE

press release

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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 July 17, 1973.

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 July 17, 1973

Domestic policy directive

The information reviewed at this meeting suggested that growth in real output of goods and services, which had expanded at an annual rate of 8 per cent in both the last quarter of 1972 and the first quarter of 1973, had grown at a much less rapid pace in the second quarter. Staff projections continued to suggest that growth would moderate further in the second half of the year.

Retail sales declined in June, according to the advance report, and in the second quarter as a whole they were about the same as in the first quarter. Industrial production continued to rise in June--reflecting further gains in output of business equipment and industrial materials--but the advance was somewhat less rapid in the second quarter than in the first. Nonfarm employment again rose substantially in June, but as in April and May, the pace of expansion was much less rapid than it had been earlier in the year. The unemployment rate declined to 4.8 per cent after having been 5.0 or 5.1 per cent for 6 months.

The advance in average hourly earnings of production workers on nonfarm payrolls, which had been moderate in the first quarter of the year, was more rapid in the second quarter. Wholesale prices of both industrial commodities and farm and food products rose sharply further from mid-May to mid-June, prior to the imposition of the price freeze announced by the President on June 13. The increase in the total wholesale price index during the first half of the year was extraordinarily large. In May the consumer price index continued to rise at about the high average rate prevailing in the first 4 months of the year; increases in retail prices were widespread and were particularly large among foods.

The latest staff projections for the second half of 1973 were similar to those of 4 weeks earlier. The anticipated expansion in business fixed investment, although substantial, was much less rapid than in the first half of the year. Moreover, it was expected that residential construction outlays would decline appreciably; that business inventory investment would increase less rapidly than in the second quarter; and that growth in personal consumption expenditures would be well below the pace in the first half.

U.S. merchandise exports continued to expand in May, but imports rose sharply--in large part because of increases in import prices--and the trade balance slipped back into deficit after having been in small surplus in April. However, the average deficit for the 2 months was substantially below that in the first quarter of 1973, which in turn was much lower than the deficit in the fourth quarter of 1972.

Since the June 18-19 meeting of the Committee, the exchange rate for the dollar had declined sharply further against those continental currencies that were floating jointly against the dollar; the decline had been most severe in the 2 weeks after June 26--when the U.S. trade deficit for May was announced--and in the week ending July 6 trading was characterized by large and erratic movements in rates. Subsequently, the dollar recovered somewhat on the basis of market expectations of official intervention to support the dollar. On July 10 the System announced that its swap arrangements with other central banks had been increased by substantial amounts. Throughout the period, the dollar had been firm against the currencies of Canada, the United Kingdom, and Japan--countries that account for the bulk of U.S. foreign trade.

At U.S. commercial banks, both total loans and holdings of securities changed little in June after having expanded sharply in May, as indicated by data for the last Wednesday of each month; over the 2 months the average rate of growth was relatively high. The rate of expansion in business loans in June, although substantial, was well below that earlier in the year. Banks raised the prime rate applicable to large corporations from 7-1/2 per cent in early June to 8-1/4 per cent by early July.

Growth in the narrowly defined money stock (M_1),[1/] which had accelerated in April and May, stepped up somewhat further in June. Although inflows of time and savings deposits other than large-denomination CD's slackened, growth in the broadly defined money stock (M_2)[2/] remained at the relatively high rate recorded in May. Expansion in the outstanding volume of large-denomination CD's slowed sharply, but growth in the bank credit proxy[3/] remained relatively fast. Over the first half of the year, M_1, M_2, and the proxy grew at annual rates of around 6, 7.5, and 14 per cent, respectively.[4/]

1/ Private demand deposits plus currency in circulation.

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

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

4/ Growth rates cited are calculated on the basis of the daily-average level in the last month of the period relative to that in the last month preceding the period.

Inflows of savings to nonbank thrift institutions, which had picked up in May, remained relatively strong in June, despite continuing advances in market interest rates. In early July, ceilings were removed from interest rates on consumer-type time deposits of at least $1,000 having maturities of 4 years or more--at commercial banks as well as at nonbank thrift institutions. At the same time maximum rates that could be paid on time and savings deposits with shorter maturities were raised. Mortgage interest rates generally continued to rise.

System open market operations since the meeting on June 18-19 had been guided by the Committee's decision to seek bank reserve and money market conditions consistent with somewhat slower growth in monetary aggregates over the months immediately ahead than appeared to be indicated for the first half of the year. Operations had been directed toward fostering growth in reserves available to support private nonbank deposits (RPD's) at an annual rate in a range of 8 to 11.5 per cent in the June-July period, while avoiding unduly sharp changes in money market conditions.

Soon after the June meeting, available data suggested that in the June-July period RPD's would grow at an annual rate above the range that the Committee had specified and that M_1

would grow at a rate in excess of an acceptable range. Data that became available after the July 4 holiday continued to suggest excessive strength in RPD's and the monetary aggregates in the June-July period, even though money market conditions had continued to tighten, and on Friday, July 6, a majority of Committee members concurred in a recommendation by the Chairman that money market conditions should be permitted to tighten to a greater extent than had been contemplated at the June meeting. The Federal funds rate, which had been about 8-3/4 per cent in the days before the June meeting, was close to 9-3/4 per cent during most of the week preceding this meeting, and in the last few days it had risen further. In the 4 weeks ending July 11, member bank borrowings averaged about \$1,965 million, up from about \$1,855 million in the preceding 5 weeks.

As money market conditions continued to firm in the inter-meeting period and private credit demands remained strong, short-term interest rates rose sharply further--in general to levels close to or above the peaks of late 1969 and early 1970. Other policy actions also affected market attitudes and developments. On June 29 reserve requirements on all but the first \$2 million of net demand deposits at member banks were increased by 1/2 percentage point, applicable to average deposits in the week beginning July 5, and Federal Reserve discount rates were raised 1/2 percentage point, to 7 per cent, effective July 2.

The market rate on 3-month Treasury bills rose from 7.20 per cent on the day before the June meeting to a peak of 7.98 per cent in early July, and on the day before this meeting it was 7.85 per cent. Over the whole period, increases in rates on bank CD's and other private instruments were larger than those for Treasury bills.

In long-term markets, interest rates in general advanced considerably, despite continuation of moderate demands for funds in the capital markets. Although the over-all volume of new public offerings of corporate and of State and local government bonds rose somewhat in June, the volume for the second quarter as a whole was low for that season of the year, and a moderate decline was in prospect for July.

The Treasury was expected to announce on July 25 the terms of its mid-August refunding. Of the maturing issues, $4.5 billion were held by the public.

The Committee agreed that the economic situation and prospects called for slower growth in monetary aggregates over the months immediately ahead than had occurred on average in the first half of the year. A staff analysis suggested that expansion in the demand for money was likely to slow considerably from the high rate recorded in the second quarter--in response to the anticipated moderation in GNP growth and to the sharp rise in short-term interest rates that had occurred in recent months. Because of the rise in short-term market rates, moreover, net expansion in consumer-type time and savings deposits at commercial banks was expected to slow appreciably despite the increase in rate ceilings announced in early July. As a consequence, it was anticipated that banks would attempt to expand the outstanding volume of large-denomination CD's; the increase in these issues in the July-August period was expected to remain relatively large.

The staff analysis suggested that a relatively rapid rate of growth in RPD's in the July-August period--at an annual rate in a range of 11-1/2 to 13-1/2 per cent--would be consistent with slower growth in the monetary aggregates over the months immediately ahead than had occurred in the first half of the year. The analysis also suggested that such a rate of growth in RPD's might be associated with little change in money market conditions but that short- and long-term market interest rates in general might be subject to additional upward pressures in further adjustment to the firming in money market conditions that had occurred in recent weeks.

The Committee decided that operations should be directed at fostering RPD growth during the July-August period at an annual rate within a range of 11-1/2 to 13-1/2 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, including recent developments in industrial production, employment, and retail sales, suggests that growth in economic activity moderated in the second quarter from the exceptionally rapid pace of the two preceding quarters. Increases in employment were relatively substantial, however, and in June the unemployment rate dropped below 5 per cent. Wage rates advanced at a faster pace during the second quarter than earlier in the year. In the months immediately preceding the price freeze imposed in mid-June, the rise in prices of both industrial commodities and farm and food products remained extraordinarily rapid.
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> The U.S. merchandise trade balance worsened in May as import prices rose sharply further, but the trade deficit remained well below the first-quarter average. In foreign exchange markets, the jointly floating continental European currencies rose sharply further against the dollar in early July. After the first week in July, the dollar recovered somewhat on the basis of market expectations of official intervention. On July 10 the Federal Reserve announced substantial increases in its swap arrangements with other central banks.

Both the narrowly and more broadly defined money stock rose sharply in May and June, although inflows of consumer-type time and savings deposits slackened somewhat in the latter month. Expansion in bank credit continued at a substantial pace. Since mid-June both short- and long-term market interest rates have advanced considerably further, with the sharpest increases in the short-term sector. On June 29 increases were announced in Federal Reserve discount rates, from 6-1/2 to 7 per cent, and in member bank reserve requirements; on July 5 ceiling interest rates were increased on time and savings deposits at commercial banks and other thrift institutions.

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 more sustainable rate of advance in economic activity, and progress toward equilibrium in the country's balance of payments.

To implement this policy, while taking account of international and domestic financial market developments and the forthcoming Treasury financing, the Committee seeks to achieve bank reserve and money market conditions consistent with slower growth in monetary aggregates over the months immediately ahead than occurred on average in the first half of the year.

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

Absent and not voting: Mr. Mitchell.

Mr. Francis dissented from this action not because he disagreed with the objectives of the policy adopted by the Committee but because he believed that--as had proved to be the case following other recent meetings--the objectives would not be achieved because of the constraint on money market conditions.

Subsequent to the meeting it appeared that in the July-August period the annual rate of growth in RPD's and in the monetary aggregates might exceed acceptable ranges, even though money market conditions had continued to tighten. On August 3, 1973, the available members--with the exception of Messrs. Bucher and Sheehan--concurred in a recommendation by the Chairman that money market conditions should be permitted to tighten still further if necessary to limit growth in RPD's.