FEDERAL RESERVE

press release

For immediate release June 17, 1974

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 March 18-19, 1974.

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 March 18-19, 1974[1/]

1. Domestic policy directive

The information reviewed at this meeting continued to suggest that real output of goods and services, which had grown at an annual rate of about 1.5 per cent in the fourth quarter of 1973, was declining in the first quarter of this year--in large part because of the oil situation--and that the GNP implicit deflator was still rising at a rapid rate. Staff projections, like those of 4 weeks earlier, suggested that real output would change little in the second quarter and that the rise in prices would remain rapid.

In February industrial production receded for the third consecutive month, as output of automobiles and auto parts and of nondurable consumer goods declined while output of business equipment changed little. Employment in durable goods manufacturing also continued to decline, but total nonfarm employment rose appreciably, returning to the peak reached in November 1973. The rate of unemployment--which had risen from a recent low of

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1/ This meeting was held over a 2-day period, beginning on the afternoon of March 18, in order to permit the Committee to review its continuing authorizations and directives without infringing on the time available for its deliberations on current monetary policy.

4.6 per cent in October to 5.2 per cent in January--was unchanged in February. Retail sales fell, reflecting decreases in sales at automobile dealerships and gasoline service stations; total retail sales for the month were slightly below the monthly average for the fourth quarter of 1973.

Wholesale prices of farm and food products and of industrial commodities rose sharply in February, although at a lesser rate than in the preceding 2 months. Price increases continued to be widespread among industrial commodities and were especially large for fuels, metals, and nonmetallic minerals. In January the consumer price index had risen substantially further, with much of the rise being caused by steep increases in retail prices of foods and fuels. In the first 2 months of the year, advances in the index of average hourly earnings of production workers on nonfarm payrolls moderated from the rapid pace in the second half of 1973.

Staff projections suggested that termination of the Arab embargo on oil shipments to the United States--reported on March 18--would have no more than a marginally expansive impact on over-all real output until the summer, although it might strengthen the automobile and housing markets promptly. Expectations for the second quarter were that expansion in business fixed investment would remain relatively strong; that growth in government purchases of goods and services would continue at a substantial rate; and that the rise in personal consumption expenditures would pick up somewhat as demands for domestic-type automobiles--which had fallen sharply in the autumn and winter months--strengthened. It was also anticipated, however, that residential construction outlays--which lag behind starts for new housing units--would decline appreciably further and that investment in business inventories would not be so large as in the two preceding quarters.

In foreign exchange markets the dollar depreciated against leading foreign currencies during the first 3 weeks of February and then changed little through mid-March, at an average level still well above that of October 1973. Moreover, the U.S. balance of payments on the official settlements basis appeared to have shifted from a substantial surplus in January to a deficit in February. In January the U.S. merchandise trade surplus--although down somewhat from December--remained large, with exports expanding almost as much as imports; a significant part of the rise in the value of imports was attributable to a sharp increase in the cost of imported petroleum products.

Growth in total loans and investments at U.S. commercial banks remained rapid in February; while expansion in most major types of loans slowed appreciably, banks' holdings of Treasury securities and loans to securities dealers rose sharply. Although businesses continued to increase their short-term borrowing at a rapid pace, they raised a large share of these funds in the commercial paper market where rates were favorable relative to effective rates on bank loans. In late February most banks reduced the prime rate applicable to large corporations from 9 to 8-3/4 per cent.

The narrowly defined money stock (M_1),2/ after having declined in January, expanded substantially in February in association with an unusually large decline in U.S. Government deposits. Rapid expansion in M_1 continued in early March. Net inflows of time and savings deposits other than large-denomination CD's remained relatively strong in February, and growth in the more broadly defined money stock (M_2)3/ accelerated to a high rate. However, the bank credit proxy4/ rose little; the large increases in private demand deposits and in consumer-type time and savings deposits were almost offset by the extraordinary decline in U.S. Government deposits and a slowing down--as compared with January--of growth in the outstanding volume of large-denomination CD's.

2/ Private demand deposits plus currency in circulation.

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

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

Net deposit inflows at nonbank thrift institutions in February, as in January, remained near the improved rate of the final months of 1973. Growth in the measure of the money stock that includes such deposits (M_3)[5/]--like growth in M_2--accelerated to a high rate. Contract interest rates on conventional mortgages declined further between early February and early March.

System open market operations since the February 20 meeting had been guided by the Committee's decision to seek bank reserve and money market conditions consistent with moderate growth in the monetary aggregates over the months ahead, while taking account of international and domestic financial market developments. Toward the end of February, incoming data suggested that in the February-March period growth in M_1 would exceed the range of tolerance specified by the Committee and that growth in M_2 and in reserves available to support private demand deposits (RPD's) would about equal the upper limits of their specified ranges. Such behavior ordinarily would have led to more restrictive reserve-supplying operations and a rise in the Federal funds rate toward the upper limit of its range of tolerance--namely, 9-1/2 per cent. On March 1, however, a majority of the available Committee members concurred in the Chairman's recommendation that, in light of the marked rise in short-term interest rates

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5/ M_2 plus time and savings deposits at mutual savings banks and at savings and loan associations.

that had occurred since the February meeting and of the highly sensitive state of the financial markets, reserve-supplying operations for the time being should be conducted in a manner expected to be consistent with maintenance of the Federal funds rate at about the 9 per cent level that had prevailed over the preceding 3 weeks.

Ten days later, in response to evidence that strong growth in the monetary aggregates was persisting, a majority of the available members concurred in the Chairman's recommendation that reserve-supplying operations should be conducted in a manner consistent with the range of tolerance for the Federal funds rate that had been agreed upon at the February meeting--although, in light of recent increases in market interest rates and the sensitive state of financial markets, the Account Manager was instructed to proceed very cautiously in operations thought likely to be consistent with a rise in the weekly average Federal funds rate above 9 per cent. In mid-March, just before this meeting, the Federal funds rate was in a range of 9-1/4 to 9-1/2 per cent; member bank borrowings averaged around $1,130 million in the 4 weeks ending March 13, almost the same as in the preceding 4 weeks.

Short-term market interest rates, which had fallen irregularly for more than 2 months, rose appreciably in the period between the

Committee's meeting on February 20 and this meeting--in large part because the Federal funds rate did not decline further as market participants had expected and because short-term credit demands remained strong. Rates advanced more for Treasury bills than for other short-term instruments, under the influence of the following: an increase in dealers' costs of financing inventories, System sales of bills to offset the reserve-supplying effects of the large reduction in U.S. Government deposits at Federal Reserve Banks, and Treasury issuance of a tax-anticipation bill for new cash. At the time of this meeting the market rate on 3-month Treasury bills was 7.95 per cent, up from 7.03 per cent on the day before the February meeting.

Yields on long-term securities, like those on short-term issues, rose appreciably in the inter-meeting period, as capital market financing remained heavy and as dealers--who had been holding substantial inventories in anticipation of continuing declines in yields--reduced their inventories when yields turned up. The over-all volume of new public offerings of corporate and State and local government bonds--although down moderately--was still relatively large in February, and a substantial increase in the volume was in prospect for March.

The Treasury planned to announce shortly a cash offering of securities amounting to $4 billion. The offering was expected to include short-term notes as well as tax-anticipation bills.

The Committee concluded that the economic situation and outlook continued to call for moderate growth in monetary aggregates over the longer run; therefore, in view of the rapid monetary expansion recently, it would seek to moderate growth in monetary aggregates over the months ahead. According to a staff analysis, pursuit of that objective would be likely to entail a further tightening of bank reserve and money market conditions in the near term and some further increases in interest rates in general. Upward pressures on interest rates might well be intensified in the weeks ahead as the market absorbed the large Treasury financing in prospect. The analysis also noted, however, that estimates of the likely strength of money demands over the spring and summer and of the relationships between monetary growth rates and market interest rates were subject to larger margins of error than usual because of the greater uncertainty attached to projections of nominal GNP and because of the difficulties of assessing how borrowers, lenders, and savers would react to the recent and prospective rates of inflation.

The staff analysis suggested that, even with the contemplated firming of bank reserve and money market conditions, expansion in M_1 would be relatively large over the March-April period, partly as a consequence of the sizable increase that had taken place in early March. Although net inflows of consumer-type time and savings deposits to banks and nonbank thrift institutions were expected to recede in response to the increases in market rates of interest, growth in M_2 also was expected to be relatively high. Thus, ranges of tolerance for the March-April period of 6-1/2 to 8-1/2 per cent and 7-3/4 to 9-3/4 per cent for M_1 and M_2, respectively, might be consistent with achievement of the Committee's longer-run objectives for the monetary aggregates.

Taking account of the staff analysis, the Committee concluded that progress toward its objective of moderating monetary growth could be achieved even with rates of expansion in the aggregates over the March-April period that were temporarily above those desired for the longer term. Accordingly, the members found the upper limits of the 2-month ranges of tolerance noted above to be acceptable. In view of the recent high rate of monetary growth, however, they agreed that the lower limits of those ranges should be reduced somewhat, so as to permit more rapid progress toward moderate monetary growth, should the growth rates in the aggregates in the period immediately ahead appear to be falling short of present expectations. Specifically, for the March-April period the Committee adopted ranges of tolerance of 5-1/2 to 8-1/2 per cent and of 6-3/4 to 9-3/4 per cent for the annual rates of growth in M_1 and M_2, respectively. The members agreed that rates of growth within those ranges would be likely to involve RPD growth during the same period at an annual rate within a 4 to 7 per cent range of tolerance, and they decided that in the period until the next meeting the weekly average Federal funds rate might be permitted to vary in an orderly fashion from as low as 9 per cent to as high as 10-1/2 per cent, if necessary, in the course of operations.

The members also agreed that, in the conduct of operations, account should be taken of international and domestic financial market developments, including the prospective Treasury financing. 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 suggests that real output of goods and services is declining in the current quarter, in large part because of the oil situation, and that prices are continuing to rise rapidly. In February industrial production and manufacturing employment declined again, while total nonfarm payroll employment recovered, and the unemployment rate was unchanged at 5.2 per cent. Prices of farm and food products and industrial commodities increased sharply, although less so than in the preceding 2 months. Increases in wage rates appear to have moderated in recent months.

After depreciating during the first 3 weeks of February, the dollar has since shown little net change against leading foreign currencies. The U.S. trade surplus remained large in January, despite a further sharp rise in the cost of petroleum imports.

The narrowly defined money stock, after having declined in January, increased sharply in February and early March. Broader measures of the money stock rose substantially in February, as net inflows of consumer-type time deposits remained relatively strong. Business short-term borrowing at banks and in the open market has continued at a rapid pace. Following earlier declines, both short- and long-term market interest rates have risen appreciably in recent weeks.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to resisting inflationary pressures, supporting a resumption of real economic growth, and maintaining equilibrium in the country's balance of payments.

To implement this policy, while taking account of international and domestic financial market developments, including the prospective Treasury financing, the Committee seeks to achieve bank reserve and money market conditions that would moderate growth in monetary aggregates over the months ahead.

Votes for this action: Messrs. Burns, Hayes, Black, Brimmer, Bucher, Clay, Holland, Kimbrel, Mitchell, Sheehan, Wallich, and Winn. Votes against this action: None.

2. Review of continuing authorizations

This being the first meeting of the Federal Open Market Committee following the election of new members from the Federal Reserve Banks to serve for the year beginning March 1, 1974, and their assumption of duties, the Committee followed its customary practice of reviewing all of its continuing authorizations and directives. Certain amendments made to the authorization for domestic open market operations and the authorization for foreign currency operations are reported in succeeding sections of this record. Except for the changes resulting from those amendments, the Committee reaffirmed the two authorizations, and also the foreign currency directive, in their existing form.

Votes for these actions: Messrs. Burns, Hayes, Black, Brimmer, Bucher, Clay, Holland, Kimbrel, Mitchell, Sheehan, Wallich, and Winn. Votes against these actions: None.

Paragraph 2 of the authorization for domestic open market operations authorizes the Federal Reserve Bank of New York (and, under certain circumstances, other Reserve Banks) to purchase short-term certificates of indebtedness directly from the Treasury, subject to certain conditions. This authorization is, in turn, based on a provision of Section 14(b) of the Federal Reserve Act authorizing the Federal Reserve Banks to buy and sell obligations of specified types "directly from or to the United States," subject to certain conditions. It was noted at this meeting that, because the statutory authority in question had expired on November 1, 1973, paragraph 2 of the authorization had been in a state of _de facto_ suspension since then, and that the paragraph would remain in suspension until pending legislation to extend the authority was enacted.

The Committee also took special note of paragraph 3 of the domestic authorization, which authorizes the Reserve Banks to engage in lending of U.S. Government securities held in the System Open Market Account under such instructions as the Committee might specify from time to time. That paragraph had been added to the authorization on October 7, 1969, on the basis of a judgment by the Committee that in the existing circumstances such lending of securities was reasonably necessary to the effective conduct of open market operations and to the effectuation of open market policies, and on the understanding that the authorization would be reviewed periodically. At this meeting the Committee concurred in the judgment of the Manager that the lending activity in question remained reasonably necessary and that, accordingly, the authorization should remain in effect subject to periodic review.

3. Amendments to authorization for domestic open market operations

On the recommendation of the System Account Manager, the Committee amended paragraph 1(a) of the authorization for domestic open market operations to raise from $2 billion to $3 billion the limit on changes between Committee meetings in System Account holdings of U.S. Government and Federal agency securities, effective March 18, 1974. The Manager noted that there had been a marked increase in recent years in the maximum net variation in System Account holdings between meeting dates as a result mainly of increased variation in market factors affecting reserves, and that in 3 of the past 12 inter-meeting periods the Committee had found it necessary to authorize temporary increases in the limit to $3 billion. The Committee concurred in the Manager's view that a permanent increase would be appropriate at this time.

The Committee also approved two clarifying changes in the language of paragraph 1(a) recommended by the Manager, effective March 18, 1974. One of these, which involved the insertion of a parenthetical phrase reading "including forward commitments" in the statement regarding changes in System Account holdings between meeting dates, was intended to make it clear that, for purpose of the limit, holdings were to be calculated on a "commitment" basis. A similar phrase had been included in the corresponding statement prior to March 1964. At that time the Committee had approved an amendment to the clause for the purpose of clarifying the language in certain other respects, and in transcribing the new language the reference to forward commitments was inadvertently omitted.

The second clarifying change, which involved the addition of the phrase "including securities of the Federal Financing Bank" in the first sentence of paragraph 1(a), was intended to make it clear that securities of that Bank, when issued, would be treated in System open market operations in the same manner as Treasury securities. The Federal Financing Bank, which had been established by legislation enacted late in 1973 for the purpose of consolidating the financing of a variety of Federal agencies and of other borrowers whose obligations are guaranteed by the Federal Government, was expected to commence operations soon. Under the terms of the legislation, the obligations of the Bank would be obligations of the United States.

Votes for these actions: Messrs. Burns, Hayes, Black, Brimmer, Bucher, Clay, Holland, Kimbrel, Mitchell, Sheehan, Wallich, and Winn. Votes against these actions: None.

On the basis of recommendations by a staff committee appointed to study System operations in bankers' acceptances, the Committee amended paragraph 1(b) of the domestic authorization, which relates to open market purchases and sales of acceptances, and the part of paragraph 1(c), governing repurchase agreements, which relates to repurchase agreements in acceptances, effective April 1, 1974. Prior to this action the domestic authorization had authorized System operations in prime bankers' acceptances "of the kinds designated in the Regulation of the Federal

Open Market Committee."[6/] One purpose of the amendments was to incorporate the rules governing System operations in bankers' acceptances directly in the Committee's domestic authorization. A second purpose was to modernize those rules by removing outdated provisions and broadening somewhat the scope of bankers' acceptances eligible for purchase by the System. The new rules broadened the types of acceptances eligible for purchase by eliminating the requirement that banks have in their possession shipping documents conveying or securing title at the time they accept drafts covering the shipment of goods in the United States; by increasing from 6 to 9 months the maximum maturity of acceptances eligible for purchase; and by authorizing the purchase of acceptances that finance the storage in the United States of any goods, rather than "readily marketable staples." Dollar exchange bills, a type of instrument that is seldom used, were eliminated from the list of acceptances authorized for purchase. No major change in System operations in bankers' acceptances was expected to result from these amendments.

One further amendment to paragraph 1(b) was made simply to remove unnecessary wording. Previous language specifying

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6/ The Committee's Regulation, in turn, had authorized operations in acceptances of the kinds made eligible for purchase by the Reserve Banks under the Board of Governors' Regulation B. In companion actions, also effective April 1, 1974, the Board of Governors rescinded its Regulation B and the Committee amended its Regulation to delete the reference to Regulation B. Notice of these regulatory actions was published in the Federal Register for April 1, 1974.

that aggregate holdings of bankers' acceptances should not exceed the lower of two figures--$125 million, or 10 per cent of the total volume of acceptances outstanding--was replaced by language specifying a single limit of $125 million. The 10 per cent limitation no longer served a useful purpose since the volume of outstanding acceptances had grown to a level in excess of $8 billion.

> Votes for these actions: Messrs. Burns, Hayes, Black, Brimmer, Bucher, Clay, Holland, Kimbrel, Mitchell, Sheehan, Wallich, and Winn. Votes against these actions: None.

In connection with the foregoing actions, the Committee instructed the staff committee to conduct further studies of the desirability of expanding System open market operations in bankers' acceptances to encompass all types of prime acceptances, including finance bills.

Reflecting the amendments to paragraphs 1(a), 1(b), and 1(c), the authorization for domestic open market operations read as follows:

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, to the extent necessary to carry out the most recent domestic policy directive adopted at a meeting of the Committee:

   (a) To buy or sell U.S. Government securities, including securities of the Federal Financing Bank, and securities that are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States in the open market, from or to securities dealers and foreign and international accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the System Open Market Account at market prices, and, for such Account, to exchange maturing U.S. Government and Federal agency securities with the Treasury or the individual agencies or to allow them to mature without replacement; provided that the aggregate amount of U.S. Government and Federal agency securities held in such Account (including forward commitments) at the close of business on the day of a meeting of the Committee at which action is taken with respect to a domestic policy directive shall not be increased or decreased by more than $3.0 billion during the period commencing with the opening of business on the day following such meeting and ending with the close of business on the day of the next such meeting;

(b) To buy or sell in the open market, from or to acceptance dealers and foreign accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the account of the Federal Reserve Bank of New York at market discount rates, prime bankers' acceptances with maturities of up to nine months at the time of acceptance that (1) arise out of the current shipment of goods between countries or within the United States, or (2) arise out of the storage within the United States of goods under contract of sale or expected to move into the channels of trade within a reasonable time and that are secured throughout their life by a warehouse receipt or similar document conveying title to the underlying goods; provided that the aggregate amount of bankers' acceptances held at any one time shall not exceed $125 million;

(c) To buy U.S. Government securities, obligations that are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States, and prime bankers' acceptances of the types authorized for purchase under 1(b) above, from nonbank dealers for the account of the Federal Reserve Bank of New York under agreements for repurchase of such securities, obligations, or acceptances in 15 calendar days or less, at rates that, unless otherwise expressly authorized by the Committee, shall be determined by competitive bidding, after applying reasonable limitations on the volume of agreements with individual dealers; provided that in the event Government securities or agency issues covered by any such agreement are not repurchased by the dealer pursuant to the agreement or a renewal thereof, they shall be sold in the market or transferred to the System Open Market Account; and provided further that in the event bankers' acceptances covered by any such agreement are not repurchased by the seller, they shall continue to be held by the Federal Reserve Bank or shall be sold in the open market.

2. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, or, if the New York Reserve Bank is closed, any other Federal Reserve Bank, to purchase directly from the Treasury for its own account (with discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury; provided that the rate charged on such certificates shall be a rate 1/4 of 1 per cent below the discount rate of the Federal Reserve Bank of New York at the time of such purchases, and provided further that the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed $1 billion.

3. In order to insure the effective conduct of open market operations, the Federal Open Market Committee authorizes and directs the Federal Reserve Banks to lend U.S. Government securities held in the System Open Market Account to Government securities dealers and to banks participating in Government securities clearing arrangements conducted through a Federal Reserve Bank, under such instructions as the Committee may specify from time to time.

4. <u>Authorization for foreign currency operations</u>

The Committee approved an increase from $2 billion to $3 billion in the System's swap arrangement with the Bank of England and the corresponding amendment to paragraph 2 of the authorization for foreign currency operations, effective March 26, 1974. With this change, paragraph 2 of the authorization read as follows:

> The Federal Open Market Committee directs the Federal Reserve Bank of New York to maintain reciprocal currency arrangements ("swap" arrangements) for the System Open Market Account for periods up to a maximum of 12 months with the following foreign banks, which are among those designated by the Board of Governors of the Federal Reserve System under Section 214.5 of Regulation N, Relations with Foreign Banks and Bankers, and with the approval of the Committee to renew such arrangements on maturity:

Foreign bank	Amount of arrangement (millions of dollars equivalent)
Austrian National Bank	250
National Bank of Belgium	1,000
Bank of Canada	2,000
National Bank of Denmark	250
Bank of England	3,000
Bank of France	2,000
German Federal Bank	2,000
Bank of Italy	3,000
Bank of Japan	2,000
Bank of Mexico	180
Netherlands Bank	500
Bank of Norway	250
Bank of Sweden	300
Swiss National Bank	1,400
Bank for International Settlements:	
Dollars against Swiss francs	600
Dollars against other European currencies	1,250

Votes for this action: Messrs. Burns, Hayes, Black, Brimmer, Bucher, Clay, Holland, Kimbrel, Mitchell, Sheehan, Wallich, and Winn. Votes against this action: None.

This action was taken after consultation with the U.S. Treasury. It was expected to contribute to international monetary stability by expanding the facilities available for coping with possible temporary pressures on sterling arising from short-run fluctuations in international payments flows.