FEDERAL RESERVE
press release

For immediate release January 13, 1975

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 October 14-15, 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 October 14-15, 1974[1/]

1. Domestic policy directive

The information reviewed at this meeting suggested that real output of goods and services--which had fallen at an annual rate of about 4.5 per cent in the first half of the year--declined somewhat further in the third quarter and that both prices and wage rates were continuing to rise at a rapid pace. Staff projections suggested that contraction in real economic activity would persist in the fourth quarter of the year and in the first half of 1975 and that the rate of increase in prices would remain rapid, although not so rapid as in the first three quarters of this year.

In September industrial production rose somewhat, for the most part as a result of settlements of work stoppages that had accounted for much of the August reduction in output, and total nonfarm payroll employment changed little. However, the unemployment rate rose from 5.4 to 5.8 per cent, reflecting an upsurge in the labor force following 10 months of slow growth. According to the advance report, retail sales declined

1/ This meeting began on the afternoon of October 14 and continued on the following morning.

in September, mainly because of decreases in sales of automobiles --after introduction of the higher-priced 1975 models--and of other consumer durable goods.

The rise in wholesale prices of industrial commodities moderated in September--although increases still were widespread and substantial--and prices of farm and food products declined moderately after having risen sharply in July and August. The index of average hourly earnings for private nonfarm production workers continued to advance at a rapid pace. In August the consumer price index had increased substantially further.

On October 8 the President recommended a program to combat inflation and to mitigate the impact of monetary and fiscal restraint on certain sectors of the economy. The proposals included a tax surcharge on corporate income and on personal incomes in the middle and upper levels; an expanded public service employment program; extended unemployment benefits; an enlarged program to improve the availability of funds for mortgages on new houses; and an increase in the investment tax credit on outlays for new production facilities. The President also indicated support for pending tax reform legislation, which included some reductions in taxes on lower incomes. The tax and expenditure measures would, on balance, have approximately a neutral effect on the size of the Federal deficit. Earlier, a Council on Wage and Price Stability had been established to monitor wage and price increases.

Staff projections for the fourth quarter of 1974 and the first half of 1975 suggested that the decline in residential construction activity would be larger and that the expansion in personal consumption expenditures would be smaller than indicated by the projections of 5 weeks earlier. As before, it appeared likely that the rise in both disposable income and personal consumption expenditures would be little, if any, greater than the increase in prices. It was still expected that the expansion in business fixed investment would taper off and that the pace of business inventory investment would moderate.

The exchange rate for the dollar against leading foreign currencies had declined since early September, after having risen persistently since May. In August the U.S. merchandise trade deficit had increased substantially further, reflecting increases in imports of petroleum and industrial materials; total exports had changed little, although exports of corn and some other agricultural commodities had declined.

Total loans and investments at U.S. commercial banks declined in September, and growth in bank credit over the third quarter was relatively slow. In September loans to security dealers dropped, and banks reduced their holdings of Treasury securities by a substantial amount. Expansion in total short-term and in long-term business credit slackened, and in part because some business borrowers shifted their short-term credit demands to the commercial paper market in response to declines in rates in that market, outstanding business loans at banks changed little. In early October banks reduced the prime rate applicable to large corporations from 12 per cent to 11-3/4 per cent.

The narrowly defined money stock (M_1)[2/] rose slightly in September; over the third quarter it grew at an annual rate of about 2 per cent, compared with a rate of 6 per cent in the first half of the year.[3/] Net inflows to banks of time and savings deposits other than large-denomination CD's were small in September, and deposit experience at nonbank thrift institutions remained weak. Consequently, the more broadly defined measures of the money stock (M_2[4/] and M_3[5/]) also increased only a little.

2/ Private demand deposits plus currency in circulation.

3/ 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.

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

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

System open market operations since the September meeting had been guided by the Committee's decision to seek bank reserve and money market conditions consistent with moderate growth in monetary aggregates over the months ahead, while taking account of developments in domestic and international financial markets. Data that had become available a few days after that meeting suggested that in the September-October period M_1 and M_2 would grow at annual rates slightly below the lower limits of the ranges of tolerance that had been specified by the Committee. Accordingly, System operations had been directed toward some easing in bank reserve and money market conditions, although in the early part of the inter-meeting period such operations had been undertaken cautiously in order to avoid encouraging an unduly rapid decline in market interest rates.

In early October the available data continued to suggest that in the September-October period the annual rates of growth in the monetary aggregates would be below the specified ranges of tolerance. The Federal funds rate--which had been about 11-3/4 per cent at the time of the September meeting--was fluctuating around 11 per cent, 1/2 percentage point above the lower limit of its specified range, and the System Account Manager was endeavoring to supply reserves at a rate consistent with some further easing in money market conditions. A majority of the members concurred in the Chairman's recommendation of October 3 that, in order to provide operating flexibility in the event of evidence of further weakening in the behavior of the aggregates, the lower limit of the funds rate constraint be reduced by 1/4 percentage point, to 10-1/4 per cent, for the period remaining until the next Committee meeting. In the statement week ending October 9, the average funds rate was slightly below 10-1/2 per cent.

Short-term market interest rates had declined considerably in the period since the Committee's meeting on September 10, in response to the continuing decline in the Federal funds rate and in anticipation of further easing in money and credit market conditions. On the last market day before this meeting the rate on 3-month Treasury bills was 7.63 per cent, down from a market rate of 9.15 per cent on the day before the September meeting.

Yields on long-term Treasury and State and local government bonds declined moderately over the inter-meeting period, but yields on long-term corporate securities rose somewhat further, on balance, as public offerings of corporate bonds--which had declined substantially in September--were expected to rise sharply in October. Contract interest rates on new commitments for conventional mortgages in the primary market also rose further between early September and early October, but yields on commitments in the secondary market for Federally underwritten mortgages eased a little.

The Treasury was expected to announce on October 30 the terms of its mid-November refunding. Of the maturing issues, $4.3 billion were held by the public.

The Committee concluded that the economic situation and outlook called for a resumption of moderate growth in the monetary aggregates over the longer run. A staff analysis suggested that--although monetary growth apparently remained sluggish in October--demand for money would pick up in the remaining months of the year, in part as a result of the lagged effects of recent interest rate declines. Nevertheless, it appeared likely that if M_1 were to grow at a rate consistent with the Committee's longer-run objectives for the monetary aggregates, money market conditions would have to ease somewhat further in the period immediately ahead. Such easing would probably lead to additional declines in other market interest rates, although the strong over-all credit demands expected over the next few weeks would tend to moderate such declines.

The staff analysis suggested that some improvement in flows of savings at both banks and nonbank thrift institutions could be expected to develop as short-term interest rates declined further. Demands for bank credit appeared likely to be moderate.

In view of the sluggish monetary growth since midyear, the Committee decided that the tolerance ranges specified for rates of expansion in the monetary aggregates over the October-November period should be wide enough to accommodate somewhat higher growth rates, if they should develop, than those presently thought to be consistent with the money market conditions contemplated. Specifically, for the October-November period the members adopted ranges of tolerance of 4-3/4 to 7-1/4 and 5-3/4 to 8-1/4 per cent for the annual rates of growth in M_1 and M_2, respectively, and they agreed that such growth rates would be likely to involve growth in reserves available to support private nonbank deposits (RPD's) within a range of 5-1/2 to 8 per cent. The members also decided that in the period until the next meeting the weekly average Federal funds rate 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. It was understood that during the inter-meeting period the weekly average funds rate would be permitted to decline gradually to about the midpoint of the specified range so long as the monetary aggregates did not appear to be growing at rates at or above the upper limits of their specified ranges.

The members also agreed that, in the conduct of operations, account should be taken of the forthcoming Treasury financing and of developments in domestic and international financial markets. 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 declined somewhat further in the third quarter and that price and wage increases continued large. In September industrial production increased somewhat, reflecting settlement of work stoppages that had reduced output in August. An upsurge in the labor force, following several months of relatively slow growth, raised the unemployment rate from 5.4 to 5.8 per cent. The rise in wholesale prices of industrial commodities moderated, although it remained substantial, and prices of farm products and foods declined after having increased sharply in July and August.

On October 8 the President recommended a program to combat inflation and to mitigate the impact of monetary and fiscal restraint on certain sectors of the economy. The tax and expenditure proposals included in the program would, on balance, have approximately a neutral effect on the size of the Federal deficit.

In recent weeks the dollar has declined against leading foreign currencies. The U.S. foreign trade deficit increased substantially in August, as imports of petroleum and industrial materials rose while exports held steady.

The narrowly defined money stock rose slightly in September and grew at an annual rate of about 2 per cent over the third quarter, compared with a rate of 6 per cent in the first half of the year. The money supply measure more broadly defined to include bank time and savings deposits other than money market CD's--as well as the measure that includes deposits at other thrift institutions--also rose only slightly in September. Over-all business credit demands slackened last month, and outstanding business loans at banks leveled off. Since early September interest rates on short-term market instruments have fallen considerably, while yields on Treasury and State and local government bonds have declined modestly. Yields on corporate bonds have risen somewhat further, on balance, reflecting the large volume of offerings in prospect.

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 achieving equilibrium in the country's balance of payments.

To implement this policy, while taking account of the forthcoming Treasury financing and of developments in domestic and international financial markets, the Committee seeks to achieve bank reserve and money market conditions consistent with resumption of moderate growth in monetary aggregates over the months ahead.

Votes for this action: Messrs. Burns, Hayes, Black, Bucher, Holland, Kimbrel, Mitchell, Sheehan, Wallich, and Winn. Vote against this action: Mr. Clay.

Mr. Clay, who dissented from this action, expressed the opinion that the recent shortfalls in growth of M_1 were not due entirely to the weakness in economic activity but were, at least in part, a lagged response to the high levels of short-term interest rates prevailing in the spring. He believed that monetary growth was likely to pick up, and he was concerned about the possibility of provoking a growth rate that was too rapid.

Subsequent to this meeting, on October 31, the available data suggested that in the October-November period the annual rate of growth in M_1 would be at the midpoint of the 4-3/4 to 7-1/4 per cent range of tolerance that had been specified by the Committee, reflecting an expectation that M_1 growth would accelerate in November from an estimated October rate that was near the lower limit of the range. The rate of growth in M_2 in the 2-month period appeared to be at the upper limit of its range. Federal funds most recently had been trading around 9-3/4 per cent, the midpoint of the 9 to 10-1/2 per cent range of tolerance that had been adopted by the Committee.

In view of the behavior of the aggregates, the System ordinarily would have become more restrictive in its reserve-supplying operations, to the extent consistent with even-keel considerations, expecting that the weekly average Federal funds rate would rise slightly above 9-3/4 per cent. However, members of the Committee, with the exception of Messrs. Clay and Coldwell, concurred in the Chairman's recommendation of October 31 that the funds rate target be reduced to 9-1/2 per cent for the time being, in view of the evidence of additional weakness in economic activity, restraint in the lending policies of banks and other institutions, and the severe financial problems of the construction industry. It was understood that the Manager's operations would need to reflect further changes in the behavior of monetary aggregates and would also have to take account of the current Treasury financing.

2. Amendment to authorization for domestic open market operations

On November 11 Committee members voted to amend paragraph 1(b) of the authorization for domestic open market operations to increase the limit on outright holdings of bankers' acceptances from $500 million to $1 billion. With this amendment, paragraph 1(b) read as follows:

> 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 $1 billion.

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

Absent and not voting: Mr. Wallich.

This action was taken on recommendation of the Account Manager who noted that, pending further review, Federal Reserve Banks, effective November 12, 1974, would no longer guarantee payment of bankers' acceptances purchased by the Federal Reserve Bank of New York for official foreign accounts. The Manager advised that the effects of this change on the acceptance market and on accepting banks could not be foreseen and that an increase in the limit in question could prove helpful in case of need for System action designed to insure a smooth market adjustment. (At its meeting on November 19 the Committee decided to retain the $1 billion limit, which was deemed consistent with longer-term needs to supply reserves.)