FEDERAL RESERVE

press release

For Use at 4:00 p.m. June 25, 1976

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 May 18, 1976.

Such records for each meeting of the Committee are made available a few days after the next regularly scheduled meeting 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 solely on the information that was available to the Committee at the time of the meeting.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on May 18, 1976

1. Domestic policy directive

Preliminary estimates of the Commerce Department indicated that growth in real output of goods and services had picked up to an annual rate of 7.5 per cent in the first quarter--from a rate of 5 per cent in the fourth quarter of 1975--and that the rise in the GNP fixed-weighted price index had slowed substantially. Staff projections suggested that growth in real output was continuing at a vigorous, although slightly less rapid, pace in the current quarter and that it was likely to be more moderate in the second half of the year. The projections also suggested that the rise in prices would be above the relatively low first-quarter rate.

Retail sales were unchanged in April. Over the period since November, however, retail sales had risen substantially reflecting in large part strong demands for automobiles and general merchandise.

Industrial production continued to recover in April at about the average rate of the preceding 4 months.

As in March, the rise reflected mainly increases in output of automobiles, other consumer goods, business equipment, and durable goods materials.

Gains in employment were large and widespread in April. The civilian labor force grew as much as total employment, however, and the over-all unemployment rate remained at 7.5 per cent. Nevertheless, the unemployment rate for heads of households and for adult males declined. In manufacturing, the average factory workweek fell, but the decrease appeared to have been related to holidays in the week used for the survey of establishments.

Private housing starts, which had rebounded sharply in February and then fallen moderately in March, declined somewhat further in April to the average level in the fourth quarter of 1975. Outstanding mortgage loan commitments at savings and loan associations had risen in March, the latest month for which data were available, and had reached the highest level in 3 years.

New orders for nondefense capital goods rose appreciably in March for the third consecutive month, but the backlog of orders declined further. Nonresidential construction activity remained depressed. However, a private survey suggested that over recent months business plant and equipment expenditures planned for this year had been raised considerably.

The index of average hourly earnings for private nonfarm production workers, which had risen at a less rapid pace over the first quarter of 1976 than it had on the average in 1975, continued to advance at a moderate rate in April. The schedule of labor contract negotiations had been light in the first 4 months of this year, and relatively few cost-of-living wage adjustments went into effect. From the fourth quarter of 1975 to the first quarter of 1976 over-all compensation per manhour in the private nonfarm economy rose as rapidly as it had on the average during 1975.

The wholesale price index for all commodities rose appreciably in April, following a 5-month period of little change. Average prices of farm and food products rose sharply, after 5 months of decline, while average prices of industrial commodities continued upward at a moderate pace. In March the rise in the consumer price index had remained at a reduced rate, in large part because retail prices of foods and fuels had continued to decline.

Staff projections now suggested that growth in real output in the current quarter would be stronger than had been projected 4 weeks earlier, provided that a current work stoppage in the rubber products industry ended before it caused significant curtailments in output in other industries. The greater strength in the quarter was attributed in large part to higher rates of business investment in fixed capital and inventories than had been projected a month ago, although a slightly faster rate of growth in personal consumption expenditures also was now anticipated.

Staff projections for the second half of the year suggested that expansion in business fixed investment would continue to accelerate and that business investment in inventories would remain at an advanced rate. It was also anticipated that growth in personal consumption expenditures would remain vigorous and that residential construction would continue to recover. However, the expansion in State and local government purchases of goods and services was expected to remain relatively slow.

The U.S. foreign trade balance was in deficit in March for the third consecutive month, and the sizable deficit for the first quarter as a whole was in sharp contrast to large surpluses in each of the four quarters of 1975. The shift to deficit in the first quarter was attributable mainly to increases in imports associated with the expansion in the domestic economy; at the same time, exports declined somewhat.

Over the period since the April 20 meeting of the Committee, the average value of the dollar against leading foreign currencies had remained relatively steady. Attention in the exchange markets during the period was focused on problems affecting the Italian lira and the

British pound, both of which fluctuated considerably. On balance, the lira rose somewhat and the pound declined somewhat in relation to the dollar.

Total loans and investments at U.S. commercial banks expanded somewhat further in April, reflecting almost entirely another large increase in bank holdings of Treasury securities. Bank holdings of other securities increased slightly. Total loans outstanding at banks declined, reflecting substantial net repayments of business and security loans. Other loans by banks continued to expand moderately.

In general, business short-term credit demands remained weak in April. The outstanding volume of commercial paper issued by nonfinancial corporations rose, but the increase was offset by the decline in outstanding bank loans to businesses.

Growth in the narrowly defined money stock--M_1--accelerated to an annual rate of about 15 per cent in April, reflecting in part a rise in private balances resulting from a large decline in U.S. Government deposits.[1/] On the average from March to April Treasury balances at Federal Reserve and commercial banks declined by almost $4 billion. M_1 had grown at a moderate rate in February and March and at a slow rate over the preceding 4 months.

The more broadly defined money stock measures--M_2 and M_3--also increased substantially in April, owing to the sharp rise in M_1 and to continuing strong inflows of time and savings deposits (other than negotiable CD's) at banks and nonbank thrift institutions. Interest rates on such deposits remained favorable relative to rates on short-term market instruments.

System open market operations since the April 20 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 period ahead, while taking account of developments in domestic and international financial markets. Immediately after the April meeting the System became less accommodative in the provision of reserves. Operations were

1/ The monetary growth rates for April reported at this meeting were based on revised measures of the monetary aggregates, reflecting new benchmark data for deposits at nonmember banks. The revised measures were published on May 20, 1976.

directed toward achieving conditions of reserve availability consistent with a Federal funds rate of 4-7/8 per cent--the midpoint of the 4-1/2 to 5-1/4 per cent operating range that the Committee had specified for the inter-meeting period and 1/8 percentage point above the rate prevailing at the time of the April meeting.

Data that had become available soon after that meeting and in each subsequent week suggested that in the April-May period growth in M_1 and M_2 would be strong relative to the ranges that had been specified by the Committee. Accordingly, the System gradually became still less accommodative in the provision of reserves. By the end of the inter-meeting period the Federal funds rate was around 5-1/4 per cent, the upper limit of the specified range, and market interest rates in general had risen. Upward pressures on market rates also reflected investor reactions to the indications of accelerated growth in the monetary aggregates and to reports suggesting vigorous economic recovery.

In the short-term area, the rise in market rates during the inter-meeting period occurred despite continued weakness in private credit demands. In addition, the Treasury cut its outstanding short-term indebtedness after midmonth by repaying a substantial amount of cash-management bills and by reducing the size of the weekly auctions of bills. On the day before this meeting the market rate on 3-month Treasury bills was 5.22 per cent, compared with 4.77 per cent on the day before the April meeting.

In the intermediate- and long-term areas, demands for funds remained relatively strong in April. Public offerings of new corporate bonds, although down from the exceptional volume in March, were still large. Offerings of new State and local government bonds also fell from the exceptional total in March, but a rebound in the volume appeared to be in prospect for May.

On April 28 the Treasury announced that it would sell $6.25 billion of notes and bonds to refund $4.1 billion of publicly held notes that were to mature on May 15 and to raise $2.2 billion of new cash. In auctions on May 4 and May 7 it sold to the public $2 billion of 2-year notes and $750 million of 23-year 9-month bonds at average prices to yield 6.61 per cent and 8.19 per cent, respectively. For the remaining $3.5 billion, the Treasury offered 10-year, 7-7/8 per cent notes at par. However, subscriptions for these notes amounted to $8.9 billion, and on May 7 the Treasury accepted $4.7 billion of them. Altogether, the Treasury sold to the public almost $7.5 billion of notes and bonds, raising $3.4 billion in new cash.

Interest rates on home mortgages in the primary market were unchanged during the inter-meeting period. In the more sensitive secondary market, yields edged up beginning in late April in reaction to the rise in other market rates of interest.

At its April meeting, the Committee had agreed that growth in the monetary aggregates on the average over the period from the first quarter of 1976 to the first quarter of 1977 at rates within the following ranges appeared to be consistent with its broad economic aims: M_1, 4-1/2 to 7 per cent; M_2, 7-1/2 to 10 per cent;

and M_3, 9 to 12 per cent. The associated range for growth in the bank credit proxy was 6 to 9 per cent. It was agreed that the longer-term ranges, as well as the particular list of aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings. It also was understood that, as a result of short-run factors, growth rates from month to month might well fall outside the ranges contemplated for annual periods.

In the discussion of current policy at this meeting, the Committee took note of a staff analysis suggesting that over the May-June period the rate of growth in M_1 was likely to subside from the rapid pace in April, which was attributable in part to the large decline in U.S. Treasury deposits. At the same time, however, it appeared that the underlying demand for money was strong and that a somewhat more typical relationship between growth in M_1 and growth in nominal GNP was in the process of being re-established. Given the rate of GNP growth projected for the current quarter, the staff analysis suggested that, if prevailing money market conditions were maintained over the 5 weeks until the next meeting, growth in M_1 over the May-June period would be within a range that was high relative to the longer-term range agreed upon by the Committee at the preceding meeting.

The staff analysis also suggested that, if prevailing money market conditions were maintained over the next inter-meeting period, growth in M_2 over the May-June period would remain relatively rapid, although less so than the average rate during the first 4 months of the year. It was expected that thrift institutions' inflows of time and savings deposits other than money market CD's would be dampened by the recent rise in interest rates and that some deposits would be withdrawn in order to make payment in mid-May for the new 10-year, 7-7/8 per cent Treasury notes.

It was noted that credit market pressures would be affected by the recent build-up in the calendar of new corporate and State and local government bond issues.

In general, demands for intermediate- and long-term funds across all market sectors were likely to remain strong. Moreover, it was not yet clear whether longer-term market rates had fully adjusted to the recent firming in money market conditions.

During the Committee's discussion, it was observed that the recovery in economic activity had proceeded in a satisfactory way, although the rate of unemployment remained high and re-intensification of inflationary pressures was a serious threat. Recent gains in production and employment had been sizable, and a significant expansion in business demands for fixed capital and for inventories appeared to be developing. Altogether, the outlook for economic activity was strong; to some members of the Committee, it appeared stronger than suggested by the staff projections.

The members agreed that growth in monetary aggregates recently had been at unacceptably high rates, especially in view of the longer-run ranges for growth that had been adopted at the preceding meeting. It was observed that the moderate monetary policy that the System had been pursuing had contributed to a return of confidence; that to sustain confidence it was important for the System to demonstrate its intention to resist unduly rapid growth in the monetary aggregates; and that pursuit of that objective would run little or no risk of aborting the recovery in economic activity.

A number of members expressed the view that failure to take additional steps now to restrain growth in the monetary aggregates might confront the Committee with the need to take stronger measures later on, if growth rates were to be held within the longer-run ranges agreed upon at the last meeting. At the same time, it was felt that the System should proceed cautiously because the exceptionally rapid growth in the monetary aggregates recently might be a temporary aberration and because some modest tightening in money market conditions already had taken place.

It was noted that the Federal funds rate had turned up from a level of around 4-3/4 per cent and had risen 50 basis points in the period since the April meeting and that interest rates in general had increased. Some concern was expressed about the rise in longer-term rates. The observation was also made, however, that rising rates would not have much impact on economic activity until late this year or early next year, and should a strong capital investment boom be under way at that time, prompt action now to restrain monetary growth would be viewed, retrospectively, as especially appropriate.

In general, Committee members favored directing operations in the period immediately ahead toward moderating growth of the monetary aggregates, and they indicated that in pursuit of that end they would accept some modest further firming in money market conditions. However, they differed in their preferences for specifics of operating instructions for the coming period. Most members favored specification of M_1 and M_2 ranges of growth for the May-June period that were close to the longer-run ranges that had been agreed upon at the last meeting. Other members preferred to specify somewhat higher ranges of growth for M_1 and M_2 over the May-June period in recognition of the growth rates that appeared to be already developing. In general, however, they were willing to accept slightly more firming in money market conditions than were members in the first group, should the 2-month rates of growth in the aggregates appear to be approaching or exceeding the upper limits of those higher ranges.

At the conclusion of the discussion the Committee decided to seek bank reserve and money market conditions consistent with moderate growth in monetary aggregates over the period ahead. Specifically, the members agreed that growth in M_1 and M_2 over the May-June period at annual rates within ranges of 4 to 7-1/2 per cent and 5 to 9 per cent, respectively, would be acceptable. They decided that, in assessing the behavior of the aggregates, approximately equal weight should be given to M_1 and M_2.

The members agreed that until the next meeting the weekly-average Federal funds rate might be expected to vary in a gradual and orderly way within a range of 5 to 5-3/4 per cent. They also agreed that, in the conduct of operations, account should be taken of developments in domestic and international financial markets.

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

> The information reviewed at this meeting suggests that growth in real output of goods and services is continuing at a vigorous pace in the current quarter. In April recovery in industrial production continued, and gains in employment were large and widespread. However, the civilian labor force also increased substantially, and the unemployment rate continued at 7.5 per cent. Retail sales remained at the March level. The wholesale price index for all commodities rose appreciably in April, reflecting a sharp increase in average prices of farm products and foods and a modest increase in prices of industrial commodities. Over recent months, the index of average wage rates has advanced moderately.
>
> The average value of the dollar against leading foreign currencies has been relatively steady in recent weeks. During the first quarter, there was a sizable U.S. foreign trade deficit, in contrast to the large surpluses in the preceding four quarters.
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> M_1, which had expanded moderately in February and March, increased sharply in April, reflecting in part a drop in U.S. Government deposits. Inflows

of time and savings deposits other than negotiable CD's were strong at banks and nonbank thrift institutions, and M_2 and M_3 increased substantially. In recent weeks, both short- and long-term market interest rates have risen.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions that will encourage continued economic recovery, while resisting inflationary pressures and contributing to a sustainable pattern of international transactions.

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

Votes for this action: Messrs. Burns, Volcker, Balles, Black, Gardner, Jackson, Kimbrel, Partee, Wallich, and Winn. Vote against this action: Mr. Coldwell.

Mr. Coldwell dissented because he did not want to provide for the possibility of a rise of as much as 1/2 percentage point in the Federal funds rate over the next inter-meeting period in addition to the rise of 1/2 percentage point that had occurred since the last meeting. In his opinion, a further rise of that amount could have an exaggerated effect on expectations in the financial markets, provoking excessive increases in interest rates. Rapid monetary growth recently, he thought, might reflect transitory forces to a significant degree, so that much further tightening in money market conditions over the next few weeks could force consideration later on of the need for a reversal. Accordingly, he favored a range of 5 to 5-1/2 per cent for the weekly average Federal funds rate until the next meeting and a range of 6 to 10 per cent for the annual rate of growth in M_1 over the May-June period.

2. Release schedule for the record of policy actions

At this meeting the Committee approved a motion that the record of policy actions for each meeting of the Committee be released to the public shortly after the next regularly scheduled meeting. A publication delay of approximately 45 days had been in effect since early 1975.

> Votes for this action: Messrs. Burns, Volcker, Balles, Black, Gardner, Jackson, Kimbrel, Partee, Wallich, and Winn. Votes against this action: None. Abstention: Mr. Coldwell.

This action was taken to provide information regarding the Committee's policy actions on a more timely basis. Since the majority of meetings are held at 4-week intervals, the delay now will most often be about a month. For the minority of meetings that are followed by a 5-week interval, the delay will be about a week longer.

From mid-1967 to early 1975, a delay of approximately 90 days had been in effect. Prior to mid-1967, when the Committee's Rules Regarding the Availability of Information were changed to comply with the Freedom of Information Act, the records of policy actions were published only in the Board's Annual Report to Congress.

In conjunction with the foregoing action, the Committee amended Section 271.5(a) of its Rules Regarding the Availability of Information to delete the sentence reading "For example, the Committee's domestic policy directive adopted at each meeting of the Committee is published in the Federal Register approximately 45 days after the date of its adoption; and no information in the records of the Committee relating to the adoption of any such directive is made available for public inspection or copying before it is published in the Federal Register or is otherwise released to the public by the Committee." With this amendment, Section 271.5(a) read as follows:

> (a) Deferred availability of information.--In some instances, certain types of information of the Committee are not published in the Federal Register or made available for public inspection or copying until after such period of time as the Committee may determine to be reasonably necessary to avoid the effects described in paragraph (b) of this section or as may otherwise be necessary to prevent impairment of the effective discharge of the Committee's statutory responsibilities.

> Votes for this action: Messrs. Burns, Volcker, Balles, Black, Coldwell, Gardner, Jackson, Kimbrel, Partee, Wallich, and Winn. Votes against this action: None.

3. Memorandum of discussion

At this meeting the Committee approved a motion that the memorandum of discussion be discontinued after the memorandum for the meeting of March 15-16, 1976.

> Votes for this action: Messrs. Burns, Volcker, Balles, Black, Gardner, Jackson, Kimbrel, Partee, Wallich, and Winn. Vote against this action: Mr. Coldwell.

This action was taken against the background of the Committee's decision to speed up publication of the records of policy actions, and of its understanding that the policy records would be expanded to include more information concerning members' views on longer-run and current policy. The memoranda of discussion are detailed accounts of proceedings at meetings of the Committee, which have been available to the public 5 years after the end of the year to which they apply. The decision to discontinue these memoranda reflected the Committee's judgment that the benefits derived from them did not justify their relatively high cost, particularly in light of the changes being made in the policy record.

Mr. Coldwell dissented from this action because he felt that the benefits of the memorandum of discussion justified its retention.

4. <u>Foreign currency operations</u>

On June 6, following consultations among members of the Foreign Currency Subcommittee of the Federal Open Market Committee, the System agreed that it would stand ready to make available $1 billion to the Bank of England under the existing reciprocal currency arrangement with that Bank. At the same time, the Treasury Department, through the Exchange Stabilization Fund, agreed that it would stand ready to make available $1 billion under a swap arrangement with the Bank of England.

The System and the Treasury participated with central banks of other Group of Ten countries, Switzerland, and the Bank for International Settlements in making available to the Bank of England standby credits totalling $5.3 billion. Those arrangements were made in the light of the recent fall in the value of the pound sterling under exchange market pressures that had led to disorderly market conditions, and in the common interest in the stability and efficient functioning of the international monetary system.