65th Annual Report 1978

Board of Governors of the Federal Reserve System

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Letter of Transmittal

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM
Washington, D.C., April 20, 1979

THE SPEAKER OF
THE HOUSE OF REPRESENTATIVES

Pursuant to the requirements of Section 10 of the Federal Reserve Act, as amended, I am pleased to submit the Sixty-Fifth Annual Report of the Board of Governors of the Federal Reserve System.

This report covers operations of the Board during the calendar year 1978.

Sincerely,

G. William Miller, *Chairman*

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Part 1

Monetary Policy and the U.S. Economy in 1978

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Introduction

U.S. economic activity remained on an upward path during 1978, making the current cyclical expansion to date the second longest of the postwar period. Employment increased substantially, and the unemployment rate declined further despite large increases in the labor force. At the same time, however, acceleration in the rate of inflation posed a threat to continued economic progress.

Inflation emerged clearly as the Nation's most urgent economic concern in 1978. The legacy of past price increases imparted a strong momentum to the inflationary process, and upward pressures on costs and prices were exacerbated by the poor performance of productivity, by adverse agricultural supply conditions, and by Government-mandated cost increases.

The deterioration in U.S. price performance added impetus to the decline in the international exchange value of the dollar that had begun in the latter part of 1977; the falling dollar in turn reinforced inflationary pressures by raising the costs of imported goods and by easing competitive constraints on the prices of domestically produced goods. By late October the decline of the dollar had become precipitous, and it imperiled the health of both the U.S. economy and the international financial system. On November 1 the Federal Reserve and the Department of the Treasury announced a package of actions intended to fight inflation and to bolster the dollar. The dollar improved markedly in subsequent weeks, but nonetheless showed a large net decline for the full year against other major currencies.

Throughout 1978 monetary policy was directed toward resisting additional inflationary pressures while providing financial conditions conducive to moderate economic expansion. Federal Reserve policy actions were designed to restrain growth of the monetary and credit aggregates and to resist further depreciation of the dollar abroad. The actions of the System, coupled with strong demands for money and credit and a heightened level of inflation, caused interest rates —especially on short-term instruments—to rise substantially.

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Despite the tightening of credit conditions, the momentum of economic expansion was sustained throughout 1978 and into 1979. A liberalization of Federal regulations on deposit interest rates prevented a recurrence of disintermediation, and banks and thrift institutions were able to supply the credit necessary to finance high levels of homebuilding and other business and consumer outlays. Monetary restraint—as well as progress toward fiscal restraint—did, however, contribute to a needed moderation of economic growth from the stronger pace earlier in the expansion. A continued slowing of growth appears in prospect for 1979; and this slowing is desirable if the Nation is to avoid further inflation emanating from increased pressure on the relatively small margin of unutilized resources of capital and skilled labor.

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The Economy in 1978

The economic expansion was maintained well into its fourth year during 1978, but was accompanied by a serious intensification of inflationary pressures. Gross national product rose 4½ per cent in real terms during the four quarters of 1978, somewhat less than during the two previous years.[1] As in 1976 and 1977, expansion of activity was uneven from quarter to quarter. Real GNP declined slightly in the first quarter due to a lengthy coal strike and an unusually severe winter, but a vigorous rebound of activity during the spring indicated considerable underlying strength in aggregate demand. Real growth moderated somewhat in the third quarter, but the pace of over-all activity picked up again in the final months of the year.

Capital spending by businesses provided a major part of the impetus for the year's advance, in contrast to the early part of the expansion, when consumption and housing were the most supportive sectors. Even so, the gain was sufficient to boost real capital spending only slightly above its prerecession peak—a performance that remains deficient by prior cyclical standards. Advances in consumer spending moderated from earlier years, apparently because of the slower growth in real after-tax incomes and record debt burdens. Expenditures for residential construction remained high in 1978, following 2 years of vigorous growth; the sustained strength of residential construction activity apparently reflected both the appeal of housing investment as a hedge against inflation and the improved ability of mortgage markets to withstand tightening financial conditions.

The slower growth of private final demands was accompanied by a smaller increase in government outlays. Federal Government purchases of goods and services declined in real terms while State and local purchases rose more moderately than during the previous year. The over-all budgetary position of the government sector became less stimulative; a decline in the Federal deficit was offset only in

[1] Unless otherwise indicated, annual figures represent changes from the end of 1977 to the end of 1978.

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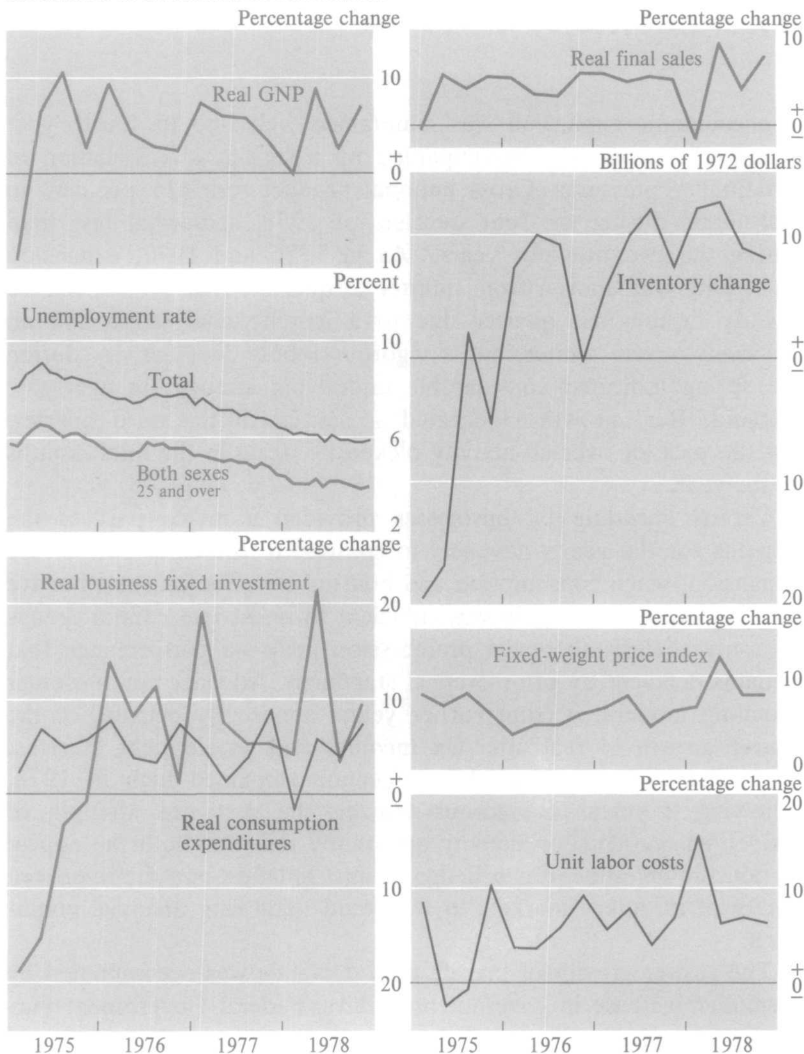
Indicators of Economic Performance



All percentage changes are measured from the previous quarter and are seasonally adjusted at annual rates.

The unemployment rate (seasonally adjusted monthly data) and the change in unit labor costs are from U.S. Department of Labor. All other data are from U.S. Department of Commerce.

The fixed-weight price index (1972 weights) is for gross domestic business product. Series designated as "real" are based on 1972 dollars.

Scales for unemployment rate and inventory change are larger than those for the other panels.

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part by a reduction of the large operating surpluses experienced by State and local governments in recent years.

Inflation worsened noticeably during 1978, with the change in most broad measures of prices about 2 percentage points larger than over the previous year. The intensification of inflation early in the year was attributable in part to rapid increases in food prices; however, homeownership costs and gasoline prices also accelerated markedly from their rates of increase in 1977. In addition, the depreciation of the dollar on international exchange markets had inflationary effects on prices of imports and many import-competing goods. Moreover, labor cost pressures intensified as sizable increases in compensation continued—in part because of a boost in the minimum wage and higher payroll taxes—and labor productivity rose relatively little over the year.

The persistence of high rates of inflation apparently influenced the pattern of economic activity in several ways. To some extent, the continued relative strength in consumer spending for durable goods reflected the desire to purchase in anticipation of price increases. The personal saving rate remained at the lower end of its postwar range and aggregate household indebtedness relative to disposable personal income reached record levels. In the business sector, accelerating inflation continued to add uncertainties that probably lessened the willingness of firms to commit funds for major capital spending projects.

The economy displayed strong momentum at the end of 1978, with sales and production registering sizable gains. Employment and personal income posted large increases, and housing starts remained strong. In the business sector, new orders for capital goods held at a high level, and inventories remained generally lean relative to sales. Even so, there were mixed signs about the longer-run economic outlook. Survey and appropriations data suggested that capital outlays by businesses would grow more slowly over 1979. Retail sales strengthened markedly during the final months of the year, and the personal saving rate edged even lower at year-end to 5 per cent—near the lower end of its postwar range. This factor, together with continuing high debt burdens and weakening consumer sentiment, could retard near-term advances in consumption. Finally, the prospects for sustained growth were clouded by the persistence of intense inflationary pressures.

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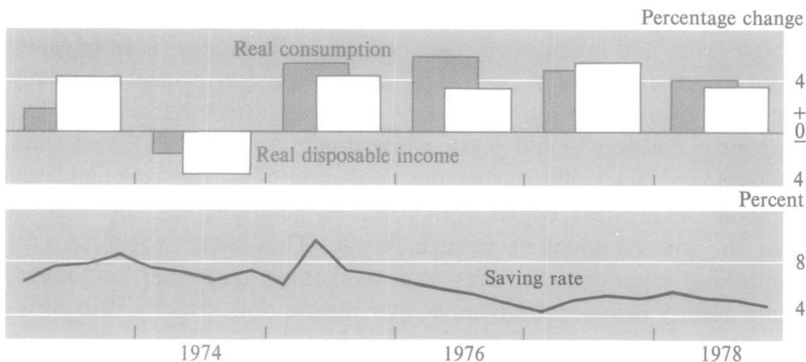
HOUSEHOLD SECTOR

Moderation of growth in real household spending accounted for much of the slowing of growth in real GNP in 1978. Consumer outlays increased 4 per cent in real terms, compared with average increases of 5¼ per cent during the three previous years. Nominal personal income rose at about the pace recorded earlier in the expansion, but inflation and higher tax burdens cut gains in real disposable income from the pace of the previous year. Wage and salary disbursements were up sharply in nominal terms, especially early in the year, and a rebound in farm income reflected higher food prices and government support programs.

Retail sales were depressed in the first quarter by severe weather, although outlays for heating increased sharply. Spending rebounded strongly in the spring, sparked by an increase in automobile sales to a near-record annual rate of 12.1 million units. In the second half of the year, growth of consumer spending was sustained at a generally rapid pace despite a slight decline in automobile sales.

In the housing sector, activity remained at a high level in 1978. Starts totaled 2 million units, up slightly from the previous year. Single-family starts edged off to 1.4 million units, while sales of new and existing homes remained at about the advanced rate of late 1977. Average prices of new units sold rose about 13 per cent during the year, in part reflecting some upgrading in quality. Starts of multifamily dwellings increased about 9 per cent to 580,000

Income, Consumption, and Saving



Based on U.S. Department of Commerce data, seasonally adjusted at annual rates. "Real" is in terms of 1972 dollars. Changes are from fourth quarter to fourth quarter.

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units; nonetheless, activity in this sector remained well below the peak levels of the early 1970's. Multifamily construction in 1978 was supported by an increase in units under the Section 8 rental subsidy program of the Department of Housing and Urban Development, which is aimed at low- and moderate-income families.

At the end of the year, housing markets remained generally firm. Sales of new single-family homes, which had dipped during the summer, turned up again during the fourth quarter, and total starts remained close to the annual rate of 2 million units that had prevailed for a year and a half. High interest rates on mortgages and already large household debt burdens are, however, likely to retard housing activity in 1979.

BUSINESS SECTOR

Business fixed investment rose over 9¼ per cent in real terms during 1978, slightly more than the 1977 gain and about twice the rate of advance in over-all economic activity. A very sharp increase in real capital spending in the first half of the year was followed by a rise of 6½ per cent in the second half. Outlays for structures began to show relatively greater strength in 1978 than in 1977, paced by large increases for industrial and commercial buildings. Investment in producers' durable equipment grew somewhat more slowly, as business purchases of motor vehicles tapered off.

Investment in the manufacturing sector continued to grow moderately as utilization rates gradually increased through the year. Gains in capital outlays were strongest among producers of durable goods, particularly in the stone, clay, and glass, electrical machinery, and aircraft industries. In the nondurable goods sector, producers of rubber and food also recorded large increases. Investment by materials producers, a group that includes some manufacturers in both the durable and the nondurable goods categories, continued to advance at a relatively modest pace, reflecting an adequate margin of unused capacity. Outside the manufacturing sector, the air transportation industry posted the largest increase in spending, and strong gains were also evident in railroads, communications, and electric utilities.

Advance indicators of capital spending were mixed at year-end. Contracts and orders for plant and equipment generally moved ahead vigorously in the fall after having been nearly unchanged over

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most of the summer. Surveys of business intentions and capital appropriations for the manufacturing sector suggested some slowing of spending during 1979.

Inventory policies were generally cautious in 1978, continuing a trend that has characterized most of the present expansion. Inventory investment declined somewhat over the year, and inventory-sales ratios for most sectors remained low to normal on an historical basis. Most of the accumulation of stocks in the manufacturing sector was at durable goods producers, reflecting the relatively more intense demand for these products. At the trade level, wholesale stocks were swollen early in the year by rapid increases in prices of agricultural products and food; in the fall some overhang did emerge at general-merchandise retailers, but the sales surge in the final quarter appears to have absorbed a good deal of this excess.

GOVERNMENT SECTOR

As is typical during a business expansion, the government sector provided less stimulus to aggregate activity in 1978 than earlier. At the Federal level, the growth of spending slowed, and large gains in nominal incomes combined with mandated tax increases to push up receipts. As a result, the Federal deficit for the calendar year declined to about $30 billion on a national income accounts basis—roughly $18 billion less than in 1977, but still large relative to similar phases of past expansions.

Federal expenditures rose 9 per cent during 1978. Purchases of goods and services—the component of spending that is included directly in GNP—declined slightly in real terms, following an increase of 6 per cent during 1977. The reduction in purchases was most noticeable in the nondefense area, as net loan redemptions by farmers under the agricultural price support program of the Commodity Credit Corporation (CCC) more than offset increases in other nondefense expenditures.[2] Real defense spending declined in 1978 following a 3 per cent rise in 1977.

Transfer payments to individuals grew only moderately, owing to a sizable decline in unemployment compensation. Grants to State

[2] CCC loans are treated as Federal purchases in the national income accounts because the value of farm products in inventory, which are used as collateral for the loans, is transferred from the farm to the government sector. Similarly, loan repayments are treated as negative purchases in the Federal Government accounts.

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and local governments rose briskly over most of the year, with an expansion in local public works and public employment programs; however, late in the year funds for the countercyclical revenue-sharing program expired and funding for public service employment began to taper off.

At the State and local government level, purchases of goods and services grew at a 3½ per cent rate in real terms over the course of 1978, somewhat below the gain of the previous year. Construction outlays, supported by Federal grants, increased sharply in real terms, dramatically reversing the trend of recent years. State and local employment, however, grew by only 200,000 jobs—about half of the average gain since 1970—as the number of jobs in the Federally supported public service employment program reached targeted levels. The operating surplus in the State and local sector—that is, the surplus excluding net savings by social insurance funds—fell sharply in 1978. Indeed, the sector's receipts and expenditures moved into virtual balance by the third quarter, marking the end of the large operating surpluses that had prevailed since late 1976.

Fiscal conservatism at all levels of government became a prominent political and economic issue in 1978, and the passage of California's Proposition 13 in early summer stimulated action in other areas of the Nation. Budget-reduction proposals appeared on the ballots of 19 other States in November, and although voters generally chose less rigid methods of holding down tax burdens, the growth of State and local government budgets is likely to be restrained for a number of years.

LABOR MARKET DEVELOPMENTS

Demand for labor remained strong during 1978. Employment in private nonfarm establishments increased by 3½ million, exceeding the exceptionally strong rise during 1977 despite the slower growth in over-all output. Construction employment rose about 450,000 to a record level, and manufacturing employment increased by more than 700,000, with sizable gains in the machinery, transportation equipment, and metals industries.

Hiring outpaced the continued rapid growth of the labor force over the year, and the unemployment rate declined 0.8 percentage point to an average of 5.8 per cent in the fourth quarter. While labor markets for experienced and skilled groups of workers tight-

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ened, joblessness was still very high at year-end among persons aged 16 to 24 and among minorities.

A major disappointment in 1978 was the poor performance of productivity: output per hour in the nonfarm business sector showed relatively little growth. Productivity growth had bounced back in a fairly typical fashion in the first 2 years of the expansion, but after 1976, growth in output per hour resumed the slow pace that had been characteristic of over-all productivity since the late 1960's. The reason for this pattern is not entirely clear, although several factors appear to have contributed to it, including the sluggish performance of capital spending in recent years, the emergence of a less experienced labor force due to demographic changes, and environmental and safety requirements that have directed resources to uses traditionally not measured as output.

Reflecting the lackluster performance of productivity and the continuing large increases in hourly compensation, the rise in unit labor costs during 1978 accelerated to about 9 per cent, the sharpest rise since 1974. Compensation in 1978 was boosted by a pronounced speed-up in wage rate increases outside the manufacturing sector. Construction wages rose sharply for the first time since 1974, and pay rates in the relatively low-wage sectors such as trade and services were pulled up in part by the legislated rise in the minimum wage. At the same time, wages in the manufacturing sector rose 8¼ per cent, about the same pace as that during 1977 despite a light schedule of collective bargaining. In addition to more rapid wage increases, higher payroll taxes for social security and unemployment insurance added further to the acceleration in hourly compensation.

PRICES

In addition to the sizable increases in unit labor costs, special developments in the food, homeownership, and international sectors contributed to the acceleration in the rate of inflation in 1978. In part because of these special factors, price increases far exceeded most forecasts made at the beginning of the year: the consumer price index rose about 9 per cent during 1978 as did the fixed-weight price index for gross business products and the producer price index for finished goods.

Retail food prices increased about 12 per cent during 1978, the largest rise since 1974. The increases at the retail level reflected a

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jump of nearly 20 per cent in prices of farm products following little change in the previous year. Price increases for meat were especially rapid and those for other food items were also quite large.

In general, prices outside the food area also rose rapidly during 1978. Energy prices increased about 8 per cent at retail. Gasoline prices changed little in the first half, but a tightening of supplies led to a sharp upturn later in the year. Natural gas prices continued to surge upward during most of the year. Consumer prices of services excluding energy accelerated to an annual rate of 9½ per cent from 8 per cent in 1977, reflecting in part the 12½ per cent rise in the homeownership component; strong demand pressures on house prices and rising mortgage interest rates were mainly responsible for that rise. Also, consumer prices were boosted by the depreciation of the dollar, which had noticeable direct impacts on the prices of imported merchandise and indirect effects on prices of domestic automobiles and other goods that are competitive with imports.

At the producer level, prices of capital equipment accelerated less during 1978 than those for finished consumer goods. Prices of crude materials—both food and nonfood commodities—were up sharply, and prices for construction materials also rose rapidly.

In an effort to restrain price increases, the President in late October announced an anti-inflation program that included a commitment to Federal budgetary restraint as well as voluntary wage and price standards and regulatory reform. The general price standard calls on firms to limit their increases to 1/2 of a percentage point below their average annual price rise during the 1976–77 period. Wage increases are to be generally limited to 7 per cent a year. The program also sets an alternative profit-margin standard, provides for public monitoring of certain price and wage increases, and includes a legislative proposal for real-wage insurance.

Although the program holds out hope for a gradual unwinding of the wage–price spiral, inflationary forces appear likely to continue strong in 1979. The collective bargaining calendar is quite heavy, and no relief from food price pressures is in sight. In addition, legislated increases in the minimum wage and in social security taxes will once again add a premium to labor costs. Furthermore, the Organization of Petroleum Exporting Countries has announced an increase in the price of oil for 1979, which will have an adverse effect on prices, as will the continuing impact of the 1978 depreciation in the international exchange value of the dollar.

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Monetary Policy and Financial Markets

Monetary policy in 1978 sought to foster financial conditions that would contribute to the reduction of inflationary pressures and the stabilization of international exchange markets while supporting moderate economic growth. During the year, the acceleration of inflation increased the public's transactions requirements for cash balances and resulted in strong demands for money. In addition, expectations of continued rapid inflation apparently encouraged many households and businesses to borrow, in the belief that the burden of debt service would diminish while the prices of real assets would rise. These factors, coupled with the need to bolster international confidence in the dollar, prompted the Federal Reserve to seek increasing tautness in financial markets.

Employing all of the major tools of monetary policy—open market operations, the discount rate, and reserve requirements—the System contributed to a progressive firming in money market conditions over the course of the year. Short-term interest rates generally rose 3 to 4 percentage points during 1978, and most long-term bond rates climbed 1 to 1¼ points. By year-end the prime lending rate at commercial banks had increased 4 percentage points to 11¾ per cent, and the average interest rate on new commitments for home mortgage loans at savings and loan associations had reached a record 10⅜ per cent. The System's actions helped to restrain the growth of money and credit. Although growth of the narrowly defined money stock, *M*-1, exceeded the announced annual growth ranges of the Federal Open Market Committee, all of the major monetary aggregates, including *M*-1, grew less rapidly than during 1977. The expansion of the total flow of credit to nonfinancial sectors of the economy also slowed.

Although conditions in credit markets had tightened considerably by year-end, there was little evidence of financial strains that would prevent further moderate expansion in over-all economic activity. Interest rates were not unduly high if allowance is made for inflationary expectations; moreover, credit generally remained in adequate supply, owing in part to changes in Federal regulations on deposit rates and to other institutional developments that enhanced the efficiency of the capital markets.

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MONETARY AGGREGATES AND INTEREST RATES

Growth rates of the major monetary aggregates varied considerably from quarter to quarter during 1978, responding in large measure to changes in interest rates and in the pace of economic expansion. In broad terms, growth in *M*-1 was a bit less rapid on average in the second half than in the first, reflecting the somewhat smaller gains in nominal GNP and the much higher short-term interest rates that characterized the last 6 months of 1978. The pattern for the interest-earning components of the broader monetary aggregates—*M*-2 and *M*-3—was quite the opposite, however, as a liberalization of Federal ceilings on rates payable on certain small-denomination time accounts resulted in stronger inflows of such deposits beginning in June. Thus

Adopted Longer-Run Growth Ranges and Actual Growth Rates of Monetary Aggregates, 1976–78[1]

Per cent

Period	*M*-1	*M*-2	*M*-3
	Annual		
1976 Q4 to 1977 Q4			
Adopted	4½–6½	7–10	8½–11½
Actual	7.9	9.8	11.7
1977 Q1 to 1978 Q1			
Adopted	4½–6½	7–9½	8½–11
Actual	7.7	8.8	10.5
1977 Q2 to 1978 Q2			
Adopted	4–6½	7–9½	8½–11
Actual	8.2	8.6	10.0
1977 Q3 to 1978 Q3			
Adopted	4–6½	6½–9	8–10½
Actual	8.1	8.6	9.6
1977 Q4 to 1978 Q4			
Adopted	4–6½	6½–9	7½–10
Actual	7.3	8.5	9.4
	Quarterly (annual rate)		
1977			
Q1	7.4	10.9	12.4
Q2	7.4	9.0	10.5
Q3	8.6	10.1	11.8
Q4	7.4	7.9	10.1
1978			
Q1	6.6	7.0	8.1
Q2	9.2	8.4	8.4
Q3	8.1	9.9	10.4
Q4	4.4	7.7	9.4

[1] Growth rates are based on quarterly averages.

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there was no recurrence of the marked disintermediation that had been a prominent feature of other recent periods when market rates of interest had moved to relatively high levels.

Monetary expansion moderated in the first quarter of 1978 from the relatively rapid pace of 1977. Growth in *M*-1—currency and bank checking accounts—decelerated to a 6½ per cent annual rate, the upper end of the Federal Open Market Committee's long-run range. The slowing apparently was attributable to the weather- and strike-associated lull in economic activity. Because the interruption of economic growth was related largely to temporary dislocations in product markets rather than to a deficiency in aggregate demand, no easing of monetary policy was warranted. Indeed, the persistent weakness of the dollar on foreign exchange markets led the System to raise the Federal Reserve discount rate from 6 to 6½ per cent in early January and to adopt a less accommodative stance in the provision of reserves to the banking system through open market operations. The interest rate on Federal funds (overnight loans of immediately available bank funds) climbed 1/4 of a percentage point over the quarter to around 6¾ per cent, and most other short- and longer-term security yields increased by similar amounts.

The advance in market interest rates during January widened the gap that had already developed in the latter part of 1977 between yields on market instruments and those on savings deposits and small-denomination time deposits with maturities of less than 4 years. Consequently, growth of the interest-bearing component of *M*-2 also slowed in the first quarter, notwithstanding heavy issuance by commercial banks of those large time deposits ($100,000 and over) included in this aggregate. *M*-3 showed an even sharper deceleration as savings and loan associations and mutual savings banks experienced substantial reductions in deposit inflows. On the other hand, net sales of money market fund shares rose sharply and noncompetitive tenders in auctions of Treasury securities also increased, suggesting a diversion of individual savers' funds from depositary institutions.

As economic activity rebounded in the second quarter, growth in *M*-1 accelerated markedly—to an annual rate of 9¼ per cent. This was well above the long-run range established by the Federal Open Market Committee; consequently, the Committee permitted the associated demand for reserves to drive up the interest rate on Federal

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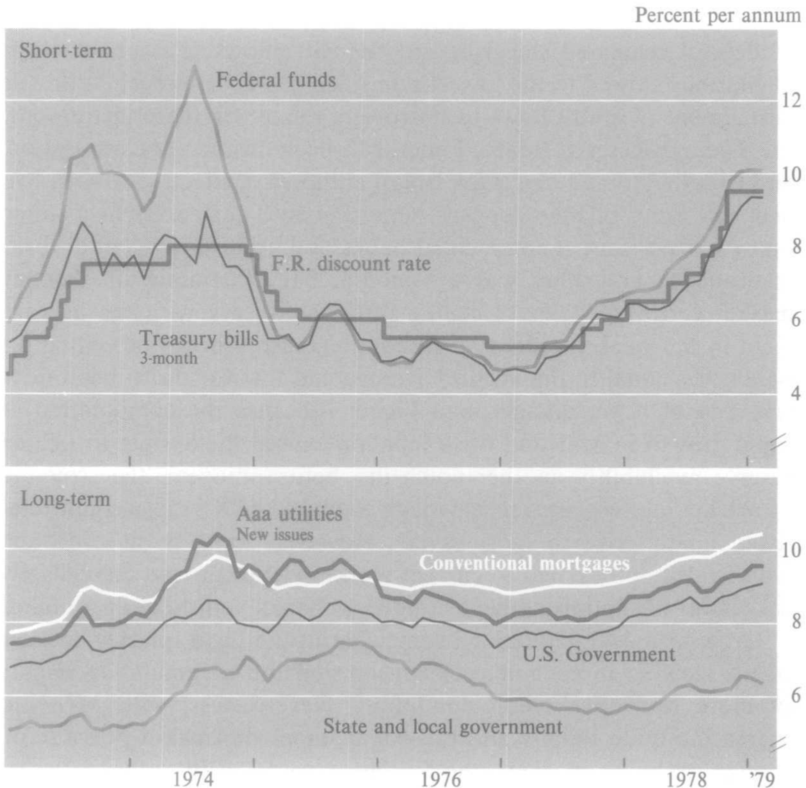
Interest Rates



Monthly averages except for conventional mortgages, which are based on quotations for one day each month. Yields: U.S. Treasury bills, market yields; prime commercial paper, dealer offering rates; conventional mortgages, rates on first mortgages in primary markets, unweighted and rounded to nearest 5 basis points, from U.S. Department of Housing and Urban Development; Aaa utility bonds, weighted averages of new publicly offered bonds rated Aaa, Aa, and A by Moody's Investors Service and adjusted to a Aaa basis; U.S. Government bonds, market yields adjusted to 20-year constant maturity by U.S. Treasury; State and local government bonds (20 issues, mixed quality), *Bond Buyer*.

funds to about 7¼ per cent in late April and then to around 7½ per cent in late May. Because the general upward movement in short-term market rates led member banks to increase their borrowing at the discount window, the Federal Reserve boosted the discount rate to 7 per cent in May. Intermediate- and long-term interest rates also climbed 25 to 50 basis points during this period as investors became more concerned about the outlook for inflation and the possibility of further increases in money market yields.

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With the additional rise in market rates early in the second quarter, growth of bank time and savings deposits other than large certificates of deposit remained sluggish, and deposit inflows at nonbank thrift institutions slowed to the lowest rate since 1974. To prevent a drastic curtailment of credit flows to borrowers reliant on these institutions, the Federal Reserve Board, Federal Deposit Insurance Corporation, and Federal Home Loan Bank Board authorized, effective June 1, two new categories of time deposits. One was an 8-year account yielding up to 7¾ per cent at commercial banks and up to 8 per cent at thrift institutions. The other was a 6-month, $10,000 minimum "money market certificate" whose ceiling rate would vary with the average yield in the weekly auction of 6-month Treasury bills; the ceiling for banks was equal to the auction average and that for thrift institutions was 1/4 of a percentage point higher. Because the combination of rapid growth in *M*-1 and brisk inflation caused the System to tighten reserve availability another notch just before midyear, the structure of market interest rates rose enough to make the 8-year account relatively unattractive to most savers. However, the 6-month account, with its ceiling rate tied to current market yields, proved immediately successful in supporting deposit flows to banks and thrift institutions.

Growth in *M*-1 moderated somewhat in the third quarter because of the slowing in economic expansion and the accumulating impact of more restrictive credit conditions. Nevertheless, with *M*-1 still increasing quite rapidly and the dollar under downward pressure on foreign exchange markets, the System moved steadily toward tighter money market conditions. The Federal funds rate rose about 1 percentage point over the quarter, to about 8¾ per cent, and the discount rate was raised in three steps from 7 to 8 per cent. Other short-term interest rates increased by similar amounts. Bond yields generally fell in late July and early August, when evidence of slowing economic activity led many investors to think that interest rates might be nearing cyclical peaks; but these long-term rates moved up again toward the end of the summer as short-term rates continued to climb and inflation showed no sign of abating.

Despite the advance in short- and intermediate-term market rates during the third quarter, growth in interest-earning deposits at commercial banks and thrift institutions continued to accelerate and thus to contribute to more rapid expansion in *M*-2 and *M*-3. The faster growth of *M*-2 reflected a sharp increase in large-denomination time deposits included in this aggregate, which are not subject to Regula-

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tion Q ceilings, and sizable sales of the new money market certificates. The 6-month certificates had an even larger impact on the growth of *M*-3, as deposit inflows at savings and loan associations and mutual savings banks accelerated sharply during the summer.

The advance of market interest rates in the third quarter was followed by an increase in the discount rate to 8½ per cent in mid-October. Despite the substantial rise of U.S. interest rates and progress toward reduction of the Federal budget deficit, participants in foreign exchange markets remained apprehensive about U.S. price and trade prospects, and the dollar came under extraordinary downward pressure. After the President announced his wage-price program on October 24 the dollar's decline accelerated, threatening to undercut the anti-inflation effort at home and to lead to greater erosion of confidence abroad.

The Federal Reserve responded by announcing on November 1 an increase of 1 percentage point in the discount rate and a supplementary reserve requirement of 2 percentage points on large-denomination time deposits. In conjunction with the Treasury, a series of actions was outlined that would increase access to foreign currencies for exchange-market intervention. The System also adjusted its open market operations to restrict further the availability of nonborrowed reserves.

As a result, the Federal funds rate rose to nearly 10 per cent, and short-term interest rates increased sharply. Bond yields initially declined, since investors apparently viewed the actions of the Government on November 1 as enhancing prospects for the control of inflation; however, they reached their highest levels of the year in December as a result of a further increase in short-term market rates, the announcement of a rise in oil prices by the Organization of Petroleum Exporting Countries that was larger than anticipated, and evidence of strong economic growth in the fourth quarter.

The appreciable rise in market interest rates likely contributed to a moderation in *M*-1 expansion in the fourth quarter to the lowest rate in 2 years. Another factor was the introduction of a new banking service on November 1 that permits individuals to have funds transferred automatically, as needed, from savings to checking accounts at commercial banks; a substantial volume of funds was shifted from demand deposits to savings deposits as customers took advantage of this new means to economize on nonearning transactions balances. Because of the slackened pace of growth in *M*-1, expansion

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of *M*-2 and *M*-3 also slowed somewhat in the fourth quarter even though inflows to money market certificates and large time deposits sustained sizable gains in the interest-earning components of the broader aggregate.

AGGREGATE FLOWS OF FUNDS

Total funds raised in domestic financial markets by all sectors are estimated to have increased from $400 billion in 1977 to $483 billion in 1978. A rise of nearly 60 per cent in funds raised by financial sectors was attributable to enlarged borrowing by both private and government-sponsored financial intermediaries. Funds raised by nonfinancial sectors of the economy increased 14 per cent, a considerably slower growth than in previous years of the cyclical upswing. The effects of tightening credit markets were perhaps most evident in the markedly decelerated growth in flows of funds to private domestic nonfinancial sectors after the second half of 1977.

The household sector borrowed a record amount in 1978. Home mortgage debt formation increased moderately from the previous year's total, as demand for housing credit remained strong despite the sharp upward movement in interest costs. Most of the rise in household credit flows, however, was in consumer credit. The annual rate of growth in such credit outstanding was about 17 per cent in each half of the year, and tracked fairly closely the strong upward movement in consumer spending on durable goods. Repayment obligations for both mortgage and consumer debt increased substantially in 1978, raising the ratio of repayments to disposable personal income to a record high.

Nonfinancial businesses also increased their demands for funds in 1978. Although nonfinancial corporations experienced an appreciable rise in reported pretax profits, growth in their outlays for inventories and fixed capital outstripped the increase in gross internal funds and caused a large increase in external financing requirements. The composition of external financing also changed, as many firms avoided issuing bonds at the relatively high interest rates prevailing and instead relied heavily on shorter-term bank loans and commercial paper. Gross public offerings of corporate bonds fell to the lowest level since 1973, owing mainly to the absence from the market of large, highly rated industrial issuers, and private place-

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ments declined somewhat from the record volume of 1977. Business use of mortgage credit increased sharply in 1978, reflecting in part the substantial improvement in commercial construction activity during the year. Historically low price-earnings multiples discour-

Net Funds Raised and Supplied in Credit Markets

Billions of dollars

Sector or type of instrument	1975	1976	1977	1978	1977[1]		1978[1]	
					H1	H2	H1	H2
Total funds raised	**219.8**	**301.7**	**399.4**	**483.2**	**363.7**	**435.0**	**481.1**	**485.3**
Sector								
Nonfinancial sectors, total	208.1	272.5	340.5	389.4	302.2	378.9	378.1	400.7
U.S. Government	85.4	69.0	56.8	53.7	42.6	71.0	58.7	48.6
State and local government	13.2	18.5	25.9	24.9	22.7	29.0	21.7	28.1
Nonfinancial business	47.7	74.4	106.0	123.9	98.1	113.7	125.5	122.2
Households	48.6	89.9	139.6	161.3	131.2	148.0	155.0	167.5
Foreign	13.2	20.7	12.3	25.7	7.5	17.2	17.2	34.1
Financial sectors, total	11.7	29.2	58.8	93.8	61.5	56.2	102.9	84.6
Sponsored credit agencies	3.2	2.9	5.8	22.6	7.2	4.4	24.9	20.2
Mortgage pools	10.3	15.7	20.5	16.5	17.9	23.1	16.6	16.3
Private financial intermediaries	−1.9	10.6	32.6	54.7	36.5	28.7	61.4	48.0
Type of instrument								
U.S. Government securities	98.2	88.1	84.3	92.8	70.0	98.6	100.3	85.2
Public debt and budget agency securities	85.5	69.1	56.9	53.8	42.6	71.0	58.8	48.7
Other	12.7	19.0	27.4	39.0	27.4	27.5	41.5	36.5
Corporate and foreign bonds	36.4	37.2	36.1	32.1	30.5	41.7	32.3	31.8
Corporate equities	10.8	12.9	4.8	3.6	2.5	7.0	3.0	4.2
Tax-exempt securities	15.6	19.0	29.2	29.6	29.3	29.0	28.5	30.7
Mortgages	57.2	87.1	134.0	145.9	121.2	146.7	140.3	151.5
Residential	41.4	67.3	106.8	112.4	98.1	115.4	110.5	114.2
Other	15.8	19.8	27.2	33.5	23.1	31.3	29.8	37.3
Bank loans, n.e.c.	−13.9	6.4	32.2	50.2	28.4	35.9	48.2	52.2
Open-market paper and repurchase agreements	−2.4	13.3	19.8	42.8	27.6	11.9	43.7	41.9
Consumer credit	9.4	23.6	35.0	50.5	35.7	34.4	49.8	51.2
Other	8.6	14.1	24.0	35.6	18.5	29.8	34.8	36.3
Total funds supplied	**219.8**	**301.7**	**399.4**	**483.2**	**363.7**	**435.0**	**481.1**	**485.3**
Sector								
Private domestic nonfinancial	41.2	40.7	55.5	84.1	44.6	66.3	88.4	79.9
Households	25.6	13.3	30.7	52.6	28.1	41.2	58.7	46.4
Nonfinancial business	12.3	12.7	−1.5	8.3	−2.0	−1.0	6.4	10.2
State and local government	3.4	14.7	26.4	23.3	26.5	26.2	23.3	23.3
Private financial intermediaries	129.6	203.7	255.7	294.3	247.4	264.2	285.3	303.5
Commercial banks	27.8	58.0	85.8	119.2	81.1	90.5	120.4	117.9
Thrift institutions	52.1	71.5	85.2	79.2	85.7	84.7	77.3	81.0
Insurance and pension funds	50.8	66.0	72.1	78.4	72.0	72.3	74.6	82.0
Other	−1.1	8.2	12.6	17.8	8.6	16.7	13.0	22.5
U.S. Government and sponsored credit agencies	19.3	13.9	18.3	45.9	14.8	21.8	47.4	44.3
Mortgage pools	10.3	15.7	20.5	16.5	17.8	23.1	16.6	16.3
Federal Reserve System	8.5	9.8	7.1	7.0	10.2	4.2	13.0	1.0
Foreign sources	10.8	17.9	42.2	35.3	28.9	55.4	30.3	40.3

[1] Half-year figures are at seasonally adjusted annual rates.

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aged new stock issues, and a sizable volume of outstanding shares was retired through repurchases and mergers. The relatively modest acquisitions of liquid assets by nonfinancial corporations in 1978, together with heavy emphasis on short- and intermediate-term borrowing, caused measures of corporate liquidity to lose much of the improvement recorded earlier in the economic expansion.

Net borrowing by State and local governments remained large in 1978, roughly equaling the previous year's unprecedented level; it included a record amount of bond issuance for advance refunding purposes. Nearly all of these advance refunding operations were conducted prior to September, when changes in rulings of the Internal Revenue Service reduced their attractiveness. Tax-exempt yields rose sharply in the final months of the year, yet remained quite low historically relative to yields on taxable bonds. Commercial banks and property-casualty insurance companies acquired the bulk of tax-exempt securities in 1978, but households were substantial buyers as well.

The U.S. Government continued to borrow a sizable volume of funds to finance its deficit in 1978. Major purchasers of Treasury securities included households, foreign central banks (which generated a large volume of investable funds through dollar-support operations in foreign exchange markets), and State and local government units (which were investing the proceeds of their advance refunding operations in special nonmarketable issues). The Treasury concentrated its marketable borrowing in coupon securities, chiefly issues with intermediate-term maturities. On balance, the outstanding supply of Treasury bills remained about unchanged in 1978, while coupon issues increased $33 billion. Net borrowing by Federally sponsored credit agencies increased sharply in 1978, reflecting primarily activities of the agencies responsible for channeling funds to the residential mortgage market.

Private financial institutions again provided the largest volume of funds to nonfinancial sectors in 1978, although the upward movement in market interest rates relative to deposit rate ceilings forced depositary intermediaries to increase their reliance on funds raised in credit markets to meet the strong loan demands. Insurance companies and pension funds continued to acquire large amounts of investable funds, and they purchased a record volume of corporate bonds in 1978. In addition, mortgage lending by insurance com-

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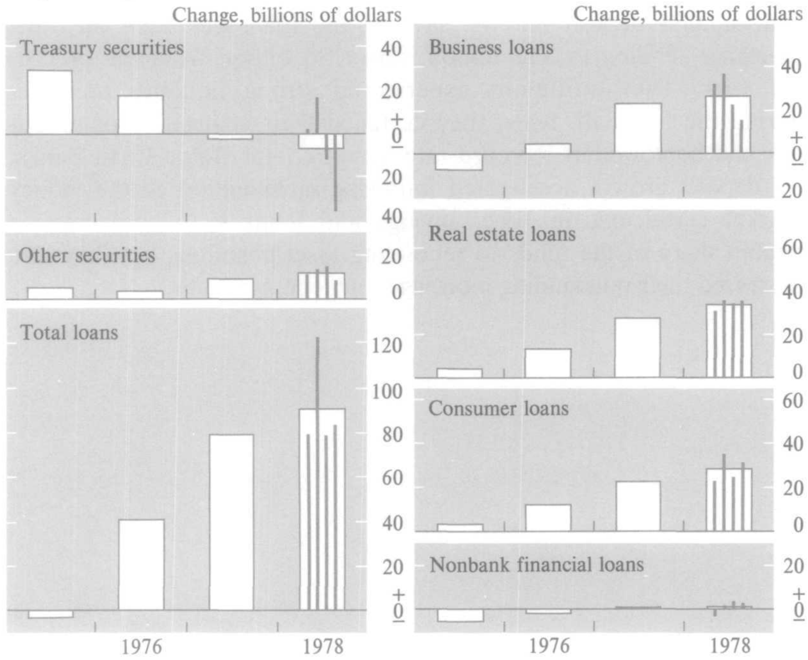
Major Components of Bank Credit



Seasonally adjusted. Total loans and business loans are adjusted for transfers between banks and their holding companies, affiliates, subsidiaries, and foreign branches.

panies reached record proportions, mainly to provide permanent financing for multifamily and commercial structures.

Total loans at commercial banks grew 14½ per cent during 1978. Real estate loans rose markedly, as banks apparently increased their lending to both residential and commercial borrowers. Consumer and business loans also grew rapidly. Inflows into demand, savings, and small-denomination time accounts were insufficient to finance the large increase in lending, and banks reduced their holding of U.S. Government securities and increased their reliance on managed liabilities. Large-denomination time deposits expanded $46 billion during 1978, and banks also obtained sizable amounts of funds from nondeposit sources such as Federal funds and security repurchase agreements. As a result, most conventional measures of aggregate commercial bank liquidity eroded steadily over the year.

At nonbank depositary institutions, total mortgage lending contracted somewhat in 1978, mainly because of a reduced pace of

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mortgage acquisition by savings and loan associations. Confronted with smaller deposit inflows, savings and loans cut back their net mortgage lending to $52 billion, down $6 billion from the preceding year. The institutions experienced strong liquidity pressures during the first half, when they curtailed their acquisition of securities and borrowed at a record rate from Federal Home Loan Banks. As deposit growth accelerated following introduction of the money market certificates in June, savings and loans initially devoted a sizable share of the funds to rebuilding asset positions, but they also increased their outstanding mortgage loan commitments.

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International Developments

The strong downward pressure on the dollar in foreign exchange markets that had begun in September 1977 continued and at times intensified during 1978, leading to the announcement on November 1 of a coordinated package of internal and external stabilization measures. A prime source of concern about the strength of the dollar was the rising rate of inflation and the continued large trade deficit of the United States. The possibility of reducing the U.S. trade deficit was limited by the relatively slow economic recovery in other industrial countries from the 1975 recession. The discrepancy between the high trade deficit and inflation rate of the United States and the trade surpluses and low inflation rates of such countries as Germany, Japan, and Switzerland resulted in a large shift in bilateral exchange rates in 1978.

In the course of the year the focus of concern about current-account imbalances shifted from the large surpluses of the Organization of Petroleum Exporting Countries (OPEC), which fell sharply to about $10 billion, to the imbalances among the United States and other major industrial countries. Although the large deficit of the less developed oil-importing countries as a group expanded further, many of these countries were able to accumulate reserves and the problems of financing the deficits of some others became less acute.

The U.S. merchandise trade deficit rose to more than $35 billion at an annual rate in the final quarter of 1977 and to more than $45 billion at an annual rate in the first quarter of 1978, giving impetus to the decline of the dollar. By the second quarter exports were rising, however, reducing the rate of deficit to about $25 billion by the end of the year. Nevertheless, this high rate of deficit, together with worsening price inflation, continued to undermine market confidence in the dollar.

The performance of U.S. nonagricultural exports was quite strong in 1978, despite slack demand in other industrial countries. Export volume of these products increased 16 per cent from the fourth quarter of 1977 to the fourth quarter of 1978 while export prices in dollar terms rose about 13 per cent. During the year the depreciation of the dollar tended to enhance the competitiveness of U.S.

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products as prices in terms of foreign currency held relatively steady. Agricultural exports grew quite rapidly, with volume up sharply and prices rising.

Imports, other than oil, also grew rapidly in 1978, although the rate of increase in volume tapered off to about 8 per cent from the fourth quarter of 1977 to the fourth quarter of 1978. The dollar price of these imports rose considerably, however, as the dollar equivalent of prices expressed in foreign currencies was raised by the depreciation of the dollar. The value of oil imports rose moderately in that period: the price declined slightly while the volume rose moderately.

U.S. International Transactions[1]

Billions of dollars

Transaction	1977		1978				
	Year	Q4	Year p	Q1	Q2	Q3	Q4 p
Current account	**−15.3**	**−6.1**	**−16.0**	**−7.6**	**−3.3**	**−3.7**	**−1.3**
Merchandise trade balance	−31.1	−9.4	−34.1	−11.9	−7.9	−8.0	−6.4
Exports	120.6	29.6	141.0	30.8	35.3	36.5	39.3
Imports	−151.7	−39.0	176.0	−42.7	−43.1	−44.5	−45.7
Investment income (net) [2]	17.5	3.8	19.9	4.9	4.6	4.9	5.6
Other services	3.0	.5	3.3	.7	1.2	.7	.7
Unilateral transfers, private and government	−4.7	−1.1	−5.1	−1.3	−1.3	−1.3	−1.2
Private capital flows	**−17.0**	**−9.3**	**−25.7**	**−12.1**	**.8**	**1.8**	**−16.2**
Bank-reported capital, net (outflow, −)	−4.7	−5.6	−17.1	−6.6	1.3	2.3	−14.2
U.S. net purchase (−) of foreign securities	−5.4	−.7	−3.4	−.9	−1.1	−.5	−.9
Foreign net purchase (+) of U.S. Treasury securities	.6	−.3	2.2	.9	.8	−1.1	1.6
Foreign net purchase (+) of other U.S. securities	2.9	.8	2.9	.5	1.3	.5	.6
U.S. direct investment abroad [2]	−12.2	−3.2	−15.4	−5.0	−4.0	−2.7	−3.7
Foreign direct investment in United States [2]	3.3	.5	5.6	.8	1.9	2.2	.7
Other corporate capital flows, net	−1.4	−.8	−.5	−1.7	.5	.8	−.3
Foreign official assets in United States (increase, +)	**37.1**	**15.5**	**34.0**	**15.8**	**−5.7**	**4.9**	**19.0**
U.S. Government foreign assets, net (increase, −)	**−3.9**	**−.8**	**−3.7**	**−.7**	**−.8**	**−1.4**	**−.9**
Reserve position in IMF	−.3	*	4.2	.3	.4	.2	3.3
Convertible currencies and other reserve assets	.1	*	−3.4	−.1	−.1	−.1	−3.1
U.S. Government foreign credits and other claims, net	−3.7	−.8	−4.7	−.9	−1.2	−1.5	−1.1
Statistical discrepancy	**−.9**	**.8**	**11.4**	**4.5**	**9.1**	**−1.6**	**−.6**

[1] Current-account items are seasonally adjusted; seasonal factors are no longer calculated for most capital transactions. Data are from U.S. Department of Commerce, Bureau of Economic Analysis. Details may not add to totals because of rounding.

[2] Includes reinvested earnings.

* Less than $50 million.

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Partly offsetting the increased deficit on merchandise trade was a gain in the net income of U.S. direct foreign investments, reflecting in part the increased dollar value of earnings in countries with appreciating currencies.

The current-account balance of the international accounts—combining trade, services, and unilateral transactions—registered a slightly higher deficit in 1978 than the year before, but the deficit declined sharply from the fourth quarter of 1977 to the fourth quarter of 1978. With export volumes rising faster than import volumes, the international sector made a small net positive contribution to the change in U.S. real product in that period.

The dollar came under severe pressure in exchange markets several times during the year, and reached a low point on October 30 just prior to the announcement of a set of measures aimed at curbing inflation and restoring exchange market stability. From the beginning of the year to the end of October the trade-weighted average value of the dollar against 10 leading currencies had declined about 14 per cent, and declines against a number of currencies had been much greater. The measures announced on November 1 included, in addition to domestic monetary actions, an increase in the Treasury monthly gold auction to 1½ million ounces starting in December; an increase in the Federal Reserve swap lines with Germany, Switzerland, and Japan by $7.6 billion to a combined total of $15 billion; sales of $2 billion equivalent of special drawing rights to those three countries; the drawing of $3 billion of foreign currencies from the International Monetary Fund; and the sale by the Treasury of up to $10 billion equivalent of securities denominated in foreign currencies. All of these measures had been initiated by the end of the year, including the sale in Germany of $1.6 billion equivalent of notes denominated in German marks.

Announcement of these measures and their forceful implementation brought a sharp rise in the dollar's exchange rate—to about the average level of August and September. However, while the market regained a measure of stability, it remained vulnerable to adverse developments. The announcement on December 17 of a larger-than-expected increase in oil prices by OPEC triggered heavy selling pressure. This was met by determined intervention by U.S. and foreign authorities, but by year-end the dollar's weighted-average exchange value was 10 per cent lower than it had been at the beginning of the year.

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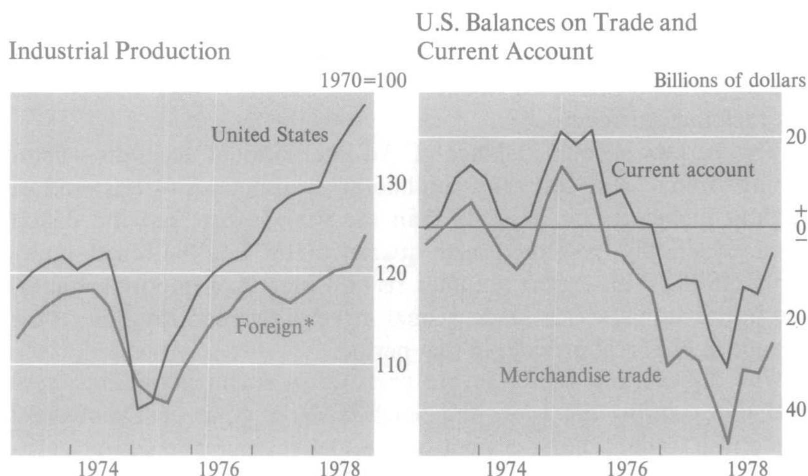

* Multilaterally weighted average of G-10 countries plus Switzerland, using 1972–76 trade weights.

Data are from the U.S. Department of Commerce and are seasonally adjusted annual rates.

Efforts by monetary authorities to combat disorderly markets and severe swings of some exchange rates vis-à-vis the dollar required large-scale purchases of dollars. Such purchases by foreign authorities accounted for most of the rise in foreign official assets in the United States (see the table), which amounted to about $34 billion for the year. The increase accrued to the Group of Ten countries and Switzerland; official holdings of OPEC countries in the United States declined slightly, after having risen by about $7 billion in 1977. U.S. authorities purchased (net) the equivalent of $0.9 billion of foreign currencies in exchange markets in the first 9 months of the year, but sold a large amount in the fourth quarter as pressure on the dollar intensified. The extent of official transactions in exchange markets reflects a number of factors, including not only reactions to the U.S. current-account balance and private capital flows but also desired increases in reserves.

Recorded private capital outflows in 1978 were considerably above the $17 billion recorded in 1977. Much of the outflow occurred early in the year, before U.S. interest rates began a steep rise, and again at the end of the year. Bank-reported capital outflows were substantially higher than in 1977, and U.S. direct foreign investment

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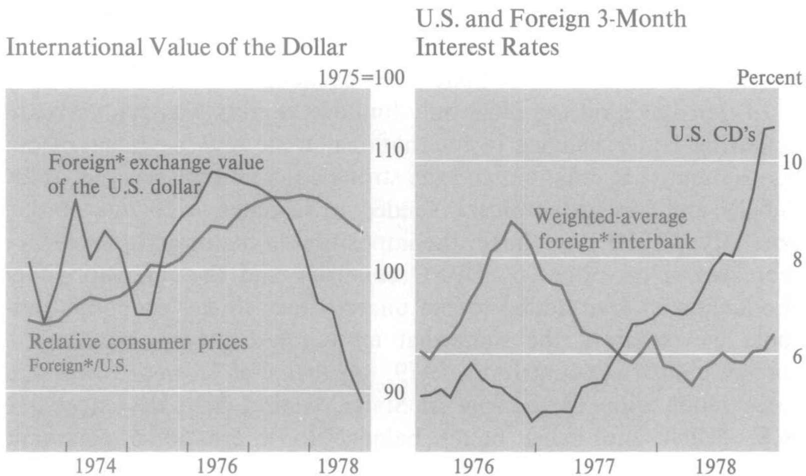

* Multilaterally weighted average of G-10 countries plus Switzerland, using 1972–76 trade weights.

abroad, including a rising amount of retained earnings, was somewhat higher. On the other hand, foreign securities were issued in the U.S. market at a reduced rate, reflecting in part the relatively high level of U.S. interest rates. The unrecorded element in the international accounts was strongly positive at times in the first half.

During the year, the fall in the external value of the dollar became an increasingly strong influence on the course of the economy. Most important, the depreciation of the dollar beginning in the fall of 1977 was greater than the difference between U.S. and foreign inflation rates and exerted a further inflationary influence. As the U.S. economy expanded, and especially as the inflation rate showed a tendency to rise, some upward tilt in interest rates was to be expected. The Federal Reserve, in determining the appropriate stance of monetary policy, emphasized the need to restore confidence in the dollar. Thus, announcements of discount rate increases, from January 6, 1978, when the rate was raised from 6 per cent to 6½ per cent, to November 1, when it was raised to 9½ per cent, stressed the urgency of stabilizing the foreign exchange value of the dollar. In contrast, interest rates in other industrial countries changed little on balance. This divergence was due in large part to the differences in the underlying economic situation between the United States and such

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countries as Japan, Germany, and Switzerland, where domestic demand was relatively slack and inflation rates were low. It also reflects, however, the response of policies to exchange market pressures.

In retrospect, during 1978 only limited progress was made toward achieving better balance in international trade and payments. Concerns about U.S. inflation, and the strong contrast between U.S. trade deficits and foreign surpluses, tended to heighten exchange market volatility. As the year ended, the imposition of major and progressive increases in oil prices by OPEC countries and the interruption of production in Iran added to the uncertainties in the economic outlook. Nevertheless, the somewhat more rapid growth expected in foreign industrial countries in 1979, together with slower growth and price moderation in the United States, should help to reduce the U.S. deficit and bring better balance to international economic relationships.

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Official Statements on Growth Ranges for Monetary Aggregates

Given below are statements by Federal Reserve Chairman G. William Miller on March 9, April 25, July 28, and November 16, 1978, in response to H. Con. Res. 133, passed March 24, 1975, concerning objectives and plans of the Federal Reserve with respect to the ranges of growth or diminution of monetary and credit aggregates in the upcoming 12 months.

STATEMENT BEFORE THE COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS, U.S. HOUSE OF REPRESENTATIVES, MARCH 9, 1978

I am pleased to appear today, for the first time, to present the report of the Board of Governors of the Federal Reserve System on the conduct of monetary policy. This will also be our first report since passage of the Federal Reserve Reform Act of 1977, which originated in this committee and which wrote into law the monetary oversight hearings that have been held quarterly in recent years. These hearings have provided a useful forum for discussion of economic and financial conditions and monetary policy. I have no doubt that they will continue to do so, and look forward to participation in them.

During the past year, the Federal Reserve continued to pursue the objective of fostering financial conditions consistent with expansion of economic activity and moderation of inflationary pressures. Gross national product (GNP)—the broadest measure of economic activity—rose 5¾ per cent in real terms during 1977, about the same rapid pace as we experienced on average in the earlier stages of the current recovery. However, the rate of inflation remained disturbingly high.

Very recently, sales and production have weakened, but this seems to reflect mainly—if not entirely—the temporary effects of the unusually severe winter weather and the coal strike. While prolongation of the strike could lead to more extensive economic disruption, basically our economy is strong, and the year 1978 should see continued expansion in economic activity at a moderate pace and a further

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reduction in the unemployment rate. At the same time, recent trends provide little basis for optimism with regard to an abatement of inflationary pressures.

The brisk increase in production last year made it possible to reduce unemployment significantly despite further large growth in the size of the Nation's labor force. In the past 12 months, the jobless rate has fallen more than a percentage point. Total employment has risen by more than 4 million, and the proportion of our population that is employed stands at the highest level in the postwar period.

The advance of production and employment during the past year was broadly based, with most of the major sectors of aggregate demand registering good gains. Consumer spending followed an uneven course during 1977, but for the year as a whole growth was substantial by historical standards. Residential construction continued to provide considerable impetus to expansion, with single-family housing starts reaching an exceptionally high level and multifamily building also posting appreciable gains from earlier depressed levels. Business fixed investment expanded somewhat more rapidly in 1977 than in earlier years of the recovery, although such investment continued to lag well behind its performance in previous cyclical upswings. The pace of governmental spending—at both the Federal and the State and local levels—also picked up last year.

As domestic activity expanded rapidly, our imports of goods from abroad continued their steep climb, boosted by our increasing appetite for imported oil. Meanwhile, the sluggish performance of economic activity in other major industrial countries limited the demand for our exports. As a result, our trade deficit deepened from about $10 billion in 1976 to more than $30 billion in 1977.

The widening of the trade deficit contributed importantly to the downward pressure on the exchange value of the dollar over the past several months. The Federal Reserve, in cooperation with the Treasury, has taken steps to counter disorder in foreign exchange markets and to emphasize U.S. concern about the integrity of the dollar. But the key to a sound dollar and a stable world financial system lies ultimately in the resolution of some of our fundamental, longer-range economic problems. In particular, we must establish an energy policy that promises to reduce our reliance on foreign sources of petroleum; we must create a better climate for business investment, so as to enhance labor productivity and to increase our international competi-

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tiveness; and most importantly, we must make progress toward the restoration of domestic price stability.

One of the great disappointments of the past year has been the lack of progress in reducing the pace of inflation. Wage increases have continued to outstrip gains in output per hour worked; unit labor costs in private industry have again risen substantially; and prices have been trending upward at about a 6 per cent annual rate.

Prudent monetary management is, of course, an essential ingredient in the control of inflation over the longer run. Too much money growth would add to inflationary pressures and would tend to encourage still larger increases in wages, costs, and prices.

Confronted with very strong demands for money and credit this past year, the Federal Reserve took actions to moderate monetary growth and to help ensure that inflationary forces would not get out of hand. Although interest rates have risen, domestic financial markets have remained supportive of economic growth. Supplies of credit have been ample, with the total volume of funds raised in the Nation's money and capital markets approaching $400 billion in 1977—a record both in dollar terms and as a percentage of GNP.

In the household sector mortgage loans accounted for the bulk of an unprecedented increase in indebtedness. Families sought mortgage credit not only to finance the purchase of homes but also to fund other expenditures and to add to their holdings of financial assets. Meanwhile, consumer instalment credit grew very rapidly, especially during the first half of the year when sales of new cars were strongest.

Borrowing by nonfinancial business firms also rose sharply in 1977. The volume of new publicly offered bond issues fell off somewhat from the preceding year, as many of the larger, higher-rated companies had completed the restructuring of their debt in 1975 and 1976. But lower-rated firms continued to place large quantities of bonds privately with life insurance companies and other lenders. And companies of all types tapped financial institutions for increased amounts of mortgage and term loans, as well as for short-term credit.

Governmental demands for credit in 1977 remained exceptionally large by historical standards. Borrowing by State and local units surpassed previous levels by a wide margin. A substantial portion of the increase in tax-exempt bond issuance was for the advance refunding of debt obligations incurred in prior years when interest rates were higher, but States and municipalities also borrowed large amounts

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for current and future capital outlays. At the Federal level, the outstanding volume of Treasury debt rose by the third largest amount in history, as a consequence of the U.S. Government's large budget deficit. Financing of the continued Federal deficit contributed to upward pressures on interest rates last year—a year in which private credit demands were especially strong.

In an environment of briskly expanding economic activity and credit demands, the monetary aggregates also tended to grow more rapidly last year. The public's demand for *M*-1—currency and checking account balances—strengthened considerably, and growth in this measure of money accelerated. Over the year as a whole, *M*-1 grew about 7½ per cent, well in excess of the range established by the Federal Reserve. The broader monetary aggregates—*M*-2 and *M*-3—grew at rates near the upper end of the ranges that had been adopted by the Federal Reserve in early 1977.

Knowing that a sustained, rapid monetary expansion would threaten a build-up over time of inflationary pressures, the Federal Reserve began in early spring to be less accommodative in its provision of reserves to the banking system. The adjustment of policy was a cautious one, in view of the possibility that the burst of monetary expansion that had developed might reflect simply a transitory swing in the public's demand for cash balances. But as relatively rapid monetary expansion continued, the Federal Reserve gradually exerted increasing restraint in the provision of bank reserves relative to the strong demands for them.

As a result, the Federal funds rate—the rate banks pay to borrow reserves from one another on an overnight basis—rose about 1¾ percentage points from April to October, reaching a level of about 6½ per cent. And the discount rate at Federal Reserve Banks was raised in two steps to 6 per cent by late October. Subsequently, in early January, the discount rate was increased to 6½ per cent and the Federal funds rate was moved slightly higher to help stabilize conditions in the market for dollars on international exchanges.

Over all, since last April short-term market rates of interest have risen about 2 percentage points. Intermediate- and long-term yields have also risen, with increases largest in the market for Treasury securities, where rates have adjusted upward by ¾ to 1½ percentage points over the past 10 months. These increases in interest rates on longer-term securities may well have reflected some increase in the

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inflation premium, as investors reacted to the lack of progress in reducing inflation. Neverthless, despite the increases of the past year, most short-term rates are still less than 1 percentage point above their levels at the beginning of the present economic expansion in early 1975, and corporate and municipal bond yields are significantly below their levels then.

Growth rates for all the monetary aggregates have slackened appreciably, on average, in the last few months. Growth in *M*-2 and *M*-3 has slowed, in part, because the rise in interest rates on market instruments has made them more attractive to some savers than interest-bearing deposits at banks and thrift institutions. At the same time, however, demands for loans at depositary institutions have remained strong. Under the circumstances, these institutions have had to supplement their deposit flows by borrowing and by reducing their holdings of liquid assets.

Although these pressures may be causing depositary institutions to become a bit more cautious in their lending policies, credit supplies still appear to be ample. Moreover, the financial condition of the key nonfinancial sectors remains generally strong. It is true that household debt burdens, as measured, for example, by the ratio of consumer and mortgage loan repayments to disposable income, are historically high, and they deserve careful monitoring. But to date, there has been no rise in delinquency rates, so families appear thus far to be handling their increased indebtedness well. Businesses added further to their liquid assets last year, and corporate balance sheets on the whole appear to be strong, although there is considerable variation from firm to firm. And State and local governments, with record operating surpluses in 1977, appear in the aggregate to enjoy a healthy financial position.

Thus, financial conditions remain supportive of expansion in economic activity. As 1977 drew to a close, aggregate demands for goods and services were strong. As I noted earlier, severe winter weather and the coal strike have caused some steep declines in economic indicators recently. However—assuming a reasonably prompt resumption of activity in the coal industry—we can expect favorable underlying trends soon to reassert themselves. Growth of employment and income has been substantial over recent quarters, and consumer confidence has remained high. Consumer spending, therefore, should grow at a reasonably good pace and would be bolstered later this

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year by the proposed tax cuts. In the business sector, new orders for nondefense capital goods have continued the uptrend that began about 3 years ago and presage further expansion in business fixed investment. In addition, the rate of inventory accumulation is likely to accelerate in coming months; inventory investment had slowed in the fourth quarter, and stocks are lean in many product lines. Moreover, with prospects for our exports improved by the likelihood of stronger economic growth abroad this year, it appears that our foreign trade deficit will not deteriorate further.

Over all, it is the Federal Reserve's judgment that trends in the national economy favor continued expansion at a moderate rate in economic activity and a further reduction in the rate of unemployment over the course of 1978. There is, however, less reason to be sanguine about progress in curbing the rate of inflation. Food and material prices have risen substantially in recent months. And labor costs continue to rise at a relatively rapid rate. The decline in the value of the dollar on international exchanges is another cause for concern. It not only contributes to upward pressures on domestic prices but also threatens to erode business confidence here and abroad.

The monetary growth ranges that were adopted by the Federal Open Market Committee (FOMC) at its February meeting are expected to prove consistent with continued expansion in economic activity, as well as with a gradual winding down of inflation over the longer run. For the year ending with the fourth quarter of 1978, the *M*-1 growth range was set at 4 to 6½ per cent. A range of 6½ to 9 per cent was established for *M*-2, which includes, in addition to *M*-1, time and savings deposits other than large certificates of deposit (CD's) at commercial banks. And a growth range of 7½ to 10 per cent was adopted for *M*-3—which includes, besides *M*-2, deposits at nonbank thrift institutions.

The ranges for *M*-1 and *M*-2 are identical to those that the Committee previously had adopted for the year ending in the third quarter of 1978. The range for *M*-3, however, has been adjusted downward by ½ percentage point in light of the higher level of market interest rates now prevailing and the apparent effect of these rates in retarding growth in time and savings deposits at thrift institutions. All of the ranges adopted by the FOMC anticipate a deceleration of monetary expansion from the growth rates actually recorded in 1977.

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Progress over time in this direction is necessary to ensure the ultimate achievement of reasonable price stability.

Specification of growth rates for the aggregates is, of course, subject to considerable uncertainty. The rate of growth in money needed to support economic expansion depends in part on changes in the velocity of money—that is, on the rate at which the public uses the existing stock of money to finance transactions. In recent years, regulatory changes and financial innovations have encouraged increases in the velocity of *M*-1 by enabling the public to economize on demand deposits. However, the retarding effect of such changes and innovations on the demand for *M*-1 apparently diminished in 1977, when *M*-1 growth accelerated. Thus far in 1978, growth in *M*-1 has been quite moderate, but it is far too early to say whether this marks a slower trend in growth or is simply a transitory development in a highly volatile series.

The behavior of the broader aggregates—*M*-2 and *M*-3—will be affected in the year ahead by the constraint placed on the ability of depositary institutions to attract funds under existing regulatory ceilings on deposit rates. Banks have adjusted to the recent marked slowing of inflows of deposits subject to rate ceilings in part by offering increased amounts of large-denomination time deposits, which are not subject to ceilings. Some of these deposits, mainly large-denomination deposits issued in nonnegotiable form, are included in *M*-2 and *M*-3; they have tended to sustain growth in these aggregates, especially *M*-2, in recent months.

There are other factors that may work to sustain growth in the broader aggregates in the year ahead. To some extent, the recent slowdown in inflows of savings and also small-denomination time deposits may represent a one-time shift of highly interest-sensitive funds; if so, once the shift has been completed, deposit growth should strengthen somewhat. Moreover, the fact that longer-term time certificates, which are subject to heavy penalties for early withdrawal, account today for a larger share of interest-bearing deposits—especially at thrift institutions—suggests that over-all deposit growth should be less volatile than in the past.

Nonetheless, if heavy demands for money and credit should place further upward pressure on market interest rates, deposits subject to regulatory rate ceilings will be placed at a substantial competitive disadvantage. In such a circumstance, growth in *M*-2 and *M*-3 could fall

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short of the ranges. Upward adjustments in the ceiling rates on some or all categories of time deposits may be required to avoid a potential distortion in the flow of credit through our financial system, to promote equity for small savers, and to ensure the availability of loans to home buyers and others who rely on institutional sources of credit.

We recognize the considerable uncertainties surrounding the shorter-run relationship between growth rates of the monetary aggregates, on the one hand, and the behavior of output and prices on the other. The Federal Reserve will continue, therefore, to maintain a vigilant and flexible approach, putting the long-run performance of the economy above the pursuit of any fixed monetary growth rates.

Economic and financial developments in the current year, it should be noted, will depend to an appreciable extent on governmental policies beyond the province of the Federal Reserve. The outcome of legislative action on energy policy and on taxation will have a considerable influence on the strength of business investment and on international confidence in the dollar. So, too, will this Nation's ability to find a way to reduce the upward wage-price pressures that continue to plague our economy.

STATEMENT BEFORE THE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS, U.S. SENATE, APRIL 25, 1978

Mr. Chairman, members of the committee, it is a pleasure to meet with you and to report, on behalf of the Board of Governors of the Federal Reserve System, about the outlook for the national economy and about the course that the Federal Reserve has chartered for monetary policy over the year ahead. I look forward to a continuing dialogue with you on these matters at this committee's regular monetary oversight hearings.

Economic Activity Is Rebounding

The economy is currently rebounding from a slack period early in the year when economic activity was constrained by severe weather and the long coal strike. Retail sales and industrial production have risen sharply since midwinter. Auto sales have strengthened. Housing starts increased markedly in March from the relatively depressed levels of January and February.

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Employment has grown steadily since the beginning of the year. Although the length of the average workweek declined in the first quarter, the number of people on the Nation's payrolls rose substantially between December and March, and the unemployment rate edged down from 6.4 to 6.2 per cent. The continuing uptrend in employment suggests that businessmen have had sufficient confidence in the underlying strength of the economy to be positioning themselves for further increases in production.

Looking ahead, growth in economic activity is expected to be sustained over future months by expanding consumer and business demands. The near-term prospects for good gains in consumer spending appear favorable, as indexes of consumer sentiment have remained at high levels.

Business spending also should provide impetus to expansion. Inventories generally remain lean, and businesses are likely to be building their stocks in the next few quarters. Business investment in plant and equipment, after lagging early in the economic upswing, has increased at a good pace over the past 2 years. Surveys of capital spending plans and other advance indicators suggest at least moderate further growth in the year ahead.

Although State and local governments by and large continue to pursue cautious financial policies, they also may register significant increases in real expenditures in the period ahead. Residential construction should show sizable increases in the next few months before tapering off gradually in the second half of this year. And the foreign trade deficit, while remaining large, should moderate somewhat from the very high first-quarter rate.

But Inflation Has Worsened

While the prospects for economic activity thus appear to remain favorable, there are other aspects of recent economic performance that reflect fundamental problems, which will not be put behind us quickly. Inflation undoubtedly is the most troubling of these to the American people. Even as growth in real gross national product was interrupted in the first quarter, the rate of increase in prices accelerated. Wholesale prices rose at a 9.6 per cent annual rate during the past 3 months —well above the already uncomfortably high rates experienced last year. Consumer price increases also accelerated. To be sure, a substantial spurt in volatile food prices contributed importantly to the

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advance in the broad price indexes, but prices of industrial commodities and of services also have continued to rise at a brisk pace. These unfavorable trends in prices are displayed in the charts.

Upward Cost Pressures Remain

There is little reason to be optimistic about the likelihood of achieving a significant reduction in underlying inflationary forces in the near future. Cost pressures remain strong. In 1977, for example, total compensation per hour in the private business sector rose almost 9 per cent, while productivity increased only 2½ per cent; as a result, unit labor costs rose more than 6 per cent. There has been no sign of any abatement of the advance in wage rates, and at this stage of economic expansion there is little likelihood of a sustained pick-up in productivity growth. Therefore, rising unit labor costs can be expected to continue to exert considerable upward pressure on prices.

Governmental Programs Have Added to Costs and Inflation

Price pressures have been exacerbated by governmental actions. Certain tax actions, while they have helped to reduce the budgetary deficit and in this way have worked to restrain one of the forces feeding inflation, simultaneously have added to labor costs. This has been the case, for instance, with increases in employer contributions for social security and unemployment insurance. Some other governmental actions also have added to inflationary forces without any compensating restraint. In this class are the increase in the minimum wage, agricultural price supports, and various import restrictions. In general, there has been a tendency by Government over the years to treat the problems of individual sectors without adequate regard to the cumulative inflationary bias that the programs have imparted to the economy.

So Too Has the Declining International Value of the Dollar

Another disturbing aspect of economic performance in the opening months of this year has been the pronounced widening of the foreign trade deficit and the weakness of the international value of the dollar. The estimated trade deficit was greatly enlarged in the first quarter of 1978, as exports remained sluggish and imports in nearly all categories increased sharply. Against this backdrop, the dollar declined in foreign exchange markets, and by the end of March its trade-weighted

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value against other major currencies was 8½ per cent lower than early last fall. The depreciation of the dollar is tending to raise the domestic price structure in various ways: higher prices of imported finished goods raise directly the prices paid by consumers; higher prices of imported materials raise the costs of domestic manufacturers; and higher prices of foreign goods reduce the pressure to hold down prices of the domestically produced goods with which they compete in our markets.

In recent weeks, the dollar has risen relative to other major currencies. Such a trend, if continued, will help moderate inflationary pressures.

The President's Anti-Inflation Program Offers Hope of Breaking Inflationary Psychology

President Carter recently outlined a broad program to help deal with the problem of inflation. The Federal Reserve welcomes this initiative. Given the support of the Congress and of the general public, the program is a constructive step toward breaking the inflationary patterns and psychology that today are so firmly entrenched. The job of containing inflation requires a concerted effort on the part of all Americans. The Federal Reserve will play its part in supporting the President's initiative by exercising appropriate restraint in the provision of bank reserves, credit, and money.

The prospects for inflation will play a major role in shaping future financial developments. The strength of the dollar on foreign exchange markets is influenced by expectations about inflation. So, too, is the level of interest rates in domestic credit markets. The increase in interest rates during the past 12 months—especially the increase of ½ to ¾ of a percentage point in long-term bond rates—may be attributable in part to heightened inflationary expectations.

Monetary Policy Has Been Adjusted To Restrain Unduly Rapid Monetary Growth

Yields on most short-term market instruments today are about 1¾ to 2 percentage points higher than a year ago. This rise has occurred gradually as the Federal Reserve adjusted its policies in light of the tendency for monetary expansion to exceed the growth ranges that had been established. The tendency was most pronounced in the case

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of the narrowly defined money stock, *M*-1, which includes only currency and demand deposits. Largely as a result of the rapid expansion of *M*-1, however, growth in the broader monetary aggregates—*M*-2 and *M*-3—also has remained near the upper ends of their ranges. *M*-2 is *M*-1 plus time and savings deposits at commercial banks (other than large negotiable certificates of deposit), while *M*-3 includes also time and savings deposits at thrift institutions.

For most of the current cyclical expansion, growth in *M*-1 has been well within the ranges established by the Federal Reserve. Indeed, early in the expansion, growth was near the low end of the range. In part, this was the result of actions by the public to shift funds from demand deposits to interest-bearing savings deposits and market instruments in response to financial innovations that made it easier to transfer funds in and out of savings deposits. In part, it seems to have reflected a lagged response to the unusually high level of interest rates reached during the 1973–74 inflation. And in part, it may also have reflected the return of confidence during economic recovery, which made the public more willing to spend out of existing cash balances and which thus reduced the need for the Federal Reserve to supply additional money to the economy.

By last year, the moderating impact on money growth of such factors had considerably lessened. Moreover, persisting upward cost and price pressures were making it difficult for the Federal Reserve to hold money growth within bounds while not risking undue interference with continued economic expansion. Finally, it is possible that the public earlier had reduced its cash balances to unsustainably low levels relative to income and that some part of the sizable expansion in money last year reflected a restoration of cash balances to more normal levels.

Money Growth Has Slowed

Growth in the monetary aggregates slowed during the latter part of 1977 and in the early months of 1978. *M*-1 has moved back within the ranges of the Federal Open Market Committee, while *M*-2 has moved from the upper limits of the ranges toward the lower limits. *M*-3 has behaved about the same as *M*-2. This moderation of monetary expansion has reflected in part the cumulative impact of the restraining actions and rise of short-term interest rates that began in the spring of last year. The influence of interest rates has been most

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evident in the case of the interest-bearing components of the monetary aggregates. As market rates of interest rose relative to deposit rate ceilings, some savers shifted their funds from deposits at banks and nonbank thrift institutions into market instruments, in the process contributing to the slowing of growth of M-2 and M-3.

With Credit Demands Strong, Liquidity of Banks and Thrifts Has Come under Pressure

The slowing of monetary expansion in recent months, in conjunction with strong credit demands, has been accompanied by some erosion in the liquidity of depositary institutions. To finance business, consumer, and mortgage credit demands, commercial banks have turned increasingly to the short-term credit markets as a source of funds. There has been marked growth in the outstanding volume of large-denomination time deposits, which are not subject to regulatory interest rate ceilings, and in the nondeposit interest-bearing liabilities of banks. At the same time, banks have appreciably reduced their holdings of Treasury securities. Despite these changes in bank portfolios, however, customary measures of bank liquidity still indicate more comfortable conditions than prevailed a few years ago.

Thrift institutions, with the exception of credit unions, have experienced much the same pressures as commercial banks since mortgage loan demand has remained strong. To accommodate that demand, institutions—in particular, savings and loan associations, which are the largest home mortgage lenders—have borrowed heavily from Federal home loan banks and curtailed their acquisition of securities.

The savings and loans have also utilized other sources of funds, including the growing markets for private mortgage-backed bonds and mortgage pass-through securities, to sustain new mortgage lending. These markets promise ultimately to give thrift institutions greater flexibility in managing their portfolios and to make the residential mortgage market less dependent on thrift institutions' deposit flows. At present, however, with deposit flows running weaker and liquidity coming under pressure, savings and loans have cut back on the outstanding volume of loan commitments since the year-end. And mortgage interest rates have risen moderately in recent months.

Credit Remains Generally Ample, However

Despite the greater pressures experienced by depositary institutions, credit generally remains in ample supply. Borrowers are experiencing

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little difficulty in raising needed funds at current interest rate levels. And while higher than a year ago, interest rates are at relatively modest levels after allowance is made for the effect of inflation.

Monetary Growth Ranges for the Year Ahead Are Expected To Support Further Economic Expansion and a Lower Unemployment Rate, but Inflation May Not Decelerate Until Later

The ranges of monetary expansion adopted by the Federal Open Market Committee for the year ending with the first quarter of 1979 reflect our belief that growth in the monetary aggregates should be moderate, with credit remaining in reasonably good supply. The Committee has specified a growth range for *M*-1 of 4 to 6½ per cent. For *M*-2, the range selected is 6½ to 9 per cent, and for *M*-3, 7½ to 10 per cent. These ranges are the same as the Committee had earlier specified for the year ending with the fourth quarter of 1978. Although the FOMC at this time has not made a further reduction in its monetary growth ranges, it remains firmly committed to a gradual reduction in monetary growth over time to rates more nearly consistent with reasonable price stability. The ranges just adopted in fact contemplate that actual monetary growth in 1978 and into early 1979 will be slower than last year. Because there have been signs of a resurgence in *M*-1 growth over the last few weeks, the Federal Reserve has recently been less accommodative in supplying reserves in order to keep monetary growth within reasonable bounds over the long run. The money market in consequence has tightened a bit over the past few days.

In addition to adopting ranges for the monetary aggregates, the FOMC also adopted an associated range for bank credit that projects an increase of between 7½ and 10½ per cent over the 1-year period ahead. Such a range would allow for continued expansion in bank credit at around its recent pace.

It was the consensus of the FOMC that expansion of monetary and credit aggregates within these ranges would be consistent with moderate growth in real GNP over the coming year and with some further decline in the unemployment rate. However, upward price pressures remain strong, and the rate of increase in the average price level, therefore, might be somewhat more rapid over the year ahead than it was in 1977. Full and effective public support of the administration's anti-inflation program, and success in keeping the budget deficit

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under control, would aid in restraining upward pressure on prices and would help create conditions whereby we could look forward to a gradual deceleration of the inflationary process.

Let me supplement this with my own views about the outlook for the economy in quantitative terms. My personal expectation is that, over the year ending with the first quarter of 1979, real GNP probably will increase in a range of 4¼ to 5 per cent, the unemployment rate probably will drop into the area of 5¾ to 6 per cent, and the GNP price deflator is likely to rise by 6¾ to 7¼ per cent. It is hardly necessary to add that quantitative projections, such as these, are subject to considerable margins of uncertainty. Necessarily they have to be re-evaluated on the basis of incoming economic data and changing conditions here and abroad.

Specifying growth rates for the monetary aggregates, too, is subject to considerable uncertainty. The growth in the narrowly defined money supply (*M*-1) needed to support economic expansion depends in part on changes in the velocity of money—that is, on the rate at which the public uses the existing stock of money to finance transactions. Velocity may rise rapidly or slowly, depending on shifting public preferences for demand deposits as compared with other assets and on the state of consumer and business confidence.

The behavior of the broader aggregates—*M*-2 and *M*-3—will be affected in the year ahead also by the constraint placed on the ability of depositary institutions to attract funds under existing regulatory ceilings on deposit rates. If heavy demands for money and credit should place further upward pressure on market interest rates, deposits subject to regulatory rate ceilings will be placed at a substantial, competitive disadvantage. In such a circumstance, growth of *M*-2 and *M*-3 could fall short of the ranges set by the FOMC, unless there are upward adjustments in the ceiling rates on some or all categories of time and savings deposits.

Federal Reserve Should Not Be Left To Combat Inflation Alone. Effective Anti-Inflation Program Requires Cooperative Effort

The Federal Reserve believes that its determination to hold monetary growth within the ranges just adopted will work to curb inflation over the longer run and at the same time provide adequate money and credit for continued economic growth. However, under current conditions—when inflationary pressures are to a great extent embodied in

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the structure of the economy—any deceleration in monetary growth rates has to be undertaken with caution. The pace of deceleration cannot proceed much more rapidly than the pace at which built-in inflationary pressures are wrung out of the economy if satisfactory economic growth is to be maintained. Thus, bringing inflation under control urgently requires the cooperative efforts of the administration, the Congress, the Federal Reserve, and the private sectors of the economy. The Federal Reserve should not be left to combat inflation alone.

STATEMENT BEFORE THE COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS, U.S. HOUSE OF REPRESENTATIVES, JULY 28, 1978

Mr. Chairman and members of this distinguished committee, it is a pleasure to meet with you to present the report of the Federal Reserve on the outlook for the economy and monetary policy.

Economic Gains Continued at a Good Pace into Fourth Year of Expansion

The current economic expansion, which began in early 1975, is now into its fourth year. Only one postwar upswing—that beginning in 1961—has lasted significantly longer. Thus, we have had an unusually durable expansion, and it has been well sustained thus far this year.

Especially encouraging has been the performance of the labor market. Payrolls have swelled by more than 2 million workers since last December. The over-all unemployment rate has dropped below 6 per cent, and the rate for heads of households is 3.6 per cent. Joblessness among youths and minorities remains disturbingly high, but these groups, too, have experienced appreciably improved employment opportunities in recent months.

And Economic Indicators Point to Further Growth

The willingness of businessmen across the country to hire in such large numbers suggests that they are looking forward to further growth of production. And indeed, economic indicators generally point in that direction. Buying sentiment still is at a high level, and

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with recent employment gains providing an impetus to income, consumer spending should continue to rise.

In the business sector, cautious inventory management has kept stocks in good balance in most sectors; rising sales are therefore likely to prompt further advances in inventory investment. Various surveys of business intentions—as well as data on equipment orders and construction contracts—suggest moderate increases in capital spending in months ahead. In addition, our net export balance, which has deteriorated over the past 2 years, is beginning to improve. Imports are likely to rise less rapidly during the next year. At the same time, exports should pick up if activity abroad increases as expected and as the changes in exchange rates that have occurred since last fall improve the competitive position of U.S. goods.

The increase in housing starts last month suggests that construction activity will remain at a high level over the near term, but it appears likely that building will begin to taper off later this year, partly as a consequence of the firmer conditions prevailing in the mortgage market. And growth in State and local government expenditures probably will remain modest, in light of the increasing pressure for restraint in public spending.

On balance, the various indicators of spending and activity suggest that the current expansion will continue in the year ahead. As an expansion matures, however, growth can be expected to moderate, and I think it is likely that over the next four quarters real GNP will grow by about 3¼ to 3¾ per cent. Such a pace should be adequate to keep unemployment from rising; during the second quarter of 1979, the unemployment rate may average 5¾ to 6 per cent.

Inflation, However, Is a Serious Concern

As an expansion continues, there is also always the danger that developing imbalances will weaken and ultimately dissipate its forward thrust. The greatest threat to the present expansion lies in accelerating inflation. Price increases have stepped up sharply so far this year—through May consumer prices rose at an annual rate in excess of 10 per cent. To be sure, much of this surge is attributable to adverse developments in the volatile agricultural sector, and relief from double-digit food price increases should be forthcoming later this year. But the prices of other goods and services also have been rising briskly recently, and the advance in unit labor costs—a key deter-

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minant of price trends—has accelerated. My best guess is that during the four quarters ahead prices in general will rise at an average rate of 7 to 7¾ per cent.

With the economy moving into a period of heavy collective bargaining, the intensified inflation we have been experiencing and the greater tautness of labor markets could be reflected in higher wage demands, and if they are met, labor costs would rise even more rapidly. As it is, these costs will be boosted early next year by additional mandated hikes in social security taxes and in the minimum wage. The continued interplay of wage and price rises, coupled with the legislated cost increases, will make it difficult to achieve much relief from underlying inflationary pressures over the next year.

The strong momentum of inflation must be a central consideration for Government policymakers today. If we pursue a course that does not soon contain the forces accelerating the advance of prices, the result will be increasing economic disruption and distortion, ending in all probability in serious recession. Monetary policy has been—and will continue to be—designed to restrain inflation. But monetary policy cannot do the job alone. Placing too great a burden on monetary policy would entail dangers of severe financial dislocation that could have unfortunate longer-run consequences for the domestic and international economies.

Financial Markets Showing Inflationary Pressures

Financial markets have already begun to show the strains of inflationary pressures. Debt burdens have grown tremendously as households and also businesses have borrowed to finance desired real outlays at rapidly rising prices. Financial institutions meanwhile have experienced declining liquidity as they have attempted to accommodate heavy loan demands. The most obvious sign of these mounting pressures of supply and demand in credit markets has been the upward path of interest rates since the spring of 1977. The increase in interest rates can be attributed in good part to the diminishing confidence of borrowers and lenders that inflation will slow in the future.

The willingness of households to go heavily into debt at relatively high interest rates in some degree reflects a feeling that it is best to buy now before prices rise still further. This sentiment undoubtedly has been a major factor in the demand for houses throughout the

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past few years, and it seems to have played an important role in the burst of sales of cars and other consumer durable goods during the first half of 1978. The volume of consumer and mortgage credit extended in connection with these purchases has been growing rapidly and so has the ratio of debt repayment obligations to disposable personal income; both have reached unprecedented heights. To date, loan delinquency experience has not deteriorated significantly, so households evidently have not encountered serious problems in meeting scheduled payments; however, this situation bears careful watching.

So, too, does the apparently declining level of corporate liquidity. During the past 2 years profits and other internal funds of businesses have fallen increasingly short of the sums needed for investment in inventories and fixed capital. The result has been a rising volume of borrowing and a declining volume of liquid asset accumulation; balance sheet ratios have been deteriorating since late 1976.

On top of these private credit demands have come sizable public demands. State and local governments have issued bonds in record volume during the past couple of years, but these governmental units also have provided funds to credit markets through a record accumulation of financial assets. The same cannot be said for the Federal Government. In financing the Federal budget deficit, the Treasury has competed actively with the private sector for credit and has added to the general upward pressure on interest rates.

Liquidity of Depositary Institutions Has Declined

During the early stages of economic recovery, commercial banks and thrift institutions were able readily to satisfy the loan demands of households and businesses while at the same time adding large amounts of Government securities to their portfolios. In the past year, by contrast, there has been a fairly steady decline in liquidity ratios of these institutions. With rising yields on Treasury bills and other market instruments diverting funds from savings and small-denomination time deposits, commercial banks, besides curtailing security acquisitions, have issued a substantial volume of large certificates of deposit (CD's) and other short-term liabilities. Meanwhile, savings and loan associations—the leading home mortgage lenders—have reduced their holdings of Treasury securities and have borrowed heavily from Federal home loan banks and other sources.

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Growth in *M*-1 High Relative to Long-Run Ranges, But *M*-2 and *M*-3 within Them

The Federal Reserve might have attempted to alleviate some of the liquidity pressures in the economy by aggressively providing bank reserves and money. But at best this would have offered no more than a temporary palliative. And it would have set the stage for an explosion of monetary expansion and exacerbated our problem of inflation.

As it is, since early 1977 there has been a rather persistent tendency for growth in the narrowly defined money stock, *M*-1, to run above the rates the System had projected. Over the past four quarters, for example, *M*-1—which includes only currency and demand deposits—increased 7.9 per cent, well above the range of 4 to 6½ per cent reported to this committee a year ago.

Over the same four-quarter span, however, the broader monetary aggregates—*M*-2 and *M*-3—recorded net increases that were well within their announced ranges. *M*-2 is *M*-1 plus time and savings deposits at commercial banks (other than large negotiable CD's). *M*-3 includes also time and savings deposits at thrift institutions.

The fact that growth rates of *M*-2 and *M*-3 remained within their ranges over the past year, while *M*-1 growth was strong, is attributable to the slowing in expansion of the interest-bearing components of the broader aggregates. A year ago, yields on shorter-term market debt instruments were below those that depositary institutions are permitted to pay on savings and small-denomination time deposits. But as market rates rose, they surpassed the regulatory ceilings, prompting many savers to divert funds from deposits to Treasury securities, money market mutual funds, and other high yielding investments.

New Certificates Enhance Growth of Time and Savings Deposits

To help preserve the competitiveness of depositary institutions—and thus to avoid the distortion of credit flows that might occur if these intermediaries were unable to accommodate borrowers who do not have access to open market sources of funds—the Federal regulatory agencies created two new deposit categories, effective June 1. One is an 8-year time deposit on which banks may pay up to 7¾ per cent and thrift institutions up to 8 per cent. The other is a 6-month, $10,000 minimum balance account whose ceiling is determined by the results of the most recent weekly auction of 6-month Treasury

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bills. Banks are permitted to pay a rate equal to the average discount yield in the auction, and thrift institutions ¼ of a percentage point more.

A noticeable pick-up in inflows to savings and small-denomination time deposits in June is evidence of the success of depositary institutions in exploiting the new certificates. The 6-month floating-ceiling certificate appears to have been quite effective in stemming the outflow of funds into market investments. An estimated $8½ billion of the new instruments were issued in June alone—$6½ billion at thrift institutions—and growth has continued brisk this month.

Need To Restrain Inflation

The Federal Open Market Committee at its meeting last week considered carefully these recent patterns of monetary expansion, as well as the prospects for the economy, in deciding on the appropriate longer-term ranges for the monetary aggregates. Although, as always, members of the committee differed somewhat in their appraisal of the outlook, there was a broad consensus that inflationary pressures would remain strong, if not strengthen, in the year ahead. While the recently published 5.7 per cent unemployment rate is not low by historical standards, most analysts agree that the unemployment levels at which inflationary pressures are likely to mount have been raised substantially by compositional changes in the labor force and by the effects of unemployment compensation and other institutional factors on decisions regarding work. Under the circumstances, it is critical that macroeconomic policy be conducted most prudently at this juncture to assure that economic expansion continues at an appropriate pace without fueling the already unacceptable intensity of inflationary pressure.

Monetary Growth Ranges Unchanged

Growth ranges for the monetary aggregates selected by the FOMC for the year ending with the second quarter of 1979 are identical to those announced 3 months earlier. The range for *M*-1 is 4 to 6½ per cent; for *M*-2, 6½ to 9 per cent; and for *M*-3, 7½ to 10 per cent. The growth range for bank credit, though, was raised to 8½ to 11½ per cent in recognition of the greater share of borrower demands being directed toward banks.

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The committee discussed at some length arguments in favor of raising the upper limit of the range for *M*-1. A major part of the discussion focused on the question of whether the persistent tendency over recent quarters for *M*-1 growth, on average, to overshoot the FOMC's longer-run range represented a fundamental shift in the demand for *M*-1 relative to GNP that should be accommodated. The committee concluded that an upward adjustment in the range at this time would be undesirable in light of continuing inflationary pressures. Nonetheless, it was recognized that, in light of the recent behavior of money demand, growth in this aggregate over the year ahead might well be around its upper limit.

Scheduled regulatory changes could lead to a lower measured growth in *M*-1, however. Once the new regulation allowing automatic transfers of funds from savings to checking accounts goes into effect this coming November, the public can be expected to economize more on demand balances and to shift some funds from demand deposits to savings deposits. Such shifts would tend to reduce growth in *M*-1 during a transition period in which bank customers adjust to the new service. But the extent to which such a shift in funds will occur over the year ahead is quite uncertain. It will depend on the structure of charges posted by banks for the new service and on the speed with which the public takes advantage of the added flexibility in cash management. In the transition period, therefore, *M*-1 will become a less reliable indicator of monetary conditions.

The broader monetary aggregates are not likely to be affected significantly by the automatic transfer regulation. They are expected to grow well within their current ranges in the months ahead, with growth sustained in part by the availability of the new certificate accounts. Thus, a generally ample flow of credit through banks and thrift institutions can be expected.

There are always great uncertainties surrounding monetary projections, but the FOMC believes that these ranges for the four quarters ahead are consistent with further moderate expansion of economic activity. Unfortunately, I cannot report that the committee expects a diminution of inflationary pressure over the coming year. A reduction in the rate of price advance will require more time if it is to be accomplished in an orderly manner, given the present built-in biases toward inflation in the country.

These biases—regulatory, legislated, and expectational—prevented

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the committee from taking a further step at this time toward the lowering of the monetary growth ranges—a process that must be continued over time if the Nation is to achieve reasonable price stability. In any event, under current circumstances, continuation of the present growth ranges for the aggregates implies a continued posture of restraint against inflationary pressures and probably involves some additional—but tolerable—liquidity pressure on financial intermediaries.

Need for a Longer-Range Effort To Treat Structural Problems

These observations underscore the limitations of monetary policy as the main bulwark against inflation and the need to mount a broad attack on the economic problems we face. A significant reduction in the Federal budget deficit would be an important first step in reducing inflationary pressures. But a longer-range effort to treat the structural problem of inflation also is necessary.

We must reshape our tax laws to make certain that there are adequate incentives for saving and investment. The Nation has for many years now devoted too large a proportion of its production to consumption and too small a share to the expansion and modernization of its industrial plant. As a result, growth in productivity has languished, with serious consequences for inflationary trends and our standard of living.

We must take steps as well to bolster our position in international trade and thereby to strengthen the dollar. We should continue to seek freer access to world markets and should attempt to make American businessmen more aware of opportunities for sales abroad.

We must seek ways of training and placing those individuals who, because of lack of skills or limited knowledge of employment opportunities, are not readily absorbed into the work force.

And we must remove the impediments to competition, relieve the undue regulatory burdens, and avoid the costly governmental actions that have contributed importantly to inflationary pressures in recent years.

It is important to take strong measures now to curb inflation, and with the continued cooperation of the administration, the Congress, the Federal Reserve, and the private sectors of the economy, I believe that within the next several years we can establish an economic environment conducive to full employment with price stability.

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STATEMENT BEFORE THE COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS, U.S. SENATE, NOVEMBER 16, 1978

Events in recent months have presented a formidable challenge to our Nation. While sustained economic expansion has led to higher levels of output and employment, continuing domestic inflation and a sharp decline in the value of the dollar on foreign exchange markets have posed growing threats to the vitality of the U.S. and world economies. Monetary policy is being directed forcefully toward helping to resolve these urgent problems.

The objective of the Federal Reserve has, for some time now, been to foster monetary and financial conditions that would lead to a reduction of inflationary pressures, while encouraging continued moderate economic growth. Real gross national product rose at a 4 per cent annual rate, on average, during the first three quarters of this year, as compared with 5½ per cent over the course of 1977. This slower pace in the expansion has been sufficient to achieve substantial further gains in employment, but at the same time it has avoided a significant overshoot of general levels of resource utilization that would have intensified inflationary demand pressures in labor and product markets.

Even so, there has been a marked pick-up in the rate of inflation. For example, consumer prices have climbed at an annual rate of 9½ per cent so far this year. A number of factors have contributed to this development. Reduced supplies of some agricultural commodities—especially meats—have caused sharply higher food prices. Legislated increases in the Federal minimum wage and in employer contributions for social security and unemployment compensation have boosted labor costs. Wage gains have been somewhat larger this year than last, on average, while our productivity performance has been lagging. And the depreciation of the dollar in international exchange has raised the prices of imports and weakened competitive restraints on the prices of domestically produced goods.

With a heavy calendar of collected bargaining in prospect for 1979 and with wage demands likely to be intensified by recent price advances, the threat of a further escalation of labor costs is very real. Furthermore, scheduled increases next year in the minimum wage and social security taxes will again provide a significant inflationary impulse to costs.

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President Carter has announced a major program to break the self-destructive cycle of wages chasing prices and prices chasing wages. The program includes quantitative guidelines that establish standards for constructive behavior on the parts of labor and management. In addition, the President has indicated that he will seek to eliminate needlessly costly and anticompetitive regulation. He has also committed his administration to the containment of Federal spending and greater fiscal restraint.

On November 1, the administration's anti-inflation program was fortified by the joint actions of the Federal Reserve and the Treasury Department to strengthen the dollar in exchange markets. The Federal Reserve discount rate was raised 1 percentage point, and reserve requirements on large-denomination time deposits were increased. In addition, $30 billion in key foreign currencies were mobilized for exchange-market intervention. The speculative assault on the dollar in international currency markets had depressed its exchange value well below what could be justified on the basis of fundamental economic considerations. The psychological momentum of the markets, if not broken, threatened to worsen our inflation problem and to undermine confidence at home and abroad. The clear willingness of the United States to intervene actively in exchange markets and the monetary actions of the Federal Reserve have led to a rebound in the exchange value of the dollar and to a more stable market environment. These should be beneficial for domestic price performance in the period ahead and bolster confidence in the Nation's economic policies.

If the cooperation of business and labor that is so essential to the success of the administration's anti-inflation program is to be obtained and if we are to gain the fullest benefit of the recent dollar-support initiatives, it is absolutely essential that monetary and fiscal policies demonstrate prudent restraint. If inflation is to be gradually slowed, aggregate demand must not be permitted to expand to the point at which it presses excessively on available supplies of labor and industrial resources. This means that real GNP at this juncture probably should not grow at an annualized rate much above 3 per cent, in line with the prospective growth of potential output. Nor, of course, do we want to see a protracted shortfall from that pace that would bring on recession and underutilization of labor and productive capacity.

Recent trends in the economy and in financial markets suggest

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that expansion likely will be sustained, but at a more moderate pace over the next year or so. One noteworthy development has been the less robust pattern of spending by households following exceptional strength earlier in the cyclical recovery. Personal consumption expenditures rose at an estimated annual rate of less than 3 per cent in real terms during the first three quarters of this year, after having advanced at an average rate of 5½ per cent in the preceding 2¾ years. Rising costs of foods and other necessities have put substantial pressure on the budgets of many families, and the proportion of disposable income spent has been unusually high. Record levels of borrowing have played an important role in supporting consumer outlays, and the heavy repayment burdens that households face are likely to be an increasing constraint on spending in the forthcoming year. As a consequence, personal consumption expenditures probably will no more than keep pace with increases in personal income.

In addition, financial factors should induce some tapering off in homebuilding in 1979. To date, housing starts have remained on a high plateau, but the effects of recent increases in interest rates will soon begin to show through. The 6-month certificates, introduced in June, have enabled thrift institutions to avoid the disintermediation that has curtailed mortgage credit availability in the past, but they have not sheltered the housing market from the effects of higher interest rates. Builders already are experiencing steeper rates on construction loans, for which charges tend to move in step with the bank rate on loans to prime business borrowers, and the stock of loan commitments for permanent mortgage financing made earlier at lower rates is being depleted. The combined effects of higher mortgage rates and inflated house prices on the cost of homeownership are likely to bring about some decline in building—although nothing approaching the disastrous drops seen in the past seems in store.

Business investment meanwhile should remain supportive of economic expansion. Inventories by and large are quite lean in relation to current sales levels, and even with a continuation of cautious inventory policies, businessmen likely will wish to expand their stocks in line with rising sales. As for spending on plant and equipment, a recent private survey of investment intentions suggests only a modest increase next year in real terms. On the other hand, contracts and orders for new plant and equipment have been running well ahead of year-earlier levels—even after adjustment for inflation.

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In general, the willingness of businessmen to commit funds for major investment projects will hinge in large part on the success of efforts to control inflation, thereby providing the basis for greater confidence in the future health of the economy.

The foreign trade sector represents an element of strength in the economic outlook. The U.S. trade deficit should continue to shrink as a result of the stronger growth in prospect for some of our major trading partners and as a result of the effects of past exchange-rate changes on our competitive position.

In all, it is my expectation that real GNP will increase by roughly 2½ to 3 per cent in the year ending with the third quarter of 1979. With growth in the labor force unlikely to be so rapid as in the past couple of years, this rise in activity should be enough to keep the unemployment rate in the area of 5¾ to 6¼ per cent.

In this projection I have assumed that inflation will slow into the range of 6¾ to 7½ per cent. There are as always many uncertainties on the price front: the effects of weather on crop harvests and the decisions of the Organization of Petroleum Exporting Countries' cartel, for example, are factors beyond the sphere of economic analysis. What is clear is that the cost increases already in train will be placing continued pressure on the price structure so that it will be difficult to break the momentum of inflation. However, if there is general compliance with the administration's guidelines, the advance of prices next year could be held to around the low end of the range I have projected. This would represent a substantial deceleration from the increase of 8¼ per cent in the GNP deflator expected for this year, and would be a good start in the difficult process of restoring price stability.

The recent credit-restraining actions of the Federal Reserve have aroused fears in some quarters that an overly restrictive monetary policy might precipitate an economic downturn. There is no doubt that domestic credit markets are tauter than they were 6 months ago. Nonetheless, current financial conditions appear consistent with the moderate economic expansion that is desirable at this juncture.

The Federal Reserve has been moving its policies in a progressively less accommodative direction this year in an effort to prevent excessively rapid growth in money and credit. In an environment of inflation and of heightened inflationary expectations, borrowers have become willing to pay higher rates of interest in order to obtain credit

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to finance acquisition of assets the values of which they anticipate will be rising more rapidly than the rate of inflation. This phenomenon is seen most clearly in the real estate market, but the behavior is common in other sectors as well. To hold down nominal rates of interest in such a circumstance is to invite a credit-financed surge in aggregate demand that would add further to inflationary pressures. Consequently, the Federal Reserve has pursued policies that have permitted market rates to rise appreciably this year. Yields on Federal funds and other short-term instruments have increased more than 3 percentage points since the beginning of 1978, while interest rates on long-term bonds and mortgages have risen about 1 percentage point.

These are sizable movements, to be sure, but the fact is that, even at current levels, real rates of interest—that is, actual rates adjusted for inflationary expectations—are not very high, and credit remains in adequate supply to finance a volume of spending that is appropriate in light of the availability of real resources in the economy. Usury ceilings, which are unrealistic in relation to present market interest rates in many States, are cutting into credit availability in some local markets, and it would be desirable if these obstacles to the efficient operation of our financial system were eliminated. But there has been nothing like a general "credit crunch," and we do not foresee one.

It is the intention of the Federal Reserve to work toward a gradual deceleration of monetary and credit expansion to a pace consistent with price stability. The speed with which we can move in that direction without severely disrupting economic activity is limited by the degree to which inflation has become embedded in our economy. But some progress has been made in the past year. While *M*-1 growth over the past four quarters—at 8 per cent—was about the same as in the previous year, growth in *M*-2 and *M*-3 decelerated to rates of 8¼ and 9¼ per cent, respectively. Growth in these broader aggregates was 3 to 3½ percentage points slower than in the previous year. The actual growth in *M*-1 over the past four quarters was well above the range of 4 to 6½ per cent set for this aggregate, but growth in the broader aggregates was within their ranges. To have achieved significantly lower growth rates for the monetary aggregates than actually developed would have required substantially higher market rates of interest and a sharper curtailment in credit supply, which in our judgment would have run an unacceptably high risk of wrenching

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financial markets so severely as to lead to an economic recession.

Growth in the monetary aggregates has to be evaluated in relation to basic economic and financial forces affecting the public's preferences for money in its various forms. During the past four quarters growth in nominal GNP has remained very rapid as moderate expansion in real output was accompanied by an accelerated rate of price increase, generating a substantial demand for money—particularly *M*-1—to finance transactions. Federal Reserve policy did not fully accommodate these strong demands, and in fact, the rate of growth in real money balances actually slowed.

The pattern of growth in the broader aggregates has been strongly influenced by the introduction at banks and thrift institutions in June of this year of a 6-month money market certificate whose ceiling varies weekly with changes in the auction yield on 6-month Treasury bills. Growth in savings and small-denomination time deposits subject to Federally regulated interest-rate ceilings had slowed markedly in the fall of 1977 and in the first half of this year as higher yields on market securities increasingly attracted funds that would otherwise have been held in accounts at banks or thrift institutions. In order to enable these institutions to compete more effectively for lendable funds, the Federal Reserve and other regulatory agencies created two new deposit categories—an 8 per cent, 8-year certificate and the 6-month money market certificate.

The money market certificates have proved especially successful. They have been widely offered, most frequently at the ceiling rates, and have resulted in a marked pick-up in consumer-type deposit growth. Growth in deposits at savings and loan associations and mutual savings banks, which averaged 6¾ per cent at an annual rate in the first 5 months of 1978, have averaged 13 per cent since the introduction of the new accounts. This growth has permitted thrift institutions to increase their commitments for mortgage loans while reducing their dependence on borrowed funds and stemming the decline in their liquidity positions. At commercial banks, which have a rate disadvantage relative to the thrift institutions of ¼ of a percentage point, there has been a less marked, but still noticeable gain in growth of the combined total of savings and small time deposits—from 3¾ per cent through May to 6½ per cent in the past 5 months. Nonetheless, with bank credit demands remaining strong, banks continued to liquidate Treasury securities and to increase short-term

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borrowings through such instruments as large certificates of deposit and Federal funds to finance these demands.

At its October meeting, the Federal Open Market Committee (FOMC) updated its longer-term rangès for the monetary aggregates. Its task was complicated by new uncertainties associated with the introduction on November 1 of automatic transfer services (ATS), which permit consumers to authorize their banks to shift funds from savings to demand deposit accounts as needed to cover checks written. The major impact of this innovation should be on *M*-1, as consumers take advantage of the opportunity to reduce their holdings of non-earning demand deposits, but the size of this effect cannot be projected with any real precision. *M*-2 and *M*-3 will be less affected because shifts of funds from thrift institutions to banks, and from market instruments to deposits, are likely to be comparatively modest.

Against that background, the continuity in the FOMC's objectives with respect to the monetary aggregates for the 1-year period from the third quarter of 1978 to the third quarter of 1979 is more clearly indicated by the broader aggregates, *M*-2 and *M*-3. The Committee re-established the ranges for these two aggregates at 6½ to 9 per cent and 7½ to 10 per cent, respectively. It is expected that growth in these aggregates will be well within these ranges as monetary policy pursues a course of responsible restraint to complement the administration's program to combat inflation through fiscal discipline, wage and price moderation, and regulatory reform. The Committee anticipates growth in bank credit at a rate of 8½ to 11½ per cent to be associated with the ranges adopted for the monetary aggregates. With regard to *M*-1, the FOMC expects growth within a range of 2 to 6 per cent over the period from the third quarter of 1978 to the third quarter of 1979. The existing range of 4 to 6½ per cent has been lowered because the public can be expected to shift funds to take advantage of the ATS service, and the range has been widened because of uncertainties about the speed and extent to which the public may undertake such shifts.

Because of uncertainties about the relationship between *M*-1 and the transactions demand for money during the transition to the new ATS service, and in view of the widening role in financing transactions played by savings accounts, the Committee also indicated a growth range for *M*-1+ (*M*-1 plus savings accounts at commercial banks, negotiable orders of withdrawal accounts, demand deposits at

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mutual savings banks, and credit union share drafts) that it expected to be generally consistent with ranges of growth in the other aggregates. This range has been set at 5 to 7½ per cent over the 1-year period ending in the third quarter of 1979.

The structure of the domestic payments system has been changing considerably over the past several years as a result of regulatory changes and financial innovations. Deposits in thrift institutions have been increasingly used for third-party payments. At banks, liquidity reserves of the public, as well as funds held against expected transactions needs, have come to be held more and more outside of demand accounts. On the other hand, banks and particularly thrift institutions have also lengthened the maturity of consumer-type time deposit liabilities, so that some deposits have become less money-like. And in general, distinctions among depositary institutions with respect to their deposits have become increasingly blurred. Existing measures of the monetary aggregates are, as a result, becoming outdated. The Federal Reserve is studying possible adjustment to these measures to reflect the changing institutional environment. The measure of *M*-1+ represents an interim step in this process, while a more comprehensive revision is under way. It should be noted that one consequence of these ongoing changes is a need for more timely and broader reporting of deposit data—not only from nonmember commercial banks but also from thrift institutions.

While monetary aggregates are useful indicators of financial conditions, the continuing change in the institutional environment and in public preferences for different deposits indicates that any single monetary measure, or even a set of several measures, can by no means be the sole focus of policy. Thus, a broad range of financial indicators—including nominal and real interest rates, credit flows, and liquidity conditions—necessarily must be considered in assessing the stance of monetary policy.

Looking beyond these relatively technical questions about how best to characterize monetary policy, it is clear that in the present environment we cannot rely solely on monetary management to contain inflationary pressures. It is essential to obtain public cooperation in the administration's anti-inflationary program and to exercise restraint in fiscal policy if the Nation is to achieve a gradual, orderly reduction in the rate of inflation. You can be assured that monetary policy will do its part in achieving that objective.

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Part 2

Records, Operations, and Organization

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Record of Policy Actions of the Board of Governors

REGULATION A (EXTENSIONS OF CREDIT BY FEDERAL RESERVE BANKS)

May 10, 1978—Interpretation

The Board adopted an interpretation of Regulation A, effective May 10, 1978, that provides that bankers acceptances secured by field warehouse receipts covering readily marketable staples are eligible for discount by a Federal Reserve Bank even though the warehouse manager is a present or former employee of the owner of the goods.

> Votes for this action: Messrs. Miller, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Gardner and Wallich.[1]

This interpretation, which superseded one that had been adopted by the Board in 1933, took into account the changes in commercial law and business practice over the last 45 years. Field warehouse receipts are not frequently offered to Reserve Banks for discounting; however, by making them eligible for discount, the new interpretation removed the reserve liability that a member bank would have incurred if it sold an acceptance that was not eligible for discount.

REGULATION B (EQUAL CREDIT OPPORTUNITY)

March 13, 1978—Amendment and Interpretation

The Board amended Regulation B, effective March 13, 1978, to clarify the definition of adverse action as it relates to point-of-sale or loan transactions and to specify the circumstances under which failure to authorize the use of an open-end credit account constitutes an adverse action.

[1] On this and subsequent pages, footnote 1 indicates that there was one vacancy on the Board at the time the action was taken

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> Votes for this action: Messrs. Wallich, Coldwell, Jackson, and Partee. Vote against this action: Mr. Miller. Absent and not voting: Messrs. Gardner and Burns.

In a second action, the Board decided to draw more narrowly the applicability of an interpretation that permitted the collection of information about a borrower's religious affiliation for marketing purposes.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Gardner and Burns.

The amendment specified three instances of denial of credit at point of sale for which the creditor must provide borrowers with an explanation: (1) a change in the terms of the account at point of sale unfavorable to the customer; (2) termination of an account at point of sale; or (3) denial of an application for an increase in the credit limit. Other instances of credit refusal at point of sale would not constitute adverse action and the creditor would not be required to explain them; these would include the use of a lost or stolen credit card or one that is not currently valid, or the malfunctioning of the card issuer's authorization center.

Chairman Miller favored an approach that would define more instances of denials as adverse actions. He preferred that the amendment define the type of credit refusals at point of sale that would not constitute adverse action, with the understanding that in all other circumstances a credit denial would necessitate an explanation. He, therefore, dissented from the Board's action.

The revised interpretation was the result of reconsideration of an official staff interpretation issued in 1977 that permitted the collection of information for marketing purposes that otherwise would be prohibited by Regulation B. The original interpretation had stated that a seller of religious goods could inquire about a customer's religion so long as the information was used for marketing purposes and was not a factor in determining whether to grant credit; the interpretation also extended to other creditors in similar circumstances.

After issuance of that interpretation, the Board received a number of requests that it limit the applicability of the interpretation;

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those requesting the change felt that permitting the collection of such information would facilitate unlawful discrimination. Consequently, the existing interpretation was rescinded, and a revised staff interpretation was issued that made more explicit the applicability of the interpretation to the particular circumstances involving the seller of religious goods.

REGULATION B (EQUAL CREDIT OPPORTUNITY) AND REGULATION Z (TRUTH IN LENDING)

April 19, 1978—Amendments

The Board amended Regulations B and Z, effective April 21, 1978, to revise the procedures for issuing official staff interpretations.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Mr. Gardner.[1]

Official staff interpretations generally are of a technical rather than a policy nature and provide a defense to any creditor who acts in good faith in conforming to them. The Board had received complaints about existing procedures for issuance of official staff interpretations; under such procedures a staff interpretation was published in the *Federal Register* within 2 weeks of issuance and became effective upon publication. Those questioning the procedures felt that an official staff interpretation should be considered a rule, as defined by the Administrative Procedure Act, and therefore should be announced and published for comment before becoming effective.

The changes adopted provide that the effective date for any staff interpretation will be delayed 30 days. If an interpretation is challenged, the effective date will be suspended and the interpretation will be published for comment. If no questions are raised about an interpretation, it will become effective 30 days after publication in the *Federal Register.*

Concurrently with these revisions, the Board also deleted from the regulations existing criteria for determining whether a question merits an official staff interpretation and the procedures for requesting reconsideration.

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REGULATION D (RESERVES OF MEMBER BANKS)

November 1, 1978—Amendment

The Board amended Regulation D by establishing a supplemental reserve requirement of 2 per cent on all time deposits of $100,000 or more and on certain other liabilities of member banks, effective with outstanding deposits beginning November 2, 1978, for reserves required to be maintained beginning November 16, 1978.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Messrs. Gardner and Jackson.

Reserve requirements were increased as one of several measures taken jointly by the Federal Reserve and the Treasury Department to improve the position of the dollar on foreign exchange markets and to reduce inflationary pressures. The action was taken to help moderate the expansion of bank credit and to increase the incentive for member banks to borrow abroad, thereby improving the demand for dollar-denominated assets.

REGULATION D (RESERVES OF MEMBER BANKS) AND REGULATION M (FOREIGN ACTIVITIES OF NATIONAL BANKS)

August 25, 1978—Amendments

The Board amended Regulations D and M to eliminate the reserve requirements imposed on foreign borrowings of member banks, effective with the reserves required to be maintained beginning October 5, 1978.

> Votes for these actions: Messrs. Miller, Gardner, Wallich, Jackson, and Partee. Votes against these actions: None. Absent and not voting: Mr. Coldwell.[1]

The amendments eliminated the 4 per cent reserve requirement that had been imposed on borrowings—primarily Euro-dollars—of member banks from their foreign branches or from other foreign banks and on assets held by foreign branches that were acquired from their domestic offices. The Board also removed the 1 per cent reserve requirement on loans of foreign branches to U.S. borrowers.

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These changes were expected to encourage member banks to borrow in the Euro-dollar market.

The Board took these actions in conjunction with other measures to combat domestic inflation and to counter the disorder that existed in foreign exchange markets.

REGULATION E (PURCHASE OF WARRANTS)

November 8, 1978—Rescission of Regulation

The Board rescinded Regulation E, effective November 9, 1978.

> Votes for this action: Messrs. Wallich, Coldwell, Jackson, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Messrs. Miller and Gardner.

As part of a comprehensive review of the Board's regulations and related rules to determine whether they need clarification, simplification, or cancellation, the Board determined that Regulation E should be rescinded.

Regulation E, which governs the purchase by Reserve Banks of short-term securities of State or local governments in anticipation of tax receipts or other assured income, was adopted in 1915 to enable the Reserve Banks to provide a source of liquidity to member banks. Since 1933, however, statutory changes to the Federal Reserve Act have expanded the System's alternatives for investing in open market instruments and have eliminated the need for Reserve Banks to purchase warrants directly from State or local governments.

REGULATION F (SECURITIES OF MEMBER STATE BANKS)

October 4, 1978—Amendment

The Board amended, effective January 29, 1979, the provisions of Regulation F that deal with disclosure of information to conform with certain changes in rules made by the Securities and Exchange Commission.

> Votes for this action: Messrs. Miller, Coldwell, Jackson, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Messrs. Gardner and Wallich.

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The amendment affects the type of information that must be disclosed and the treatment of information in the following six areas: (1) confidential treatment of preliminary proxy materials; (2) proposals by security holders; (3) dissemination of proxy material to beneficial owners of registered securities; (4) tender offer statements; (5) consolidation and revision of several reports; and (6) stock appreciation rights.

REGULATION G (SECURITIES CREDIT BY PERSONS OTHER THAN BANKS, BROKERS, OR DEALERS), REGULATION T (CREDIT BY BROKERS AND DEALERS), AND REGULATION U (CREDIT BY BANKS FOR THE PURPOSE OF PURCHASING OR CARRYING MARGIN STOCKS)

May 10, 1978—Amendments

The Board amended Regulations G, T, and U, effective June 15, 1978, to revise the requirements for inclusion on the Board's list of over-the-counter (OTC) stocks subject to margin requirements.

> Votes for this action: Messrs. Miller, Gardner, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Mr. Wallich.[1]

The amendments provide that the OTC list will include only those stocks for which dealers submit bona fide bids and offers to an automated quotation system.

The amendments also revise certain procedures for determining the stocks to be included on or deleted from the list. The use of an automated quotation system will reduce the time needed to review stock market data and will allow publication of the OTC list more promptly.

REGULATION G AND REGULATION U

June 21 and 29, 1978—Interpretations

On June 21 the Board adopted an interpretation of Regulation G, effective June 29, 1978, that permits a lender, in connection with certain types of consumer loans, to accept purpose statements by mail, without

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the need for a face-to-face interview with the borrower, provided that the lender institutes certain procedural safeguards to establish the borrower's good faith.

> Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None.[1]

On June 29, effective immediately, the Board adopted an interpretation of Regulation U, superseding an earlier interpretation, that permits banks to accept mailed purpose statements under the same conditions as those set forth in the June 21 interpretation of Regulation G.

> Votes for this action: Messrs. Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Miller and Gardner.[1]

A 1965 interpretation of Regulation U had required that a borrower furnish the loan officer with a statement of the purpose of the loan during a personal interview to permit the officer to obtain sufficient information about the circumstances of the loan. Since 1965, however, several safeguards have been added to the Board's securities credit regulations that make a face-to-face interview unnecessary if other protective measures are instituted.

The interpretation of Regulation G allows acceptance of mailed purpose statements if the lender establishes a program to obtain sufficient information about a borrower and adopts procedures to verify the accuracy of the information received. The interpretation of Regulation U allows the mailing of purpose statements under the same conditions as those set forth in Regulation G.

REGULATION H (MEMBERSHIP OF STATE BANKING INSTITUTIONS IN THE FEDERAL RESERVE SYSTEM)

April 19, 1978—Amendment

The Board amended Regulation H, effective April 20, 1978, to make the provisions governing real estate loans by State member banks in flood-hazard areas conform to recent changes in the national flood insurance program.

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Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Mr. Gardner.[1]

The Housing and Community Development Act of 1977 removed the prohibitions against making loans secured by improved real estate or a mobile home located in a flood-hazardous area of a community that does not participate in the national flood insurance program. For loans made in flood-hazardous areas—including communities that do not participate in the flood insurance program—the act also required a notice to inform borrowers that a flood hazard exists and to indicate whether Federal disaster relief assistance is available.

REGULATION K (CORPORATIONS ENGAGED IN FOREIGN BANKING AND FINANCING UNDER THE FEDERAL RESERVE ACT)

November 6, 1978—Amendment

The Board amended Regulation K, effective November 16, 1978, to conform to the International Banking Act of 1978.

Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Mr. Gardner.

The International Banking Act removed the statutory 10 per cent minimum reserve requirement imposed on U.S. deposits of Edge corporations. The amendment eliminates the 10 per cent minimum requirement from Regulation K, leaving Edge corporations subject to the same reserve requirements as those imposed by Regulation D on member banks.

REGULATION M (FOREIGN ACTIVITIES OF NATIONAL BANKS)

August 25, 1978—Amendment

This amendment is discussed under Regulation D.

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REGULATION O (LOANS TO EXECUTIVE OFFICERS OF MEMBER BANKS)

February 22 and June 29, 1978—Amendments

On February 22 the Board amended Regulation O, effective March 24, 1978, to increase from $1,000 to $5,000 the amount of credit that a member bank may extend to its executive officers through the use of bank credit cards or similar plans.

Votes for this action: Messrs. Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Burns, Gardner, and Lilly.

The Board increased the limit on officer indebtedness in recognition of the general rise in price levels since the adoption of the $1,000 limit in 1967. The Board also noted that the use of credit cards in general had become more widespread since that time and that the lines of credit extended under credit-card plans likewise had grown; therefore it considered an increase in the exemption for credit-card indebtedness by bank officers to be appropriate.

On June 29 the Board adopted a clarifying amendment, effective June 30, 1978, to specify that an executive officer may not become indebted to a member bank under a bank credit-card, check-credit, or similar plan with terms more favorable than those offered to the general public.

Votes for this action: Messrs. Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Miller and Gardner.[1]

After adoption of the amendment in February the Board received several inquiries about provisions of the amendment that appeared to conflict with an existing interpretation. The clarifying amendment stipulates that the regulation precludes any type of credit-card arrangement under which an executive officer would receive special terms that are not offered to all cardholders.

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REGULATION Q (INTEREST ON DEPOSITS)

May 1, 1978—Amendment

The Board amended Regulation Q, effective November 1, 1978, to permit member banks to transfer funds automatically from the savings account of a depositor to a demand deposit or other account.

> Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, and Partee. Votes against this action. None.[1]

The amendment enables individuals to authorize their bank to transfer funds automatically and without penalty from savings accounts to checking accounts. The service is not available to businesses or governmental units.

The automatic transfer service may be offered in addition to telephonic transfer and preauthorized bill-paying services, which previously had been authorized for member banks, and it would provide depositors with an alternative to arrangements such as automatic loans to cover overdrafts of checking accounts. The Board set an effective date of November 1 to provide banks sufficient time to prepare for the new service.

The amendment was expected to improve the efficiency of the System's check-clearing operations by reducing the number of checks that are returned for insufficient funds.

May 10 and 26, 1978—Amendments

On May 10 the Board amended Regulation Q to permit member banks to offer two new categories of time deposits beginning June 1, 1978: (1) a deposit of $1,000 or more with a maturity of 8 years or longer on which banks could pay a maximum interest rate of 7¾ per cent; and (2) a short-term time deposit of $10,000 or more that would mature in 26 weeks and would earn interest at a rate equal to the discount rate on 26-week Treasury bills. The amendment also had the effect of raising to 8 per cent the maximum rate payable on funds deposited on or after June 1 in individual retirement accounts (IRA's) and Keogh plan retirement accounts.

> Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, and Partee. Votes against this action: None. Absent and not voting: Mr. Jackson.[1]

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The 8-year time deposit category was established to help lengthen the maturity of bank liabilities and to promote greater stability in the cost and availability of funds. The short-term time deposit category would assist banks in attracting funds that otherwise might be invested in money market instruments. Both changes were made to assure continued flows of funds for mortgages.

On May 26 the Board amended its May 10 action to permit the new 8 per cent ceiling rate on IRA's and Keogh retirement accounts to be applicable to funds already deposited in such accounts as well as to new deposits, effective June 1, 1978.

> Votes for this action: Messrs. Miller, Wallich, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Gardner and Coldwell.[1]

The amendments announced on May 10 drew comments from many banks that the new rate structure for IRA's and Keogh accounts would result in operating problems because only the new deposits would earn interest at the higher rate. Banks indicated that maintaining a dual interest rate structure for a single pool of retirement funds would be difficult, and they also thought customers might become confused by the dual rates. Therefore, they requested reconsideration of the Board's decision not to allow the higher rate to be paid on funds already deposited in IRA's and Keogh accounts. In view of these problems and because retirement accounts function more as open-end accounts—with periodic deposits—than as ordinary time deposits, the Board approved an amendment establishing the 8 per cent ceiling for all deposits in IRA's and Keogh accounts.

December 6, 1978—Amendment and Interpretation

The Board amended Regulation Q, effective immediately, to modify the interest penalty applicable to early withdrawal of funds from Keogh plan and individual retirement accounts and certain other time deposits. The Board also adopted an interpretation to permit depositors to withdraw without penalty the interest earned on a time deposit.

> Votes for these actions: Messrs. Miller, Wallich, Coldwell, Partee, and Mrs. Teeters. Votes against these actions: None.[2]

[2] On this and subsequent pages, footnote 2 indicates that there were two vacancies on the Board at the time the action was taken.

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The amendment applies to (1) time deposit open accounts in which the deposit of additional funds automatically resets the maturity of all funds in the account and (2) time deposits that may not be withdrawn prior to the expiration of a specified period of notice (notice accounts). Previously, when funds were withdrawn from such accounts prior to maturity, Regulation Q required member banks to impose an interest forfeiture penalty retroactive to the date of the original deposit. The amendment reduces the severe impact that the early withdrawal penalty would have had on longer-term deposits.

The amendment changes the penalty rule for early withdrawal of these types of time deposits. For time deposit open accounts with automatically resetting maturities, such as individual retirement accounts and Keogh plan accounts, the amendment allows banks to treat each deposit as though it had a separate maturity equal to the maturity of the original deposit. The penalty for early withdrawals from such accounts is calculated on the basis of the length of the maturity period specified for the original deposit. For notice accounts, the penalty is imposed for a period of time no greater than that specified by the notice.

The interpretation authorizes member banks to permit the withdrawal of interest earned on a time deposit without penalty, regardless of the method used by the bank to compound or credit such interest. Previously, banks had been advised that when interest is credited to an account, it becomes part of the underlying time deposit and subject to the same penalty for early withdrawal.

REGULATION T (CREDIT BY BROKERS AND DEALERS)

May 10, 1978—Amendment

This amendment is discussed under Regulation G.

July 12, 1978—Amendment

The Board amended Regulation T, effective July 12, 1978, by broadening the conditions under which a broker or dealer can make subordinated capital loans to other brokers and dealers.

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Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Mr. Gardner.[1]

The amendment permits any individual or firm that is subject to Regulation T to extend subordinated credit to other brokers or dealers for capital purposes. Previously, only those who were members of a national exchange could make such loans, and the loans were limited to intracompany loans or loans between members of the same exchange. Also, the amendment removes certain restrictions on the use of the proceeds of the loan if the borrower has no other customer relationship with the lender.

September 20, 1978—Amendment

The Board amended Regulation T, effective October 30, 1978, to permit brokers and dealers, under certain circumstances, to extend credit on nonconvertible corporate debt securities that are not listed on a national securities exchange.

Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, Partee, and Mrs. Teeters. Votes against this action: None.

The amendment provides that brokers may extend margin credit on an unlisted corporate bond if the bond satisfies certain criteria relating to the size of issue, the availability of information on the security, and the status of principal and interest payments of the corporate issuer. The amount of credit that may be extended is the amount that the broker ordinarily would extend on nonconvertible securities traded on national exchanges.

REGULATION U (CREDIT BY BANKS FOR THE PURPOSE OF PURCHASING OR CARRYING MARGIN STOCKS)

May 10, 1978—Amendment

This amendment is discussed under Regulation G.

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June 29, 1978—Interpretation

This interpretation is discussed under Regulation G.

REGULATION Y (BANK HOLDING COMPANIES)

January 18, 1978—Termination of Rulemaking

The Board decided to terminate the rulemaking proceedings relating to a proposed amendment to Regulation Y that would have permitted bank holding companies to underwrite and deal in U.S. Government securities, State government securities, and municipal securities. Instead, the Board agreed to review applications to underwrite and deal in such securities on a case-by-case basis.

> Votes for this action: Messrs. Burns, Gardner, Coldwell, Partee, and Lilly. Votes against this action: None. Absent and not voting: Messrs. Wallich and Jackson.

The Board had been considering an amendment to Regulation Y that would have permitted bank holding companies to engage in the activities of underwriting and dealing in government securities, municipal securities, and any other security in which a State member bank is permitted to deal. The amendment, first proposed in 1974, was occasioned by an application by a bank holding company to form a subsidiary that would deal in municipal securities.

When the Board considered the application in October 1976, it decided that the proposed activity was closely related to banking, but suspended further consideration of the proposal. The second part of the two-step test to determine if a proposed activity is permissible for holding companies requires a finding that the activity is a proper incident to banking. Rather than making that finding for purposes of amending Regulation Y during its current consideration of the issue, and thereby permitting the activity generally, the Board preferred to process applications to engage in these activities on a case-by-case basis.

The Board took this action because of the belief that it should move cautiously in expanding the list of activities permissible for holding companies and because it preferred to delay action until it could assess the effects of the activity on individual bank holding companies. Consequently, the Board decided to process hold-

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ing company applications involving securities underwriting on a case-by-case basis, in lieu of amending Regulation Y.

January 25, 1978—Interpretation and Termination of Rulemaking

The Board adopted an interpretation, effective January 25, 1978, that codified past applications of the divestiture provisions of Regulation Y. At the same time, the Board terminated a rulemaking proposal that would have amended Regulation Y by establishing additional presumptions for determining whether a holding company continued to control divested activities when certain debt or officer relationships continue to exist.

Additionally, the Board agreed to terminate the practice of publishing in the *Federal Register* notices of routine applications for determinations that divestitures had been completed. Virtually no comments had been submitted on such applications.

> Votes for these actions: Messrs. Gardner, Coldwell, Jackson, and Partee. Votes against these actions: None. Absent and not voting: Messrs. Burns, Wallich, and Lilly.

A majority of the comments received on the proposed rulemaking had opposed the amendment because the scope of the proposal was too broad. The Board withdrew the proposed amendment and instead issued an interpretation specifying that if a bank holding company transfers shares to a company that is indebted to the holding company or has an officer or director relationship with the holding company, then control of the transferred shares is presumed not to have changed unless the Board determines otherwise. The interpretation defines the criteria the Board will consider when determining whether control relationships have been terminated.

March 6, 1978—Amendment

The Board amended Regulation Y, effective April 5, 1978, to require bank holding companies that are authorized to deal in municipal securities to provide certain information about persons who serve as their municipal securities principals and representatives.

> Votes for this action: Messrs. Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Burns and Gardner.[1]

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In August 1977 the Board considered amendments to Regulation H (Membership of State Banking Institutions in the Federal Reserve System) and Regulation Y that would require those State member banks that engage in municipal securities activities to provide the Board with certain information about persons whom they employ as principals or representatives. The amendment to Regulation H was adopted, but the Board deferred action on the proposal to amend Regulation Y pending a decision whether to permit bank holding companies to underwrite and deal in municipal securities.

On January 18, 1978, the Board decided to review on a case-by-case basis applications by bank holding companies to deal in municipal securities. Accordingly, the Board adopted notification requirements for municipal securities principals and representatives associated with holding companies similar to those required of State member banks.

December 15, 1978—Amendment

The Board amended the provisions of Regulation Y pertaining to public notice of applications by bank holding companies to engage *de novo* in permissible nonbank activities both domestically and abroad. The amendment is effective with applications accepted after December 31, 1978.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Partee, and Mrs. Teeters. Votes against this action: None.[2]

The amendment eliminates the requirement that a bank holding company publish in newspapers serving the relevant local communities notice of any proposal to engage *de novo* in nonbank activities or to acquire companies engaged in such activities. Instead, the Board will publish such notices in the *Federal Register.*

The amendment also eliminates the requirement of publishing notices in local newspapers in connection with *de novo* expansion outside the United States. Bank holding companies and their domestic nonbank subsidiaries may engage in permissible nonbank activities in foreign countries by complying with the established procedures for domestic applications. These procedures, however, do not apply to foreign activities of foreign bank holding companies or to the foreign operations of domestic bank holding companies conducted through foreign subsidiaries.

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REGULATION Z (TRUTH IN LENDING)

January 25, 1978—Amendment

The Board amended Regulation Z, effective March 28, 1978, to modify the descriptive billing requirements for nonsale credit transactions, such as cash-advance check transactions, on open-end credit accounts.

> Votes for this action: Messrs. Gardner, Coldwell, and Jackson. Vote against this action: Mr. Partee. Absent and not voting: Messrs. Burns, Wallich, and Lilly.

The amendment allows creditors to use, under certain circumstances, the date on which a cash-advance check is charged to the customer's account (the debiting date) as a means of identifying on the billing statement transactions under open-end credit plans. The Board adopted the amendment because some creditors had experienced difficulty with the descriptive billing provisions of the regulation, which generally require identification on the customer's account of the date of transactions, including those involving cash-advance checks. The Board agreed to permit creditors to use the debiting date on the billing statement for these transactions provided that (1) the debiting date was properly identified as such; (2) the creditor treated any subsequent inquiry about the transaction as notification of an erroneous billing, thus invoking the provisions of the Fair Credit Billing Act for settling billing errors; and (3) the customer was furnished with documentary evidence of the transaction in connection with any such inquiry.

Governor Partee objected to the amendment because he believed the billing problems that some creditors experienced were primarily operational and could be resolved, albeit with some inconvenience, by changes in their data processing systems. He felt that customers were being inconvenienced for the sake of more efficient computer systems. Governor Lilly, although not present at the meeting, had indicated his objection to the amendment for reasons similar to those expressed by Governor Partee.

April 19, 1978—Amendment

This amendment is discussed under Regulation B.

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May 1, 1978—Supplement

The Board adopted a supplement to Regulation Z, effective immediately, that prescribes the procedures and criteria under which a State may apply either for an exemption from the consumer leasing provisions of the Truth in Lending Act and the regulation, or for a determination that a State's leasing law is not inconsistent with or pre-empted by the act and the regulation. In connection with this action, the Board also amended its Rules regarding Delegation of Authority to permit the Director of the Division of Consumer Affairs to grant exemptions from the requirements of the regulation to States that satisfy the criteria.

> Votes for these actions: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against these actions: None. Absent and not voting: Mr. Gardner.[1]

The Truth in Lending Act authorizes the Board to grant to individual States exemptions from the consumer leasing provision of the act if it is determined that a State imposes requirements substantially similar to those of the act or gives greater protection and benefit to the consumer, and that such law contains adequate provision for enforcement. The supplement adopted by the Board explains the procedures and requirements for obtaining such an exemption.

The supplement also sets forth the criteria under which a State may apply for a determination that a State law is consistent with the Federal statutes; those criteria include factors such as provision in the State law for greater protection or benefit to lessees than in Federal law.

In addition, the Board delegated to the Director of the Division of Consumer Affairs authority to review applications for exemptions and to grant (but not to deny or revoke) such exemptions when appropriate.

May 19, 1978—Amendment

The Board amended Regulation Z, effective immediately, to require that certain creditors extend the minimum 2-year retention period for all records of compliance with the disclosure provisions of the regulation until (1) uniform guidelines for Truth in Lending have been adopted, (2) an examination for compliance has been conducted, and (3) any required corrective action has been taken.

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Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None.[1]

Prior to adoption of this amendment, the regulation allowed creditors to dispose of credit records 2 years after the date of the transaction. The Board and the four other Federal financial regulatory agencies (the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, and the National Credit Union Administration) have proposed uniform guidelines for institutions under their supervision to enforce Truth in Lending, one provision of which would require corrective action for violations that occurred more than 2 years previously. The Board amended the regulation to prevent routine destruction of evidence of possible violations before the guidelines were adopted and to preserve the Board's supervisory alternatives should the guidelines as finally adopted by the five agencies require corrective action for violations that occurred more than 2 years prior to discovery.

June 21 and October 18, 1978—Amendment and Interpretations

The Board amended Regulation Z, effective August 3, 1978, to establish an alternative method of complying with the rescission provisions for individual transactions under certain open-end credit plans that are secured by borrowers' residences.

Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None.[1]

In certain situations, Regulation Z requires a creditor to notify a borrower who pledges his home as collateral for a consumer credit transaction that he has the right to rescind the transaction within three business days. Creditors who wished to offer open-end credit plans (such as cash-advance check plans and overdraft checking arrangements) secured by a customer's residence had requested that the regulation be amended to facilitate the offering of these types of credit plans by exempting individual transactions from the 3-day rescission right. The Board adopted an amendment covering loan transactions and three-party transactions (in which the seller is not

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the creditor); the existing provisions for two-party sale transactions remain in effect.

The amendment exempts individual transactions but stipulates that customers must be informed of their right of rescission in the following four instances: (1) when the open-end credit plan is first opened; (2) when the credit limit is increased; (3) when the terms of the account are changed; and (4) when a security interest in a home is added to an existing open-end credit arrangement. Additionally, creditors must remind customers annually that their homes have been pledged as security for the account.

Concurrent with this action, the Board issued an interpretation of the regulation that provided sample disclosure forms for use by creditors to satisfy the requirements of the regulation.

> Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None.[1]

After the interpretation was issued, the Board received comment suggesting that one of the sample forms was not sufficiently informative regarding the customer's rights.

On October 18 the Board issued a revised interpretation that clarified the disclosure.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Mr. Gardner.

The disclosure form provided with the June interpretation stated that a borrower could refuse a change in the terms of the plan and had 3 days within which to decide. If the change was refused, the form stated that the creditor had the right to refuse to extend further credit under the plan and to require repayment of any existing obligation.

Comment received about the disclosure statement approved in June suggested that the language of the form might not sufficiently inform consumers of their rights and, in fact, might create the impression that the right to repay an existing obligation without a change in terms is a penalty to consumers who refuse the change. Thus, the Board

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issued a revised interpretation that modified the wording of the sample form. The new form stated that if a customer refused a change in terms, he would have the right to repay any outstanding debt under the terms of the existing plan. Creditors, however, would then have the right to refuse to extend further credit. In adopting the new form, the Board specified that use of the disclosure form approved in June would not be a violation of the regulation.

August 23, 1978—Interpretation and Amendment

The Board revised an interpretation of Regulation Z to simplify the computation of annual percentage rates for certain transactions with varying repayment schedules. Concurrently, the Board amended the regulation to permit disclosure of the complete repayment schedule on the reverse of the disclosure statement or on a separate page or pages for transactions in which the payments vary. Both actions were effective August 31, 1978.

> Votes for these actions: Messrs. Miller, Wallich, Jackson, and Partee. Votes against these actions: None. Absent and not voting: Messrs. Gardner and Coldwell.[1]

The revised interpretation permits an irregular initial payment period of up to 62 days to be considered regular for computation of the annual percentage rate (APR) for transactions involving a repayment period of 10 years or more. The change would facilitate the use of APR computation tables for certain long-term transactions, such as graduated-payment mortgages.

The amendment provides that the required disclosure of the complete repayment schedule may be made on as many pages as necessary for credit transactions with monthly payments of varying amounts, such as a mortgage loan with mortgage insurance in which the amount of the monthly payment declines.

October 18, 1978—Enforcement Guidelines

The Board adopted guidelines for the enforcement of the Truth in Lending Act, effective January 4, 1979. The four other Federal financial regulators also established guidelines on the same date.

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Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Mr. Gardner.

The five agencies (the Board, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, and the National Credit Union Administration) adopted the guidelines to promote uniformity in the administrative actions to be taken when violations that result in overcharges to customers are detected. The guidelines specify the criteria that the agencies will use in enforcing the requirements of Truth in Lending for disclosing the cost of credit transactions.

The enforcement policy applies specifically to transactions other than open-end credit; violations of the disclosure requirements for open-end credit transactions will be treated on a case-by-case basis but will be subject to the same general treatment as other violations under the guidelines. Violations of the disclosure requirements that result in an overcharge of one dollar or more must be reimbursed and the borrower must be informed of the reason for the reimbursement. Reimbursement will be required for violations involving outstanding loans made after October 28, 1974, and on terminated loans originated within the 2-year period prior to the financial examination in which the violation was discovered.

REGULATION BB (COMMUNITY REINVESTMENT)

October 4, 1978—Adoption of Regulation and Interpretation

The Board adopted Regulation BB, effective November 6, 1978, to implement the Community Reinvestment Act of 1977. The other Federal financial regulators issued similar regulations on the same date.

Votes for this action: Messrs. Miller, Coldwell, Partee, and Mrs. Teeters. Vote against this action: Mr. Jackson. Absent and not voting: Messrs. Gardner and Wallich.

The Community Reinvestment Act required the four Federal regulators of financial institutions (the Board, the Comptroller of the Cur-

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rency, the Federal Deposit Insurance Corporation, and the Federal Home Loan Bank Board) to have in place by November 6, 1978, regulations that would encourage lenders to help meet the credit needs of their local communities, including the low- and middle-income neighborhoods. The act also required that each agency take into account an institution's record of meeting local credit needs when reviewing applications for acquisitions, mergers, insurance, and certain other matters.

The regulations adopted by the four agencies stipulate that each lending institution must: (1) prepare a map delineating the local community; (2) adopt a statement defining the local community and specifying the types of credit the lender is prepared to extend; (3) make available to local residents a notice of the requirements of the act; and (4) maintain a record of comments received from the public regarding the institution's local lending practices. The statement as well as the record of public comments will be reviewed and assessed during the periodic examination of the institution by representatives of the agencies.

Governor Jackson opposed adoption of the regulation because he thought that its thrust was contrary to the intent of the Congress. He believed the regulations were more burdensome than the Congress had contemplated and that they would be inflationary because the lenders would pass on to borrowers the higher operating costs associated with complying with the act.

Concurrently, the Board adopted an interpretation of Regulation BB exempting certain banking facilities that do not provide routine lending services.

> Votes for this action: Messrs. Miller, Coldwell, Jackson, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Messrs. Gardner and Wallich.

The interpretation exempts from the regulation institutions that do not provide commercial or retail banking services; these would include facilities that serve solely as correspondent banks, as trust companies, or as clearing agents.

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POLICY STATEMENTS AND ACTIONS

January 5, 1978—Improper Payments by Banks

The Board issued a policy statement jointly with the Comptroller of the Currency and the Federal Deposit Insurance Corporation regarding improper or illegal payments by banks and bank holding companies to domestic or foreign officials. The three agencies adopted the policy, effective January 13, 1978.

> Votes for this action: Messrs. Gardner, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Burns, Wallich, and Lilly.

The statement notified banks and bank holding companies that improper political contributions and certain other questionable payments may be regarded as unsound banking practices. In order to prevent these practices, the agencies will use appropriate corrective action, including issuance of cease-and-desist orders and referral to law enforcement agencies for possible prosecution, when such payments are discovered. Improper payments may also be taken into account when the agencies review applications submitted by organizations that have made such payments.

March 17, 1978—Use of Inside Investment Information

The Board adopted a policy statement, effective March 17, 1978, reflecting its view that misuse by banks of material inside information in connection with securities transactions constitutes an unsafe and unsound banking practice. The statement also called the attention of State member banks to the penalties for violations.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Gardner and Burns.

The statement pertains to information about securities that banks obtain in confidence and notes that Federal law prohibits the use of such material information until the information is publicly disclosed. The statement notifies State member banks that misuse of material inside information in connection with securities transactions or recommendations about such transactions constitutes an unsound

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banking practice. Banks are expected to adopt procedures to ensure that material information is not misused because violations could expose them to financial penalties and criminal charges.

April 14, 1978—Funds Transfer and Clearing Services

The Board approved two actions, effective immediately, to promote greater efficiency in the Nation's payments system. The first action permitted member banks to use their reserve balances at Federal Reserve Banks to make net settlement for funds transferred electronically through a private communications network.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Mr. Gardner.[1]

The second action authorized Federal Reserve Banks to provide services that would link automated clearinghouse (ACH) facilities throughout the country.

> Votes for this action: Messrs. Miller, Coldwell, Jackson, and Partee. Vote against this action: Mr. Wallich. Absent and not voting: Mr. Gardner.[1]

The first change resulted from a request by a nationwide association of commercial banks that members of the association that are also members of the Federal Reserve System be permitted to use their reserve balances at the Reserve Banks to settle for payments transactions exchanged through the association's network. This action was expected to facilitate member bank participation in private-sector clearing arrangements and to provide same-day fund availability for member banks using the service. The Board felt that assisting in such a service also would promote initiatives by the private sector to improve the efficiency of the Nation's payments mechanism.

The second change, which allowed the Reserve Banks to provide interregional clearing and settlement services for electronic payments made through ACH's, would link such associations into a nationwide network for electronic exchange of payments information.

Governor Wallich dissented from the second action. He thought that several years would elapse before the savings to the System from the reduced processing costs associated with the interregional ACH expansion would offset the equipment acquisition and the develop-

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mental and operating costs of the new service. He noted that projected savings to the System depended upon the electronic processing of a large volume of items and he felt that the volume projections were overly optimistic.

September 20, 1978—Intercorporate Tax Practices of Bank Holding Companies

The Board adopted a policy statement pertaining to certain accounting transactions of State member banks and bank holding companies that divert income from a subsidiary bank to its parent or nonbank affiliates.

> Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, Partee, and Mrs. Teeters. Votes against this action: None.

The Board had become concerned about certain intercorporate tax accounting procedures that result in the transfer of assets or income from a bank to its parent holding company or an affiliate without any offsetting benefit to the bank. The policy statement clarifies the Board's position on such tax practices and indicates that the Board will apply appropriate supervisory remedies, including cease-and-desist action if warranted, when it finds inequitable tax treatment of subsidiary banks.

1978—DISCOUNT RATES

The Board approved seven increases in the discount rate during 1978, from a level of 6 per cent at the start of the year to 9½ per cent by year-end. The Board also voted on fourteen occasions to turn down requests by individual Federal Reserve Banks to raise the rate. No requests to lower the rate were submitted by the Reserve Banks during 1978.

The specific reasons for the Board's decisions are reviewed below. In reaching those decisions the Board also took into account general economic and financial developments, including those affecting the value of the dollar in foreign exchange markets. These developments are covered in more detail elsewhere in this REPORT, especially in the quarterly reports to the Congress on the System's monetary growth ranges and in the Record of Policy Actions of the Federal Open Market Committee.

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A listing of the Board's discount rate actions during 1978, including the votes on the actions and reasons for dissents, follows this review.

Early January: Increase Approved

On January 6 the Board approved an increase in the discount rate from 6 to 6½ per cent. This action was taken in light of continuing unsettled conditions in foreign exchange markets. A majority of the Board believed that such conditions constituted a serious threat not only to the orderly expansion of the international economy but to the domestic economy as well. In their judgment the increase was desirable to help demonstrate the intention of U.S. authorities to deal with the current weakness of the dollar and also to supplement the policy of more active intervention in foreign exchange markets that had been announced on January 4 by the Treasury and the Federal Reserve.

Mid-January to Early May: No Change

Following the increase in early January, no requests to change the discount rate were submitted by any Federal Reserve Bank until April. Market interest rates rose during the first part of January, but most rates subsequently fluctuated within relatively narrow ranges until the latter part of March. They then came under some upward pressure, especially in long-term debt markets. Nonetheless, the discount rate remained in fairly close alignment with short-term interest rates until the latter part of April.

During April the Board turned down requests by seven Federal Reserve Banks to increase the discount rate from 6½ per cent to 6¾ or 7 per cent. The remaining Banks proposed that the current rate be maintained. In rejecting the pending actions, the Board indicated its preference for a market-following move rather than an anticipatory increase that might signal a more restrictive monetary policy. Uncertainty was expressed about the vigor of the economy's rebound from its midwinter pause and about the significance of the recent acceleration in the growth of the monetary aggregates. Under prevailing conditions the Board preferred to wait for further developments before approving a higher discount rate. Nonetheless, as April

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progressed it was recognized that an increasingly strong case could be made on both economic and financial grounds for raising the discount rate.

Mid-May to Mid-October: Five Increases Approved

On May 10 the Board voted unanimously to raise the discount rate from 6½ to 7 per cent. The action was taken in recognition of the appreciable increases in short-term market rates over the course of previous weeks and was designed to bring the discount rate into closer alignment with short-term rates generally. In particular, the Federal funds rate had risen to a level well above the discount rate as System open market operations had moved toward increasing restraint in an effort to curb accelerating rates of monetary expansion. Other short-term rates had also advanced, and the widening spread between market rates and the discount rate had fostered a sharp rise in member bank borrowings. In these circumstances, a higher discount rate was widely anticipated and the increase in question was believed likely to have little or no impact on other interest rates.

On June 30 the Board approved another increase in the discount rate to 7¼ per cent. This action was taken in recognition of the further increases in other short-term rates. It was again viewed as a market-following move designed to bring the discount rate into closer alignment with other short-term rates, thereby reducing the rate incentive that had recently contributed to another bulge in member bank borrowings.

Before reaching this decision the Board had acted on June 23 to disapprove rate increases of ¼ or ½ percentage point that were pending at five Federal Reserve Banks. The Board did not believe that interest rate differentials had widened sufficiently by that date to establish a compelling case for raising the discount rate. It also concluded that, in the context of the very sensitive conditions then prevailing in financial markets, such a move might cause a misreading of monetary policy intentions and thus complicate the implementation of that policy through open market operations.

The next discount rate increase was approved on August 18, when the rate was raised by ½ percentage point to 7¾ per cent. In announcing this action the Board cited the disorderly conditions that had recently developed in foreign exchange markets and the serious

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inflationary problem that was continuing to affect the domestic economy. Other developments weighed by the Board included the mid-August decision by the Federal Open Market Committee to raise the objective for the Federal funds rate and the recent sizable increases in Treasury bill rates. While the vote for a higher discount rate was unanimous, two Board members indicated that they would have preferred an increase of ¾ percentage point to provide a stronger signal of support for the dollar and for the System's anti-inflationary policy.

The Board's decision on August 18 was preceded by disapprovals during the second half of July of then pending requests at five Federal Reserve Banks to raise the discount rate by ¼ percentage point. The Board had concluded that a higher discount rate was not desirable at that time in light of indications that monetary growth was well within the short-run ranges of tolerance established by the Federal Open Market Committee, and no increase in the Federal funds rate was contemplated. Moreover, Treasury bill rates had fallen considerably during the second half of July when foreign central banks made large bill purchases. Despite these disapprovals, the Board recognized that inflationary developments in the domestic economy and re-emerging pressures on the dollar in foreign exchange markets pointed to the possible need for a higher discount rate at a later date.

Advances in the discount rate were subsequently approved on September 22, when the rate was raised from 7¾ to 8 per cent, and on October 13, when the rate was moved up to 8½ per cent. Both actions were taken in recognition of increases in other short-term interest rates, thereby bringing the discount rate into closer alignment with such rates. The actions were also intended to provide some support to the dollar, which had continued under considerable pressure in foreign exchange markets. In announcing the increase of ½ percentage point on October 13, the Board also cited the continuing high rate of inflation and the recent rapid expansion in the monetary aggregates.

During September and October the Board also turned down pending rate increases of ¼ or ½ percentage point on three occasions. The reasons for the disapprovals related in part to timing, especially vis-a-vis actions being implemented at the direction of the Federal Open Market Committee to control the growth of the monetary

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aggregates. Other reasons were more technical and included the rate spreads between the discount rate and other short-term rates and the level of member bank borrowings.

November 1: Increase of 1 Percentage Point Approved

On November 1 the Board approved an increase of a full percentage point in the discount rate to a level of 9½ per cent. The increase, the largest in 45 years, was one of the measures developed as part of a broad Government program to strengthen the dollar in foreign exchange markets and thereby to counter continuing domestic inflationary pressures. These measures included use of other monetary policy instruments, discussed elsewhere in this REPORT, such as reserve requirements, open market operations, and expanded reciprocal currency arrangements with certain central banks abroad.

Subsequently, during the second half of December, the Board turned down requests to raise the discount rate by ¼ or ½ percentage point that were pending at three Federal Reserve Banks. Current indications of weakness in the monetary aggregates were the major reason for the Board's decisions. In the circumstances, the Board concluded that it preferred a steady course for monetary policy as it continued to assess economic and financial developments.

Votes on Reserve Bank Actions to Change the Discount Rate

Under the provisions of the Federal Reserve Act, the boards of directors of the Federal Reserve Banks are required to establish rates on discounts for and advances to member banks at least every 14 days and to submit such rates to the Board for review and determination. The Board votes listed below are those that involved approval or disapproval of actions to change the rate. Specific reference is made to the rate on discounts for and advances to member banks under Sections 13 and 13a of the Federal Reserve Act.

A corresponding change in the rates under other sections of the Federal Reserve Act was approved each time the rate under Sections 13 and 13a was raised during 1978. As of December 31, 1978, the structure of rates was as follows: 9½ per cent for borrowings under Sections 13 and 13a; 10 per cent for borrowings at the regular rate and 10½ per cent for borrowings at the special rate under Section

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10(b); and 12½ per cent for borrowings by individuals, partnerships, or corporations other than member banks under the last paragraph of Section 13.

January 6, 1978

Effective January 9, 1978, the Board approved actions taken by the directors of the Federal Reserve Banks of New York and Chicago to increase the discount rate from 6 per cent to 6½ per cent.

> Votes for this action: Messrs. Burns, Gardner, Wallich, and Coldwell. Votes against this action: Messrs. Partee and Lilly. Absent and not voting: Mr. Jackson.

The Board subsequently approved similar actions taken by the directors of the Federal Reserve Banks of Boston, Minneapolis, and Kansas City, effective January 10; the Federal Reserve Banks of Richmond, St. Louis, Dallas, and San Francisco, effective January 13; the Federal Reserve Bank of Atlanta, effective January 16; and the Federal Reserve Banks of Philadelphia and Cleveland, effective January 20.

Messrs. Partee and Lilly dissented from this action because they felt higher interest rates posed undue risks from the standpoint of the domestic economy, whose further recovery they regarded as uncertain, and because they feared such higher rates might seriously inhibit the continuing ability of thrift institutions to attract deposits subject to rate ceilings.

April 7, 1978

The Board disapproved an action taken by the directors of the Federal Reserve Bank of Chicago on April 6 to increase the discount rate to 6¾ per cent.

> Votes for this action: Messrs. Miller, Wallich, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Gardner and Coldwell.[3]

[3] From the time this action was taken through mid-September, there was one vacancy on the Board.

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April 17, 1978

The Board disapproved actions taken by the directors of the Federal Reserve Bank of St. Louis on April 13 and by the directors of the Federal Reserve Bank of Atlanta on April 14 to increase the discount rate to 7 per cent.

> Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None.

April 21, 1978

The Board disapproved actions taken on April 20 by the directors of the Federal Reserve Banks of Philadelphia and Kansas City to increase the discount rate to 6¾ per cent and by the directors of the Federal Reserve Bank of New York to increase the discount rate to 7 per cent.

> Votes for this action: Messrs. Miller, Gardner, Wallich, Jackson, and Partee. Votes against this action: None. Absent and not voting: Mr. Coldwell.

April 24, 1978

The Board disapproved an action taken by the directors of the Federal Reserve Bank of Richmond on April 21 to increase the discount rate to 6¾ per cent.

> Votes for this action: Messrs. Miller, Gardner, Coldwell, and Partee. Votes against this action: Messrs. Wallich and Jackson.

Messrs. Wallich and Jackson dissented from this action because they believed the proposed increase was warranted on general economic grounds and was desirable to bring the discount rate into closer alignment with market interest rates and to help support the dollar in foreign exchange markets.

May 10, 1978

Effective May 11, 1978, the Board approved actions taken by the directors of the Federal Reserve Banks of New York, Philadelphia, Cleveland, Richmond, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, and San Francisco to increase the discount rate to 7 per cent.

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Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, and Partee. Votes against this action: None. Absent and not voting: Mr. Jackson.

The Board subsequently approved similar actions taken by the directors of the Federal Reserve Banks of Boston and Dallas, effective May 12.

June 23, 1978

The Board disapproved actions taken on June 22 by the directors of the Federal Reserve Banks of Philadelphia, Chicago, Dallas, and San Francisco to increase the discount rate to 7¼ per cent and by the directors of the Federal Reserve Bank of Minneapolis to increase the discount rate to 7½ per cent.

Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None.

June 30, 1978

Effective July 3, 1978, the Board approved actions taken by the directors of the Federal Reserve Banks of Boston, New York, Cleveland, Richmond, Chicago, St. Louis, Minneapolis, Dallas, and San Francisco to increase the discount rate to 7¼ per cent.

Votes for this action: Messrs. Wallich, Coldwell, and Jackson. Votes against this action: Messrs. Miller and Partee. Absent and not voting: Mr. Gardner.

The Board subsequently approved similar actions taken by the directors of the Federal Reserve Banks of Philadelphia and Kansas City, effective July 7; and by the directors of the Federal Reserve Bank of Atlanta, effective July 10.

Messrs. Miller and Partee dissented from this action because they preferred a steady policy course for the immediate future. In their judgment, more time was needed to assess current uncertainties in the economic outlook, the recent moderation in monetary growth rates, and the less accommodative monetary policy implemented since mid-April. In their view, an increase in the discount rate under prevailing circumstances might also trigger unwarranted increases in other interest rates.

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June 30, 1978

The Board disapproved an action taken by the directors of the Federal Reserve Bank of New York on June 29 to increase the discount rate to 7½ per cent.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Mr. Gardner.

July 19, 1978

The Board disapproved actions taken by the directors of the Federal Reserve Bank of Richmond on July 13 and by the directors of the Federal Reserve Bank of Atlanta on July 14 to increase the discount rate to 7½ per cent.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Mr. Gardner.

July 21, 1978

The Board disapproved an action taken by the directors of the Federal Reserve Bank of New York on July 20 to increase the discount rate to 7½ per cent.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, and Jackson. Votes against this action: None. Absent and not voting: Messrs. Gardner and Partee.

July 31, 1978

The Board disapproved actions taken by the directors of the Federal Reserve Banks of Cleveland and Minneapolis on July 27 and by the directors of the Federal Reserve Bank of Atlanta on July 28 to increase the discount rate to 7½ per cent.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, and Partee. Votes against this action: None. Absent and not voting: Messrs. Gardner and Jackson.

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August 18, 1978

Effective August 21, 1978, the Board approved actions taken by the directors of all the Federal Reserve Banks to increase the discount rate to 7¾ per cent.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None. Absent and not voting: Mr. Gardner.

September 13, 1978

The Board disapproved an action taken by the directors of the Federal Reserve Bank of Minneapolis on September 1 to increase the discount rate to 8 per cent.

> Votes for this action: Messrs. Miller, Gardner, Wallich, Coldwell, Jackson, and Partee. Votes against this action: None.

September 22, 1978

Effective September 22, 1978, the Board approved actions taken by the directors of all the Federal Reserve Banks to increase the discount rate to 8 per cent.

> Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Mr. Gardner.

October 6, 1978

The Board disapproved an action taken by the directors of the Federal Reserve Bank of Boston on October 3 to increase the discount rate to 8¼ per cent.

> Votes for this action: Messrs. Miller, Wallich, Jackson, and Partee. Votes against this action: None. Absent and not voting: Messrs. Gardner, Coldwell, and Mrs. Teeters.

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October 13, 1978

Effective October 16, 1978, the Board approved actions taken by the directors of the Federal Reserve Banks of Boston, New York, Cleveland, Richmond, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, Dallas, and San Francisco to increase the discount rate to 8½ per cent.

Votes for this action: Messrs. Miller, Wallich, Coldwell, Jackson, and Partee. Votes against this action: Mr. Gardner and Mrs. Teeters.

The Board later approved a similar action taken by the directors of the Federal Reserve Bank of Philadelphia, effective October 20.

Mr. Gardner and Mrs. Teeters voted against this action in light of the substantial monetary restraint already implemented over the course of recent months and the evidence that growth in economic activity appeared to be moderating. They concluded that it was now desirable to await further developments before considering any additional monetary restraint.

October 27, 1978

The Board disapproved an action taken by the directors of the Federal Reserve Bank of Boston on October 26 to increase the discount rate to 9 per cent.

Votes for this action: Messrs. Miller, Wallich, Coldwell, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Messrs. Gardner and Jackson.

November 1, 1978

Effective November 1, 1978, the Board approved actions taken by the directors of the Federal Reserve Banks of New York and Minneapolis to increase the discount rate to 9½ per cent.

Votes for this action: Messrs. Miller, Wallich, Coldwell, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Messrs. Gardner and Jackson.

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The Board subsequently approved similar actions taken by the directors of the Federal Reserve Banks of Boston, Philadelphia, Cleveland, Richmond, Chicago, St. Louis, Kansas City, Dallas, and San Francisco, effective November 2; and by the directors of the Federal Reserve Bank of Atlanta, effective November 3.

December 15, 1978

The Board disapproved an action taken by the directors of the Federal Reserve Bank of Richmond on December 14 to increase the discount rate to 9¾ per cent.

> Votes for this action: Messrs. Wallich, Coldwell, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Mr. Miller.[4]

December 22, 1978

The Board disapproved actions taken by the directors of the Federal Reserve Bank of Boston on December 20 to increase the discount rate to 10 per cent and by the directors of the Federal Reserve Bank of Atlanta on December 22 to increase the discount rate to 9¾ per cent.

> Votes for this action: Messrs. Wallich, Coldwell, Partee, and Mrs. Teeters. Votes against this action: None. Absent and not voting: Mr. Miller.

[4] There were two vacancies on the Board at the time of this action.

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Record of Policy Actions of the Federal Open Market Committee

The record of policy actions of the Federal Open Market Committee is presented in the ANNUAL REPORT of the Board of Governors pursuant to the requirements of Section 10 of the Federal Reserve Act. That section provides that the Board shall keep a complete record of the actions taken by the Board and by the Federal Open Market Committee on all questions of policy relating to open market operations, that it shall record therein the votes taken in connection with the determination of open market policies and the reasons underlying each such action, and that it shall include in its ANNUAL REPORT to the Congress a full account of such actions.

In the pages that follow, there are entries with respect to the policy actions taken at the meetings of the Federal Open Market Committee held during the calendar year 1978, including the votes on the policy decisions made at those meetings as well as a résumé of the basis for the decisions. The summary descriptions of economic and financial conditions are based on the information that was available to the Committee at the time of the meetings, rather than on data as they may have been revised later.

It will be noted from the record of policy actions that in some cases the decisions were by unanimous vote and that in other cases dissents were recorded. The fact that a decision in favor of a general policy was by a large majority, or even that it was by unanimous vote, does not necessarily mean that all members of the Committee were equally agreed as to the reasons for the particular decision or as to the precise operations in the open market that were called for to implement the general policy.

During 1978 the policy record for each meeting was released a few days after the next regularly scheduled meeting and was subsequently published in the *Federal Reserve Bulletin* as well as in this ANNUAL REPORT.

Policy directives of the Federal Open Market Committee are issued to the Federal Reserve Bank of New York as the Bank selected by

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the Committee to execute transactions for the System Open Market Account. In the area of domestic open market activities, the Federal Reserve Bank of New York operates under two separate directives from the Open Market Committee, an Authorization for Domestic Open Market Operations and a domestic policy directive. In the foreign currency area, it operates under an Authorization for Foreign Currency Operations and a foreign currency directive. These four instruments are shown below in the form in which they were in effect at the beginning of 1978. Changes in the instruments during the year are reported in the records for the individual meetings.

AUTHORIZATION FOR DOMESTIC OPEN MARKET OPERATIONS

In effect January 1, 1978

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) When appropriate, 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

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market discount rates, prime bankers' acceptances with maturities of up to 9 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 $100 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 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, under special circumstances, such as when 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 ¼ 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 $2 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

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Open Market Account to Government securities dealers and to banks participating in Government securities clearing arangements conducted through a Federal Reserve Bank, under such instructions as the Committee may specify from time to time.

DOMESTIC POLICY DIRECTIVE

In effect January 1, 1978

The information reviewed at this meeting suggests that real output of goods and services is growing in the current quarter at about the pace in the third quarter. The dollar value of total retail sales, which had increased sharply in October, rose considerably further in November. Industrial production continued to expand, and employment increased substantially. However, the unemployment rate, at 6.9 per cent, remained in the narrow range prevailing since April. The wholesale price index for all commodities rose sharply in November for the second successive month, reflecting another large increase in average prices of farm products and foods. However, the rise in average prices of industrial commodities was less rapid than in the preceding 2 months. The index of average hourly earnings has advanced at a somewhat faster pace so far this year than it had on the average during 1976.

The dollar has been under considerable pressure in foreign exchange markets in recent weeks, and its trade-weighted value against major foreign currencies has declined more than 3 per cent further since mid-November. In October the U.S. foreign trade deficit widened sharply, primarily as a result of the dock strike at many U.S. ports.

M–1—which had expanded substantially in October—declined slightly in November, and *M*–2 increased relatively little. The total of savings deposits and small-denomination time deposits at commercial banks declined somewhat, but growth in large-denomination time deposits accelerated sharply further as credit demands remained strong. Inflows to nonbank thrift institutions slowed further in November. Market interest rates have changed relatively little since mid-November.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster bank reserve and other financial conditions that will encourage continued economic expansion and help resist inflationary pressures, while contributng to a sustainable pattern of international transactions.

At its meeting on October 18, 1977, the Committee agreed that growth of *M*–1, *M*–2, and *M*–3 within ranges of 4 to 6½ per cent, 6½ to 9 per

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cent, and 8 to 10½ per cent, respectively, from the third quarter of 1977 to the third quarter of 1978 appears to be consistent with these objectives. These ranges are subject to reconsideration at any time as conditions warrant.

At this time, the Committee seeks to maintain about the prevailing money market conditions during the period immediately ahead, provided that monetary aggregates appear to be growing at approximately the rates currently expected, which are believed to be on a path reasonably consistent with the longer-run ranges for monetary aggregates cited in the preceding paragraph. Specifically, the Committee seeks to maintain the weekly-average Federal funds rate at about the current level, so long as *M*–1 and *M*–2 appear to be growing over the December–January period at annual rates within ranges of 2½ to 8½ per cent and 6 to 10 per cent, respectively.

If, giving approximately equal weight to *M*–1 and *M*–2, it appears that growth rates over the 2-month period are approaching or moving beyond the limits of the indicated ranges, the operational objective for the weekly-average Federal funds rate shall be modified in an orderly fashion within a range of 6¼ to 6¾ per cent. In the conduct of day-to-day operations, account shall be taken of emerging financial market conditions, including the unsettled conditions in foreign exchange markets.

If it appears during the period before the next meeting that the operating constraints specified above are proving to be significantly inconsistent, the Manager is promptly to notify the Chairman, who will then decide whether the situation calls for supplementary instructions from the Committee.

AUTHORIZATION FOR FOREIGN CURRENCY OPERATIONS

In effect January 1, 1978

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, for System Open Market Account, to the extent necessary to carry out the Committee's foreign currency directive and express authorizations by the Committee pursuant thereto, and in conformity with such procedural instructions as the Committee may issue from time to time:

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A. To purchase and sell the following foreign currencies in the form of cable transfers through spot or forward transactions on the open market at home and abroad, including transactions with the U.S. Exchange Stabilization Fund established by Section 10 of the Gold Reserve Act of 1934, with foreign monetary authorities, with the Bank for International Settlements, and with other international financial institutions:

Austrian schillings
Belgian francs
Canadian dollars
Danish kroner
Pounds sterling
French francs
German marks
Italian lire
Japanese yen
Mexican pesos
Netherlands guilders
Norwegian kroner
Swedish kronor
Swiss francs

B. To hold balances of, and to have outstanding forward contracts to receive or to deliver, the foreign currencies listed in paragraph A above.

C. To draw foreign currencies and to permit foreign banks to draw dollars under the reciprocal currency arrangements listed in paragraph 2 below, provided that drawings by either party to any such arrangement shall be fully liquidated within 12 months after any amount outstanding at that time was first drawn, unless the Committee, because of exceptional circumstances, specifically authorizes a delay.

D. To maintain an over-all open position in all foreign currencies not exceeding $1.0 billion, unless a larger position is expressly authorized by the Committee. For this purpose, the over-all open position in all foreign currencies is defined as the sum (disregarding signs) of open positions in each currency. The open position in a single foreign currency is defined as holdings of balances in that currency, plus outstanding contracts for future receipt, minus outstanding contracts for future delivery of that currency, i.e., as the sum of these elements with due regard to sign.

2. 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:

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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	360
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 authorized European currencies other than Swiss francs	1,250

Any changes in the terms of existing swap arrangements, and the proposed terms of any new arrangements that may be authorized, shall be referred for review and approval to the Committee.

3. Currencies to be used for liquidation of System swap commitments may be purchased from the foreign central bank drawn on, at the same exchange rate as that employed in the drawing to be liquidated. Apart from any such purchases at the rate of the drawing, all transactions in foreign currencies undertaken under paragraph 1(A) above shall, unless otherwise expressly authorized by the Committee, be at prevailing market rates.

4. It shall be the normal practice to arrange with foreign central banks for the coordination of foreign currency transactions. In making operating arrangements with foreign central banks on System holdings of foreign currencies, the Federal Reserve Bank of New York shall not commit itself to maintain any specific balance, unless authorized by the Federal Open Market Committee. Any agreements or understandings concerning the administration of the accounts maintained by the Federal Reserve Bank of New York with the foreign banks designated by the Board of Governors under Section 214.5 of Regulation N shall be referred for review and approval to the Committee.

5. Foreign currency holdings shall be invested insofar as practicable, considering needs for minimum working balances. Such investments shall be in accordance with Section 14(e) of the Federal Reserve Act.

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6. All operations undertaken pursuant to the preceding paragraphs shall be reported daily to the Foreign Currency Subcommittee. The Foreign Currency Subcommittee consists of the Chairman and Vice Chairman of the Committee, the Vice Chairman of the Board of Governors, and such other member of the Board as the Chairman may designate (or in the absence of members of the Board serving on the Subcommittee, other Board Members designated by the Chairman as alternates, and in the absence of the Vice Chairman of the Committee, his alternate). Meetings of the Subcommittee shall be called at the request of any member, or at the request of the Manager, for the purposes of reviewing recent or contemplated operations and of consulting with the Manager on other matters relating to his responsibilities. At the request of any member of the Subcommittee, questions arising from such reviews and consultations shall be referred for determination to the Federal Open Market Committee.

7. The Chairman is authorized:

A. With the approval of the Committee, to enter into any needed agreement or understanding with the Secretary of the Treasury about the division of responsibility for foreign currency operations between the System and the Treasury;

B. To keep the Secretary of the Treasury fully advised concerning System foreign currency operations, and to consult with the Secretary on policy matters relating to foreign currency operations;

C. From time to time, to transmit appropriate reports and information to the National Advisory Council on International Monetary and Financial Policies.

8. Staff officers of the Committee are authorized to transmit pertinent information on System foreign currency operations to appropriate officials of the Treasury Department.

9. All Federal Reserve Banks shall participate in the foreign currency operations for System Account in accordance with paragraph 3G(1) of the Board of Governors' Statement of Procedure with Respect to Foreign Relationships of Federal Reserve Banks dated January 1, 1944.

FOREIGN CURRENCY DIRECTIVE

In effect January 1, 1978

1. System operations in foreign currencies shall generally be directed at countering disorderly market conditions, provided that market exchange rates for the U.S. dollar reflect actions and behavior consistent with the proposed IMF Article IV, Section 1.

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2. To achieve this end the System shall:

A. Undertake spot and forward purchases and sales of foreign exchange.

B. Maintain reciprocal currency ("swap") arrangements with selected foreign central banks and with the Bank for International Settlements.

C. Cooperate in other respects with central banks of other countries and with international monetary institutions.

3. Transactions may also be undertaken:

A. To adjust System balances in light of probable future needs for currencies.

B. To provide means for meeting System and Treasury commitments in particular currencies, and to facilitate operations of the Exchange Stabilization Fund.

C. For such other purposes as may be expressly authorized by the Committee.

4. System foreign currency operations shall be conducted:

A. In close and continuous consultation and cooperation with the United States Treasury;

B. In cooperation, as appropriate, with foreign monetary authorities; and

C. In a manner consistent with the obligations of the United States in the International Monetary Fund regarding exchange arrangements under the proposed IMF Article IV.

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MEETING HELD ON JANUARY 17, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested that real output of goods and services had grown in the fourth quarter of 1977 at a pace close to that of the third quarter, which the Commerce Department had revised upward to an annual rate of 5.1 per cent. At the same time the rise in average prices, as measured by the fixed-weighted price index for gross domestic business product, appeared to have stepped up somewhat from the annual rate of 5.0 per cent estimated for the third quarter. Staff projections for the year from the fourth quarter of 1977 to the fourth quarter of 1978—which now were based on assumptions that included reductions next fall in Federal income taxes—suggested a moderately faster expansion than the projections prepared just before the December meeting of the Committee. According to the latest projections, growth in real gross national product (GNP) would be sustained at a good pace throughout 1978. It was also expected that the rise in prices would remain relatively rapid and that the unemployment rate would decline moderately further over the year ahead.

The staff estimates for the fourth quarter of 1977 suggested that final sales of goods and services had risen substantially more than in the third quarter, but that the rate of business inventory accumulation had slowed considerably after a slight rise in the third quarter. With respect to final sales in real terms, gains had been particularly strong in consumer spending for both durable and nondurable goods and in residential construction.

Staff projections for the year ahead reflected expectations that the growth of consumer spending in real terms would moderate during the first quarter from the exceptionally rapid pace in the fourth quarter of 1977 and then would pick up as the year progressed—particularly during the fourth quarter, following the reduction in personal income taxes assumed to take effect on October 1. Busi-

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ness fixed investment was projected to expand moderately, owing in part to stimulative modifications of the investment tax credit that were assumed to be retroactive to the beginning of 1978. It was still anticipated that the rise in residential construction outlays would taper off as the year progressed and that the increase in Federal purchases of goods and services would be smaller than over the past year.

In December industrial production expanded 0.2 per cent, compared with 0.4 per cent in November. However, the December increase was held down by a strike that had caused a reduction of nearly 50 per cent in output of bituminous coal. Auto assemblies were curtailed somewhat, but output of other consumer goods and of business equipment continued to rise. For the fourth quarter as a whole, growth in industrial production slowed to an annual rate of about 2¼ per cent from about 4¼ per cent in the third quarter, reflecting in part the reduction in the rate of business inventory accumulation.

Nonfarm payroll employment continued to rise in December, and after adjustment for strikes, the gain was as large as in November. Employment increases were again substantial in trade, services, and State and local government. In manufacturing too, the gain was sizable, but the average workweek declined, in part because of the curtailment in assemblies of autos. The unemployment rate dropped to 6.4 per cent in December from a (revised downward) rate of 6.7 per cent in November.

The dollar value of retail sales, according to the Census Bureau's advance estimate, had declined a little in December after having risen sharply in the preceding 2 months. For the fourth quarter as a whole sales rose by almost 4 per cent, about equaling the large rise in the fourth quarter of 1976. Unit sales of new domestic and foreign autos increased somewhat in December, returning to about the October level, and sales were almost as high in the fourth quarter as in the third.

Private housing starts, as had been reported before the Committee's December meeting, edged down in November to an annual rate of about 2.1 million units. The average number of starts for October and November was 5 per cent above the third-quarter average, which in turn was the highest of the current expansion.

The latest Department of Commerce survey of business spending

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plans, taken in late November and December, suggested that spending for plant and equipment would expand 10.1 per cent in 1978. Such spending had increased 13.7 per cent in 1977.

Manufacturers' new orders for nondefense capital goods declined 5 per cent in November, but the October–November average was about 6½ per cent above the third-quarter average. Contract awards for commercial and industrial buildings—measured in terms of floor space—advanced sharply in November after having declined in October. The average for the 2 months was somewhat higher than that for the third quarter.

The index of average hourly earnings for private nonfarm production workers increased relatively little in December, as it had in November. However, from December 1976 to December 1977 the index rose 7.4 per cent, which compared with an increase of 6.9 per cent over the preceding 12 months.

The wholesale price index for all commodities rose 0.5 per cent in December, considerably less than in October and November. Average prices of farm products and foods advanced only 0.4 per cent in December, compared with an average increase of 1.8 per cent over the preceding 2 months. The 0.5 per cent rise in prices of industrial commodities in December equaled the October–November average.

The consumer price index rose 0.5 per cent in November, somewhat more than in any of the preceding 4 months. Retail prices of foods increased 0.6 per cent, in contrast with an average between 0.1 and 0.2 per cent in the July–October period. The pace of advance in nonfood commodities also picked up, mainly because of increases for new autos, but the rise in prices of services remained at a reduced rate.

In foreign exchange markets the dollar continued under strong downward pressure from mid-December to just after the turn of the year, and during that period its trade-weighted value against major foreign currencies declined about 2½ per cent. On January 4, 1978, it was announced that the Exchange Stabilization Fund of the U.S. Treasury would henceforth be utilized actively, together with the swap network operated by the Federal Reserve System, to check speculation and to help re-establish order in the foreign exchange markets. On January 6 the Board of Governors announced approval of an increase in Federal Reserve discount rates from 6 to 6½ per cent, and in an accompanying press release noted that the recent

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disorder in foreign exchange markets constituted a threat to orderly expansion of the domestic and international economy. The Board expressed the hope that the need for this increase would prove temporary. It also noted that the condition of the domestic economy was sound and that credit supplies to sustain the economic expansion would remain ample. From January 4 to the time of this meeting the trade-weighted value of the dollar recovered about 1¾ per cent.

The U.S. foreign trade deficit declined substantially in November after a sharp increase in October. The dock strike that had halted containerized shipments through Atlantic and Gulf Coast ports between October 1 and November 29 appeared to have depressed recorded exports and imports by similar amounts in November, whereas in October the strike had caused much more of a reduction in recorded exports than imports.

At U.S. commercial banks, total credit contracted slightly in December, but because it had grown rapidly in October and November, expansion for the fourth quarter as a whole remained close to the third-quarter pace. The December halt in growth of bank credit reflected both a sharp slackening in loan expansion and a further contraction in holdings of securities.

While the reduced loan expansion at banks in December stemmed in part from a large net reduction in securities loans, business loan growth also slowed appreciably. Sales of commercial paper expanded by a roughly similar amount, however, so total short-term credit to nonfinancial businesses from these sources rose at about the same pace in December as in November.

The narrowly defined money stock (*M*-1)[1] grew at a 7.6 per cent annual rate in December and at a 6.8 per cent annual rate for the fourth quarter as a whole. From the fourth quarter of 1976 to the fourth quarter of 1977, *M*-1 grew 7.4 per cent, compared with 5.6 per cent in 1976 and 4.4 per cent in 1975.

In the third quarter of 1977 *M*-1 had grown nearly as fast as nominal GNP, so the income velocity of *M*-1—the ratio of nominal GNP to *M*-1—had shown little change. It appeared, however, that income velocity had increased significantly in the fourth quarter as a result of both faster growth in GNP and a slower rise in *M*-1.

[1] *M*-1 is composed of private demand deposits and currency in circulation.

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Growth in *M*-2[2] increased somewhat in December from the low November rate. Virtually all of the growth in the time and savings deposit component of *M*-2 occurred in large-denomination time deposits not subject to ceiling rates; savings deposits remained about unchanged for the second consecutive month and small-denomination time deposits, which had contracted in November, expanded only a little. From the fourth quarter of 1976 to the fourth quarter of 1977, *M*-2 grew 9.6 per cent, compared with 10.9 per cent in 1976 and 8.3 per cent in 1975.

Deposit growth at nonbank thrift institutions slowed further in December, and *M*-3[3] expanded at a 7.5 per cent annual rate—about the same as in November. Most of the December growth in deposits at thrift institutions presumably occurred in longer-maturity instruments on which the effective offering rates still exceeded yields available on Treasury securities of comparable maturity. For 1977 as a whole, *M*-3 grew 11.6 per cent.

At its December meeting the Committee had decided that operations in the period immediately ahead should be directed toward maintaining about the prevailing money market conditions, provided that the monetary aggregates appeared to be growing at approximately the rates then expected. Specifically, the Committee sought to maintain the weekly-average Federal funds rate at about 6½ per cent, so long as *M*-1 and *M*-2 appeared to be growing over the December–January period at annual rates within ranges of 2½ to 8½ per cent and 6 to 10 per cent, respectively. However, members also agreed that if growth in the aggregates appeared to approach or move beyond the limits of their specified ranges, the operational objective for the weekly-average Federal funds rate should be varied in an orderly fashion within a range of 6¼ to 6¾ per cent.

The Committee also had included in its directive to the Federal Reserve Bank of New York the following sentence: "In the conduct of day-to-day operations, account shall be taken of emerging financial market conditions, including the unsettled conditions in foreign exchange markets." This instruction had been added to provide the Manager with somewhat greater flexibility, in part because of the

[2] *M*-2 includes *M*-1 and commercial bank time and savings deposits other than large-denomination certificates of deposit.

[3] *M*-3 includes *M*-2 and deposits at nonbank thrift institutions (savings and loan associations, mutual savings banks, and credit unions).

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Committee's view that pressures on the dollar in foreign exchange markets might appropriately influence the nature and timing of domestic open market operations from day to day.

With the monetary aggregates apparently expanding at rates well within the Committee's specified ranges, the Manager of the System Account continued to aim for a Federal funds rate of around 6½ per cent in the last weeks of December and the first statement week of January. Due to technical factors, however—including the usual money market churning around year-end—Federal funds actually traded at rates somewhat above this level. The Manager in early January also shaded his Federal funds rate objective slightly upward because of downward pressures on the dollar in foreign exchange markets. On January 9, following the January 6 increase in Federal Reserve discount rates to 6½ per cent, the Federal Open Market Committee concurred in the Chairman's recommendation to raise the inter-meeting range for the Federal funds rate to 6½ to 7 per cent and to instruct the Manager to aim for a rate of around 6¾ per cent over the next few days. In the days remaining until this meeting, the funds rate averaged 6.75 per cent.

During the initial weeks of the inter-meeting period other short-term interest rates showed little net change, while longer-term rates tended to move higher. After the discount rate action and the increase in the funds rate to 6¾ per cent, short-term market rates adjusted sharply upward, with the largest net increases—ranging from 35 to 45 basis points—occurring on Treasury bills. Bond yields also rose somewhat further over this period but significantly less than bill rates.

Auctions of 2-year notes and 15-year bonds netted the U.S. Treasury $2.7 billion of new money during the inter-meeting period—including $600 million of 2-year notes sold directly to foreign official institutions on a noncompetitive basis. For the fourth quarter as a whole, net Treasury sales of marketable debt to the public totaled nearly $19 billion, a substantial share of which was purchased by foreign official institutions.

The volume of bonds offered publicly by nonfinancial corporations in December was somewhat less than in previous months, as industrial firms reduced their flow of new issues. Financial concerns continued to borrow heavily in long-term debt markets, however.

Offerings of State and local government bonds expanded con-

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traseasonally in December, raising the total for the fourth quarter almost to the high level of the third quarter. Most of the December rise was attributable to advance refunding issues.

Net mortgage lending in the fourth quarter appeared to be running close to the record third-quarter rate. Savings and loan associations managed to sustain an unusually high level of lending—notwithstanding their slower deposit inflows—by increasing their borrowings, particularly from Federal home loan banks. Such borrowing rose $2.6 billion during the quarter, the largest expansion in more than 3 years.

In the Committee's discussion of the economic situation, most members agreed that the staff's projection of the growth rate in real GNP over the full year 1978 was reasonable. However, there was some difference of opinion regarding the probable profile of the expansion during the course of the year. Specifically, a number of members thought that growth might be faster in the first half of 1978 and slower in the second half than had been projected.

In this connection, it was suggested that in the early part of 1978 production would be stimulated by business efforts to restore inventories depleted by the surge in sales that had occurred in the fourth quarter of 1977. It was observed, however, that if production increased as expected and growth in sales slowed, the consequent inventory build-up could lead to a need for correction and hence to slower growth in output later in the year. There was some feeling also that the proposed reductions in Federal income taxes might have less stimulative effect in the fourth quarter than expected by the staff, and it was noted that payroll taxes for social security and unemployment insurance were scheduled to rise at the beginning of 1979. One member was of the opinion that a number of forces, including the depreciation of the dollar that had occurred in foreign exchange markets, would induce a faster rise in prices than the staff had anticipated and that inflation would tend to slow the expansion in activity as the year progressed. However, none of the members who expressed concern about the growth of real GNP late in the year anticipated that the economy would move into a recession during 1978.

Other members were more optimistic about the economic outlook. One noted that at this time of the year forecasters almost invariably expressed more uncertainty about the prospects for the

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second half than for the first half. Another indicated that he expected the expansion to be sustained by a gradual improvement in business and consumer confidence. This member and others also stressed the stimulative effects of the prospective tax reduction, and one noted that if necessary the reduction could be larger than presently contemplated.

These differences of view were generally associated with different expectations for major sectors of the economy. Thus, one member expressed the opinion that residential construction activity would remain at a high level during 1978, in part because individuals were tending to perceive homeownership as an effective hedge against inflation. At the same time, this member noted that the recent spurt in consumer spending had been financed in considerable measure by credit; he did not expect the rapid expansion to continue, and he thought it would be an unhealthy development if it did. Another member said he anticipated an appreciable decline in the rate of housing starts during the year, and a third expressed concern about the possible consequences for housing activity if thrift institutions should cut back significantly on new mortgage commitments because of the record volume already outstanding and because of increased uncertainty about the pace of deposit inflows. The latter member also doubted that consumer purchases of new automobiles would be sustained at the levels of 1976 and 1977 for another year, as projected by the staff, especially in view of the downtrend in sales that appeared to have been under way since last spring.

With respect to business fixed investment, the results suggested by the recent Commerce Department survey of business spending plans for 1978 were described as disappointing. It was also observed, however, that a more favorable outlook for capital investment was presented by such indicators as new orders for nondefense capital goods, construction contracts for commercial and industrial buildings, formation of new businesses, and newly approved capital appropriations, and that over the years such measures had provided better indications of future business fixed investment than had surveys of spending plans. It was noted that the administration's tax program would include new incentives for business fixed investment, and one member suggested that such investment was likely to be stimulated by rising rates of capacity utilization, such as those being forecast for the coming year. However, another member

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offered the hypothesis that the need for new plants in this country was being reduced by a trend toward remodeling and re-equipping existing structures and by a tendency for multinational corporations to rely on their plants abroad for needed capacity.

It was observed during the discussion that the course of business fixed investment depended on the state of business confidence in general and on profit expectations in particular. Some members reported that they had recently detected some deterioration of business confidence, but others felt that the state of confidence had remained unchanged or had improved. One member remarked that businessmen had long been deeply disturbed about the persistence of inflation, and that recently some who followed monetary developments closely had begun to question the System's determination to slow the rates of growth of the monetary aggregates. One member observed that the recent behavior of the stock market—including the low levels to which price/earnings ratios had fallen—was not indicative of the kind of business confidence that normally would be accompanied by rising investment. Another member remarked that low price/earnings ratios probably reflected in part the realization by investors that reported earnings overstated real earnings as a result of the use of conventional accounting procedures in a period of inflation. It also was suggested that in making investment decisions businessmen were now insisting on shorter expected "payout" periods than they had earlier because they perceived the risks to be greater.

Serious concern continued to be expressed about the dollar's weakness in foreign exchange markets, although it was noted that the dollar had recovered somewhat over the past 2 weeks. The observation was made that the conventional theory concerning depreciation of a currency did not apply to the dollar because of its special role in international trade and finance. Specifically, it was suggested that depreciation of the dollar tended to weaken confidence here and abroad and to cause postponement of decisions to spend or to invest in new facilities; that the counterpart of the dollar's depreciation—appreciation of foreign currencies—adversely affected exports of other major countries and generated risks of stagnation or recession in economic activity; and that this negative impact on aggregate demand abroad could have adverse effects on the U.S. foreign trade balance that greatly outweighed the

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favorable effects of the improved competitiveness of U.S. products in markets here and abroad. As at the December meeting, the observation was made that the position of the dollar would be strengthened by adoption in this country of an effective energy program, of a tax policy conducive to business investment here, and of a more effective attack on inflation, as well as by pursuit abroad of faster rates of economic growth.

At its meeting in October 1977 the Committee had agreed that from the third quarter of 1977 to the third quarter of 1978 average rates of growth in the monetary aggregates within the following ranges appeared to be consistent with broad economic aims: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 8 to 10½ per cent. The associated range for the rate of growth in commercial bank credit was 7 to 10 per cent. It had also been agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings. However, no further modification was made at this meeting.

In the Committee's discussion of policy for the period immediately ahead, a number of members suggested that any significant easing of money market conditions would be undesirable at this time because of the weakness of the dollar in foreign exchange markets and—in the view of some—because of the cumulative growth rates in the monetary aggregates over recent months. Each of the three members who had dissented from the decision of January 9 to seek a higher Federal funds rate indicated that he would not now advocate a rollback since that decision had been implemented and absorbed by the financial markets. At the same time, there was little sentiment for further firming actions in the coming inter-meeting period unless the monetary aggregates appeared to be growing at rapid rates.

Consistent with these views, most members expressed a preference for continuing to give greater weight than usual to money market conditions in conducting operations in the period until the next meeting of the Committee. However, a few favored basing operating decisions primarily on the behavior of the monetary aggregates, particularly if growth rates appeared to be higher than desired. While there was general agreement that operations should be directed initially toward maintaining the current Federal funds

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rate of about 6¾ per cent, various suggestions were made with respect to the range in which the funds rate might be varied if the growth rates in the monetary aggregates appeared to be deviating markedly from expectations. Thus, some members favored retaining the present range of 6½ to 7 per cent, but others were inclined to raise the lower limit to 6⅝ or 6¾ per cent; some in the latter group also suggested raising the upper limit.

In addition, there were some differences of view with respect to the specifications for growth in *M*-1 over the January–February period, relating to both the width and the level of the range. A number of members suggested that the range be narrowed from the spread of 6 percentage points used in the last few directives to one of 5 or 4 points, while others were willing to retain the wider range. Suggestions for the lower limit of the *M*-1 range varied from 1½ to 3½ per cent and those for the upper limit varied from 7 to 8½ per cent. For *M*-2 the majority of members favored a range of 5 to 9 per cent, although one advocated a substantial reduction in the lower limit and another was inclined to reduce both limits slightly.

At the conclusion of the discussion the Committee decided that operations in the period immediately ahead should be directed toward maintaining prevailing money market conditions, as represented by the current 6¾ per cent level of the Federal funds rate. However, the members agreed that if growth in the aggregates should appear to approach or move beyond the limits of their specified ranges, the operational objective for the weekly-average Federal funds rate should be varied in an orderly fashion within a range of 6½ to 7 per cent. It was understood that very strong evidence of weakness in the monetary aggregates would be required before operations were directed toward reducing the Federal funds rate from its current level. For the annual rates of growth in *M*-1 and *M*-2 over the January–February period, the Committee specified ranges of 2½ to 7½ per cent and 5 to 9 per cent, respectively. It also agreed that in assessing the behavior of the aggregates, the Manager should give approximately equal weight to the behavior of *M*-1 and *M*-2.

The Committee decided to retain in the directive the sentence calling for account to be taken of "emerging financial market conditions, including the unsettled conditions in foreign exchange markets" in the conduct of day-to-day open market operations. As

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already noted, this instruction had been included in the previous directive in part because of the Committee's view that the nature and timing of operations might appropriately be influenced by pressures on the dollar in foreign exchange markets.

As customary, 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.

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 in the fourth quarter was close to the pace in the third quarter. The dollar value of total retail sales declined in December, but the gain from the third to the fourth quarter was substantial. Industrial production expanded somewhat further in December, although the rise was limited by a strike in coal mining. Employment increased appreciably, and the unemployment rate declined from 6.7 per cent to 6.4 per cent. The wholesale price index for all commodities rose considerably less in December than in the preceding 2 months, reflecting a much smaller increase in average prices of farm products and foods. Prices of industrial commodities advanced at about the average pace in the preceding 2 months. The index of average hourly earnings advanced slightly faster during 1977 than it had during 1976.
>
> Exchange market pressure on the dollar has continued in recent weeks. On January 4 it was announced that the Exchange Stabilization Fund would be utilized actively together with the swap network operated by the Federal Reserve System to help re-establish order in the foreign exchange markets. On January 6 an increase in Federal Reserve discount rates from 6 to 6½ per cent was announced. The trade-weighted value of the dollar against major foreign currencies declined about 2½ per cent further from mid-December to the early days of January but subsequently recovered about 1¾ per cent.
>
> *M*-1—which had declined slightly in November—rose in December. Growth in *M*-2 remained relatively slow, as inflows to banks of time and savings deposits other than negotiable CD's were sharply curtailed. Inflows to nonbank thrift institutions slowed somewhat further. Market interest rates edged up in late December, and rates—particularly for short-term securities—rose substantially further in the early weeks of January.

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

At its meeting on October 18, 1977, the Committee agreed that growth of *M*-1, *M*-2, and *M*-3 within ranges of 4 to 6½ per cent, 6½ to 9 per cent, and 8 to 10½ per cent, respectively, from the third quarter of 1977 to the third quarter of 1978 appears to be consistent with these objectives. These ranges are subject to reconsideration at any time as conditions warrant.

At this time, the Committee seeks to maintain about the prevailing money market conditions during the period immediately ahead, provided that monetary aggregates appear to be growing at approximately the rates currently expected, which are believed to be on a path reasonably consistent with the longer-run ranges for monetary aggregates cited in the preceding paragraph. Specifically, the Committee seeks to maintain the weekly-average Federal funds rate at about the current level, so long as *M*-1 and *M*-2 appear to be growing over the January–February period at annual rates within ranges of 2½ to 7½ per cent and 5 to 9 per cent, respectively. If, giving approximately equal weight to *M*-1 and *M*-2, it appears that growth rates over the 2-month period are approaching or moving beyond the limits of the indicated ranges, the operational objective for the weekly-average Federal funds rate shall be modified in an orderly fashion within a range of 6½ to 7 per cent. In the conduct of day-to-day operations, account shall be taken of emerging financial market conditions, including the unsettled conditions in foreign exchange markets.

If it appears during the period before the next meeting that the operating constraints specified above are proving to be significantly inconsistent, the Manager is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

> Votes for this action: Messrs. Burns, Volcker, Coldwell, Gardner, Guffey, Lilly, Mayo, Morris, Partee, Roos, and Wallich. Votes against this action: None. Absent and not voting: Mr. Jackson.

2. Authorization for Foreign Currency Operations

Paragraph 1D of the Committee's authorization for foreign currency operations authorizes the Federal Reserve Bank of New York for

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the System Open Market Account to maintain an over-all open position in all foreign currencies not exceeding $1.0 billion, unless a larger position is expressly authorized by the Committee. On January 6, 1978, the Committee had authorized an open position of $1.5 billion.

At this meeting the Committee authorized an open position of $1.75 billion. This action was taken in view of the scale of recent and potential Federal Reserve operations in the foreign exchange markets undertaken pursuant to the Committee's foreign currency directive.

> Votes for this action: Messrs. Burns, Volcker, Coldwell, Gardner, Guffey, Lilly, Mayo, Morris, Partee, Roos, and Wallich. Votes against this action: None. Absent and not voting: Mr. Jackson.

3. Authorization for Domestic Open Market Operations

At this meeting the Committee amended, effective immediately, the authorization for domestic open market operations by adding the following paragraph, designated paragraph 4:

> In order to ensure the effective conduct of open market operations, while assisting in the provision of short-term investments for foreign and international accounts maintained at the Federal Reserve Bank of New York, the Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, (a) for System Open Market Account, to sell U.S. Government securities to such foreign and international accounts on the bases set forth in paragraph 1(a) under agreements providing for the resale by such accounts of those securities within 15 calendar days on terms comparable to those available on such transactions in the market; and (b) for New York Bank account, when appropriate, to undertake with dealers, subject to the conditions imposed on purchases and sales of securities in paragraph 1(c), repurchase agreements in U.S. Government and agency securities, and to arrange corresponding sale and repurchase agreements between its own account and foreign and international accounts maintained at the Bank. Transactions undertaken with such accounts under the provisions of this paragraph may provide for a service fee when appropriate.

> Votes for this action: Messrs. Burns, Volcker, Coldwell, Gardner, Guffey, Lilly, Mayo, Morris,

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Partee, Roos, and Wallich. Votes against this action: None. Absent and not voting: Mr. Jackson.

Since mid-1974 the Federal Reserve Bank of New York had made available to its foreign official accounts a facility for making repurchase agreements (Rp's) involving U.S. Government and Federal agency securities. The facility not only provided a service for foreign central banks but also added a useful dimension of flexibility to System open market operations. In arranging Rp's for foreign official accounts the New York Bank had—depending on the System's operating objectives at the moment—either served as an agent in arranging the transactions with the market or made the transactions with the System Open Market Account (SOMA). Arrangements of the former type were not under the jurisdiction of the Federal Open Market Committee; those of the latter type were authorized by the Committee under the general authority to buy or sell U.S. Government or agency securities for SOMA contained in paragraph 1(a) of the authorization for domestic open market operations.

In May 1977 the New York Bank had learned of an Internal Revenue Service (IRS) ruling on the treatment of Rp's by a taxpayer that suggested that a tax liability might be incurred in connection with income earned by some foreign official accounts on Rp's with the market. At the same time it did not appear probable that a tax liability would be incurred in the case where Rp's were arranged between foreign official accounts and some entity of the Federal Reserve System. Accordingly, after Committee discussion, the New York Bank ceased acting as agent for foreign official accounts in making Rp's with the market, and it requested an IRS determination of the tax consequences of Rp's made for foreign official accounts with various entities. The IRS subsequently ruled that income received by foreign central banks on Rp's made with SOMA, or with the Federal Reserve Bank of New York acting as a principal, was exempt from Federal income tax.

In light of that ruling, the Committee amended its authorization for domestic open market operations to authorize the New York Bank to arrange foreign official account Rp's with the Bank as a principal, and to make corresponding Rp's with the market, again with the Bank acting as principal. It was understood that such

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"back-to-back" arrangements would be undertaken under circumstances similar to those in which, before May 1977, the Bank had served as agent in arranging foreign official account Rp's with the market. While the authority for the New York Bank to make foreign official account Rp's with SOMA had been viewed as contained in paragraph 1(a) of the authorization, for the sake of clarity and completeness the Committee decided to include language explicitly authorizing such transactions in the new paragraph 4, along with the authority for the New York Bank to act as a principal in "back-to-back" Rp transactions.

Subsequent to this meeting, on February 15, 1978, Committee members voted to increase from $3 billion to $4 billion the limit of changes between Committee meetings in System Account holdings of U.S. Government and Federal agency securities specified in paragraph 1(a) of the authorization for domestic open market operations, effective immediately, for the period ending with the close of business on February 28, 1978.

> Votes for this action: Messrs. Burns, Volcker, Coldwell, Gardner, Guffey, Jackson, Mayo, Morris, Partee, and Roos. Votes against this action: None. Absent and not voting: Messrs. Lilly and Wallich.

This action was taken on recommendation of the System Account Manager. The Manager had advised that large-scale sales of Treasury securities since the January meeting—required mainly to counter the effect of seasonal declines in required reserves and currency in circulation—had reduced the leeway for further sales to $780 million, and that it appeared likely that the leeway would shortly be reduced further, to $300 million or less, as a result of the completion of an anticipated transaction with a foreign account. The Manager also noted that the current inter-meeting period had been lengthened by a change in the date of the next meeting from February 22 to February 28, and that projections suggested the need for further reserve-absorbing operations during the interval ending with the latter date.

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MEETING HELD ON FEBRUARY 28, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested that retail sales, industrial production, and housing starts had been adversely affected in January by unusually severe weather. It appeared, however, that there had been little change in the underlying economic situation.

In the fourth quarter of 1977, according to estimates of the Commerce Department, real output of goods and services had grown at an annual rate of 4.0 per cent, down from a rate of 5.1 per cent in the third quarter. However, final sales in real terms had expanded at a considerably faster pace than in the third quarter, and the rate of business inventory accumulation had slowed sharply. The rise in average prices, as measured by the fixed-weighted price index for gross domestic business product, had stepped up somewhat to an annual rate of 5.5 per cent in the fourth quarter from 5.0 per cent in the third.

Staff projections for the year 1978, like those prepared just before the Committee's meeting in mid-January, were based on assumptions that included reductions next fall in Federal income taxes. The projections continued to suggest that growth in real GNP would be sustained at a good pace throughout the year, although the over-all rate was somewhat below that anticipated earlier because of scaled-down projections for housing starts, auto sales, and total government purchases of goods and services. It was still expected that the rise in prices would remain relatively rapid and that the unemployment rate would decline moderately further over the year.

The latest projections suggested that growth in output would be less rapid in the first quarter of 1978 than had been expected earlier, in large part because of the adverse weather, but that the weather-related losses would be about made up later. Thus, it was expected

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that growth of consumer spending in real terms—which had been exceptionally rapid in the fourth quarter of 1977—would slow even more in the current quarter than had been anticipated and that expansion in business fixed investment and in residential construction also would fall short of earlier expectations. It was anticipated that growth in consumer spending would pick up in subsequent quarters—particularly in the fourth quarter, following the reduction in personal income taxes assumed to take effect on October 1. Business fixed investment was still projected to expand moderately over the remaining quarters of 1978, owing in part to stimulative modifications of the investment tax credit that were assumed to be retroactive to the beginning of the year. It was now anticipated, however, that residential construction activity would begin to edge down after midyear in response to the less favorable mortgage market conditions that now appeared to be developing.

In January industrial production declined 0.7 per cent—about as much as it had risen over the preceding 3 months—as the unusually severe weather caused widespread absenteeism, reduced workweeks, and disruptions to supplies. Moreover, auto manufacturers curtailed assemblies in an effort to control dealers' inventories, and the ongoing strike of mineworkers reduced production of coal further.

Nonfarm payroll employment continued to expand in January, and after adjustment for strikes, the gain was in line with the monthly-average rise during the second half of 1977. Increases were again sizable in manufacturing, trade, and services. Because of the unfavorable weather, however, construction employment declined, and the average workweek of production workers in nonfarm establishments fell sharply. The unemployment rate edged down to 6.3 per cent from 6.4 per cent in December.

The total value of retail sales declined about 3 per cent in January, according to the Census Bureau's advance estimate, after having expanded 5 per cent over the preceding 3 months. Sizable decreases in January were reported for almost all major categories of stores, at least in part because of the weather. Unit sales of new domestic autos declined 10 per cent to the lowest rate since late 1976, when supplies had been limited by a strike in the auto industry.

Private housing starts fell from an annual rate of 2.2 million units in December to 1.5 million units in January. Declines occurred in all

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regions of the country and were especially large in areas that had suffered major storms.

Manufacturers' new orders for nondefense capital goods fell 5 per cent in January after having risen about 9 per cent in December. However, the machinery component changed little in January after an increase of almost 8 per cent in December.

The index of average hourly earnings for private nonfarm production workers rose sharply in January, in part as a result of the increase in the Federal minimum wage from $2.30 to $2.65 per hour at the beginning of the year. Increases were especially large in trade and services, where adjustments in the minimum wage have tended to have more widespread effects.

The consumer price index for all urban consumers rose 0.8 per cent in January, almost twice the monthly-average increase in the second half of 1977. About two-thirds of the rise in January was attributed to price increases for foods and beverages and for housing, although prices advanced for all major categories of expenditures.

The increase in the wholesale price index for January—0.9 per cent—also was considerably more than the average rise during the second half of 1977. In January average prices both of farm products and foods and of industrial commodities advanced substantially.

In foreign exchange markets, after almost a month of calm, the dollar came under renewed downward pressure around mid-February, and its trade-weighted value against major foreign currencies declined about 1½ per cent during the second half of the month. Almost all major currencies rose against the dollar; the largest appreciations were registered by the Swiss franc and the German mark.

The U.S. foreign trade deficit increased appreciably in the fourth quarter of 1977. It appeared that the dock strike, which halted containerized shipments through Atlantic and Gulf Coast ports between October 1 and November 29, had depressed recorded exports more than recorded imports. After allowance for the apparent effects of the strike, the deficit was still slightly larger in the fourth quarter than in any of the first three quarters of the year. A deficit of $31 billion (international accounts basis) was estimated for 1977 as a whole, up from $9 billion in 1976.

At U.S. commercial banks, total credit expanded substantially in

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January, after having changed little in December. The January expansion, which was about in line with the average rate of growth during the fourth quarter of 1977, was attributable chiefly to a rebound in loan expansion. Growth in business loans and in loans to finance security holdings accelerated, and expansion in real estate and consumer loans apparently remained large. As in earlier months, banks financed a sizable part of the January increase in total loans by reducing their holdings of Treasury securities.

For nonfinancial businesses the January pick-up in loan growth was especially evident at smaller banks. Lending to nonfinancial businesses also rose somewhat at large banks during January, but it remained below the pace of late 1977, and these businesses managed a sizable net run-off of their outstanding commercial paper.

The narrowly defined money supply (*M*-1) expanded at an annual rate of 7¼ per cent in January, but data for early February suggested a decline from the January level. From the fourth quarter of 1976 to the fourth quarter of 1977, *M*-1 had grown 7.4 per cent, compared with 5.6 per cent in 1976 and 4.4 per cent in 1975.[1]

Growth in *M*-2 picked up in January to an annual rate of about 8¼ per cent—from 5¾ per cent in December—reflecting some strengthening in inflows to banks of time and savings deposits other than negotiable CD's. From the fourth quarter of 1976 to the fourth quarter of 1977, *M*-2 had grown 9.6 per cent, compared with 10.9 per cent in 1976 and 8.3 per cent in 1975.

Deposit growth at nonbank thrift institutions continued to slow in January, and *M*-3 expanded at an annual rate of 8 per cent—about the same as in December. Over the four quarters of 1977, *M*-3 had grown 11.6 per cent.

At its January meeting the Committee had decided that operations in the period immediately ahead should be directed toward maintaining about the prevailing money market conditions, provided that the monetary aggregates appeared to be growing at approximately the rates then expected. Specifically, the Committee sought to maintain the weekly-average Federal funds rate at about 6¾ per cent, so long

[1]At the time of this meeting, revision of the measures of the monetary aggregates to reflect, among other things, new benchmark data for deposits at nonmember banks had nearly been completed. It was reported at the meeting that, according to tentative estimates, the benchmark adjustment would raise the 1977 growth rates of *M*-1 and *M*-2 by 0.4 and 0.2 of a percentage point, respectively.

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as M-1 and M-2 appeared to be growing over the January–February period at annual rates within ranges of 2½ to 7½ per cent and 5 to 9 per cent, respectively. The members also agreed that if growth in the aggregates appeared to be approaching or moving beyond the limits of their specified ranges, the operational objective for the weekly-average Federal funds rate should be varied in an orderly fashion within a range of 6½ to 7 per cent. It was understood that very strong evidence of weakness in the monetary aggregates would be required before operations were directed toward reducing the Federal funds rate below the 6¾ per cent level.

Data that became available during the inter-meeting period suggested that growth in the monetary aggregates over the January–February period would be well within the specified ranges. The Manager of the System Open Market Account, therefore, continued to aim for a Federal funds rate of around 6¾ per cent. Over the 6-week inter-meeting period, the funds rate averaged 6.76 per cent, and weekly averages showed only minor deviations from that level.

Other short-term interest rates also changed little on balance over the inter-meeting period, even though short-term credit demands remained relatively strong. Longer-term interest rates showed mixed changes for the period. Yields on State and local government bonds declined somewhat further, whereas those on Treasury, Federal agency, and corporate securities edged higher.

Interest rates on mortgages rose during January, and some tightening of nonrate terms was reported as well. In order to cover mortgage takedowns in the face of weakening deposit flows, savings and loan associations increased their reliance on advances from the Federal home loan banks and other nondeposit sources of funds. This contrasted with the typical pattern in January of reductions in borrowings.

In the Committee's discussion of the economic situation and prospects, the members agreed that the expansion in activity was likely to continue throughout 1978. Most members thought that the staff's GNP projection was reasonable, but two or three members believed that growth in real GNP would fall somewhat short of the projected rate. Several members emphasized that the degree of uncertainty with regard to economic prospects and projections had been increasing.

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It was observed that at the current stage of this business expansion some deceleration in growth toward a rate that could be sustained for the longer term would be a desirable development. The comment was also made that some deceleration would be acceptable in light of the inflationary pressures in the economy and of recent developments in the foreign exchange markets.

Considerable concern was expressed that the rate of inflation might accelerate significantly as the year progressed. The comment was made that prospects for inflation had been inhibiting business decisions to invest in fixed capital, and it was suggested that an acceleration would adversely affect confidence and would dampen expansion in spending of other kinds. Such price behavior, it was noted, would pose difficult questions concerning the appropriate role of monetary policy.

Two members expressed the view that over the year the rate of unemployment was unlikely to decline very much. Another member believed that a realistic objective for the unemployment rate now was considerably higher than it used to be, perhaps as high as 5½ to 6 per cent.

One of the members who thought that the staff's projection for real GNP represented the most likely outcome nevertheless cited certain elements in the situation that could cause growth in output to fall short of the rates projected. He suggested, first, that the sizable decline in stock prices over the 6 weeks since the January meeting of the Committee indicated a continuing lack of confidence in prospects for business activity and profits, which could undermine the progress of the expansion. Like others, he agreed with the staff expectation that the economy would rebound from the effects of the severe weather and the coal strike. Nevertheless, he was concerned about the possibility that the loss of income because of those developments, even though temporary, could have enduring effects on consumer demands and on the general course of the economy. With respect to the U.S. foreign trade position, he did not see clear signs of the sort of expansion in activity abroad that would significantly reduce the trade deficit. Another member expressed agreement with this view of prospects for the trade deficit, while a third was somewhat more optimistic.

One of the members who believed that growth in real GNP would fall somewhat short of the rate projected by the staff also believed

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that the shortfall would be concentrated in the second half of the year. In his view, growth in output would be buoyed until midyear by a rebuilding of inventories as well as by the recovery from the effects of adverse weather and of the coal strike. However, he thought that problems would develop later in the year in residential construction and in some other sectors of the economy. Another member expressed the view that the staff expectations for housing starts, even though scaled down since the January meeting, were still too high.

Several members commented that they agreed with the scaled-down projections for both housing starts and auto sales, and some noted that for several months they had viewed the staff projections for those sectors as too high. It was observed that the outlook for those sectors was still relatively strong and that demands were likely to be supported by adequate supplies of credit and a willingness of consumers to assume debt. With respect to housing, the tendency of consumers to perceive homeownership as a good form of investment in a period of inflation also was mentioned as a factor likely to support demand.

It was observed in the discussion that the current business expansion—now about 3 years old—had developed some serious imbalances. U.S. merchandise imports were much too high relative to the behavior of the world economy. Business fixed investment was low in relation to growth in over-all production, and a few members expressed doubts of significant improvement during 1978. State and local governments were running a sizable surplus in their accounts, thereby draining purchasing power from the private sector. Outstanding consumer credit was high in relation to personal income. Wage increases were high in relation both to improvements in productivity and to the level of unemployment. Corporate profits were low in relation to personal income and to costs of production. Prices of common stock were low relative to corporate profits. And the state of general confidence appeared to be unduly low in relation to the actual performance of the economy.

One member expressed the view that confidence was being adversely affected by the large deficit in the Federal budget. He added that the budget estimates were based on the assumption of continued moderate growth in economic activity, and that if a recession should develop the deficit could swell to such a size that it

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might take many years to return to financial stability. Another member noted that under present fiscal policies the Federal deficit apparently would remain substantial even if a state of high employment were reached.

At this meeting the Committee reviewed its 12-month ranges for growth in the monetary aggregates. At its meeting in October 1977, the Committee had specified the following ranges for growth over the period from the third quarter of 1977 to the third quarter of 1978: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 8 to 10½ per cent. The associated range for growth in commercial bank credit was 7 to 10 per cent. The ranges being considered at this meeting were for the period from the fourth quarter of 1977 to the fourth quarter of 1978.

In the Committee's discussion of the 12-month ranges, all but one member expressed a preference for retaining the existing range for *M*-1. This member suggested that the upper limit for *M*-1 be reduced by ½ of a percentage point and the lower limit be raised by a corresponding amount, yielding a range of 4½ to 6 per cent. In the case of the broader aggregates, most members favored no change in the existing range for *M*-2 and a reduction of ½ of a percentage point in the range for *M*-3. Two members, however, preferred a reduction of ½ point in the range for *M*-2. One of them also suggested a reduction of 1 point, while the other advocated a reduction of either 1 or 1½ points, in the *M*-3 range.

The nearly unanimous preference of members for retaining the range of 4 to 6½ per cent for *M*-1 reflected several considerations. First, it was observed that any increase in the 6½ per cent upper limit of the range could strengthen inflationary expectations, which already appeared to be intensifying, and could accentuate the current weakness of the dollar in foreign exchange markets. Second, because the rate of growth of *M*-1 in 1977—about 7½ per cent—had significantly exceeded the upper limit of the Committee's earlier ranges, it was suggested that a decision now to reduce the range might lack credibility. Third, it was noted that if the actual rate of growth in *M*-1 during 1978 were to fall within a 4 to 6½ per cent range, that would represent a significant slowing from the 1977 rate. Indeed, one Committee member observed that if—as seemed likely—some slackening were under way in the processes of financial innovation that recently had been facilitating economies in

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transactions balances, an unchanged rate of growth in M-1 could be interpreted as involving an increase in monetary restraint. Finally, it was suggested that current uncertainties regarding the economic outlook militated against an adjustment in the M-1 range. While Committee members found these considerations persuasive, it was observed in the discussion that further gradual reductions in monetary growth ranges would be needed over time if growth rates consistent with general price stability were to be achieved.

Several Committee members noted that if during the coming year M-1 growth were to be constrained within a 4 to 6½ per cent range and nominal GNP were to expand as fast as economic forecasters were generally projecting, an appreciable increase in the velocity of M-1 would be required. While they believed that such an increase in velocity might develop, they indicated that they would be prepared to accept M-1 growth rates that were relatively high with respect to the range if the increase in velocity fell short of the required amount. Other members stressed the importance of constraining growth in M-1 within the range specified.

The member who preferred the growth range of 4½ to 6 per cent for M-1 based his recommendation on two considerations. First, by lowering the upper limit of the range, the Committee would be providing a further indication of its resolve to resist inflationary pressures and in the process perhaps help to provide some near-term support for the dollar. Second, by raising the lower limit of the range, the Committee might offer some reassurance to those who had expressed concern that the Federal Reserve might not be sufficiently alert to the possibility of a softening in the economy later this year. Other members of the Committee took exception to this proposal. In addition to the arguments offered against a reduction in the upper limit of the M-1 range already noted, it was suggested that a narrowing of the range would imply much greater certainty than in fact existed regarding the precise rate of monetary growth appropriate under present circumstances.

In considering the longer-run growth ranges for M-2 and M-3, members took note of the sharp reduction in flows of savings to depositary institutions that had occurred during recent months. It was suggested that part of the cutback in such inflows might reflect temporary factors, and that over coming months growth in large-denomination time deposits not subject to interest rate ceilings could

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well expand further, providing some offset to the continued slow growth expected in other deposits. It was noted that in the past the large-denomination deposit instruments of the types included in *M*-2 and *M*-3 had been issued primarily by banks, but it was suggested that in the present circumstances thrift institutions might begin to make greater use of such instruments as a source of funds.

In view of these considerations, most members of the Committee were inclined to retain the existing range for *M*-2 and to reduce the range for *M*-3 by only ½ of a percentage point. The members recognized that the attainment over the coming year of growth rates for *M*-2 and *M*-3 within such ranges might require an increase in the regulatory ceilings on deposit rates. The two members who suggested some reduction in the *M*-2 growth range and a reduction of more than ½ of a percentage point in the *M*-3 range believed that under present circumstances the ranges favored by the majority were higher than those appropriately associated with a 4 to 6½ per cent range for *M*-1.

At the conclusion of its discussion the Committee decided to retain the existing ranges for *M*-1 and *M*-2 and to reduce both the upper and lower limits of the range for *M*-3 by ½ of a percentage point. Thus, the new ranges, which applied to the period from the fourth quarter of 1977 to the fourth quarter of 1978, were 4 to 6½ per cent for *M*-1, 6½ to 9 per cent for *M*-2, and 7½ to 10 per cent for *M*-3. The associated range for growth in commercial bank credit remained 7 to 10 per cent. It was agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings. It was also understood that short-run factors might cause growth rates from month to month to fall outside the ranges contemplated for the year ahead.

> The Committee adopted the following ranges for rates of growth in monetary aggregates for the period from the fourth quarter of 1977 to the fourth quarter of 1978: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent.

> Votes for this action: Messrs. Burns, Volcker, Coldwell, Guffey, Jackson, Mayo, Morris, Partee, Roos, and Wallich. Votes against this action: None. Absent and not voting: Mr. Gardner.

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In the Committee's discussion of policy for the period immediately ahead, it was suggested that recent developments in the foreign exchange markets militated against any marked easing of money market conditions at this time, and that the uncertainties in the economic situation militated against any marked firming. All of the members favored directing initial open market operations during the coming inter-meeting period toward the objective of maintaining the Federal funds rate at about the prevailing level of 6¾ per cent, and a majority preferred to continue giving greater weight than usual to money market conditions in the conduct of operations until the next meeting. With respect to the range in which the funds rate might be varied if the February–March growth rates in the monetary aggregates appeared to be deviating markedly from expectations, most members advocated retention of the 6½ to 7 per cent range agreed upon at the January meeting. However, two members suggested narrowing the range to 6¾ to 7 per cent, and one proposed widening it to 6½ to 7¼ per cent.

The members did not differ greatly in their preferences for growth in the monetary aggregates for the February–March period; most favored ranges of 1 to 6 per cent for *M*-1 and 4½ to 8½ per cent for *M*-2. However, a few members were inclined to set the lower limit of the 2-month range for *M*-1 at zero, on the grounds that the acceptance of temporary weakness in the monetary aggregates that might develop from time to time would improve the chances of holding average growth over the coming year within the longer-run range agreed upon earlier in this meeting. One of these members also suggested that, given the relative volatility of *M*-1 and *M*-2, a range for *M*-2 that was 4 percentage points wide might best be associated with an *M*-1 range 6 points in width; accordingly, he favored a 2-month range of 0 to 6 per cent for *M*-1. Another member suggested that the ranges for both *M*-1 and *M*-2 be narrowed to 3 percentage points, in order to achieve prompter adjustment of the funds rate to growth rates in the aggregates that were unduly rapid or slow.

At the conclusion of the discussion the Committee decided that operations in the period immediately ahead should continue to be directed toward maintaining prevailing money market conditions, as represented by the current 6¾ per cent level of the Federal funds rate. However, the members agreed that if growth in the aggregates should appear to approach or move beyond the limits of their

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specified ranges, the operational objective for the weekly-average Federal funds rate should be varied in an orderly fashion within a range of 6½ to 7 per cent. For the annual rates of growth in *M*-1 and *M*-2 over the February–March period, the Committee specified ranges of 1 to 6 per cent and 4½ to 8½ per cent, respectively. It was understood that in assessing the behavior of the aggregates, the Manager should give approximately equal weight to the behavior of *M*-1 and *M*-2. The members also agreed that in the conduct of day-to-day operations, account should be taken of emerging financial market conditions, including the conditions in foreign exchange markets.

As customary, 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.

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

> The information reviewed at this meeting suggests that retail sales, industrial production, and housing starts were adversely affected in January by unusually severe weather. It appears, however, that there has been little change in the underlying economic situation. Employment increased further in January and the unemployment rate edged down from 6.4 to 6.3 per cent. Both the consumer price index and the wholesale price index rose substantially. The index of average hourly earnings advanced sharply, as higher minimum wages became effective at the beginning of the year.
>
> After a period of calm, the dollar came under renewed downward pressure around mid-February, and its trade-weighted value against major foreign currencies has declined about 1½ per cent. The Swiss franc and the German mark have registered the most pronounced appreciations against the dollar.
>
> *M*-1 expanded appreciably in January but declined somewhat in early February. Growth in *M*-2 picked up in January, reflecting some strengthening in inflows to banks of time and savings deposits other than negotiable CD's. Inflows to nonbank thrift institutions continued to slow. Market interest rates have changed little in recent weeks.
>
> In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster bank reserve and other financial conditions that will encourage continued economic expansion and

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help resist inflationary pressures, while contributing to a sustainable pattern of international transactions.

Growth of *M*-1, *M*-2, and *M*-3 within ranges of 4 to 6½ per cent, 6½ to 9 per cent, and 7½ to 10 per cent, respectively, from the fourth quarter of 1977 to the fourth quarter of 1978 appears to be consistent with these objectives. These ranges are subject to reconsideration at any time as conditions warrant.

At this time, the Committee seeks to maintain about the prevailing money market conditions during the period immediately ahead, provided that monetary aggregates appear to be growing at approximately the rates currently expected, which are believed to be on a path reasonably consistent with the longer-run ranges for monetary aggregates cited in the preceding paragraph. Specifically, the Committee seeks to maintain the weekly-average Federal funds rate at about the current level, so long as *M*-1 and *M*-2 appear to be growing over the February–March period at annual rates within ranges of 1 to 6 per cent and 4½ to 8½ per cent, respectively. If, giving approximately equal weight to *M*-1 and *M*-2, it appears that growth rates over the 2-month period are approaching or moving beyond the limits of the indicated ranges, the operational objective for the weekly-average Federal funds rate shall be modified in an orderly fashion within a range of 6½ to 7 per cent. In the conduct of day-to-day operations, account shall be taken of emerging financial market conditions, including the conditions in foreign exchange markets.

If it appears during the period before the next meeting that the operating constraints specified above are proving to be significantly inconsistent, the Manager is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

> Votes for this action: Messrs. Burns, Volcker, Coldwell, Guffey, Jackson, Mayo, Morris, Partee, Roos, and Wallich. Votes against this action: None. Absent and not voting: Mr. Gardner.

Subsequent to the meeting, on March 10, nearly final estimates indicated that in February *M*-1 had declined and *M*-2 had increased relatively little. For the February–March period staff projections suggested that the annual rate of growth in *M*-1 would be below the lower limit of the 1 to 6 per cent range specified by the Committee in the next-to-last paragraph of the domestic policy directive issued at the February meeting. Growth in *M*-2 for the 2-month period was projected to be close to the lower limit of the Committee's range of

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4½ to 8½ per cent for that aggregate. It appeared, however, that the weakness in the aggregates might reflect the prolongation of the coal strike and the severe winter weather and, therefore, might prove to be temporary.

During recent weeks the Federal funds rate had averaged about 6¾ per cent. In light of the behavior of the aggregates, the Manager would, under normal circumstances, have sought to reduce the funds rate within its specified range of 6½ to 7 per cent.

Against that background, and in view of recent developments in foreign exchange markets, Chairman Miller recommended at a telephone conference meeting on March 10 that the Manager be instructed to continue aiming at a Federal funds rate of 6¾ per cent for the time being.

On March 10, 1978, the Committee modified the domestic policy directive adopted at its meeting of February 28, 1978, to call for open market operations directed at maintaining the Federal funds rate at about the prevailing level of 6¾ per cent for the time being.

Votes for this action: Messrs. Miller, Volcker, Burns, Coldwell, Eastburn, Jackson, Wallich, Willes, Winn, and Kimbrel. Votes against this action: None. Absent and not voting: Messrs. Baughman, Gardner, and Partee. (Mr. Kimbrel voted as alternate for Mr. Baughman.)

2. Authorization for Foreign Currency Operations

Paragraph 1D of the Committee's authorization for foreign currency operations authorizes the Federal Reserve Bank of New York for the System Open Market Account to maintain an over-all open position in all foreign currencies not exceeding $1.0 billion, unless a larger position is expressly authorized by the Committee. On January 17, 1978, the Committee had authorized an open position of $1.75 billion.

At the meeting on February 28 the Committee authorized an open position of $2.0 billion. This action was taken in view of the scale of recent and potential Federal Reserve operations in the foreign exchange markets undertaken pursuant to the Committee's foreign currency directive.

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Votes for this action: Messrs. Burns, Volcker, Coldwell, Guffey, Jackson, Mayo, Morris, Partee, Roos, and Wallich. Votes against this action: None. Absent and not voting: Mr. Gardner.

On March 10, following the telephone conference held on that day, Committee members voted to approve a delegation of authority to Chairman Miller to negotiate an increase in the System's swap arrangement with the German Federal Bank of an amount up to $2 billion if he determined that the detailed arrangements were satisfactory. The Committee also voted to approve a concurrent amendment to paragraph 2 of the authorization for foreign currency operations to raise correspondingly the amount specified there for the swap arrangement with the German Federal Bank. The Chairman approved an increase of $2 billion on March 11. Accordingly, paragraph 2 of the authorization was amended, effective on that date, to 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	4,000
Bank of Italy	3,000
Bank of Japan	2,000
Bank of Mexico	360
Netherlands Bank	500
Bank of Norway	250
Bank of Sweden	300
Swiss National Bank	1,400

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Foreign bank	Amount of arrangement (millions of dollars equivalent)
Bank for International Settlements:	
Dollars against Swiss francs	600
Dollars against authorized European currencies other than Swiss francs	1,250

Votes for this action: Messrs. Miller, Volcker, Burns, Coldwell, Eastburn, Jackson, Partee, Wallich, Willes, Winn, and Kimbrel. Votes against this action: None. Absent and not voting: Messrs. Baughman and Gardner. (Mr. Kimbrel voted as alternate for Mr. Baughman.)

This action, which enlarged the System's swap network with 14 central banks and the Bank for International Settlements to $22.16 billion, was taken as part of the cooperative effort announced on March 13 by U.S. Secretary of the Treasury Blumenthal and Minister Matthoefer of the Federal Republic of Germany.

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MEETING HELD ON MARCH 21, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested that growth in real output of goods and services in the first quarter of 1978 had been adversely affected by unusually severe weather and by the lengthy strike in coal mining but that the underlying economic situation had changed little. It now appeared that growth in the current quarter had slowed from the pace in the fourth quarter of 1977, estimated by the Commerce Department to have been at an annual rate of 3.8 per cent. Staff projections suggested, however, that the shortfall in growth from the rate expected at the time of the February meeting would be about made up over the next quarter or two and that on the average over the four quarters of 1978 output would grow at a good pace.

The rise in average prices—as measured by the fixed-weighted price index for gross domestic business product—appeared to have stepped up in the first quarter from the annual rate of 5.4 per cent estimated for the fourth quarter of 1977, mainly because of large increases in prices of farm products and foods. It was expected that over the remaining quarters of 1978 the rate of increase in prices would be below that of the first quarter but would remain above that of the fourth quarter of 1977. It was also anticipated that the unemployment rate would move downward gradually over the year.

In the first quarter, according to staff estimates, expansion in final sales in real terms had slowed much more than growth in output, and the rate of business inventory accumulation had picked up from the sharply reduced pace in the final quarter of 1977. Consumer expenditures for goods in real terms—which had grown at a rapid pace in the fourth quarter—apparently declined in the first quarter, at least in part because of the severe weather. Moreover, construction activity—public as well as private—was adversely affected by the weather.

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The staff projections for the rest of 1978 suggested that consumer spending for goods in real terms would rebound in the second quarter and would continue to grow thereafter—particularly in the fourth quarter, following the reduction in personal income taxes assumed to take effect on October 1. It was anticipated that business fixed investment would expand moderately, owing in part to stimulative modifications of the investment tax credit that were assumed to be retroactive to the beginning of the year, but that residential construction would begin to edge down after midyear in response to the less favorable mortgage market conditions that appeared to be developing.

In February the index of industrial production rose 0.5 per cent, recovering more than half of the decline in January that was attributable in large part to the severe weather and to the coal strike. Unfavorable weather in some parts of the country continued to restrict output in February, and the ongoing strike held coal mining at a reduced level. Dwindling supplies of coal in some areas caused limitations on industrial use of electric power, but secondary effects of the strike appeared to have been small.

Nonfarm payroll employment increased considerably further between mid-January and mid-February. Employment in the service-producing industries continued to grow at about the average rate of the second half of 1977. In manufacturing the gain in employment was sizable for the third successive month, and the average workweek recovered part of the weather-induced decrease of January. As measured by the survey of households, total employment edged up in February while the labor force changed little, and the unemployment rate declined 0.2 of a percentage point to 6.1 per cent—1.5 percentage points below a year earlier and the lowest figure since late 1974.

According to the Census Bureau's advance estimate, total retail sales in February had recovered only a small portion of the substantial decline of the month before, at least in part because of continuing unfavorable weather. Unit sales of new automobiles—domestic and foreign combined—rose 5 per cent, retracing half of the January drop, and sales rose further in early March.

Private housing starts—which had declined from an annual rate of 2.20 million units in December to 1.55 million units in January—recovered only to 1.58 million units in February, as adverse

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weather apparently remained a significant inhibiting factor. Regionally, changes from January to February were quite diverse: Starts rose 43 per cent in the North Central States and 5 per cent in the West, while they declined 10 per cent in the South and 39 per cent in the Northeast.

The latest Department of Commerce survey of business spending plans, taken in late January and February, suggested that spending for plant and equipment would expand 10.9 per cent in 1978, whereas the survey taken in late November and December had suggested an increase of 10.1 per cent. However, the increment of 0.8 of a percentage point reflected a downward revision in the estimated level of spending for 1977. The expansion in 1977 now was indicated to have been 12.7 per cent, compared with the previous estimate of 13.7 per cent.

The index of average hourly earnings for private nonfarm production workers was unchanged in February, after having increased sharply in January when higher minimum wage rates became effective. Over the 2-month period the index rose at an annual rate of 7.6 per cent, about the same as the average rate of increase during 1977.

The wholesale price index for all commodities rose 1.1 per cent in February, compared with 0.9 per cent in January and an average rise of 0.6 per cent in the preceding 3 months. In February the increase in the index for prices of farm products and processed foods was more than twice as large as the average for the preceding 4 months. Average prices of industrial commodities continued to rise at a somewhat faster pace than in the latter part of 1977.

In foreign exchange markets the trade-weighted value of the dollar against major foreign currencies rose sharply on March 9 and 10 in anticipation of the conclusion of discussions between the governments of the United States and Germany. In a joint statement on March 13, 1978, U.S. and German authorities announced that continued forceful action would be taken to counter disorderly conditions in exchange markets and that close cooperation to that end would be maintained. Included in the cooperative effort were an increase of $2 billion in the System's swap arrangement with the German Federal Bank, an arrangement for the U.S. Treasury to sell SDR 600 million (approximately $740 million) to purchase German marks, and a willingness of the United States

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to draw on its reserve position in the IMF (automatically available in amounts up to approximately $5 billion) if and as necessary to acquire additional foreign exchange. The authorities also announced that developments during the first quarter of 1978 would be particularly important in determining the course of economic policies in Germany directed toward the objective of noninflationary growth and that in the United States high priority would be given to swift and resolute action to conserve energy and to develop new sources. Nevertheless, market participants apparently were disappointed by the announcements, and the value of the dollar receded to about its level in the last few days of February.

The U.S. foreign trade deficit remained very large in January. Interpretation of the data for recent months had been complicated by the 2-month dock strike that had ended on November 29 and by changes in the method for compiling the statistics, but it appeared that imports had continued to rise along with expansion in economic activity in the United States, while exports had shown no upward momentum.

At U.S. commercial banks growth in total credit during February was close to the sizable rate in January and about in line with the average for 1977. In February bank holdings of Treasury securities expanded substantially following a series of monthly declines. However, growth of total loans slowed, reflecting a sharp contraction in loans to finance holdings of securities. Growth in real estate and consumer loans apparently slowed a little, while expansion in business loans remained at about the average pace in 1977. Large banks significantly expanded their lending to manufacturing companies and to wholesale and retail trade concerns, but their lending to public utilities declined as the utilities drew down their inventories of coal.

For nonfinancial businesses the general pattern of short-term borrowing in February was little changed from that in January. Continued strong expansion in borrowings from banks was offset only in part by a further net run-off of outstanding commercial paper. Utilities accounted for much of the further decline in outstanding commercial paper issued by nonfinancial businesses.

At this meeting revised measures of the monetary aggregates incorporating the effects of new benchmark data for deposits at nonmember banks and revised seasonal factors were available to

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the Committee. These revised data, scheduled for publication on March 23, indicated that in February, *M*-1 had contracted at an annual rate of about 1 per cent. On the basis of the revised series, *M*-1 had grown at an annual rate of about 4¼ per cent during the first 2 months of 1978 and about 7¾ per cent during 1977. After revisions *M*-2 had grown at rates of about 4½ per cent in February, 6¾ per cent over the January–February period, and 9¼ per cent during 1977.

Inflows to commercial banks of the interest-bearing deposits included in *M*-2 were about maintained in February, but they consisted almost entirely of large-denomination time deposits (in amounts of $100,000 or more) exempt from Regulation Q ceilings on interest rates. Inflows of time and savings deposits subject to such ceilings slowed to a low rate, as yields on market instruments of comparable maturities remained above the ceiling rates throughout the month. To finance credit expansion in the face of the slowing in over-all inflows of deposits included in *M*-2, large banks issued a substantial volume of negotiable CD's and raised a sizable amount of funds from nondeposit sources.

Deposit growth at nonbank thrift institutions remained slow in February. Like the savings and smaller time accounts at commercial banks, deposits at the thrift institutions continued to be adversely affected by competition from market securities. Only the longest-term deposits at the thrift institutions provided effective yields above those available on competitive market securities.

At its February meeting the Committee had decided that operations in the period immediately ahead should be directed toward maintaining about the prevailing money market conditions, provided that the monetary aggregates appeared to be growing at approximately the rates then expected. Specifically, the Committee had sought to maintain the weekly-average Federal funds rate around 6¾ per cent, so long as *M*-1 and *M*-2 appeared to be growing over the February–March period at annual rates within ranges of 1 to 6 and 4½ to 8½ per cent, respectively. The members also agreed that if growth in the aggregates appeared to be approaching or moving beyond the limits of their specified ranges, the operational objective for the weekly-average Federal funds rate should be varied in an orderly fashion within a range of 6½ to 7 per cent. It was understood that in assessing the behavior of

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the aggregates, the Manager of the System Open Market Account should give approximately equal weight to the behavior of *M*-1 and *M*-2.

As the inter-meeting period progressed, it became evident that in February *M*-1 had contracted somewhat and *M*-2 had increased relatively little. Staff projections for the February–March period suggested that *M*-1 would grow at a rate below the lower limit of the range specified by the Committee and that *M*-2 would grow at a rate close to its lower limit. It also appeared, however, that the weakness in the aggregates might reflect the prolongation of the coal strike and the severe winter weather and thus would prove to be temporary. Against this background, and in view of recent developments in foreign exchange markets, the Committee voted on March 10 to instruct the Manager to continue aiming at a Federal funds rate of 6¾ per cent for the time being. For the full inter-meeting period, the funds rate averaged 6¾ per cent.

Market interest rates in general changed little over the inter-meeting period, reflecting the stability in the Federal funds rate and, apparently, more or less of a balance among developments affecting the public's expectations concerning monetary policy—namely, some slowing of the economic expansion and of growth in the monetary aggregates on one side, and some pick-up in the rate of increase in prices and continuing uncertainties in foreign exchange markets on the other. However, Treasury bill rates declined somewhat, in large part because of demands for bills from foreign central banks.

Borrowing by the U.S. Treasury remained relatively strong during the inter-meeting period. In addition to regular debt roll-overs, $3.3 billion of securities were auctioned to raise new money—$3.0 billion of short-term cash-management bills and $300 million of bills added to the regular weekly and monthly auctions. Incoming data on Treasury receipts and expenditures and on the cash balance implied, however, that Federal financing through the first quarter would be significantly smaller than had been suggested in late January. Borrowing by Federally sponsored credit agencies rose to $1.6 billion in February from the already expanded volume of $1.0 billion in January, in large part because of the midquarter financing of the Federal Home Loan Bank System.

Mortgage lending by private institutions apparently continued

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to slacken in February from the record pace of late 1977. At commercial banks the increase in mortgage loans was the smallest in about a year. In January, the latest month for which data were available, mortgage acquisitions by savings and loan associations slowed significantly. Also, mortgage lending commitments outstanding at these associations declined for the first time in 3 years.

In the Committee's discussion of the economic situation and prospects, the members agreed—as they had at other recent meetings—that the expansion in activity was likely to be sustained throughout 1978. The range of views with respect to the average rate of growth in real GNP over the four quarters of the year was not wide. Half of the members present believed that real output would grow at about the rate projected by the staff; of the remainder, some thought that output would grow somewhat less than projected, and some thought that it would grow somewhat more.

One of the members who thought that growth in real GNP would fall somewhat short of the rate projected by the staff believed that the shortfall would be concentrated in the second half of the year. In his view, the second-quarter rebound in growth from the weather-retarded pace in the first quarter might be greater than projected by the staff, and the magnitude of that rebound—in conjunction with some acceleration in the rate of inflation—might generate forces that would adversely affect construction activity and consumer spending in the second half.

Attention was drawn to the considerable improvement in the employment situation in recent months. The pace of growth in payroll employment over the past 6 months was regarded as indicative of near-term strength in the expansion of output. One member remarked that the unemployment rate had come close to the zone that he would characterize as reflecting full employment, suggesting that there was less time than he had anticipated earlier for growth in output to diminish toward a rate that could be sustained for the longer term. However, another member noted that the substantial decline in the unemployment rate in recent months—from 6.7 per cent in November to 6.1 per cent in February—reflected in part a sharp deceleration in growth of the civilian labor force. If, as he suspected, that deceleration proved to be an aberration in the statistics, the decline in the unemployment rate might well be reversed to some degree in coming months.

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The Committee members agreed that the rate of price advance was likely to remain relatively rapid in 1978, and they expressed a great deal of concern about this prospect. The comment was made that the pace of increase in prices appeared to be accelerating in this country while decelerating in European countries. Several members observed that inflation led to recession, and it was suggested that the greater the inflation, the worse the ensuing recession. For that reason, it was suggested, special emphasis should be given to the Committee's long-standing objective of helping to resist inflationary pressures while simultaneously encouraging continued economic expansion. It was noted that an effective program to reduce the rate of inflation had to extend beyond monetary policy.

At its meeting in February the Committee had agreed that from the fourth quarter of 1977 to the fourth quarter of 1978 average rates of growth in the monetary aggregates within the following ranges appeared to be consistent with broad economic aims: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for the rate of growth in commercial bank credit was 7 to 10 per cent. It had also been agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings.

In the Committee's discussion of policy for the period immediately ahead, it was suggested that an easing of money market conditions would be inappropriate in light of the outlook for prices, the recent behavior of the dollar in foreign exchange markets, and the likelihood that the demand for money would strengthen substantially again as growth of nominal GNP picked up. It was also suggested that a firming of money market conditions in the absence of actual evidence of excessive growth of the monetary aggregates would be premature, given the weakness of recent economic statistics, the still unsettled coal strike, and uncertainty about the strength of the prospective rebound in economic activity. However, a number of members favored some firming of money market conditions during the inter-meeting period with a view to keeping under control the anticipated pick-up in monetary growth, unless data for the first 2 weeks of the period suggested that monetary growth over the March–April period was likely to be significantly

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weaker than expected. There was also some sentiment for a slight easing if the incoming data suggested unexpected weakness in monetary growth.

These differences of emphasis notwithstanding, members of the Committee did not differ greatly in their preferences for operating specifications for the period immediately ahead, and all favored a return to basing decisions for open market operations between meeting dates primarily on the behavior of the monetary aggregates. In its previous five directives the Committee had called for giving greater weight than usual to money market conditions in conducting operations in the period until the next meeting.

For the annual rate of growth in *M*-1 over the March–April period most members favored ranges with an upper limit of 8 or 9 per cent and a lower limit of 4 or 4½ per cent; one member indicated a preference for a range of 2 to 7 per cent. For the growth rate in *M*-2 over the 2 months, the members' preferences for the upper limit ranged from 9 to 10 per cent and for the lower limit from 5 to 6 per cent.

All of the members favored directing open market operations during the coming inter-meeting period initially toward the objective of maintaining the Federal funds rate at about the prevailing level of 6¾ per cent. Views differed somewhat with respect to the degree of leeway for operations during the inter-meeting period in the event that growth in the aggregates appeared to be deviating significantly from the midpoints of the specified ranges. Some members favored retaining the present range of 6½ to 7 per cent for the funds rate but others preferred 6¾ to 7¼ per cent and one advocated 6¾ to 7 per cent. Some who wished to retain the 6½ to 7 per cent range suggested an understanding to the effect that operations would not be directed toward a rate below 6¾ per cent before the Committee had had an opportunity for further consultation.

At the conclusion of the discussion the Committee decided that growth in *M*-1 and *M*-2 over the March–April period at annual rates within ranges of 4 to 8 per cent and 5½ to 9 per cent, respectively, would be appropriate. It was understood that in assessing the behavior of these aggregates the Manager should continue to give approximately equal weight to the behavior of *M*-1 and *M*-2.

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It was the Committee's judgment that such growth rates were likely to be associated with a weekly-average Federal funds rate of about 6¾ per cent. The members agreed that if growth rates of the aggregates over the 2-month period appeared to be deviating significantly from the midpoints of the indicated ranges, the operational objective for the weekly-average Federal funds rate should be modified in an orderly fashion within a range of 6½ to 7 per cent. It was also agreed, however, that a reduction in the rate below 6¾ per cent would not be sought until the Committee had had an opportunity for further consultation.

As customary, 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. The members also agreed that in the conduct of day-to-day operations, account should be taken of emerging financial market conditions, including the conditions in foreign exchange 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 has been adversely affected in the current quarter by unusually severe weather and the lengthy strike in coal mining but that there has been little change in the underlying economic situation. In February industrial production recovered much of the decline of the preceding month, and nonfarm payroll employment increased considerably further. The unemployment rate declined from 6.3 to 6.1 per cent. Retail sales picked up somewhat from the sharply reduced level of January. The pace of the rise in prices stepped up in February, reflecting large increases in farm products and processed foods. The index of average hourly earnings was unchanged, after having advanced sharply in January when higher minimum wages became effective.
>
> The trade-weighted value of the dollar against major foreign currencies rose sharply in anticipation of the U.S.-German announcements on March 13. Subsequently, the dollar declined to about the level at the end of February. The U.S. trade statistics reported for January showed a continuing large deficit.
>
> *M*-1 declined and *M*-2 increased relatively little in February, apparently in part because of the economic effects of the coal strike

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and the severe weather. Inflows to banks of the interest-bearing deposits included in *M*-2 were about maintained, but the inflows were almost entirely into large-denomination time deposits exempt from ceilings on interest rates. Inflows to nonbank thrift institutions remained slow. Market interest rates have changed little in recent weeks.

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

At its meeting on February 28, 1978, the Committee agreed that growth of *M*-1, *M*-2, and *M*-3 within ranges of 4 to 6½ per cent, 6½ to 9 per cent, and 7½ to 10 per cent, respectively, from the fourth quarter of 1977 to the fourth quarter of 1978 appears to be consistent with these objectives. These ranges are subject to reconsideration at any time as conditions warrant.

The Committee seeks to encourage near-term rates of growth in *M*-1 and *M*-2 on a path believed to be reasonably consistent with the longer-run ranges for monetary aggregates cited in the preceding paragraph. Specifically, at present, it expects the annual growth rates over the March–April period to be within ranges of 4 to 8 per cent for *M*-1 and 5½ to 9 per cent for *M*-2. In the judgment of the Committee such growth rates are likely to be associated with a weekly-average Federal funds rate of about 6¾ per cent. If, giving approximately equal weight to *M*-1 and *M*-2, it appears that growth rates over the 2-month period will deviate significantly from the midpoints of the indicated ranges, the operational objective for the Federal funds rate shall be modified in an orderly fashion within a range of 6½ to 7 per cent. In the conduct of day-to-day operations, account shall be taken of emerging financial market conditions, including the conditions in foreign exchange markets.

If it appears during the period before the next meeting that the operating constraints specified above are proving to be significantly inconsistent, the Manager is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Jackson, Partee, Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Messrs. Burns and Gardner.

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2. Authorization for Foreign Currency Operations

Paragraph 1D of the Committee's authorization for foreign currency operations authorizes the Federal Reserve Bank of New York, for the System Open Market Account, to maintain an over-all open position in all foreign currencies not to exceed $1.0 billion unless a larger position is expressly authorized by the Committee. On February 28, 1978, the Committee had authorized an open position of $2.0 billion.

At this meeting the Committee authorized an open position of $2.25 billion. This action was taken in view of the scale of recent and potential Federal Reserve operations in the foreign exchange markets undertaken pursuant to the Committee's foreign currency directive.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Jackson, Partee, Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Messrs. Burns and Gardner.

3. Procedural Instructions with Respect to Operations Under the Foreign Currency Documents

Paragraph 1B of the procedural instructions with respect to the conduct of operations under the Committee's foreign currency authorization and directive instructed the Manager to clear with the Foreign Currency Subcommittee or, under certain circumstances, with the Chairman of the Committee any transactions that would result in gross transactions (excluding swap drawings and repayments) in a single foreign currency exceeding $100 million on any day or $300 million since the most recent regular meeting of the Committee.

At this meeting the Committee amended paragraph 1B to raise the levels of gross transactions beyond which clearance is required to $200 million on any day and to $500 million since the most recent regular meeting, and to clarify its intention that the measure of gross transactions used for this purpose should exclude not only swap drawings and repayments but also purchases and sales of currencies incidental to such repayments. This action was taken

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to relax the dollar limits on gross transactions, which had on occasion hampered ongoing operations, and to remove an ambiguity in the language.

As amended, paragraph 1B read as follows:

1. The Manager shall clear with the Subcommittee (or with the Chairman, if the Chairman believes that consultation with the Subcommittee is not feasible in the time available):

* * * * *

B. Any transaction which would result in gross transactions (excluding swap drawings and repayments, and purchases and sales of any currencies incidental to such repayments), in a single foreign currency exceeding $200 million on any day or $500 million since the most recent regular meeting of the Committee.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Jackson, Partee, Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Messrs. Burns and Gardner.

4. Review of Continuing Authorizations

This being the first regular 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, 1978, the Committee followed its customary practice of reviewing all of its continuing authorizations and directives. The Committee reaffirmed the authorization for domestic open market operations, the authorization for foreign currency operations, and the foreign currency directive, in the forms in which they were presently outstanding. The Committee also reaffirmed the procedural instructions with respect to operations under the foreign currency documents not affected by the action described in the preceding section.

Votes for these actions: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Jackson, Partee, Wallich, Willes, and Winn. Votes against these actions: None. Absent and not voting: Messrs. Burns and Gardner.

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In reviewing the authorization for domestic open market operations, the Committee took special note of paragraph 3, which authorizes the Reserve Banks to engage in the 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.

5. Agreement to "Warehouse" Currencies for the Exchange Stabilization Fund (ESF)

At its meeting of January 17–18, 1977, the Committee had agreed to a suggestion by the Treasury that the Federal Reserve undertake to "warehouse" foreign currencies held by the ESF—that is, to make spot purchases of foreign currencies from the ESF and simultaneously to make forward sales of the same currencies to the ESF—if that should prove necessary to enable the ESF to deal with potential liquidity strains. Specifically, the Committee had agreed that the Federal Reserve would be prepared, if requested by the Treasury, to warehouse up to $1½ billion of eligible foreign currencies, of which half would be for periods of up to 12 months and half for periods of up to 6 months. It was noted that the agreement to warehouse currencies would be subject to review by the Committee at its organizational meeting each March in connection with the regular review of all outstanding authorizations. At this meeting the Committee reaffirmed the agreement.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Eastburn, Jackson, Partee, Wallich, Willes, and Winn. Vote against this action: Mr. Coldwell. Absent and not voting: Messrs. Burns and Gardner.

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MEETING HELD ON APRIL 18, 1978

Domestic Policy Directive

The information reviewed at this meeting suggested that growth in real output of goods and services had been small in the first quarter of 1978, owing in part to the unusually severe weather and the lengthy strike in coal mining, but that economic activity was rebounding in the latter part of the period. Staff projections suggested that the first-quarter shortfall in growth from the rate expected earlier would be about made up in the current quarter and that over the year ahead output would grow at a moderate pace.

The rise in average prices—as measured by the fixed-weighted price index for gross domestic business product—appeared to have stepped up considerably in the first quarter from the annual rate of 5.4 per cent estimated for the fourth quarter of 1977, reflecting for the most part reduced supplies of meats and increases in payroll taxes and in minimum wages at the beginning of the year. The staff's latest projections of the rise in prices, which were somewhat higher than those made 4 weeks earlier, suggested that the rate over the year ahead would remain well above that in the fourth quarter of 1977. It was also anticipated that the unemployment rate would move downward gradually over the period.

In the first quarter, according to the latest staff estimates, growth in real GNP had slowed much more than had been anticipated a month earlier—mainly because an expected improvement in net exports of goods and services apparently had failed to develop but also because adverse weather had impeded residential, business, and public construction more than had been thought previously. It was still estimated that consumer expenditures for goods in real terms, after having grown rapidly in the fourth quarter of 1977, had declined in the first quarter of 1978. Altogether, final sales

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in real terms had slowed much more than growth in output, and the rate of business inventory accumulation had picked up from the sharply reduced pace in the preceding quarter.

The staff projections suggested that consumer spending for goods in real terms and both private and public construction would rebound in the second quarter, that the rate of inventory accumulation would increase somewhat further, and that net exports of goods and services would improve moderately. It was anticipated that in the remaining two quarters of the year real consumption expenditures and real business fixed investment would expand moderately but that the foreign trade position would change little and that residential construction would begin to edge down in response to the less favorable mortgage market conditions that had been developing recently.

In March the index of industrial production increased 1.4 per cent, following a rise of 0.3 per cent in February and a decline of 0.8 per cent in January. Thus, the index for March was about 1 per cent above that for December, although the average for the first quarter of 1978 was about the same as that for the fourth quarter of 1977.

Nonfarm payroll employment rose sharply further in March, and gains were widespread among industry groups. In manufacturing, the increase was sizable for the fourth successive month, and the average workweek recovered to the November–December level. The unemployment rate edged up 0.1 of a percentage point to 6.2 per cent, as the civilian labor force expanded substantially after having been unchanged in February.

Total retail sales in February, according to revised estimates, had recovered much more of the January drop than had been reported earlier, and they expanded substantially further in March. Nevertheless, total sales were about the same in the first quarter as in the fourth quarter of 1977. Unit sales of new automobiles, domestic and foreign combined, rose sharply in March, carrying the first-quarter total up to the level of each of the two preceding quarters.

The index of average hourly earnings for private nonfarm production workers rose at an annual rate of about 9 per cent from December to March, compared with a rate of about 8 per cent over the preceding 3 months. The acceleration in the first quarter

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resulted in large part from the increase in minimum wages at the beginning of the year.

The wholesale price index for all commodities rose 1 per cent in March, the same as in February, reflecting further large increases in prices of farm products and foods. In February the consumer price index for all urban consumers had continued to advance at a faster pace than in the second half of 1977, owing to large increases in retail prices of foods and in rates for natural gas and electricity.

The U.S. foreign trade deficit increased significantly in February, as the value of imports rose sharply while the value of exports changed little. After the trade statistics had been announced on March 31, the trade-weighted value of the dollar declined nearly 1 per cent. In the week preceding this meeting, however, the dollar recovered to about the same level as that 4 weeks earlier.

The rate of expansion in total credit at U.S. commercial banks during March was close to that in February. Growth in loans, particularly business loans and real estate loans, accelerated. At the same time banks reduced their holdings of Treasury securities—resuming the pattern of net liquidation of investments that had been interrupted by substantial acquisitions of Treasury securities in February. Over the first quarter, total bank credit grew at an annual rate of about 10½ per cent, compared with 8½ per cent in the second half of 1977. Business loans (net of bankers acceptances) increased in March at an annual rate of 23 per cent, approaching the rapid pace recorded in the first half of 1974.

Outstanding commercial paper of nonfinancial businesses rose sharply in March, almost offsetting the sizable decreases in the preceding 2 months. Public utilities accounted in large part for both the rise in March and the earlier declines.

The narrowly defined money supply (*M*-1), which had declined in February, rose moderately in March, and in the first quarter—on a quarterly-average basis—it expanded at an annual rate of 5 per cent. From the first quarter of 1977 to the first quarter of 1978, *M*-1 grew about 7¼ per cent.

Inflows to banks of time and savings deposits other than negotiable CD's and inflows of deposits to nonbank thrift institutions remained slow in March, and growth rates for *M*-2 and *M*-3 were near the reduced rates in February. From the first quarter of 1977

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to the first quarter of 1978, *M*-2 and *M*-3 grew about 8½ and 10½ per cent, respectively.

At its March meeting the Committee had decided that during the March–April period growth in *M*-1 and *M*-2 within ranges of 4 to 8 and 5½ to 9 per cent, respectively, would be appropriate. It had judged that these growth rates were likely to be associated with a weekly-average Federal funds rate of about 6¾ per cent. The Committee had agreed that if growth rates in the aggregates over the 2-month period appeared to be deviating significantly from the midpoints of the indicated ranges, the operational objective for the weekly-average Federal funds rate should be modified in an orderly fashion within a range of 6½ to 7 per cent. The members also agreed, however, that a reduction in the rate below 6¾ per cent would not be sought until the Committee had had an opportunity for further consultation.

Projections made on the basis of data that had become available in the days immediately following the March meeting suggested that over the March–April period both *M*-1 and *M*-2 would grow at rates that were high within their specified ranges. The figures were regarded as especially tentative, however, since the strength was concentrated in the part of the period for which growth rates were projected. Consequently, the Manager of the System Open Market Account continued to seek a Federal funds rate of about 6¾ per cent. Data becoming available later in the inter-meeting period suggested more moderate rates of growth in the monetary aggregates, and the weekly-average funds rate remained close to 6¾ per cent throughout the period.

Market interest rates in general were subjected to upward pressure during much of the inter-meeting period, apparently because of investor concerns about the deterioration in the balance of U.S. foreign trade, the acceleration of the rise in prices, and the possibility of a surge in monetary growth in April. Most interest rates—especially longer-term rates—increased somewhat on balance over the period. Recently, however, Treasury bill rates had declined, and on the day before this meeting the 3-month bill rate was somewhat below its level just before the March meeting.

Treasury borrowing remained relatively strong during the inter-meeting period. In addition to issuing $6.0 billion of short-term, cash-management bills, the Treasury raised $300 million of new

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money in its regular weekly bill auctions and more than $3 billion through sales of 2- and 5-year notes. The Treasury also announced that on April 19, the day after this meeting, it would auction about $2.2 billion of 2-year notes to refund the same amount of publicly held notes maturing on April 30. The Treasury was expected to announce the terms of its mid-May refunding on April 26.

Mortgage lending in March apparently picked up somewhat from the reduced pace of January and February, but in the first quarter as a whole the volume was below the peak reached in the fourth quarter of 1977. In February, the latest month for which data were available, mortgage commitment activity at nonbank thrift institutions weakened further as these institutions continued to experience reduced inflows of deposits. Average interest rates on new commitments for conventional home loans at savings and loan associations edged up further during the inter-meeting period to a level about 35 basis points above that in late December. Yields in the secondary markets for mortgages also continued upward, rising to a level 40 to 50 basis points higher than in late December.

In the Committee's discussion of the economic situation, most members indicated little or no disagreement with the staff projection of moderate growth in real GNP over the year ahead, following the current rebound from the slow pace estimated for the first quarter. However, several members expressed the view that growth would be stronger in the current quarter than had been projected. Of these members, two believed that growth would then slow significantly in the second half of 1978.

Concerning the current rebound in growth, one member thought that it could be considerably greater than had been projected, owing to the dynamics of the process of income creation, and that such additional strength at the current stage of the business expansion could have adverse consequences. In any case, he saw grounds for concern in the way the economic situation might be developing.

One of the members who thought that the near-term strength in activity would give way to very slow growth in the second half of the year believed that residential construction, and perhaps also consumer spending, would be weaker in that period than had been projected. At the same time, he expected the country's foreign trade position to be stronger than had been projected. The second member who anticipated a marked slowing of growth later in the

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year felt that such a development would not be undesirable; he shared the opinion of another member that the unemployment rate was approaching the level where unused labor resources of many kinds might be limited. A third member expressed disagreement with that view of the unemployment situation. He suggested that it was not widely held and that any tendency for the unemployment rate to stabilize near its current level was likely to lead to some sort of stimulative governmental policy measures.

One member commented that output could continue to grow at a moderate pace without generating unusual pressures because some slack still existed in the utilization of industrial capacity and of the labor force. With respect to the latter, he pointed out that a large number of persons in public service jobs created under Federal programs were available for other types of employment, even though they were not counted among the unemployed. He also noted that business fixed investment in real terms had not yet recovered to its previous high and that the inventory situation was favorable. Nevertheless, in his view, growth in over-all output might be held down if inflationary expectations led to increases in interest rates—thereby adversely affecting residential construction and business fixed investment—and if the international economic situation proved to have an adverse influence on the domestic economy.

Committee members in general were deeply concerned about price prospects. Views were expressed to the effect that people in both the public and private sectors appeared as yet not to be making the sorts of difficult decisions required to reduce the pace of the rise in prices; that expectations of a high rate of inflation seemed to be growing and, as a result, actions of businessmen and consumers might tend to make their expectations self-fulfilling; that the rate of increase in wage rates might well accelerate if prices rose at the projected rate or if the labor contract recently negotiated in the coal industry were viewed as a pattern-setter; and that individual efforts to profit from inflation could lead to some speculative activity. The comment was also made that in the past several weeks the public's attention increasingly had been focused on the problem of inflation.

It was noted that the current rise in prices was more rapid than the rate that had been projected early in 1977. Questions were

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raised as to whether the recent acceleration of the rise was attributable primarily to special factors affecting foods and to the depreciation of the dollar in foreign exchange markets or whether it reflected more general influences, such as the pressures that frequently emerge in the latter phase of a business upswing or the effect of the rate of monetary growth during 1977. As at other recent meetings, the observation was made that monetary policy could be no more than one element in an effective program to fight inflation.

At this meeting the Committee reviewed its 12-month ranges for growth in the monetary aggregates. At its meeting in February 1978 the Committee had specified the following ranges for growth over the period from the fourth quarter of 1977 to the fourth quarter of 1978: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for growth in commercial bank credit was 7 to 10 per cent. The ranges being considered at this meeting were for the period from the first quarter of 1978 to the first quarter of 1979.

In the Committee's discussion of the appropriate ranges, the members were unanimous in favoring retention of the existing range for *M*-1. It was suggested that it might be desirable, for technical reasons, to reduce the ranges for *M*-2 and *M*-3—or the range for *M*-3 alone. However, that suggestion had little support; most of the members advocated retaining the existing ranges for all of these aggregates.

In recognition of the Committee's continuing objective to move gradually toward longer-run rates of monetary expansion consistent with general price stability, several members expressed the view that it was more important at this time to pursue measures that would hold monetary growth within the existing ranges than it was to make further reductions in the ranges themselves. In this connection, it was pointed out that since the fourth quarter of 1976 the rate of growth of *M*-1 had exceeded the 6½ per cent upper limit of the longer-run range in every quarter except the one just ended. In view of that record, it was suggested, the Committee could most effectively demonstrate its adherence to its longer-run objective and lend support to the administration's anti-inflation program by succeeding in holding monetary growth within the existing range.

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The point was stressed that retention of the existing ranges for the year ahead should be interpreted as constituting a tighter monetary posture than had been contemplated when the ranges were adopted in February 1978. It was observed that since then the prospective rate of inflation had increased—which implied, other things being equal, that nominal GNP and the associated transactions demand for money would expand more rapidly than had been anticipated at that time. It was recognized that such an implication could form the basis of an argument for raising the 12-month range for *M*-1, or at least its upper limit. It was suggested, however, that the ultimate conclusion of such an argument was a monetary policy that always accommodated the existing rate of inflation and that could be expected to lead to still higher rates of inflation and still more rapid monetary growth.

In the discussion of the longer-run ranges for *M*-2 and *M*-3, it was observed that inflows of time and savings deposits to commercial banks and to nonbank thrift institutions might continue to be impeded by the margin by which market interest rates exceeded the Regulation Q ceiling rates on deposits other than large-denomination CD's. It was suggested, therefore, that a reduction in the range for *M*-3, and perhaps in the ranges for both *M*-2 and *M*-3, might be viewed as consistent with a retention of the existing range for *M*-1. In opposition to this view, it was noted that commercial banks would probably continue to expand substantially the outstanding volume of large-denomination CD's not subject to rate ceilings and that the nonbank thrift institutions also were becoming more aggressive in selling such instruments. It was recognized, moreover, that the probability of attaining growth rates for *M*-2 and *M*-3 within the existing ranges over the coming year could be influenced by an increase in the Regulation Q ceilings on deposit rates.

At the conclusion of its discussion the Committee decided to retain the existing ranges for the monetary aggregates. Thus, the ranges for the period from the first quarter of 1978 to the first quarter of 1979 were 4 to 6½ per cent for *M*-1, 6½ to 9 per cent for *M*-2, and 7½ to 10 per cent for *M*-3. The associated range for growth in commercial bank credit was set at 7½ to 10½ per cent. It was agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would

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be subject to review and modification at subsequent meetings. It was also understood that short-run factors might cause growth rates from month to month to fall outside the ranges anticipated for the year ahead.

> The Committee adopted the following ranges for rates of growth in monetary aggregates for the period from the first quarter of 1978 to the first quarter of 1979: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for bank credit is 7½ to 10½ per cent.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Gardner, Jackson, Partee, Wallich, Willes, and Winn. Votes against this action: None.

In considering the language of the domestic policy directive to be adopted at this meeting, Committee members agreed that in the statement of the Committee's general policy stance in the fourth paragraph more weight should be given to the objective of resisting inflationary pressures by citing that objective first. As revised, the statement said that "it is the policy of the Federal Open Market Committee to foster bank reserve and other financial conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions."

In the discussion of policy for the period immediately ahead, members of the Committee took account of the likelihood that the demand for money would expand significantly in association with the current rebound in economic activity and of the early indications that *M*-1 was growing rapidly in April. All of the members agreed that operations designed to achieve firmer money market conditions needed to be undertaken promptly if *M*-1 growth were to be held to a path reasonably consistent with the Committee's longer-run range. At the same time the members felt that, pending additional evidence on the pace of monetary expansion, the degree of firming sought should be modest.

Although members of the Committee were in general agreement on objectives for the period immediately ahead, they differed somewhat in their preferences for operating specifications. For the annual rate of growth in *M*-1 over the April–May period, most

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members favored ranges of 4 to 8 per cent or 5 to 9 per cent, but a few expressed a preference for 5½ to 9½ per cent. Two members advocated wider ranges because of the month-to-month volatility of the measure of monetary growth; one suggested a range of 4 to 9 per cent, and the other a range of 2 to 8 per cent. For *M*-2 most members advocated ranges of 5½ to 9½ per cent or 6 to 10 per cent, but there was some sentiment for slightly lower ranges.

All of the members favored directing open market operations during the coming inter-meeting period initially toward a Federal funds rate slightly above the current level of 6¾ per cent. Views differed somewhat with respect to the degree of leeway for operations during the inter-meeting period in the event that growth in the monetary aggregates appeared to be deviating significantly from the midpoints of the specified ranges. Most members favored a range for the weekly-average Federal funds rate extending from 6¾ to 7¼ or to 7½ per cent, but there was some sentiment for a lower limit of 6½ per cent. Those advocating a lower limit of 6¾ per cent suggested that any decline in the weekly-average funds rate from the current level would be inappropriate, particularly in view of recent developments in foreign exchange markets. At the same time several members suggested that if the Committee allowed for an increase in the funds rate of as much as ¾ of a percentage point over the inter-meeting period by setting the upper limit of the range at 7½ per cent, it should also reach an understanding that operations would not be directed toward achieving a rate above 7¼ per cent before the Committee had had an opportunity for further consultation.

At the conclusion of the discussion the Committee decided that growth in *M*-1 and *M*-2 over the April–May period at annual rates within ranges of 4 to 8½ per cent and 5½ to 9½ per cent, respectively, would be appropriate. It was understood that in assessing the behavior of these aggregates the Manager should continue to give approximately equal weight to the behavior of *M*-1 and *M*-2.

In the judgment of the Committee such growth rates were likely to be associated with a weekly-average Federal funds rate slightly above the current level of 6¾ per cent. The members agreed that if growth rates of the aggregates over the 2-month period appeared

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to be deviating significantly from the midpoints of the indicated ranges, the operational objective for the weekly-average Federal funds rate should be modified in an orderly fashion within a range of 6¾ to 7½ per cent. It was also agreed, however, that an increase in the rate above 7¼ per cent would not be sought until the Committee had had an opportunity for further consultation.

As customary, 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. The members also agreed that in the conduct of day-to-day operations, account should be taken of emerging financial market conditions, including the conditions in foreign exchange 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 was small in the first quarter, owing in part to the unusually severe weather and the lengthy strike in coal mining, but that economic activity was rebounding in the latter part of the period. In March industrial production and nonfarm payroll employment increased sharply further. The unemployment rate edged up from 6.1 to 6.2 per cent, as the civilian labor force expanded substantially. Retail sales recovered much more in February than had been reported earlier, and sales rose considerably further in March. The pace of the rise in wholesale prices remained rapid, reflecting further large increases in farm products and processed foods. The index of average hourly earnings accelerated in the first quarter, largely because of the increase in minimum wages at the beginning of the year.
>
> The trade-weighted value of the dollar against major foreign currencies declined sharply after the March 31 announcement of a very large increase in the U.S. foreign trade deficit for February. But over the past week the dollar has recovered to about its level of 4 weeks ago.
>
> *M*-1, which had declined in February, rose moderately in March. Inflows to banks of time and savings deposits other than negotiable CD's and inflows to nonbank thrift institutions remained slow. Most market interest rates, especially longer-term rates, have increased somewhat on balance in recent weeks.
>
> In light of the foregoing developments, it is the policy of the

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Federal Open Market Committee to foster bank reserve and other financial conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions.

Growth of *M*-1, *M*-2, and *M*-3 within ranges of 4 to 6½ per cent, 6½ to 9 per cent, and 7½ to 10 per cent, respectively, from the first quarter of 1978 to the first quarter of 1979 appears to be consistent with these objectives. The associated range for bank credit is 7½ to 10½ per cent. These ranges are subject to reconsideration at any time as conditions warrant.

The Committee seeks to encourage near-term rates of growth in *M*-1 and *M*-2 on a path believed to be reasonably consistent with the longer-run ranges for monetary aggregates cited in the preceding paragraph. Specifically, at present, it expects the annual growth rates over the April–May period to be within ranges of 4 to 8½ per cent for *M*-1 and 5½ to 9½ per cent for *M*-2. In the judgment of the Committee such growth rates are likely to be associated with a weekly-average Federal funds rate slightly above the current level. If, giving approximately equal weight to *M*-1 and *M*-2, it appears that growth rates over the 2-month period will deviate significantly from the midpoints of the indicated ranges, the operational objective for the Federal funds rate shall be modified in an orderly fashion within a range of 6¾ to 7½ per cent. In the conduct of day-to-day operations, account shall be taken of emerging financial market conditions, including the conditions in foreign exchange markets.

If it appears during the period before the next meeting that the operating constraints specified above are proving to be significantly inconsistent, the Manager is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Gardner, Jackson, Partee, Wallich, Willes, and Winn. Votes against this action: None.

Subsequent to the meeting, on May 5, a telephone conference meeting was held to consult about System open market operations, pursuant to the decision at the April meeting that an increase in the Federal funds rate above 7¼ per cent, within the specified range of 6¾ to 7½ per cent, would not be sought until the Committee had had an opportunity for further consultation.

The latest estimates had indicated that *M*-1 had grown at a very

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rapid pace in April. For the April–May period staff projections had suggested that the annual rate of growth in *M*-1 would be well above the upper limit of the range of 4 to 8½ per cent specified by the Committee in the next-to-last paragraph of the domestic policy directive issued at the meeting of April 18. Growth in *M*-2 for the 2-month period had been projected to be at about the upper limit of the Committee's range of 5½ to 9½ per cent for that aggregate. During the preceding week the Federal funds rate had averaged about 7¼ per cent, ½ of a percentage point above the level prevailing at the time of the April meeting.

It was reported during the telephone conference that the Commerce Department's preliminary estimates indicated that real GNP had declined at an annual rate of 0.6 per cent in the first quarter, a somewhat weaker performance than had been anticipated at the time of the April meeting, but that real GNP appeared to be rising more rapidly in the second quarter than the staff had projected at that time. The behavior of GNP in both quarters was importantly affected by temporary influences.

The acceleration of growth of nominal GNP in the current quarter from the reduced pace in the first quarter appeared to be the main factor explaining the sharp acceleration of monetary growth in April. Other transitory forces—specifically, mobilization of cash by the public to make unusually large payments of Federal income taxes not withheld, somewhat slower processing of tax returns, and the upsurge in the volume of trading on the stock exchanges—might also have contributed to the April rate of monetary growth.

In its discussion the Committee agreed that, while the firming in money market conditions that had been accomplished since the meeting of April 18 had clearly been appropriate, there was some question as to whether further firming at this point would be desirable. Specifically, the Committee concluded that it would be appropriate to await some further evidence on the economic outlook and some indication of the extent to which the April surge in *M*-1 would subside.

At the conclusion of the discussion the Committee directed the Manager, until further instructed, to seek to maintain the weekly-average Federal funds rate at about 7¼ per cent, with any deviations tending to be in the direction of higher rather than lower funds rates.

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On May 5, 1978, the Committee modified the domestic policy directive adopted at its meeting of April 18, 1978, to direct the Desk, until further instructed, to seek to maintain the weekly-average Federal funds rate at about the prevailing level of 7¼ per cent, with any deviations tending to be in the direction of higher rather than lower funds rates.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Gardner, Jackson, Partee, Wallich, and Winn. Votes against this action: Messrs. Black and Willes. Absent and not voting: Messrs. Coldwell and Eastburn. (Mr. Black voted as alternate for Mr. Eastburn.)

Messrs. Black and Willes dissented from this action because they preferred to make use of the full range that had been specified for the Federal funds rate. They believed that, given the accelerated pace of expansion in nominal GNP, growth of both *M*-1 and *M*-2 would be subjected to persistent upward pressure throughout the rest of the second quarter and that a further upward adjustment in the funds rate at this time would be helpful in moderating such pressures and, like the firming that had already occurred, would be regarded as a positive step in resisting inflationary pressures.

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MEETING HELD ON MAY 16, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested that real output of goods and services was growing at a rapid rate in the current quarter, after having declined somewhat in the first quarter when activity was adversely affected by the unusually severe weather and the lengthy strike in coal mining. The rise in the fixed-weighted price index for gross domestic business product—which had stepped up in the first quarter to an annual rate of 6.6 per cent from 5.4 per cent in the fourth quarter of 1977—appeared to be still faster in the current quarter.

Staff projections continued to suggest that output would grow at a moderate pace over the year ahead, although the projected rate of growth was slightly less than that of a month earlier. It was expected that real consumption expenditures and business fixed investment would expand at moderate rates but that residential construction would decline throughout the period. The projections also suggested that the rate of increase in prices over the year ahead would be significantly below the rate in the current quarter but would remain somewhat above that in the first quarter. It was also anticipated, as it had been 4 weeks earlier, that the unemployment rate would decline gradually over the period.

In April the index of industrial production increased about 1 per cent to a level about 2¼ per cent above that in November, before activity was adversely affected by the weather and the coal strike. A significant part of the April increase in the index was attributable to recovery in output of coal and steel from reduced levels, but assemblies of autos rose further to an advanced level, in response to rising sales of domestic models, and production of business equipment continued to expand.

Nonfarm payroll employment continued to rise at a rapid pace in April, even after allowance for the return to work of large numbers of coal miners, and gains again were widespread among industry groups. The unemployment rate declined 0.2 of a percentage point to 6.0 per cent.

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Total retail sales expanded substantially further in April to a level 3¾ per cent above the monthly average for the first quarter. Unit sales of new automobiles, already at an advanced rate in March, edged up further in April.

The index of average hourly earnings for private nonfarm production workers rose at an annual rate of about 9½ per cent in April, little changed from the rapid rate of advance during the first quarter. The wholesale price index for all commodities continued its rapid rise in April, reflecting chiefly further large increases in prices of farm products and foods. In March the consumer price index for all urban consumers had continued to advance at a considerably faster pace than in the second half of 1977, owing not only to additional large increases in foods but also to sizable increases in the apparel and housing components.

In foreign exchange markets the trade-weighted value of the dollar rose about 1¾ per cent over the inter-meeting period, recovering to the level that had prevailed at the start of the year. While appreciating against all major currencies except the Canadian dollar, the dollar advanced most against the Swiss franc and the German mark.

The U.S. foreign trade deficit declined considerably in March, but because it had been at a record level in February, the deficit in the first quarter as a whole was greater than the large deficit incurred in the final quarter of 1977. In the first quarter the value of exports recovered from a fourth-quarter level that had been somewhat depressed by the dock strike. However, the value of imports expanded substantially, despite a decline in imports of petroleum.

The rate of expansion in total bank credit accelerated sharply in April, reflecting an unusually large increase in security loans and sizable additions to bank holdings of both U.S. Government and other securities. Business and real estate loans grew at about the same pace as in March. Outstanding commercial paper of nonfinancial businesses rose substantially in April, although by much less than in March. The sum of business loans (net of bankers acceptances) and nonfinancial commercial paper grew at an annual rate of nearly 25 per cent, compared with about 28 per cent in March.

The narrowly defined money supply (*M*-1), which had grown

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at an annual rate of 5 per cent in the first quarter on a quarterly-average basis, expanded at a rate of 19 per cent in April. The renewed strength in economic activity increased the demand for money, but the high rate of monetary growth in April was also influenced by the public's mobilization of cash for unusually large payments of Federal income taxes not withheld and by relatively slow processing of tax returns. The latest weekly data suggested that growth of *M*-1 would slow substantially in May.

Growth in *M*-2 and *M*-3 also accelerated in April but by much less than growth in *M*-1 because inflows of the interest-bearing deposits included in the broader aggregates remained slow. Thus, *M*-2 and *M*-3 grew in April at annual rates of about 11¼ and 10 per cent, respectively, compared with about 6½ and 7½ per cent in the first quarter.

At its meeting on April 18 the Committee had decided that during the April–May period growth in *M*-1 and *M*-2 within ranges of 4 to 8½ and 5½ to 9½ per cent, respectively, would be appropriate, and it had judged that these growth rates were likely to be associated with a weekly-average Federal funds rate slightly above the level of 6¾ per cent prevailing at that time. The Committee had agreed that if growth rates in the aggregates over the 2-month period appeared to be deviating significantly from the midpoints of the indicated ranges, the operational objective for the weekly-average Federal funds rate should be modified in an orderly fashion within a range of 6¾ to 7½ per cent. It was also agreed, however, that an increase in the rate above 7¼ per cent would not be sought until the Committee had had an opportunity for further consultation.

In accordance with the Committee's decision, the Manager of the System Open Market Account began immediately after the April meeting to seek bank reserve conditions consistent with a firming of the Federal funds rate to around 7 per cent. As the inter-meeting period progressed, data becoming available suggested that over the April–May period *M*-1 would grow at a rate close to or above the upper limit of the range specified by the Committee and that *M*-2 would grow at a rate in the upper part of the range specified for that aggregate. Therefore, the Manager sought conditions consistent with a Federal funds rate of 7¼ per cent, and the rate rose to about that level in the statement week ending May 3.

In early May estimates indicated that *M*-1 had grown at a very

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rapid pace in April, and staff projections suggested that for the April–May period, growth in *M*-1 would be well above the upper limit of its range and growth in *M*-2 at about its upper limit. On May 5 the Committee voted to direct the Manager, until further instructed, to seek to maintain the weekly-average Federal funds rate at about 7¼ per cent, with any deviations tending to be in the direction of higher rather than lower funds rates. At the time of this meeting the funds rate was in the area of 7¼ to 7⅜ per cent.

The rise in the Federal funds rate was accompanied by upward pressures on interest rates in general. Increases in short-term market rates ranged from about 20 to 45 basis points and those in longer-term rates from about 10 to 35 basis points. In early May commercial banks raised the rate on loans to prime business borrowers from 8 to 8¼ per cent.

On May 11 the Board of Governors announced its approval of actions by directors of all 12 Federal Reserve Banks raising the discount rate from 6½ to 7 per cent. In announcing the approval, the Board stated that the action had been taken in recognition of increases that had already occurred in other short-term interest rates and that it would bring the discount rate into closer alignment with short-term rates generally.

Mortgage lending in April apparently was at about the pace of the first quarter, which was below the peak reached in the fourth quarter of 1977. In March, the latest month for which data were available, mortgage commitments outstanding at savings and loan associations continued to decline, as new commitments remained near the reduced rate in February and takedowns of outstanding commitments picked up. During the inter-meeting period, there was a further rise both in average interest rates on new commitments for conventional home loans at those associations and in yields in the secondary markets for mortgages.

In the Committee's discussion of the economic situation and outlook, the members generally agreed that real output of goods and services was growing rapidly in the current quarter, but they differed on the likely course of activity in succeeding quarters. Many members concurred with the staff's view that output would grow at a moderate pace over the year ahead, but some thought that the pace would be a little faster while others thought that it

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would be a little slower. A few members observed that the surge in the current quarter could generate forces that would sustain growth at a fairly rapid pace for a while but might then bring on a period of adjustment at some point in 1979. However, another member said he saw no evidence suggesting that such forces were likely to develop.

To some extent differences of opinion concerning developments in the period ahead reflected varying assessments of the likely behavior of consumers. A number of members anticipated relatively strong consumer demand. One observed that the demand for new domestic autos would be sustained at fairly high levels by various new features, including greater fuel efficiency. On the other hand, one member expressed the view that demands by consumers would be weakened in the second half of the year by their accumulation of debt.

It was stressed that consumer spending was particularly difficult to forecast because of uncertainty concerning consumers' responses to inflation. One member observed that, in contrast with other recent episodes of inflation in this country, consumers now appeared to be more inclined to buy in anticipation of price increases. A second member suggested that consumers might respond to the current inflation by expanding credit-financed expenditures for durable goods while economizing on expenditures for nondurable goods and services. Another member believed that inflation at the rates generally expected would have an adverse impact on confidence sooner or later, causing consumers and others to retrench.

Some differences of opinion were expressed concerning other sectors as well. Thus, one member thought that housing activity would be stronger over the year ahead than the staff projections suggested, but another believed that it would be weaker. The view was expressed that business fixed investment currently was gaining strength, but it was also observed that increases in interest rates might dampen such investment in 1979. With respect to business inventories, it was suggested that an excessive build-up could develop in the near future, setting the stage for a subsequent correction.

Committee members were deeply concerned about the recent acceleration of inflation and about prospects for prices. Several expressed the view that the rise was likely to be more rapid than

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projected by the staff. Thus, it was suggested that the supply-related increase in prices of foods over the remainder of 1978 would exceed the staff projection and that the effect on the over-all price level this year would influence the outcome of labor contract negotiations in 1979. It was also suggested that pressures had begun to develop on labor resources, particularly skilled labor, and on some types of capacity. A few members observed that in these circumstances it would be desirable for growth in real output to diminish in the second half of this year toward a rate that could be sustained for the longer term.

At its meeting in April the Committee had agreed that from the first quarter of 1978 to the first quarter of 1979 average rates of growth in the monetary aggregates within the following ranges appeared to be consistent with broad economic aims: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for the rate of growth in commercial bank credit was 7½ to 10½ per cent. It had also been agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings.

Committee members differed somewhat in their judgments concerning the course of policy for the period immediately ahead, in part because of varying views about the current and prospective economic situation and in part because of differing judgments about the appropriate response to the surge of *M*-1 in April. The differences essentially concerned the degree of any further firming of money market conditions that might be pursued during the next few weeks. No member advocated an easing of money market conditions.

Several reasons were advanced for pursuing a very cautious approach to any further firming at this time, including the fact that transitory influences had contributed to the April surge in *M*-1. It was observed that, despite the surge, the annual rate of growth of *M*-1, and also of *M*-2, over the 3, 6, and 12 months ending in April had been lower than growth over the four quarters of 1977. It was also noted that a significant degree of firming of money market conditions had been achieved since the April meeting of the Committee. Moreover, it was pointed out, the administration's new tax proposals—which had just been announced—were consid-

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erably less stimulative than the earlier ones, particularly as they affected the fourth quarter of 1978. It was suggested that further significant monetary firming at this time might risk provoking dislocations in financial markets that would contribute eventually to the onset of a downturn in economic activity. Finally, it was argued, a very cautious approach would give the Committee time to evaluate incoming evidence concerning both the underlying strength of economic activity and the consequences of the firming that had already been achieved.

In support of a somewhat more restrictive posture, it was suggested that the relatively low rate of growth of *M*-1 in the first quarter of 1978 represented an aberration related to the temporary weakening in the pace of economic activity and that, abstracting from that aberration, the trend of monetary expansion had accelerated. Views were expressed to the effect that further significant firming of money market conditions in the coming period in order to moderate growth of the monetary aggregates would have a beneficial effect on public confidence; that partly for that reason, such firming would reduce the chances of a further build-up of inflationary forces, and that it would increase the chances of achieving a rate of growth in real output that could be sustained for the longer term. In this connection, it was suggested that at times in the past when high levels of resource use had been approached, lags in the application of monetary restraint had contributed to bringing on a downturn in economic activity and to increasing the depth and duration of the downturn. The comment was made that if further significant action were not taken in the present circumstances, current monetary policy might be found in retrospect to have been procyclical.

With respect to operating specifications for the period ahead, most members preferred ranges of tolerance for the annual rate of growth in *M*-1 over the May–June period that more or less encompassed the Committee's longer-run range of 4 to 6½ per cent; the preferences centered on 3 to 8 per cent. However, some members preferred to widen the range by reducing the lower limit, on the ground that, given the April surge, growth somewhat slower than 3 per cent could be tolerated for a time and should not form the basis for an easing of money market conditions. One member, believing that the upper limit of the 2-month range should not be

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above 6½ per cent in view of the April surge, favored a range of 2½ to 6½ per cent. For *M*-2 most members advocated a range of 4 to 9 per cent, but there was some sentiment for ranges of both 5 to 9 and 4 to 8 per cent.

All of the members favored directing operations during the coming inter-meeting period initially toward a Federal funds rate slightly above the current rate, which was in the area of 7¼ to 7⅜ per cent. Views differed somewhat with respect to the degree of leeway for operations during the inter-meeting period in the event that growth in the monetary aggregates appeared to be deviating significantly from the midpoints of the specified ranges. Most members favored a range for the weekly-average Federal funds rate extending from 7¼ to 7¾ per cent, but there was some sentiment for an upper limit of 8 per cent.

At the conclusion of the discussion the Committee decided that the ranges of tolerance for the annual rates of growth in *M*-1 and *M*-2 over the May–June period should be 3 to 8 and 4 to 9 per cent, respectively. It was understood that in assessing the behavior of these aggregates the Manager should continue to give approximately equal weight to the behavior of *M*-1 and *M*-2.

In the judgment of the Committee such growth rates were likely to be associated with a weekly-average Federal funds rate slightly above the current level of 7¼ to 7⅜ per cent. The members agreed that if growth rates of the aggregates over the 2-month period appeared to be deviating significantly from the midpoints of the indicated ranges, the operational objective for the weekly-average Federal funds rate should be modified in an orderly fashion within a range of 7¼ to 7¾ per cent.

As is customary, 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. The members also agreed that in the conduct of day-to-day operations, account should be taken of emerging financial market conditions.

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 growing at a rapid rate in the current quarter,

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after having declined somewhat in the first quarter when activity was adversely affected by the unusually severe weather and the lengthy strike in coal mining. In April retail sales, industrial production, and nonfarm payroll employment increased substantially further and the unemployment rate declined from 6.2 to 6.0 per cent. The pace of the rise in wholesale prices remained rapid, reflecting mainly further large increases in farm products and processed foods. The index of average hourly earnings continued to advance at about the fast pace that it had on the average during the first quarter.

The trade-weighted value of the dollar against major foreign currencies has risen over the past 4 weeks to the level prevailing at the beginning of the year. The trade deficit in the first quarter widened substantially from the already large deficit recorded in the final quarter of 1977.

M-1, which had grown moderately in the first quarter, rose sharply in April. Growth in *M*-2 and *M*-3 also stepped up but much less than growth in *M*-1, because inflows of the interest-bearing deposits included in these aggregates remained slow. Market interest rates have increased in recent weeks. On May 11 an increase in Federal Reserve discount rates from 6½ to 7 per cent was announced.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster bank reserve and other financial conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions.

At its meeting on April 18, 1978, the Committee agreed that growth of *M*-1, *M*-2, and *M*-3 within ranges of 4 to 6½ per cent, 6½ to 9 per cent, and 7½ to 10 per cent, respectively, from the first quarter of 1978 to the first quarter of 1979 appears to be consistent with these objectives. The associated range for bank credit is 7½ to 10½ per cent. These ranges are subject to reconsideration at any time as conditions warrant.

The Committee seeks to encourage near-term rates of growth in *M*-1 and *M*-2 on a path believed to be reasonably consistent with the longer-run ranges for monetary aggregates cited in the preceding paragraph. Specifically, at present, the ranges of tolerance for the annual growth rates over the May–June period will be 3 to 8 per cent for *M*-1 and 4 to 9 per cent for *M*-2. In the judgment of the Committee such growth rates are likely to be associated with a weekly-average Federal funds rate slightly above the current level. If, giving approximately equal weight to *M*-1 and *M*-2, it appears

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that growth rates over the 2-month period will deviate significantly from the midpoints of the indicated ranges, the operational objective for the Federal funds rate shall be modified in an orderly fashion within a range of 7¼ to 7¾ per cent. In the conduct of day-to-day operations, account shall be taken of emerging financial market conditions.

If it appears during the period before the next meeting that the operating constraints specified above are proving to be significantly inconsistent, the Manager is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Gardner, Jackson, Partee, Wallich, and Winn. Vote against this action: Mr. Willes.

Mr. Willes dissented from this action because he favored more vigorous measures to reduce the rate of monetary growth, given the acceleration of the rate of inflation and its adverse effect on consumer and business confidence and spending plans. Specifically, he preferred a range of 2½ to 6½ per cent for the annual rate of growth in *M*-1 over the May–June period and an inter-meeting range of 7¼ to 8 per cent for the Federal funds rate.

Subsequent to the meeting, on June 15, revised projections based on newly available data suggested that *M*-1 would grow in the May–June period at an annual rate of about 7½ per cent, near the upper limit of the range of tolerance of 3 to 8 per cent specified in the Committee's directive. *M*-2 also was projected to grow in the 2-month period at a 7½ per cent annual rate, but this was well within the range of 4 to 9 per cent specified for that aggregate.

In general, the strength of the aggregates suggested a need for Committee consultation, looking toward further instruction to the Desk. In view of the proximity of the Committee meeting scheduled for June 20, Chairman Miller recommended that the Desk be instructed to continue aiming for a Federal funds rate of 7½ per cent at this time.

On June 16, 1978, the Committee modified the domestic policy directive adopted at its meeting on May 16, 1978, to instruct the Desk to continue aiming for a weekly-average Federal funds rate of 7½ per cent at this time.

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Votes for this action: Messrs. Miller, Baughman, Coldwell, Eastburn, Gardner, Partee, Wallich, Willes, Winn, and Timlen. Votes against this action: None. Absent and not voting: Messrs. Volcker and Jackson. (Mr. Timlen voted as alternate for Mr. Volcker.)

2. Authorization for Foreign Currency Operations

Paragraph 1D of the Committee's authorization for foreign currency operations authorizes the Federal Reserve Bank of New York, for the System Open Market Account, to maintain an over-all open position in all foreign currencies not to exceed $1.0 billion, unless a larger position is expressly authorized by the Committee. On March 21, 1978, the Committee had authorized an open position of $2.25 billion in view of the scale of recent and potential Federal Reserve operations in the foreign exchange markets undertaken pursuant to the Committee's foreign currency directive.

At this meeting the Committee voted to reduce the authorized open position to $2 billion. This action was taken in view of the decrease in the open position that had occurred in recent weeks.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Gardner, Jackson, Partee, Wallich, Willes, and Winn. Votes against this action: None.

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MEETING HELD ON JUNE 20, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested that output of goods and services had expanded rapidly on the average in the second quarter, reflecting the economy's rebound in late winter and early spring from the effects of the unusually severe winter weather and the lengthy coal strike. More recently, however, the rate of expansion appeared to have slowed. The rise in average prices—as measured by the fixed-weighted price index for gross domestic business product—accelerated markedly in the second quarter, due in large measure to substantial increases in food prices.

Staff projections continued to suggest moderate expansion in output over the year ahead. The anticipated rate of growth was slightly lower than that projected a month earlier, mainly because the assumptions regarding fiscal policy were modified to reflect the administration's decision to delay the proposed tax cut from October 1 to January 1 and to reduce its size. The projected rate of price advance had been raised slightly from that of a month earlier, but it was still well below the rate in the second quarter. The projections also suggested that the unemployment rate would decline a bit further over the coming year.

Growth in production and employment moderated in May from the rapid rates of preceding months. Thus, the industrial production index increased 0.6 per cent, compared with gains of 1.2 and 1.4 per cent in March and April, respectively; and the rise in nonfarm payroll employment in May was less than one-half the average increase earlier in the year. In manufacturing, the gain in employment was relatively small and the average workweek declined. The labor force continued to grow substantially, and the unemployment rate edged up to 6.1 per cent from 6.0 per cent in April.

Total retail sales were about unchanged in May, following 3 months of exceptionally large gains. Unit sales of new automobiles

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rose slightly further to a new high for the current expansion. It appeared that some consumers were buying new cars in anticipation of further price increases.

The latest Department of Commerce survey of business spending plans, taken in late April and May, suggested that outlays for plant and equipment would expand 11.2 per cent in 1978; this rate was marginally above that reported in the February survey. Other indicators of capital spending plans, such as manufacturers' capital appropriations, contracts for commercial and industrial buildings, and new orders for nondefense capital goods, appeared generally consistent with continued moderate expansion in investment outlays.

The index of average hourly earnings for private nonfarm production workers rose at an annual rate of about 3 per cent in May, following increases averaging close to 10 per cent in earlier months of 1978. For the first 5 months of the year the index had increased at a somewhat faster rate than it had on the average in 1977. The advance in the wholesale price index for all commodities also slowed in May, reflecting smaller increases in prices of farm and food products as of the time of the survey. Later in the month, however, prices of a number of farm products advanced. In April the consumer price index for all urban consumers rose at an accelerated annual rate of nearly 11 per cent, owing to further large increases in food prices and to higher service costs, especially those relating to homeownership. In general, prices had increased considerably faster in early 1978 than during the year 1977.

In foreign exchange markets the trade-weighted value of the dollar reached a peak for 1978 in late May. Subsequently the dollar declined by about 2 per cent, but it remained above the low for the year that had been recorded in early April.

The renewed downward pressure on the dollar appeared to reflect market concern about the high rate of inflation in the United States relative to rates in other industrial countries and about the continuation of large deficits in U.S. foreign trade and surpluses in the trade of Germany and Japan. The deficit in April was about the same as that in March but lower than the high level of the first quarter. Both exports and imports rose considerably in April.

The rate of expansion in total bank credit, which had accelerated sharply in April, slackened somewhat in May but remained above the average for other recent months. Bank holdings of securities

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changed little, but total loans, led by a surge in business loans, grew at an exceptional pace. Outstanding commercial paper of nonfinancial businesses declined slightly in May.

Growth in the narrowly defined money supply (*M*-1) moderated in May to an annual rate of about 6½ per cent from the extraordinarily rapid rate of 19 per cent in April. Growth in *M*-2 and *M*-3 also slowed in May, reflecting the deceleration in *M*-1. Inflows of the interest-bearing deposits included in *M*-2 generally were greater than in April as commercial banks issued a substantial volume of large-denomination time deposits to finance the sharp increase in business loans. However, inflows of funds into savings deposits and small-denomination time deposits remained slow both at banks and at thrift institutions. Preliminary data for the first part of June suggested that growth in *M*-1 and *M*-2 would accelerate in that month.

At its meeting on May 16 the Committee had decided that the ranges of tolerance for the annual rates of growth in *M*-1 and *M*-2 during the May–June period should be 3 to 8 per cent and 4 to 9 per cent, respectively, and it had judged that such growth rates were likely to be associated with a weekly-average Federal funds rate slightly above the level of 7¼ to 7⅜ per cent prevailing at that time. The Committee had agreed that if growth rates in the aggregates over the 2-month period appeared to be deviating significantly from the midpoints of the indicated ranges, the operational objective for the weekly-average Federal funds rate should be modified in an orderly fashion within a range of 7¼ to 7¾ per cent.

In accordance with the Committee's decision, the Manager of the System Open Market Account began after the May meeting to seek bank reserve conditions consistent with a firming of the Federal funds rate to around 7½ per cent. Incoming data throughout most of the inter-meeting period suggested that growth in the monetary aggregates would be well within the ranges specified by the Committee, and the Manager continued to seek conditions consistent with a Federal funds rate of 7½ per cent.

Data that became available a few days before this meeting suggested that *M*-1 would grow in the May–June period at an annual rate of about 7½ per cent, close to the upper limit of its range. *M*-2 also was projected to grow in the 2-month period at a 7½ per cent rate, in the upper half of the range specified for that

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aggregate. These data suggested the need for Committee consultation, and on June 16, in view of the proximity of the meeting scheduled for June 20, the Committee voted to direct the Manager to continue for the time being to aim for a Federal funds rate of 7½ per cent.

Other market interest rates had risen further in recent weeks. Reflecting not only the rise in the funds rate but also substantial business credit demands, market rates on short-term securities had increased from 30 to 60 basis points since mid-May, and commercial banks had raised the rate on loans to prime business borrowers in two steps from 8¼ to 8¾ per cent. Yields on long-term securities rose 5 to 20 basis points over the same period, apparently in response to the rise in short-term rates and investor concerns about the prospects for inflation.

Conditions in mortgage markets had continued to tighten recently as strong demands for credit pressed against reduced availability of funds at lending institutions. At savings and loan associations, net mortgage lending activity in April—the latest month for which data were available—was close to its reduced rate in the weather-affected first quarter, and mortgage commitments outstanding declined further. During the inter-meeting period there were further increases in interest rates on new commitments for conventional home loans at the associations and, in most regions, a tightening of nonrate terms as well. Yields in the secondary market for home mortgages also had generally increased in recent weeks.

In the Committee's discussion of the economic situation and outlook, the members generally agreed that the growth in real output of goods and services over the coming three quarters would be substantially slower on the average than it had been in the unusually strong quarter just ending. However, they still expected real GNP to grow at a moderate, average rate during the year ending with the second quarter of 1979. While some members thought that average growth for that period would probably be at or a little below the rate projected by the staff, others expected somewhat faster growth. A majority feared that the rise in prices would be greater than the staff anticipated. Most members thought that the unemployment rate at the end of the period would be little changed from the rates recently prevailing.

With respect to the months immediately ahead, a majority of

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the Committee members thought that the economy was likely to show more strength than the staff projection suggested. These members noted that both consumer and business sentiment appeared to be strong, and they interpreted the latest data on consumer behavior as evidence that many households were adopting a speculative approach to spending—anticipating needs for housing and other durables, and in the process adding willingly to already heavy debt burdens. While these members acknowledged that national economic data did not yet suggest similar anticipatory spending on the part of businesses, several noted that many businessmen appeared to be optimistic about the prospects for their own firms and industries and that such optimism might soon be reflected in a step-up in over-all business inventory accumulation and investment outlays. A number of these members expressed concern about the indications that inflationary expectations were strengthening and that both business and labor were intensifying their efforts to protect themselves through price and wage increases.

Two of the members who anticipated relatively strong growth in the near term thought that the economy was likely to generate sufficient momentum to maintain a favorable rate of expansion beyond mid-1979. Others in this group were concerned, however, that insofar as near-term spending of consumers and businesses embodied speculative tendencies, the resulting economic distortions might lead to significantly slower growth in 1979.

Of the Committee members who anticipated less near-term strength in the economy, some suggested that current business optimism might well reflect an overemphasis on the sharp rebound that had occurred in recent months rather than a considered assessment by businessmen of prospects for the future. These members thought it unlikely that growth in consumer outlays would continue at the recent rate, and they saw no obvious source of offsetting strength. They expected outlays for housing to slacken; they noted that surveys of business investment plans did not reflect much ebullience; and they thought businessmen would follow a cautious approach to inventory expansion. Finally, they noted that Federal fiscal policy would be less stimulative than anticipated earlier in the year.

Several members of the Committee observed that relatively slow economic growth would tend to dampen inflationary pressures and

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to bolster the position of the dollar in foreign exchange markets. One of these members noted that economic activity in major industrial countries abroad was expected to strengthen, and that such a development would help to limit any deceleration in the U.S. expansion. He added that a failure of activity abroad to strengthen as expected would increase the chances of unsatisfactory growth in the United States and would create additional problems with respect to the U.S. current account.

At its meeting in April the Committee had agreed that from the first quarter of 1978 to the first quarter of 1979 average rates of growth in the monetary aggregates within the following ranges appeared to be consistent with broad economic aims: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for the rate of growth in commercial bank credit was 7½ to 10½ per cent. It had also been agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings.

At this meeting, in discussing policy for the period immediately ahead, Committee members expressed considerable concern about recent rates of growth in the monetary aggregates, particularly in light of the continuing strength of inflationary pressures and expectations. The members agreed that open market operations in the inter-meeting period should be directed initially toward achieving slightly firmer money market conditions, and that later in the period the objectives of operations should depend on incoming data for *M*-1 and *M*-2.

As at the preceding meeting, there were differences of view with respect to the degree of firming that might be undertaken. These differences were reflected in opinions on such issues as the magnitude and speed of the initial move toward firmer money market conditions and the amount of leeway—in terms of the inter-meeting range specified for the Federal funds rate—for further firming later in the period.

As to the initial move, most members favored seeking an increase in the Federal funds rate to 7¾ per cent from the prevailing level of 7½ per cent within a few days after this meeting. However, one member suggested that this quarter-point increase be achieved over a somewhat longer period, and another proposed that the initial

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increase be limited to one-eighth of a point. With respect to the inter-meeting range for the Federal funds rate, most members favored 7½ to 8 per cent, but a number preferred 7½ to 8¼ per cent.

There was greater diversity of views with respect to the ranges of tolerance to be specified for the annual rates of growth in *M*-1 and *M*-2 in the June–July period. Of the ranges suggested for *M*-1, the lowest was 3½ to 8½ per cent, and the highest was 6½ to 10½ per cent; for *M*-2 the suggestions covered a similar span. It was noted during the discussion that if the monetary aggregates accelerated in June, as suggested by early data, growth over the June–July period at rates near the midpoints of some of the lower ranges proposed could be achieved only if there were to be a sharp slowing in July. Some members, who were inclined to stress the risks to the economy of rapid firming of money market conditions, saw this circumstance as an argument for specifying relatively high 2-month ranges for *M*-1 and *M*-2. Other members, who placed more stress on the importance at this time of limiting growth in the aggregates for the sake of moderating inflationary pressures and expectations, thought such firming would be called for if the growth in the aggregates did not in fact slow sharply.

At the conclusion of the discussion the Committee decided that the ranges of tolerance for the annual rates of growth over the June–July period should be 5 to 10 per cent for *M*-1 and 6 to 10 per cent for *M*-2. The Committee agreed that during the coming inter-meeting period operations should be directed initially toward a Federal funds rate of 7¾ per cent, slightly above the prevailing level of 7½ per cent. Subsequently, if the 2-month growth rates of *M*-1 and *M*-2 appeared to be significantly above or below the midpoints of the indicated ranges, the objective for the funds rate was to be raised or lowered in an orderly fashion within a range of 7½ to 8 per cent. It was understood that in assessing the behavior of the aggregates the Manager should continue to give approximately equal weight to the behavior of *M*-1 and *M*-2.

It was also understood that the Chairman might call upon the Committee to consider the need for supplementary instructions if the rates of growth in the aggregates appeared to be above the upper limit or below the lower limit of the indicated ranges at a time when the objective for the funds rate had already been moved to the corresponding limit of its range.

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At this meeting the Committee considered certain proposed modifications in the language customarily employed in the concluding paragraphs of the domestic policy directive. It was noted that, perhaps because of the manner in which the directive was worded, the 2-month ranges of tolerance for *M*-1 and *M*-2 were subject to misinterpretation as embodying the Committee's short-run targets for these aggregates, intended to be achieved by appropriate changes in the Federal funds rate. In fact, however, the Manager could not be expected regularly to achieve 2-month growth rates in *M*-1 and *M*-2 within the specified ranges for various reasons—including the lag between changes in the Federal funds rate and changes in these growth rates, and the brevity of the period to which the operational paragraphs of any single directive applied.

It was noted in the discussion that the Committee's objectives for the monetary aggregates were embodied in the 1-year ranges established at quarterly intervals, and that the adjustments made from time to time in the Federal funds rate were intended to increase the likelihood that the longer-run growth rates would fall within these ranges. The purpose of the 2-month ranges was to provide the Manager with an indicator for determining when changes in the funds rate were appropriate; specifically, the Manager was expected to adjust the funds rate within its range when the latest projections of 2-month growth rates in *M*-1 and *M*-2 deviated significantly from the midpoints of their ranges (or, if the Committee so indicated in the directive, when the projections for the aggregates approached or moved beyond the limits of their ranges).

At the May meeting, following a preliminary discussion of this matter, the Committee had deleted one potentially misleading phrase from the language previously employed, to the effect that the Committee "expects" the 2-month growth rates to be within the indicated ranges. At this meeting the Committee agreed upon a more thorough revision of the customary language, in an effort to reduce the chances of misinterpretations.

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 has grown rapidly on the average in the current quarter as activity rebounded from the effects of the unusually severe winter weather and the lengthy coal strike, but the rate of advance

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most recently appears to be slowing. Following substantial gains in March and April, increases in industrial production and nonfarm payroll employment moderated in May and retail sales changed little. The unemployment rate edged up from 6.0 to 6.1 per cent in association with a large increase in the civilian labor force. Average wholesale prices rose somewhat less rapidly in May than earlier in 1978, reflecting smaller reported increases in farm products and processed foods. So far this year prices have increased at a considerably faster rate than they had on average during 1977. The index of average hourly earnings also has increased at a somewhat faster pace so far in 1978 than during 1977.

Since the end of May the trade-weighted value of the dollar against major foreign currencies has declined about 2 per cent, but it remains above its early-April low. The trade deficit in April was down somewhat from its very high first-quarter rate.

Growth in *M*-1 moderated in May from the extraordinarily rapid pace in April, and as a result growth in *M*-2 and *M*-3 also slowed. Inflows of the interest-bearing deposits included in *M*-2 picked up somewhat as commercial banks increased their reliance on large-denomination time deposits to finance an unusually sharp increase in business loans. Market interest rates have risen somewhat further in recent weeks.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster monetary and financial conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions. At its meeting on April 18, 1978, the Committee agreed that these objectives would be furthered by growth of *M*-1, *M*-2, and *M*-3 from the first quarter of 1978 to the first quarter of 1979 at rates within ranges of 4 to 6½ per cent, 6½ to 9 per cent, and 7½ to 10 per cent, respectively. The associated range for bank credit is 7½ to 10½ per cent. These ranges are subject to reconsideration at any time as conditions warrant.

In the short run, the Committee seeks to achieve bank reserve and money market conditions that are broadly consistent with the longer-run ranges for monetary aggregates cited above, while giving due regard to developing conditions in financial markets more generally. During the period until the next regular meeting, System open market operations shall be directed initially at attaining a weekly-average Federal funds rate slightly above the current level. Subsequently, operations shall be directed at maintaining the weekly Federal funds rate within the range of 7½ to 8 per cent. In deciding

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on his specific objective for the Federal funds rate the Manager shall be guided mainly by the relationship between the latest estimates of annual rates of growth in the June–July period of *M*-1 and *M*-2 and the following ranges of tolerance: 5 to 10 per cent for *M*-1 and 6 to 10 per cent for *M*-2. If, giving approximately equal weight to *M*-1 and *M*-2, their rates of growth appear to be significantly above or below the midpoints of the indicated ranges, the objective for the funds rate shall be raised or lowered in an orderly fashion within its range.

If the rates of growth in the aggregates appear to be above the upper limit or below the lower limit of the indicated ranges at a time when the objective for the funds rate has already been moved to the corresponding limit of its range, the Manager is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Gardner, Jackson, Partee, and Wallich. Votes against this action: Messrs. Willes and Winn.

Messrs. Willes and Winn dissented from this action because they favored more vigorous measures to curb the rate of growth in the monetary aggregates. Both preferred ranges of tolerance for the 2-month growth rates in *M*-1 and *M*-2 lower than those approved by the majority; in addition, Mr. Willes favored an upper limit for the funds rate range of 8¼ per cent.

Mr. Willes, citing strong consumer and business credit demands at prevailing interest rates, felt that a further rise in short-term interest rates would not significantly damage economic prospects and that, to the extent that such a rise tended to moderate inflationary expectations, it would have a positive impact on the economy. Mr. Winn felt that if the Committee did not act now to assure a reduction in the rates of growth of the aggregates, an excessively restrictive policy would be required later on if the Committee's longer-range objectives were to be achieved.

2. Operations in Federal Agency Securities

At this meeting the Committee discussed its procedures with respect to open market operations in Federal agency securities. The dis-

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cussion arose because of a potential problem posed by a statutory requirement that Federal Reserve note liabilities be collateralized by eligible assets, which included direct obligations of the Treasury but not Federal agency issues. At times recently, the margin of actual collateral over that required had been relatively small. The Board of Governors had proposed legislation that would make Federal agency issues eligible as collateral, but the Congress had not yet acted on the proposal.

It was noted that the problem of maintaining sufficient collateral for Federal Reserve notes could become critical at some point before the enactment of such legislation if, for example, a need arose to sell a substantial volume of Treasury securities to absorb redundant member bank reserves. It was also noted that the problem would be mitigated by some slowing of the rate of growth in System holdings of agency securities and a correspondingly larger increase in holdings of Treasury securities.

Paragraph 1(a) of the Committee's authorization for domestic open market operations authorizes the Federal Reserve Bank of New York to sell, as well as to buy, Federal agency securities for the System Open Market Account. Historically, however, sales of such securities have been quite infrequent. It was the sense of the Committee that modest sales of agency issues would be appropriate from time to time, but only when market circumstances permitted and when sales of securities were consistent with the objectives of open market operations. It was noted in the discussion that, even apart from the problem of collateral requirements, occasional sales of agency issues would help enhance the flexibility of open market operations. The Committee also agreed that the Desk should reduce somewhat the volume of agency issues it purchased when supplying reserves, and that occasionally, when there was a need to absorb reserves, it should redeem maturing agency issues for cash rather than routinely exchange them for new issues.

3. Authorization for Foreign Currency Operations

At this meeting the Committee approved a technical amendment to paragraph 1D of the authorization for foreign currency operations, under which the definition contained in the second sentence

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of that paragraph of "over-all open position in all foreign currencies" is given as "the sum (disregarding signs) of net positions in individual currencies" rather than as "the sum (disregarding signs) of open positions in each currency." This change was approved in the interest of clarity, and to make the language of this paragraph conform to certain new language concurrently introduced in the procedural instructions governing foreign currency operations, as described below.

With this amendment, paragraph 1D read as follows:

> To maintain an over-all open position in all foreign currencies not exceeding $1.0 billion, unless a larger position is expressly authorized by the Committee. For this purpose, the over-all open position in all foreign currencies is defined as the sum (disregarding signs) of net positions in individual currencies. The net position in a single foreign currency is defined as holdings of balances in that currency, plus outstanding contracts for future receipt, minus outstanding contracts for future delivery of that currency, i.e., as the sum of these elements with due regard to sign.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Jackson, Partee, Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Mr. Gardner.

Under the first sentence of paragraph 1D, which was not affected by the foregoing amendment, the Federal Reserve Bank of New York is authorized, for System Open Market Account, to maintain an over-all open position in all foreign currencies not exceeding $1.0 billion, unless a larger position is expressly authorized by the Committee. On March 21, 1978, the Committee had authorized an open position of $2.25 billion in view of the scale of recent and potential System operations in foreign currencies. On May 16, 1978, the Committee had reduced this limit to $2.0 billion, in light of decreases in the System's open position. Against the background of further decreases in the open position, the Committee reduced the limit to $1.5 billion at this meeting.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Jackson, Partee, Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Mr. Gardner.

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4. Procedural Instructions with Respect to Operations Under the Foreign Currency Documents

In December 1976 the Committee had adopted certain procedural instructions for the purpose of clarifying the respective roles of the Committee, the Foreign Currency Subcommittee designated in paragraph 6 of the authorization for foreign currency operations, and the Chairman in providing guidance to the Manager of the System Open Market Account with respect to proposed or ongoing foreign currency operations under the authorization and the foreign currency directive. Paragraph 1B of the instructions called for clearance of any transactions that would result in gross transactions in a single foreign currency exceeding $100 million on any day or $300 million since the most recent regular meeting of the Committee. At its meeting in March 1978 the Committee amended paragraph 1B to increase these dollar limits, which had occasionally hampered ongoing operations, and to remove an ambiguity in the language.

At this meeting the Committee decided to discontinue the use of the concept of gross transactions in the procedural instructions. In its stead it introduced (a) a clearance requirement formulated in terms of daily and inter-meeting changes in the System's net position in a single foreign currency and (b) a requirement for clearance of any operation that might generate a substantial volume of trading in a particular currency by the System, regardless of the effect on the System's net position in that currency. The purpose of these changes was to improve the effectiveness of the consultation procedure. In addition, for the sake of clarity the word "transaction" was replaced by the word "operation" wherever the former had occurred in the instructions.

The two new provisions were identified as paragraphs 1B and 1C. Paragraph 1A, which refers to daily and inter-meeting changes in the System's over-all open position in foreign currencies, was retained, and the paragraph previously designated 1C, which relates to swap drawings by foreign central banks, was redesignated 1D.

With these changes, the procedural instructions read as follows:

> In conducting operations pursuant to the authorization and direction of the Federal Open Market Committee as set forth in the Authorization for Foreign Currency Operations and the Foreign

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Currency Directive, the Federal Reserve Bank of New York, through the Manager of the System Open Market Account, shall be guided by the following procedural understandings with respect to consultations and clearance with the Committee, the Foreign Currency Subcommittee, and the Chairman of the Committee. All operations undertaken pursuant to such clearances shall be reported promptly to the Committee.

1. The Manager shall clear with the Subcommittee (or with the Chairman, if the Chairman believes that consultation with the Subcommittee is not feasible in the time available):

A. Any operation which would result in a change in the System's over-all open position in foreign currencies exceeding $100 million on any day or $300 million since the most recent regular meeting of the Committee.

B. Any operation which would result in a change in the System's net position in a single foreign currency exceeding $100 million on any day or $300 million since the most recent regular meeting of the Committee.

C. Any operation which might generate a substantial volume of trading in a particular currency by the System, even though the change in the System's net position in that currency might be less than the limits specified in 1B.

D. Any swap drawing proposed by a foreign bank not exceeding the larger of (i) $200 million or (ii) 15 per cent of the size of the swap arrangement.

2. The Manager shall clear with the Committee (or with the Subcommittee, if the Subcommittee believes that consultation with the full Committee is not feasible in the time available, or with the Chairman, if the Chairman believes that consultation with the Subcommittee is not feasible in the time available):

A. Any operation which would result in a change in the System's over-all open position in foreign currencies exceeding $500 million since the most recent regular meeting of the Committee.

B. Any swap drawing proposed by a foreign bank exceeding the larger of (i) $200 million or (ii) 15 per cent of the size of the swap arrangement.

3. The Manager shall also consult with the Subcommittee or the Chairman about proposed swap drawings by the System, and about any operations that are not of a routine character.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Jackson, Partee, Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Mr. Gardner.

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MEETING HELD ON JULY 18, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested that growth in economic activity had slowed in recent months. From the first to the second quarter, however, real output of goods and services appeared to have expanded sharply, reflecting the rebound in activity from the adverse effects of the severe winter and the lengthy coal strike. The rise in average prices—as measured by the fixed-weighted price index for gross domestic business product—accelerated markedly in the second quarter, largely because of substantial increases in food prices.

The staff continued to project moderate expansion in output from the second quarter of 1978 through the second quarter of 1979. The staff projections also suggested that the price advance would remain rapid, although not so rapid as in the second quarter of 1978, and that the unemployment rate would change little from its current level.

In June the index of industrial production rose an estimated 0.3 per cent, down from 0.6 per cent in May and much below the substantial gains in March and April. Total nonfarm payroll employment rose considerably in June, but the advance, like May's, was well below the increases in March and April. In manufacturing, employment and the average workweek were about unchanged in June. The over-all unemployment rate fell 0.4 of a percentage point to 5.7 per cent, its lowest level in nearly 4 years.

Total retail sales changed little in June for the second consecutive month, following 3 months of exceptionally large gains. Unit sales of new automobiles remained at a high level.

The advance in the index of average hourly earnings for private nonfarm production workers moderated in May and June, but it was somewhat faster over the first half of 1978 than during 1977.

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Average prices of producer goods rose less rapidly in May and June than earlier in the year, but their increase over the first half was considerably faster than the pace during 1977. In May the consumer price index for all urban consumers rose sharply further, led by rises in food, housing, and energy; over the first 5 months of the year the annual rate of increase averaged slightly above 10 per cent.

In foreign exchange markets the trade-weighted value of the dollar against major foreign currencies declined about 2 per cent further from mid-June to the date of this meeting, reaching its lowest point so far in 1978. The downward pressure on the dollar in recent weeks appeared to reflect heightened market concern about the high rate of inflation in the United States relative to rates abroad and about the persistence of extremely large current-account surpluses in Japan and Germany and a large deficit in the United States. In May the U.S. trade deficit was somewhat lower than its very high average rate in the first 4 months of the year.

The expansion in total credit at U.S. commercial banks slowed substantially in June from the unusually rapid rates in the preceding 2 months, as growth of business loans decelerated sharply after a surge in May. Growth of other types of loans moderated as well, but bank holdings of Treasury securities increased. Outstanding commercial paper of nonfinancial businesses increased substantially in June. Nevertheless, expansion of total short-term credit to nonfinancial businesses by banks and through the paper market was well below the exceptionally rapid pace earlier in the second quarter.

Growth of the narrowly defined money supply (*M*-1) moderated in May and June from the extraordinarily rapid pace in April, but growth from the first to the second quarter was at an annual rate of 9½ per cent. Growth in *M*-2 and *M*-3 had been moderate over recent months. In June inflows of small-denomination time deposits to banks and to nonbank thrift institutions picked up, following introduction on the first of the month of a short-term money market certificate with a ceiling interest rate for new deposits that changes weekly with the average discount rate on new issues of 6-month Treasury bills. Preliminary reports indicated relatively strong investor interest in these certificates.

Over the year from the second quarter of 1977 to the second

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quarter of 1978, growth in *M*-1 was about 8 per cent—above the 4 to 6½ per cent range for that period adopted by the Committee in July 1977. However, growth in *M*-2 and in *M*-3 over the period was within the ranges for those aggregates adopted at that time: *M*-2 expanded by about 8½ per cent, compared with its range of 6½ to 9 per cent; *M*-3 grew about 10 per cent, compared with its range of 8 to 10½ per cent.

At its meeting on June 20 the Committee had decided on ranges of tolerance for the annual rates of growth in *M*-1 and *M*-2 during the June–July period of 5 to 10 per cent and 6 to 10 per cent, respectively. The Committee had agreed that during the coming inter-meeting period operations should be directed initially toward a Federal funds rate of 7¾ per cent, slightly above the prevailing level of 7½ per cent. Subsequently, if the 2-month growth rates of *M*-1 and *M*-2 appeared to be significantly above or below the midpoints of the indicated ranges, the objective for the funds rate was to be raised or lowered in an orderly fashion within a range of 7½ to 8 per cent.

In accordance with the Committee's decision, the Manager of the System Open Market Account began immediately after the June meeting to seek bank reserve conditions consistent with a firming of the Federal funds rate to a weekly average of around 7¾ per cent. Incoming data throughout the inter-meeting period suggested that growth in the monetary aggregates would be well within the ranges that had been specified by the Committee, and the Manager continued to seek reserve conditions consistent with a Federal funds rate averaging about 7¾ per cent. In the final days of the period the funds rate fluctuated around a level somewhat above 7¾ per cent.

Market interest rates on both long- and short-term securities had shown further increases since the June meeting of the Committee, ranging from about ⅛ to ⅜ of a percentage point. In addition, commercial banks raised the rate on loans to prime business borrowers from 8¾ to 9 per cent. Interest rates on new commitments for conventional mortgage loans at savings and loan associations had changed little during the inter-meeting period, while yields in the secondary market for home mortgages had risen somewhat further.

On June 30 an increase in Federal Reserve discount rates from

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7 to 7¼ per cent was announced by the Board of Governors. The Board stated that the action was taken in recognition of increases that had already occurred in other short-term interest rates and that it would bring the discount rate into closer alignment with short-term rates generally.

In the Committee's discussion of the economic situation and outlook, there was general agreement among the members that over the year ending in the second quarter of 1979 output of goods and services was most likely to grow at about the moderate pace projected by the staff. However, a number of the members anticipated a little less growth and a few anticipated a little more.

Despite the consensus that continuing moderate growth in real GNP was still the most likely development, some members suggested that for a number of reasons—including the high rate of inflation and developing financial stringencies—the probabilities of such an outcome were lower than they had seemed to be earlier. A few members observed that the chances of a decline in output during the period had increased. In the opinion of one of these members, the prospects for a gradual slowing of growth in output toward a rate that might be sustainable for the longer term had been diminished by the recent rapid decline in the unemployment rate and by the development of some imbalances in the economy. Another member expected that consumer buying of houses and durable goods, which had been stimulated in recent months by anticipations of further increases in prices, would weaken in the period immediately ahead. He was concerned, moreover, that financial strains might develop to the point of bringing on a downturn in activity, although he did not regard such a development as inevitable.

Other members of the Committee felt more confident that a recession would not develop during the four quarters ahead and that output would grow moderately. One of these members thought that expectations of further price increases might well sustain consumer buying—and perhaps business buying, at least to some extent—during the second half of 1978 and that reductions in Federal taxes would strengthen demands in the first half of 1979. Similarly, another member believed that expansive elements in the economy were sufficient to sustain a moderate growth in output, and that distortions were not developing to the point that they would

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overcome those expansive influences. In his view, it remained possible to slow growth to a rate sustainable for the longer term. Another member agreed that there was still time to achieve such a slowing of growth, given appropriate Government policies.

All members of the Committee expected a continuation of a rapid rate of inflation over the period to the second quarter of 1979—in the view of several members, even more rapid than the pace projected by the staff. It was observed that in 1979 strong pressures for large increases in wages would tend to spread throughout the economy from the many industries in which new contracts would be negotiated. It was also noted that minimum wage rates and social security taxes were scheduled to go up again at the beginning of the new year, exerting upward pressure on costs and prices.

Most members of the Committee thought that the unemployment rate a year ahead, in the second quarter of 1979, would be little changed from the average rate in recent months, which was well below the level that had been expected earlier. It was suggested that the rate of participation in the labor force would continue to rise, in part because of the pressure of inflation on family budgets.

At this meeting the Committee reviewed its 12-month ranges for growth in the monetary aggregates. At its meeting in April 1978 the Committee had specified the following ranges for the period from the first quarter of 1978 to the first quarter of 1979: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for growth in commercial bank credit was 7½ to 10½ per cent. The ranges being considered at this meeting were for the period from the second quarter of 1978 to the second quarter of 1979.

The Committee members differed principally in their preferences for the 12-month range for *M*-1: A majority favored retention of the existing range, while a number favored an increase in its upper limit. In the case of the broader aggregates, most members expressed a preference for retaining the existing ranges; one member suggested that the lower limits be reduced by ½ of a percentage point, yielding ranges of 6 to 9 per cent for *M*-2 and 7 to 10 per cent for *M*-3.

An increase in the upper limit of the range for *M*-1 was advocated on the expectation that, over the coming year, growth of *M*-1 would have to exceed the 6½ per cent upper limit of the existing range,

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as it had over the past year, if strains in the financial markets were not to be so severe as to threaten an economic downturn. That expectation was based on the probable rates of inflation and on the recent behavior of the income velocity of money. In this connection it was emphasized that the high rate of inflation in prospect for the quarters immediately ahead was attributable in part to governmental actions and to some strong forces in the private sector—including the effects of the depreciation of the dollar—that were not likely to be moderated appreciably by the stance of monetary policy. In these circumstances, it was argued, the Committee ought to raise the upper limit of the range for *M*-1 to allow for a growth rate that—given upward cost pressures on prices—was more nearly consistent with the generally anticipated rate of growth in real and nominal GNP for the year ahead and that, consequently, was more likely to be achieved.

Several arguments were advanced in favor of retaining the existing range of 4 to 6½ per cent for *M*-1. First, *M*-1 growth in the second quarter—at an annual rate of 9½ per cent, on a quarterly-average basis—had exceeded the upper limit of the Committee's range by a considerable margin, so that retention of the existing range for the year from the second quarter of 1978 to the second quarter of 1979 would allow for growth considerably faster than 6½ per cent over the five-quarter period beginning the first quarter of 1978. Second, for a considerable period of time growth in *M*-1 on the average had exceeded the range adopted by the Committee and a reduction of growth to a rate within the existing range would be an important step toward moderating inflation. Also, such a reduction would have a positive effect on the economic outlook.

Moreover, any increase in the range could be misleading: Such an action, no matter what reasons might be offered for it, was likely to be interpreted both in this country and abroad as a signal of a shift in System policy toward less emphasis on fighting inflation. Since that was not the case, it would be consistent to retain the existing range, although the rate of growth over the period might be around the upper limit of the range. The members also noted that authorization for automatic transfers of funds into checking accounts from savings deposits at commercial banks was scheduled to become effective on November 1, 1978, and that

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during a transition period such transfers would tend to reduce the demand for *M*-1 and increase its income velocity.

With regard to *M*-2 and *M*-3, it was observed that growth over the year ending in the second quarter of 1978 had been within the Committee's longer-run ranges. One member proposed that in formulating policy for the period ahead the Committee begin to increase the emphasis given to *M*-2 and reduce that given to *M*-1. That proposal did not attract support from other members of the Committee.

At the conclusion of its discussion the Committee decided to retain the existing ranges for the monetary aggregates. Thus, the ranges for the period from the second quarter of 1978 to the second quarter of 1979 were 4 to 6½ per cent for *M*-1, 6½ to 9 per cent for *M*-2, and 7½ to 10 per cent for *M*-3. The associated range for growth in commercial bank credit was raised to 8½ to 11½ per cent in recognition of the greater share of borrower demands being directed toward banks. It was agreed that the longer-run ranges, as well as the particular aggregates for which longer-run ranges were specified, would be subject to review and modification at subsequent meetings. It was also understood that short-run factors might cause growth rates from one month to the next to fall outside the ranges anticipated for the year ahead.

> The Committee adopted the following ranges for rates of growth in monetary aggregates for the period from the second quarter of 1978 to the second quarter of 1979: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for bank credit is 8½ to 11½ per cent.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Wallich, Willes, and Winn. Votes against this action: Messrs. Jackson and Partee. Absent and not voting: Mr. Gardner.

Messrs. Jackson and Partee dissented from this action because they preferred to raise the upper limit of the range for *M*-1 to a level more nearly consistent with the anticipated growth in GNP—Mr. Jackson, to 7½ per cent; Mr. Partee, to 8 per cent.

In the discussion of policy for the period immediately ahead, the members differed mainly in their views as to whether, and

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to what degree, additional firming in money market conditions should be sought during the next few weeks for the purpose of restraining monetary growth in coming months. No sentiment was expressed for easing money market conditions.

Several members proposed that for the time being operations be directed toward maintaining the money market conditions currently prevailing. It was argued that, in light of increased uncertainties in the economic outlook, such a "pause" would afford the Committee an opportunity to evaluate additional evidence on the current situation and outlook. It was suggested that, coming on top of the considerable firming in money market conditions over the past year or so, further significant firming would risk bringing on a recession. It was also observed that the restraining effects of the rise in interest rates over the past month had not yet been fully felt and that any additional firming that might be appropriate could be achieved at a later time.

On the other hand, a number of members favored a prompt further firming of money market conditions. Such a course was needed, it was suggested, to bring growth in *M*-1 within the Committee's longer-run range. Given the rate of inflation, it was argued, current levels of interest rates were relatively low and were much less restrictive in real terms than their nominal levels might suggest. And the point was made that failure to pursue additional firming at this time might well create a need for a greater degree of firming later.

In considering the ranges for the annual rates of growth in the monetary aggregates to be specified for the July–August period, the members took account of the indications that growth in *M*-1 might accelerate in July. Most members preferred ranges of tolerance for growth in *M*-1 over the 2-month period extending from a lower limit of 4 or 5 per cent to an upper limit of 8 or 9 per cent. One favored a higher range, from 5 to 10 per cent, and another a lower range, from 3 to 7 per cent. For *M*-2, most members favored ranges extending from 6 or 7 per cent to 10 or 11 per cent; one member preferred a range of 5 to 10 per cent.

With respect to the Federal funds rate, most members favored ranges centered either on 7¾ per cent, the midpoint of the 7½ to 8 per cent range specified at the June meeting, or on the somewhat higher level that had developed in the most recent days;

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their proposals included ranges having a lower limit of 7½ per cent or slightly above, and an upper limit of 8 per cent or slightly above. However, a number of members advocated a range centered on 8 per cent and extending from 7¾ to 8¼ per cent. A majority of the members favored giving greater weight than usual to money market conditions in the conduct of open market operations until the next meeting.

At the conclusion of the discussion the Committee decided that operations in the period immediately ahead should be directed toward maintaining the weekly-average Federal funds rate within a range of 7¾ to 8 per cent. The members agreed that, in deciding on the specific objective for the Federal funds rate, the Manager should be guided mainly by the relation between the latest estimates of annual rates of growth in *M*-1 and *M*-2 over the July–August period and the following ranges of tolerance: 4 to 8 per cent for *M*-1 and 6 to 10 per cent for *M*-2. It was also agreed that if, giving approximately equal weight to *M*-1 and *M*-2, their rates of growth appeared to be close to or beyond the limits of the indicated ranges, the Manager should raise or lower the objective for the funds rate in an orderly fashion within its range.

As is customary, 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.

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 economic activity has slowed in recent months. Following substantial gains in March and April, increases in industrial production and nonfarm payroll employment moderated in May and June and retail sales changed little. In June, however, the unemployment rate dropped 0.4 of a percentage point to 5.7 per cent. Average producer prices rose somewhat less rapidly in May and June than earlier in 1978, but over the first half of this year prices increased at a considerably faster rate than they had on the average during 1977. The advance in the index of average hourly earnings also moderated in May and June but was at a somewhat faster pace over the first half of 1978 than during 1977.

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Since mid-June the trade-weighted value of the dollar against major foreign currencies has declined further to its lowest level of the year. The U.S. trade deficit in May was lower than the very high rate of the first 4 months of the year.

Growth in *M*-1 moderated in May and June, but reflecting the extraordinarily rapid pace in April, growth from the first to the second quarter was relatively high. Growth in *M*-2 and *M*-3 has been moderate over recent months. In June inflows of small-denomination time deposits to commercial banks and other thrift institutions picked up, following introduction of the new 6-month certificate. Market interest rates have risen further in recent weeks. On June 30 an increase in Federal Reserve discount rates from 7 to 7¼ per cent was announced.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster monetary and financial conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions. The Committee agreed that these objectives would be furthered by growth of *M*-1, *M*-2, and *M*-3 from the second quarter of 1978 to the second quarter of 1979 at rates within ranges of 4 to 6½ per cent, 6½ to 9 per cent, and 7½ to 10 per cent, respectively. The associated range for bank credit is 8½ to 11½ per cent. These ranges are subject to reconsideration at any time as conditions warrant.

In the short run, the Committee seeks to achieve bank reserve and money market conditions that are broadly consistent with the longer-run ranges for monetary aggregates cited above, while giving due regard to developing conditions in financial markets more generally. During the period until the next regular meeting, System open market operations shall be directed at maintaining the weekly-average Federal funds rate within the range of 7¾ to 8 per cent. In deciding on the specific objective for the Federal funds rate the Manager shall be guided mainly by the relationship between the latest estimates of annual rates of growth in the July–August period of *M*-1 and *M*-2 and the following ranges of tolerance: 4 to 8 per cent for *M*-1 and 6 to 10 per cent for *M*-2. If, giving approximately equal weight to *M*-1 and *M*-2, their rates of growth appear to be close to or beyond the upper or lower limits of the indicated ranges, the objective for the funds rate shall be raised or lowered in an orderly fashion within its range.

If the rates of growth in the aggregates appear to be above the upper limit or below the lower limit of the indicated ranges at a time when the objective for the funds rate has already been moved

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to the corresponding limit of its range, the Manager is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

> Votes for this action: Messrs. Miller, Volcker, Coldwell, Eastburn, Jackson, Partee, and Wallich. Votes against this action: Messrs. Baughman, Willes, and Winn. Absent and not voting: Mr. Gardner.

Messrs. Baughman, Willes, and Winn dissented from this action because they favored more vigorous measures to curb the rates of growth in the monetary aggregates. All three preferred a directive that would have instructed the Manager to direct operations initially toward an increase in the Federal funds rate to 8 per cent and that would have provided for a further increase in the rate to a level of 8¼ per cent, if growth in the monetary aggregates over the July–August period appeared to be strong relative to the specified ranges. In addition, Mr. Willes favored specifying a 2-month range for *M*-1 of 3 to 7 per cent, somewhat lower than the range agreed upon by the majority.

2. Authorization for Domestic Open Market Operations

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 April 30, 1978, 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 the enactment of expected legislation extending the authority.

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MEETING HELD ON AUGUST 15, 1978

Domestic Policy Directive

The information reviewed at this meeting suggested that real output of goods and services was growing moderately in the current quarter, although the rate of expansion appeared to be a little below the average pace in the first two quarters of the year. The rise in prices—as measured by the fixed-weighted price index for gross domestic business product—seemed to have slowed appreciably from the second-quarter rate but was still well above the rise in other recent quarters.

Staff projections for the year ending in the second quarter of 1979 were little changed from a month earlier. They continued to suggest that output would grow at a moderate pace, with the unemployment rate projected to decline slightly from its July level. The rate of inflation was expected to remain rapid but to moderate considerably from its pace in the second quarter of 1978.

In July the index of industrial production increased an estimated 0.5 per cent, equal to the gains now indicated for May and June but well below the rapid advances in March and April. Total nonfarm payroll employment rose in July at close to the May–June pace, after exceptional gains in March and April. In manufacturing, employment rose slightly in July while the average workweek was unchanged. The over-all unemployment rate jumped 0.5 of a percentage point, following a decline of 0.4 of a percentage point in June; the July level of 6.2 per cent was about the same as the average in the first 5 months of the year.

In June, private housing starts exceeded an annual rate of 2 million units for the fourth consecutive month. Starts averaged 2.1 million units in the second quarter, about the same as in the second half of 1977 and well above the rate for the first quarter of 1978.

Total retail sales changed little in July for the third consecutive

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month following exceptional gains earlier in the year. Unit sales of new automobiles fell somewhat in July from the very rapid pace in the second quarter, while dollar sales of other durable goods rose considerably further.

The index of average hourly earnings for private nonfarm production workers increased at an annual rate of nearly 10 per cent in July; over the first 7 months of the year the index had risen at an annual rate of close to 9 per cent, considerably above its advance in 1977. The rise in average prices of producer goods moderated somewhat in July as prices of consumer goods declined after moving up rapidly in most earlier months of the year. In June the consumer price index for all urban consumers continued to rise at a rapid pace; over the first half of the year the index advanced at an annual rate of more than 10 per cent.

In foreign exchange markets the trade-weighted value of the dollar had declined nearly 6 per cent further since mid-July to a level about 10 per cent below the 1978 peak in May. The downward pressure on the dollar appeared to reflect widespread concern about the outlook for inflation in the United States and the persistence of large imbalances in the international payments positions of the United States and some of its major trading partners. The U.S. trade deficit, however, had declined in the second quarter from an extraordinarily high rate in the first quarter.

Following a substantial slowdown in June, the expansion in total credit at U.S. commercial banks accelerated in July to a pace close to the unusually rapid growth experienced in April and May. Expansion in bank loans was very strong in July and included growth in all major loan categories. Banks also made sizable additions to their holdings of U.S. Treasury and other securities. While growth in business loans was above the reduced pace in June, it remained well below the average rate in the first half of the year. Outstanding commercial paper of nonfinancial businesses continued to expand rapidly in July.

Growth of the narrowly defined money supply (*M*-1) remained moderate in July. Growth in *M*-2 and *M*-3 also continued moderate, as substantial inflows of funds into large-denomination time deposits at banks and into the new money market certificates at nonbank thrift institutions were partly offset by weakness in savings and small-denomination time deposits.

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At its meeting on July 18 the Committee had decided that the ranges of tolerance for the annual rates of growth in *M*-1 and *M*-2 during the July–August period should be 4 to 8 per cent and 6 to 10 per cent, respectively. The Committee had agreed that during the coming inter-meeting period operations should be directed toward maintaining the weekly-average Federal funds rate within a range of 7¾ to 8 per cent. It was also agreed that if, with approximately equal weight given to *M*-1 and *M*-2, growth rates of the aggregates appeared to be close to or beyond the limits of the indicated ranges, the objective for the funds rate was to be raised or lowered in an orderly fashion within its specified range.

Following the July 18 meeting the Manager of the System Open Market Account sought bank reserve conditions consistent with a weekly-average Federal funds rate somewhat above 7¾ per cent. Data that became available throughout the inter-meeting interval suggested that growth in the monetary aggregates over the July–August period would be well within the Committee's ranges and the Manager continued to seek conditions consistent with a Federal funds rate within a range of 7¾ to 8 per cent. The average rate during the inter-meeting period was about 7⅞ per cent.

Market interest rates on most short- and long-term securities had declined 10 to 30 basis points since mid-July. The fall in rates apparently reflected a shift in expectations that was influenced by the recent pattern of moderate growth in the monetary aggregates, a smaller rise in the Federal funds rate than many had anticipated, and signs of some slowing in economic expansion. Declines in Treasury bill rates were also encouraged by sizable investments by foreign central banks of dollars obtained in currency support operations.

Conditions in mortgage markets, which had tightened significantly during the first half of the year, had stabilized in recent weeks. Interest rates on new commitments for conventional mortgage loans at savings and loan associations had changed little during the inter-meeting period, while yields in the secondary market for home mortgages had declined in line with reductions in most other market rates.

In the Committee's discussion of the economic situation, there was general agreement that the outlook for economic activity had changed little since the July meeting, and that in the year ending

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with the second quarter of 1979 output of goods and services was most likely to grow at about the moderate pace projected by the staff. This judgment was qualified by the recognition that the weakness of the dollar in foreign exchange markets might have unfavorable repercussions on the domestic economy.

Committee members who differed with the staff economic projection all expected average growth to be a little less than the staff figure. A few members, while anticipating somewhat greater growth than the staff was projecting for the last half of 1978, continued to believe that growth in 1979 would slow more abruptly.

Several members noted that although economic growth had moderated recently, the pattern of expansion appeared to be well balanced. In their judgment none of the key economic sectors was exhibiting either serious sluggishness or unsustainably rapid growth; there was little evidence of developing capacity constraints and inventory surpluses were not a problem.

One negative element in this pattern, which seriously concerned all members of the Committee, was the unexpectedly high recent rate of inflation in prices and wages and the related possibility that an appreciable slowing of inflation would prove more difficult to achieve than previously had been anticipated. It was observed in this connection that the declining value of the dollar in foreign exchange markets was contributing significantly to inflation in the United States. Nearly all the Committee members expected price increases for the year ahead to be more rapid than the staff was projecting.

One member suggested that although the economy appeared to be fairly well balanced by the usual standards, there were potential problem areas: He identified the heavy reliance of consumers on credit to finance their spending; growing, if still limited, capacity constraints and materials shortages; and, of particular concern to him, the likely inflationary effects of impending wage settlements. Because of these generally strong inflationary pressures, he thought the risks of an early end to the expansion had become greater.

Other members of the Committee suggested that an important change in the outlook since the July meeting was an apparent stiffening in the resolve of labor leaders to hold out in forthcoming contract negotiations for sizable wage settlements. One member also cited apparent efforts by some businessmen to accelerate

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increases in wages and prices because of their concern that controls might be imposed.

Committee members differed little in their estimates of the likely unemployment rate in the second quarter of 1979. Those estimates were all relatively close to the average rate thus far in 1978. It was suggested that productivity would show little increase over the projection period.

At its meeting in July the Committee had agreed that from the second quarter of 1978 to the second quarter of 1979 average rates of growth in the monetary aggregates within the following ranges appeared to be consistent with broad economic aims: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for the rate of growth in commercial bank credit was 8½ to 11½ per cent. It had also been agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings.

In the discussion of policy for the period immediately ahead, most members expressed a preference for some slight firming of money market conditions. Several members emphasized the need to restrain the expansion of the monetary aggregates, especially in light of current and prospective inflationary pressures. It was suggested that an indication at this time of the System's continued determination to resist inflation would have a favorable impact on confidence, both in the domestic economy and in foreign exchange markets. With regard to the latter, the members were seriously concerned about the weakness of the dollar. They recognized that interrelated governmental actions would be needed to make progress in this area.

No sentiment was expressed at this meeting for an easing of money market conditions. On the other hand, it was suggested that a sharp move toward restraint under present circumstances might incur an undue risk of precipitating a recession. Two members preferred to retain current money market conditions for the time being.

There were only small differences among most Committee members in their preferences for operating specifications for the period immediately ahead. They were nearly unanimous in favoring a return to basing decisions for open market operations between

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meetings primarily on the behavior of the monetary aggregates. In its previous directive the Committee had called for giving greater weight than usual to money market conditions.

For the annual rate of growth in *M*-1 over the August–September period, most members favored ranges of 4 to 8 per cent or 5 to 9 per cent, but two members also found acceptable a range of 3 to 8 per cent and one preferred a lower range of 3 to 7 per cent. For *M*-2 most members advocated ranges of 6 to 10 per cent or 6½ to 10½ per cent and one proposed a range of 6 to 11 per cent. One member preferred narrower ranges for both *M*-1 and *M*-2 that would be relatively close to the 12-month ranges adopted by the Committee; for *M*-1 he suggested a range of 5½ to 7½ per cent and for *M*-2 a range of 6½ to 8½ or 9 per cent. Other members, while preferring wider 2-month ranges, also felt that those ranges should more or less encompass the 12-month ranges in order to facilitate achievement of the Committee's objectives.

Most of the members favored directing open market operations toward a Federal funds rate of about 8 per cent shortly after today's meeting, but two members urged some delay in order to assess further information on the monetary aggregates and developments in foreign exchange markets. One member preferred to continue aiming initially for a Federal funds rate of around 7⅞ per cent in light of uncertainties about the economic outlook and the related performance of the monetary aggregates.

With respect to the inter-meeting range for the Federal funds rate, all but two members favored 7¾ to 8¼ per cent; one preferred 8 to 8¼ per cent and another 7¾ to 8½ per cent. The latter member felt that more leeway should be provided for raising the rate in the event that the monetary aggregates appeared to be growing rapidly in relation to the Committee's preferences for the August–September period. However, a majority of the members indicated that they did not want to see the Federal funds rate exceed 8¼ per cent without further assessment of new developments and the opportunity for consultation among the members.

At the conclusion of the discussion the Committee decided that ranges of tolerance for the annual rates of growth in *M*-1 and *M*-2 over the August–September period should be 4 to 8 per cent and 6 to 10 per cent, respectively. With regard to the Federal funds

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rate, the Manager was instructed to seek a rate of around 8 per cent early in the period following today's meeting. Subsequently, if the 2-month growth rates of *M*-1 and *M*-2 appeared to be significantly above or below the midpoints of the indicated ranges, the objective for the funds rate was to be raised or lowered in an orderly fashion within a range of 7¾ to 8¼ per cent. It was also agreed that in assessing the behavior of the aggregates, the Manager should give approximately equal weight to the behavior of *M*-1 and *M*-2.

The Committee decided to include in its directive a reference to developments in foreign exchange markets as well as the usual reference to conditions in domestic financial markets. The purpose of the added instruction was to provide the Manager with some flexibility to adjust the nature and timing of his operations in light of possible pressures on the dollar in foreign exchange markets.

As is customary, 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.

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 growing moderately in the current quarter, although the pace is a little less than the average for the first two quarters of the year. In July retail sales remained at about the advanced level reached in April. Industrial production and nonfarm payroll employment continued to expand at lower rates than in the early spring months. The unemployment rate, which had dropped 0.4 of a percentage point in June, jumped 0.5 of a percentage point in July to 6.2 per cent, about the average rate in the first 5 months of the year. Average prices of goods and services have continued to rise rapidly, although producer prices of foods and foodstuffs declined in July. The advance in the index of average hourly earnings has been somewhat faster so far in 1978 than it had been on the average during 1977.
>
> Since mid-July the trade-weighted value of the dollar against major foreign currencies has declined sharply further. The U.S. trade deficit was lower in the second quarter than the very high rate of the first quarter.

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Growth in *M*-1 remained moderate in July. Inflows of the interest-bearing deposits included in *M*-2 and *M*-3 picked up, owing to substantial flows into large-denomination time deposits at banks and into the new money market certificates at nonbank thrift institutions. Nevertheless, expansion in the broader aggregates also remained moderate in July. Most market interest rates have declined appreciably on balance in recent weeks.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster monetary and financial conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions. At its meeting on July 18, 1978, the Committee agreed that these objectives would be furthered by growth of *M*-1, *M*-2, and *M*-3 from the second quarter of 1978 to the second quarter of 1979 at rates within ranges of 4 to 6½ per cent, 6½ to 9 per cent, and 7½ to 10 per cent, respectively. The associated range for bank credit is 8½ to 11½ per cent. These ranges are subject to reconsideration at any time as conditions warrant.

In the short run, the Committee seeks to achieve bank reserve and money market conditions that are broadly consistent with the longer-run ranges for monetary aggregates cited above, while giving due regard to developing conditions in domestic and international financial markets more generally. Early in the period until the next regular meeting, System open market operations shall be directed at attaining a weekly-average Federal funds rate slightly above the current level. Subsequently, operations shall be directed at maintaining the weekly-average Federal funds rate within the range of 7¾ to 8¼ per cent. In deciding on the specific objective for the Federal funds rate the Manager shall be guided mainly by the relationship between the latest estimates of annual rates of growth in the August–September period of *M*-1 and *M*-2 and the following ranges of tolerance: 4 to 8 per cent for *M*-1 and 6 to 10 per cent for *M*-2. If, giving approximately equal weight to *M*-1 and *M*-2, their rates of growth appear to be significantly above or below the midpoints of the indicated ranges, the objective for the funds rate shall be raised or lowered in an orderly fashion within its range.

If the rates of growth in the aggregates appear to be above the upper limit or below the lower limit of the indicated ranges at a time when the objective for the funds rate has already been moved to the corresponding limit of its range, the Manager is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

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Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Gardner, Jackson, Wallich, and Winn. Votes against this action: Messrs. Partee and Willes.

Mr. Partee dissented from this action because he favored a 2-month range of tolerance for growth in *M*-1 that was somewhat higher than the range advocated by the majority. He did not believe that a further move toward firmer money market conditions was warranted unless monetary expansion proved to be distinctly on the high side, especially in view of the marked slowing in real economic growth that now appeared to be in progress.

Mr. Willes dissented because he favored a more vigorous effort to curb the expansion of the monetary aggregates in light of current and expected inflationary pressures in the domestic economy and the weakness of the dollar in foreign exchange markets. He preferred to specify a 2-month range of tolerance for *M*-1 below the range agreed upon by the majority.

Subsequent to the meeting, on September 8, the Committee held a telephone conference meeting pursuant to its decision on August 15 to consult further if the rates of growth in the monetary aggregates appeared to be above or below the limits of the Committee's ranges of tolerance for the August–September period and the Federal funds rate had already moved to the corresponding limit of its range. The latest staff projections suggested that *M*-1 and *M*-2 would grow at annual rates of 9.0 and 11.3 per cent, respectively, over the August–September period; the ranges of tolerance established at the August 15 meeting were 4 to 8 per cent for *M*-1 and 6 to 10 per cent for *M*-2. The Manager had been aiming for a funds rate of about 8¼ per cent, the top of the range that the Committee had specified at its August meeting, and the average rate in each of the two latest statement weeks was at about that level.

Against this background, the Committee decided to raise the upper limit of the range for the Federal funds rate to 8½ per cent and to instruct the Manager to aim promptly for a weekly-average Federal funds rate of about 8⅜ per cent. It was understood that the funds rate might be raised to the upper limit of the range if new data suggested that the aggregates were strengthening further,

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or be reduced slightly if such data suggested significant weakening from current projections.

On September 8, 1978, the Committee modified the domestic policy directive adopted at its meeting of August 15, 1978, by increasing the upper limit of the 7¾ to 8¼ per cent range specified for the Federal funds rate to 8½ per cent and by calling for operations directed at raising the weekly-average Federal funds rate promptly to 8⅜ per cent.

Votes for this action: Messrs. Miller, Volcker, Coldwell, Eastburn, Gardner, Jackson, Partee, Willes, Winn, and Kimbrel. Votes against this action: None. Absent and not voting: Messrs. Baughman and Wallich. (Mr. Kimbrel voted as alternate for Mr. Baughman.)

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MEETING HELD ON SEPTEMBER 19, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested that real output of goods and services had been growing moderately in the current quarter, but the rate of expansion appeared to be somewhat below the average annual rate of about 4 per cent estimated by the Commerce Department for the first two quarters of the year. The rise in average prices—as measured by the fixed-weight price index for gross domestic business product—slowed considerably from the exceptional pace in the second quarter, but the rise was still relatively rapid.

Staff projections for the period from the current quarter through the second quarter of 1979 were little changed from those of a month earlier. They continued to suggest that output would grow moderately over the period and that the rate of inflation would be rapid, although considerably below the average pace in the first two quarters of 1978. The unemployment rate was expected to change little from its August level.

In August the index of industrial production increased an estimated 0.5 per cent, close to the moderate gains in the preceding 3 months but well below the large increases in March and April. Nonfarm payroll employment rose further in August, but the gain was about half the monthly increase in the preceding 3 months. In manufacturing, employment declined somewhat and the average workweek continued to change little at a relatively high level. The unemployment rate fell 0.3 of a percentage point to 5.9 per cent, a rate slightly below the average in the first 7 months of the year.

Total private housing starts edged down in July. At an annual rate of nearly 2.1 million units, however, starts were close to the pace in the second quarter of 1978 and in the second half of 1977.

The latest Department of Commerce survey of business plans, taken in late July and August, suggested that spending for plant

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and equipment would be 12.3 per cent greater in 1978 than in 1977, a somewhat larger increase than had been indicated 3 months earlier. Businesses spent more in the second quarter of 1978 than had been anticipated, and the latest survey still implied less expansion in spending over the second half of the year than over the first half.

The dollar value of total retail sales rose in August, but the increase followed a decline now indicated for July; on balance sales had changed little since April. Unit sales of new automobiles, which had declined in July, recovered in August almost to the advanced pace of the second quarter.

The index of average hourly earnings for private nonfarm production workers rose little in August following a substantial increase in July; over the first 8 months of the year the index advanced at an annual rate of about 8 per cent, somewhat more than it had during 1977. Declines in prices of food products contributed to a moderation in the rise of the consumer price index in July and to a slight reduction in average prices of producer finished goods in August; both price measures had risen at very rapid rates in the first half of the year.

The trade-weighted value of the dollar against major foreign currencies, which had declined sharply in early August, subsequently recovered against a background of uncertain conditions in exchange markets. The recovery was triggered early in the intermeeting period by expressions of concern by U.S. officials, and was reinforced by subsequent increases in U.S. short-term interest rates and the announcement of expanded gold sales by the U.S. Treasury. However, the dollar weakened in late August, when it was announced that the U.S. trade deficit had increased sharply in July, and at the time of this meeting the dollar was somewhat below its level at the end of July.

After a surge in July, total credit at U.S. commercial banks expanded at a substantially slower rate in August, mainly because of large declines in bank holdings of U.S. Treasury securities and in security loans. Growth in business loans accelerated further but remained well below the average rate in the first half of 1978. Outstanding commercial paper of nonfinancial businesses contracted slightly, following a sharp expansion in June and July.

Growth of the narrowly defined money supply (*M*-1), which had

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been at an average annual rate of about 5¾ per cent in June and July, picked up in August to a rate of about 7¾ per cent, roughly the same as the average in the first two quarters of the year.[1] Weekly data suggested a further pick-up in September. Inflows of the interest-bearing deposits included in *M*-2 and *M*-3 also accelerated somewhat in August, reflecting primarily substantial flows of funds into large-denomination time deposits at banks and into the 6-month money market certificates at nonbank thrift institutions. As a result, growth in the broader monetary aggregates was relatively rapid.

At its meeting on August 15 the Committee had decided on ranges of tolerance for the annual rates of growth in *M*-1 and *M*-2 over the August–September period of 4 to 8 per cent and 6 to 10 per cent, respectively. The Committee had agreed that early in the coming inter-meeting period operations should be directed toward a Federal funds rate of around 8 per cent. Subsequently, if the 2-month growth rates of *M*-1 and *M*-2 appeared to be significantly above or below the midpoints of the indicated ranges, the objective for the funds rate was to be raised or lowered in an orderly fashion within a range of 7¾ to 8¼ per cent.

Immediately following the August 15 meeting the Manager of the System Open Market Account began to seek bank reserve conditions consistent with an increase in the weekly-average Federal funds rate to around 8 per cent. Later in August, incoming data suggested that growth in *M*-1 would be at the upper limit of the range specified by the Committee and that growth in *M*-2 would be close to the upper limit of its range. Accordingly, the Manager sought reserve conditions consistent with a further increase in the Federal funds rate to 8¼ per cent, the upper limit of the 7¾ to 8¼ per cent range specified for the inter-meeting period.

In early September, available data suggested that both *M*-1 and *M*-2 would grow at rates significantly above the upper limits of their respective ranges. With the Federal funds rate already at its upper limit, the Committee decided on September 8, at a telephone

[1] Revised measures of the monetary aggregates, reflecting new benchmark data for deposits at nonmember banks and certain technical adjustments, were available to the Committee at the time of this meeting and were published on September 21, 1978. On the basis of these revised figures, the annual rate of growth in *M*-1 was about 8¾ per cent in August and about 8 per cent on the average in the first two quarters of the year.

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conference meeting, to raise the upper limit of the range for the Federal funds rate to 8½ per cent and to instruct the Manager to aim promptly for a weekly-average Federal funds rate of about 8⅜ per cent. In the days remaining before this meeting the funds rate fluctuated around 8⅜ per cent.

The rise in the Federal funds rate during the inter-meeting period was accompanied by appreciable increases in rates on other short-term market instruments. Yields on long-term securities, however, generally edged down. In mid-September commercial banks raised the rate on loans to prime business borrowers from 9¼ to 9½ per cent.

On August 18 the Board of Governors announced an increase in Federal Reserve discount rates from 7¼ to 7¾ per cent. In announcing the increase, the Board stated that the action had been taken in view of recent disorderly conditions in foreign exchange markets as well as the continuing serious domestic inflationary problem.

Conditions in residential mortgage markets, which had tightened significantly during the first half of the year and then stabilized, apparently had eased somewhat in recent weeks. Interest rates on new commitments for conventional home mortgage loans at savings and loan associations edged down during the inter-meeting interval, and yields in the secondary mortgage market declined moderately.

In the Committee's discussion of the economic situation and outlook, the members generally concurred with the staff's view that real output of goods and services would grow at a moderate pace over the period from the second quarter of 1978 to the second quarter of 1979. At the same time, a number of members anticipated a little less growth than the staff projected and one anticipated a little more. The observation was made that even a slight shortfall in growth of output from the rate projected by the staff implied an upward drift in the unemployment rate.

All members of the Committee expected a continuation of a rapid rate of inflation over the period to the second quarter of 1979—in the view of several members, even more rapid than the pace projected by the staff. As at other recent meetings, it was observed that in 1979 pressures for large increases in wage rates would be strong. It was also noted that in the near future the administration was expected to announce a new anti-inflation program and that

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the way in which such a program was perceived by businessmen and consumers could have a considerable impact on attitudes and expectations.

Although the members differed little in their assessments of the most likely rate of growth in output over the next few quarters, some of them called attention to elements of potential weakness or strength in the current situation that could contribute to a different outcome. One member observed, for example, that the business expansion, having endured for a long time by historical standards, was exhibiting some signs of potential weaknesses that were to be expected at this stage. On the other hand, this member also saw some indications of a pick-up in business activity in other industrial countries that might be of sufficient magnitude to raise demands for U.S. exports significantly—thereby enhancing growth in output in this country, strengthening the dollar in foreign exchange markets, and contributing generally to improvement in confidence.

A second member saw little, if any, evidence of the major cyclical imbalances that characteristically developed during business expansions and brought on downturns in activity. Therefore, the expansion appeared likely to continue. However, the very high rate of inflation at present was seen as the main threat to a sustained expansion.

Another member, noting that a recent survey had pointed to some deterioration in business assessments of prospects for their own companies as well as for the economy as a whole, suggested that business investment spending in 1979—especially for fixed capital, but also for inventories—could prove to be disappointing. And with respect to fiscal policy, a member observed that the Federal budget on the high employment basis had recently swung in the direction of restraint, and that the stimulative impact of the prospective reduction in Federal taxes would depend heavily on final decisions concerning both its composition and its timing.

The one member who anticipated slightly faster growth than the staff projected for the period through the first half of 1979 expressed concern about certain developments that could have adverse consequences further in the future. Specifically, the current high rate of construction of commercial buildings and of apartment houses could lead to an excessive supply of such facilities and to a

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consequent drop in construction. At about the same time, in this member's view, a sharp cyclical downswing in credit-financed buying of certain consumer durable goods might develop.

At its meeting in July the Committee had agreed that from the second quarter of 1978 to the second quarter of 1979 average rates of growth in the monetary aggregates within the following ranges appeared to be consistent with broad economic aims: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for the rate of growth in commercial bank credit was 8½ to 11½ per cent. It had also been agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings.

In the discussion of policy for the period immediately ahead, considerable concern was expressed about recent rates of monetary growth. It was observed that for an extended period of time *M*-1 had been growing at rates in excess of the longer-run range adopted by the Committee and that a slowing of growth was necessary in pursuit of the Committee's objective of resisting inflationary pressures while encouraging continued moderate economic expansion. Most members believed that some additional firming in money market conditions during the next few weeks was needed to help assure a slowing in growth of money over the months ahead, although they differed with respect to the degree of firming that they thought the Committee ought to contemplate.

In this connection, the comment was made that current levels of interest rates were not exerting as much restraint on credit flows as might be supposed. Thus, it was observed, interest rates adjusted for expected rates of inflation were not high and might even be negative. Moreover, the degree of nonprice rationing of credit, particularly credit for housing, had been reduced by such structural changes in the financial system as the introduction of the 6-month money market certificates.

Two members, stressing the magnitude of the increases in interest rates that had already occurred, proposed that for the time being operations be directed toward maintaining the money market conditions currently prevailing. It was argued that, in light of the recent slowing of the expansion in economic activity and of uncertainties in the economic outlook, such a "pause" would afford the Com-

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mittee an opportunity to evaluate additional evidence on the current situation, including the effects of the recent increases in interest rates. It was observed that, historically, growth in output had never been held at about its trend rate for very long and that further increases in interest rates at this time might slow growth to a rate below trend or might even provoke an actual downturn.

With respect to operating specifications for the period immediately ahead, the most frequently proposed ranges for the annual rate of growth in *M*-1 over the September–October period were 4 to 8 per cent and 5 to 9 per cent; a narrower range of 6 to 8 per cent was also suggested. A few members proposed somewhat higher ranges—in at least one case, because the lower ranges in combination with the strong growth indicated for September implied more of a moderation of growth in October than appeared likely. One member advocated a lower range. For *M*-2, the most common range suggested was 6 to 10 per cent. Some members advocated somewhat higher ranges, indicating, in a few cases, a willingness to accept the continuing effects that the introduction of the 6-month money market certificate was having on expansion of time deposits at commercial banks.

Most of the members favored directing open market operations toward an increase in the Federal funds rate to about 8½ per cent shortly after this meeting. In general, these members favored an inter-meeting range of 8¼ to 8¾ per cent, but two of them were willing to accept, and another advocated, an upper limit of 9 per cent. One member proposed directing open market operations toward an increase in the funds rate to 8¾ per cent early in the period and setting an inter-meeting range of 8½ to 9¼ per cent. And the two members who indicated a preference for maintenance of the prevailing money market conditions suggested an inter-meeting range of 8¼ to 8½ per cent.

At the conclusion of the discussion the Committee decided that ranges of tolerance for the annual rates of growth in *M*-1 and *M*-2 over the September–October period should be 5 to 9 per cent and 6½ to 10½ per cent, respectively. With regard to the Federal funds rate, the Manager was instructed to seek a rate of around 8½ per cent early in the period until the next regular meeting. Subsequently, if the 2-month growth rates of *M*-1 and *M*-2 appeared to be significantly above or below the midpoints of the indicated

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ranges, the objective for the funds rate was to be raised or lowered in an orderly fashion within a range of 8¼ to 8¾ per cent. It was also agreed that in assessing the behavior of the aggregates, the Manager should give approximately equal weight to the behavior of *M*-1 and *M*-2.

As is customary, 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.

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 has grown moderately in the current quarter, although the pace is somewhat below the average for the first two quarters of the year. In August the dollar value of total retail sales rose, after having declined in July, but remained close to the level reached in April. Industrial production continued to expand at about the moderate pace of the preceding 3 months, and nonfarm payroll employment rose somewhat further. The unemployment rate declined from 6.2 to 5.9 per cent, slightly below the average rate in the first 7 months of the year. Since midyear average prices of goods and services have risen less rapidly than earlier, in large part because of declines in prices of foods. The advance in the index of average hourly earnings has been somewhat faster so far in 1978 than it had been on the average during 1977.
>
> After a sharp decline in early August, the trade-weighted value of the dollar against major foreign currencies has recovered against a background of uncertain conditions in exchange markets. In late August it was announced that the U.S. trade deficit had increased sharply in July.
>
> Growth in *M*-1 picked up in August to about the average rate in the first two quarters of the year. Inflows of the interest-bearing deposits included in *M*-2 and *M*-3 also accelerated somewhat, and expansion in the broader aggregates was relatively rapid. Short-term market interest rates have risen appreciably since mid-August, but longer-term rates generally have edged down further. On August 18 an increase in Federal Reserve discount rates from 7¼ to 7¾ per cent was announced.
>
> In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster monetary and financial

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conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions. At its meeting on July 18, 1978, the Committee agreed that these objectives would be furthered by growth of *M*-1, *M*-2, and *M*-3 from the second quarter of 1978 to the second quarter of 1979 at rates within ranges of 4 to 6½ per cent, 6½ to 9 per cent, and 7½ to 10 per cent, respectively. The associated range for bank credit is 8½ to 11½ per cent. These ranges are subject to reconsideration at any time as conditions warrant.

In the short run, the Committee seeks to achieve bank reserve and money market conditions that are broadly consistent with the longer-run ranges for monetary aggregates cited above, while giving due regard to developing conditions in domestic and international financial markets more generally. Early in the period until the next regular meeting, System open market operations shall be directed at attaining a weekly-average Federal funds rate slightly above the current level. Subsequently, operations shall be directed at maintaining the weekly-average Federal funds rate within the range of 8¼ to 8¾ per cent. In deciding on the specific objective for the Federal funds rate the Manager shall be guided mainly by the relationship between the latest estimates of annual rates of growth in the September–October period of *M*-1 and *M*-2 and the following ranges of tolerance: 5 to 9 per cent for *M*-1 and 6½ to 10½ per cent for *M*-2. If, giving approximately equal weight to *M*-1 and *M*-2, their rates of growth appear to be significantly above or below the midpoints of the indicated ranges, the objective for the funds rate shall be raised or lowered in an orderly fashion within its range.

If the rates of growth in the aggregates appear to be above the upper limit or below the lower limit of the indicated ranges at a time when the objective for the funds rate has already been moved to the corresponding limit of its range, the Manager is promptly to notify the Chairman who will then decide whether the situation calls for supplementary instructions from the Committee.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Gardner, Jackson, Partee, Mrs. Teeters, and Mr. Winn. Votes against this action: Messrs. Wallich and Willes.

Messrs. Wallich and Willes dissented from this action because they favored more vigorous measures to curb the rates of growth in the monetary aggregates. They believed that such measures were

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essential to deal with the problem of inflation and that they could be undertaken without a significant risk of precipitating a recession. In their view, current levels of interest rates adjusted for expected rates of inflation were not high.

2. Authorization for Domestic Open Market Operations

At this meeting, Committee members voted to increase from $3 billion to $4 billion the limit on changes between Committee meetings in System Account holdings of U.S. Government and Federal agency securities specified in paragraph 1(a) of the authorization for domestic open market operations, effective immediately, for the period ending with the close of business on October 17, 1978.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Gardner, Jackson, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None.

This action was taken on the recommendation of the Management of the System Account. The Management had advised that large-scale purchases of Treasury and Federal agency securities over the coming inter-meeting interval might be needed to counter the effect on member bank reserves of a projected increase in Treasury balances at the Reserve Banks arising from corporate tax receipts in mid-September.

Subsequent to this meeting, on October 10, 1978, the Committee voted to approve an additional increase of $1 billion, to $5 billion, in the limit on changes between Committee meetings in U.S. Government and Federal agency securities specified in paragraph 1(a) of the authorization for domestic open market operations, effective immediately, for the period ending with the close of business on October 17, 1978.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Gardner, Jackson, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None.

This action was taken on recommendation of the Management of the System Account. The Management had advised that, even

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though the Committee had voted at its September 19 meeting to raise the limit from $3 billion to $4 billion, large-scale purchases of Treasury and Federal agency securities had reduced the leeway for further purchases during the inter-meeting period to about $335 million. It now appeared likely that additional purchases would be required as currency in circulation and other factors were absorbing reserves while Treasury balances continued at a high level, in part because of purchases of special Treasury securities by foreign central banks in association with their recent intervention in the foreign exchange markets.

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MEETING HELD ON OCTOBER 17, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested that output of goods and services had expanded moderately in the third quarter, but that the rate of growth appeared to be somewhat below the average annual rate of about 4¼ per cent estimated by the Commerce Department for the first two quarters of the year. The rise in average prices—as measured by the fixed-weight price index for gross domestic business product—was rapid in the third quarter, although it was well below the annual rate of about 12 per cent in the second quarter.

Staff projections for the year ending in the third quarter of 1979 were little changed from those of a month earlier. They continued to suggest that output of goods and services would grow somewhat more slowly than over the first three quarters of 1978. The rate of inflation was expected to remain rapid, although also moderating a bit from its pace thus far in 1978. The unemployment rate was projected to change little from its September level.

In September the index of industrial production increased an estimated 0.5 per cent, close to the average rate of expansion in the preceding 4 months. Nonfarm payroll employment changed little in September following relatively small increases in July and August. In manufacturing, employment was essentially unchanged in September and the average workweek held steady at an advanced level. The unemployment rate edged up from 5.9 to 6.0 per cent, the rate prevailing on the average since the first quarter of the year.

Total private housing starts declined slightly in August, but they remained above an annual rate of 2 million units. Sales of new houses fell for the third consecutive month; however, a surge in sales of existing dwellings raised total sales of single-family homes to a new high.

The dollar value of total retail sales was estimated to have increased considerably in September following the large rise now

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indicated for August. For the third quarter as a whole, however, the advance in retail sales was substantially below the exceptional gain in the second quarter. Unit sales of new automobiles fell in September to an annual rate well below the average pace since early spring.

Newly revised data suggested that the index of average hourly earnings of private nonfarm production workers had risen at an annual rate of 7.9 per cent through September 1978 compared with an increase of 7.4 per cent for 1977 as a whole. In August, as in July, the consumer price index rose more moderately than in most earlier months of the year, as prices of some foods declined substantially. In September, however, producer prices of food products turned up sharply and contributed to a marked rise in prices of producer finished goods. Announcement of a new Government program aimed at moderating increases in prices and wages was expected to be made shortly after this meeting.

The trade-weighted value of the dollar against major foreign currencies fell substantially from mid-September to mid-October in frequently volatile exchange markets. The U.S. trade deficit declined sharply in August, reversing the pronounced increase in July; for the 2 months the deficit was close to the rate for the second quarter and well below the high rate for the first quarter.

The expansion in total credit at U.S. commercial banks, which had slowed in August, accelerated in September nearly to the pace experienced on the average in earlier months of the year. Bank investments and security loans rose in September after having declined in August, while growth in real estate and business loans moderated only slightly from the rapid rates recorded in other recent months. Outstanding commercial paper of nonfinancial businesses rose somewhat in September following a small decline in August.

Growth in the narrowly defined money supply (*M*-1) accelerated further in September to an annual rate of about 14 per cent from 8.5 per cent in August. However, data for early October suggested a sharply reduced growth rate in the current month. Inflows of the interest-bearing deposits included in *M*-2 and *M*-3 remained strong in September, and growth in the broader monetary aggregates also accelerated somewhat.

At its meeting on September 19 the Committee had decided on ranges of tolerance for the annual rates of growth in *M*-1 and *M*-2

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during the September–October period of 5 to 9 per cent and 6½ to 10½ per cent, respectively. The Committee had agreed that early in the coming inter-meeting period operations should be directed toward a Federal funds rate of around 8½ per cent, slightly above the prevailing level of about 8⅜ per cent. Subsequently, if the 2-month growth rates of *M*-1 and *M*-2 appeared to be significantly above or below the midpoints of the indicated ranges, the objective for the funds rate was to be raised or lowered in an orderly fashion within a range of 8¼ to 8¾ per cent.

Following the September 19 meeting the Manager of the System Open Market Account began to seek bank reserve conditions consistent with an increase in the weekly-average Federal funds rate to around 8½ per cent. As September progressed, incoming data suggested that growth in *M*-1 would be around the upper limit of the range specified by the Committee and that growth in *M*-2 would be in the upper portion of its range. Accordingly, the Manager sought reserve conditions consistent with further increases in the Federal funds rate, and by late September the rate was around 8¾ per cent, the upper limit of the inter-meeting range specified by the Committee. During the first half of October the objective for the funds rate remained 8¾ per cent, although on many days the rate was above or below that level for technical reasons.

A considerable rise in interest rates on most short-term market instruments was associated with the increase in the Federal funds rate during the inter-meeting period. Yields on Treasury and corporate bonds also moved somewhat higher, but they remained below their July peaks. Yields on State and local government bonds changed little, reflecting in part a markedly reduced volume of new issues. In late September commercial banks increased the rate on loans to prime business borrowers from 9½ to 9¾ per cent; in mid-October this rate was raised further to 10 per cent.

The Board of Governors announced an increase in Federal Reserve Bank discount rates from 7¾ to 8 per cent on September 22 and a further increase to 8½ per cent on October 13. Both actions were taken primarily to bring the discount rate into closer alignment with other short-term interest rates, but also in recognition of conditions affecting the dollar in foreign exchange markets. The Board indicated in addition that the increase of ½ percentage point in mid-October was approved in light of the continued high

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rate of inflation and the recent rapid expansion of the monetary aggregates.

In the Committee's discussion of the economic situation and outlook, the members generally agreed that real output of goods and services was likely to grow moderately over the year ending in the third quarter of 1979, at a rate about or a little below that projected by the staff. Given their expectations for output, the members anticipated that over the period the unemployment rate would change little from its recent level or would increase somewhat. All members expected that average prices of goods and services would continue to rise rapidly.

Despite the general agreement that real output was likely to grow moderately over the next four quarters, some members cited elements in the current situation that could contribute to a downturn in activity before the end of the period. It was pointed out, for example, that the current business expansion—now well into its fourth year—had lasted for a long time by historical standards and that the dynamics of business fluctuations suggested that a downturn might well develop sometime within the coming year. Also, business-cycle history provided little encouragement for the expectation that growth in output could gradually be slowed to a pace more or less consistent with its long-run potential and with relative stability in the unemployment rate. Moreover, rapid inflation was viewed as a serious threat to the sustainability of the expansion in output, although buying of goods might be buoyed for a time by anticipation of further price increases.

At the same time, attention was drawn to favorable elements in the economic situation. Specifically, housing starts and residential construction had been maintained at higher levels than had been expected earlier, and the outlook for business fixed investment seemed to have strengthened lately. Altogether, final sales apparently had picked up in recent months while growth in output had moderated, tending to improve prospects for activity in the months immediately ahead. Finally, there were grounds for believing that improvement in the net export position would lend strength to domestic output.

At this meeting the Committee reviewed its 12-month ranges for growth in the monetary aggregates. At its meeting in July 1978 the Committee had specified the following ranges for the period

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from the second quarter of 1978 to the second quarter of 1979: *M*-1, 4 to 6½ per cent; *M*-2, 6½ to 9 per cent; and *M*-3, 7½ to 10 per cent. The associated range for growth in commercial bank credit was 8½ to 11½ per cent. The ranges being considered at this meeting were for the period from the third quarter of 1978 to the third quarter of 1979.

In contemplating ranges for growth of the monetary aggregates over the year ahead, the Committee faced unusual uncertainties. First, commercial banks were authorized to introduce an automatic transfer service (ATS) on November 1, although there was a chance that introduction would be stayed by court action; and in the closing days of the session of the Congress just ended, Federally chartered depositary institutions in New York State were authorized to offer NOW accounts. ATS would provide for automatic shifts of funds from interest-earning savings accounts to demand accounts, and thus would enable customers to hold much lower balances in demand accounts. This service, therefore, seemed likely to alter substantially the relationship between growth of *M*-1 and growth of nominal GNP.

Second, no authoritative information was yet available on the President's new program to moderate increases in wages and prices, which was expected to be announced shortly after this meeting. In the Committee's discussion of longer-run ranges, the point was stressed that the program would have its greatest potential for moderating inflationary expectations if it were perceived by the public as an additional measure in the campaign against inflation and not as a substitute for fiscal and monetary restraint.

With respect to ATS, a staff analysis had suggested that during a transition period a significant shift in funds from demand deposits to savings deposits at commercial banks was almost sure to occur, but its size was uncertain. Therefore, the rate of growth of *M*-1 over the year ahead was likely to be lower than otherwise, but the amount of the reduction could be within a fairly wide range. Growth of *M*-2, on the other hand, might be raised marginally, reflecting minor shifts of deposits from nonbank thrift institutions to savings accounts at commercial banks. It appeared unlikely that growth of *M*-3 would be noticeably affected.

A new measure of money, designated *M*-1+, had been developed by the staff to provide background information with regard to the

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behavior of money, particularly the transactions demand for money, during the transition period. Growth of this aggregate—defined as *M*-1 plus savings deposits at commercial banks, NOW accounts at nonbank thrift institutions, and demand deposits at mutual savings banks—would not be affected by shifts from demand deposits to savings deposits at commercial banks.

Members of the Committee suggested different approaches to take account of the uncertainties noted above in setting the longer-run ranges for the aggregates. One proposal was to adopt ranges for *M*-1, *M*-2, and *M*-3 as before, in the expectation that introduction of ATS would have little effect on growth of the aggregates in the few months before the Committee would again consider its longer-run ranges. Under this approach, a supplementary range for growth in *M*-1 adjusted for estimated effects of ATS and a range for growth in *M*-1+ might be indicated as "memorandum items" for monitoring purposes.

Another proposal was to drop *M*-1 from the list of aggregates, adopting longer-run ranges only for *M*-2 and *M*-3 at this time. It was suggested, along with this proposal, that additional work on the concepts and measurement of money be undertaken with a view to adopting new measures when the Committee next considered its longer-run ranges.

Additional proposals involved retaining *M*-1 and adopting ranges for *M*-1, *M*-2, and *M*-3 as before, with specific adjustments to take account of the special uncertainties. One proposal was to adjust downward both the upper and the lower limits of the range for *M*-1 by an estimate of the probable effects of ATS. Another was to widen the range for *M*-1, chiefly by reducing the lower limit. A third was to couple such a widening of the range for *M*-1 with notation of a supplementary range for *M*-1+ to aid in evaluating the behavior of both *M*-1 and *M*-2.

At the conclusion of the discussion, the Committee decided that the existing ranges for *M*-2 and *M*-3 provided for rates of monetary growth over the year ahead that were consistent with a moderation of inflation under the President's program. Thus, the Committee adopted ranges of 6½ to 9 per cent for *M*-2 and 7½ to 10 per cent for *M*-3 for the period from the third quarter of 1978 to the third quarter of 1979. The Committee also indicated that it expected growth of *M*-1 to be within a range of 2 to 6 per cent over that

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period. That range was both lower and wider than the range of 4 to 6½ per cent that had been adopted in July, in recognition of the uncertainty concerning the size and speed of the expected shift of deposits from demand to savings accounts resulting from the introduction of ATS. The associated range for commercial bank credit was 8½ to 11½ per cent. The Committee also decided that growth of *M*-1+ within a range of 5 to 7½ per cent appeared to be generally consistent with the ranges of growth for the other monetary aggregates.

> The Committee adopted the following ranges for rates of growth in monetary aggregates for the period from the third quarter of 1978 to the third quarter of 1979: *M*-2, 6½ to 9 per cent; *M*-3, 7½ to 10 per cent. *M*-1 was expected to grow within a range of 2 to 6 per cent over the period, depending in part on the speed and extent of transfers from demand to savings deposits resulting from the introduction of ATS. The associated range for bank credit is 8½ to 11½ per cent. Growth of *M*-1+ (*M*-1 plus savings deposits at commercial banks and NOW accounts) in a range of 5 to 7½ per cent was thought to be generally consistent with the ranges for the foregoing aggregates.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Jackson, Partee, and Mrs. Teeters. Votes against this action: Messrs. Wallich, Willes, and Winn. Absent and not voting: Mr. Gardner.

Messrs. Wallich, Willes, and Winn dissented from this action because, with the Committee's longstanding objective of slowing the rate of inflation in mind, they preferred to specify an upper limit of less than 6 per cent for the rate of growth of *M*-1, adjusted for the estimated effects of ATS. In their view, the upper limit of 6 per cent, adjusted for ATS, represented an unwarranted increase from the 6½ per cent upper limit of the existing (pre-ATS) range.

In the discussion of policy for the period immediately ahead, members of the Committee noted that the uncertainties associated with introduction of ATS would affect growth of the monetary aggregates in the October–November period—the 2-month period for which growth ranges were being considered—in much the same way as they would growth over the year ahead. Specifically, growth

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of *M*-1 over the 2-month period might well be less than otherwise by a significant but undetermined amount, and growth of *M*-2 might be marginally greater.

As in the case of the longer-run ranges, various proposals were advanced for taking account of the unusual uncertainties. In general, these proposals involved placing less emphasis on the behavior of *M*-1 as a guide to operations in the inter-meeting period and more on the behavior of *M*-2, rather than the approximately equal weight that typically had been given to the two aggregates. One proposal was to drop *M*-1 altogether as an operating guide. Another was to give primary emphasis to *M*-2 and to specify only an upper limit for *M*-1 rather than a range, reflecting a judgment that rapid growth in *M*-1 would have significance for policy while slow growth might represent chiefly transfers from demand to savings accounts because of the introduction of ATS. A third proposal was to widen the range for *M*-1, while indicating a range for *M*-1+ as an aid in evaluating the behavior of the other monetary aggregates. At the same time, most members of the Committee favored giving greater weight than usual to money market conditions in the conduct of operations in the period until the next meeting of the Committee.

In the discussion, concern was expressed about recent rates of monetary growth, and most members believed that some additional firming in money market conditions in the period immediately ahead was needed to help assure a slowing in growth over the months ahead. They favored directing open market operations toward an increase in the Federal funds rate to about 9 per cent shortly after this meeting, with an inter-meeting range of 8¾ per cent to either 9¼ or 9½ per cent.

Other members believed that for the time being operations should be directed toward maintaining the money market conditions currently prevailing, as represented by a Federal funds rate of about 8⅞ per cent, because they felt that such a pause was needed to evaluate the lagged impact of the substantial increases in interest rates over recent months. These members suggested an inter-meeting range of 8¾ to 9 per cent.

With respect to the monetary aggregates, a number of members proposed a range of ½ to 6½ per cent for the annual rate of growth in *M*-1 over the October–November period. Those members who

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preferred to specify only an upper limit, rather than a range, for growth in *M*-1 over the 2-month period suggested limits of 5, 6, and 7 per cent. For *M*-2, a range of 5½ to 9½ per cent was proposed by the largest number of members; one slightly higher and one slightly lower were also suggested.

At the conclusion of the discussion the Committee agreed to instruct the Manager to seek a Federal funds rate of around 9 per cent early in the period before the next regular meeting and subsequently to maintain the rate within a range of 8¾ to 9¼ per cent. With regard to the specific objective for the Federal funds rate within that range, the Committee instructed the Manager to be guided mainly by a range of tolerance for the annual rate of growth in *M*-2 over the October–November period of 5½ to 9½ per cent, provided that the rate of growth in *M*-1 over that period did not exceed 6½ per cent.

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 grew moderately in the third quarter, although the pace was somewhat below the average for the first two quarters of the year. In September, as in August, the dollar value of total retail sales rose considerably. Industrial production continued to expand while nonfarm payroll employment changed little. The unemployment rate edged up from 5.9 to 6.0 per cent. Average producer prices of finished goods rose substantially in September, as prices of foods increased sharply after having declined for 2 months. The advance in the index of average hourly earnings has been somewhat faster so far in 1978 than it was on the average during 1977.
>
> The trade-weighted value of the dollar against major foreign currencies has declined further since mid-September in frequently volatile exchange markets. The U.S. trade deficit fell sharply in August, reversing the jump recorded in July; for the 2 months the deficit was close to the rate for the second quarter.
>
> Growth in *M*-1, which had been rapid in August, accelerated in September. Inflows of the interest-bearing deposits included in *M*-2 and *M*-3 remained strong, and expansion in the broader aggregates also accelerated somewhat. Short-term market interest rates have risen further in recent weeks; long-term rates also have increased, but they remain below their July peaks. An increase in

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Federal Reserve discount rates from 7¾ to 8 per cent was announced on September 22; another increase to 8½ per cent was announced on October 13.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster monetary and financial conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions. In setting ranges for the monetary aggregates, the Committee recognized the uncertainties concerning the effects that the November 1 introduction of the automatic transfer service (ATS) would have on measures of the money supply, especially *M*-1. Against that background, the Committee agreed that appropriate monetary and financial conditions would be furthered by growth of *M*-2 and *M*-3 from the third quarter of 1978 to the third quarter of 1979 within ranges of 6½ to 9 per cent and 7½ to 10 per cent, respectively. The narrowly defined money supply (*M*-1) was expected to grow within a range of 2 to 6 per cent over the period, depending in part on the speed and extent of transfers from demand to savings deposits resulting from the introduction of ATS. The associated range for bank credit is 8½ to 11½ per cent. Growth of *M*-1+ (*M*-1 plus savings deposits at commercial banks and NOW accounts) in a range of 5 to 7½ per cent was thought to be generally consistent with the ranges of growth for the foregoing aggregates. These ranges are subject to reconsideration at any time as conditions warrant.

In the short run, the Committee seeks to achieve bank reserve and money market conditions that are broadly consistent with the longer-run ranges for monetary aggregates cited above, while giving due regard to developing conditions in domestic and international financial markets more generally and to uncertainties associated with the introduction of ATS. Early in the period before the next regular meeting, System open market operations shall be directed at attaining a weekly-average Federal funds rate slightly above the current level. Subsequently, operations shall be directed at maintaining the weekly-average Federal funds rate within the range of 8¾ to 9¼ per cent. In deciding on the specific objective for the Federal funds rate the Manager shall be guided mainly by a range of tolerance for growth in *M*-2 over the October–November period of 5½ to 9½ per cent, provided that growth of *M*-1 over that period does not exceed an annual rate of 6½ per cent.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Jackson, Partee,

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> Wallich, and Winn. Votes against this action: Mrs. Teeters and Mr. Willes. Absent and not voting: Mr. Gardner.

Mrs. Teeters dissented from this action because she believed that for the time being operations should be directed toward maintaining the money market conditions currently prevailing. In her view, the Committee should wait to evaluate the effects of the substantial increases in interest rates over recent months before contemplating additional firming in money market conditions.

Mr. Willes dissented from this action because he believed that it allowed for unacceptably rapid monetary growth. He preferred an upper limit of 5 per cent for growth of *M*-1 over the October–November period; with respect to the Federal funds rate, he favored raising the objective to 9¼ per cent during the inter-meeting period, barring unforeseen weakness in monetary growth, and providing leeway to raise the objective to 9½ per cent if the monetary aggregates appeared to be growing more rapidly than expected.

Subsequent to the meeting, on October 31, the Committee voted to approve a delegation of authority to Chairman Miller to take certain actions in implementation of a broad Government program to strengthen the dollar in foreign exchange markets and thereby to counter continuing domestic inflationary pressures, if he determined that the arrangements with the U.S. Treasury and with certain foreign monetary authorities were substantially as contemplated in a consultation among the members of the Committee on the preceding day.

Early on the morning of November 1 the Treasury and the Federal Reserve announced measures being taken to implement such a program. Specifically, the Board of Governors approved (1) an increase of 1 percentage point, from 8½ to 9½ per cent, in the discount rate at the Federal Reserve Bank of New York, effective immediately, and (2) establishment of a supplementary reserve requirement, in addition to the existing reserve requirements on deposits at member banks, equal to 2 per cent of time deposits in denominations of $100,000 or more. At the same time the System announced increases in its reciprocal currency (swap) arrangements with the central banks of Germany, Japan, and Switzerland by a total of $7.6 billion, to $15 billion, and activation of the swap

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arrangement with the Bank of Japan. It further stated that the foreign currencies available under the expanded arrangements would be used along with foreign currencies available to the Treasury in a program of forceful intervention in the exchange markets in coordination with foreign central banks to correct recent excessive movements in exchange rates.

In a joint Treasury–Federal Reserve statement, other measures to mobilize key foreign currencies were announced. They included drawings on the U.S. reserve tranche in the International Monetary Fund, for part of which activation of the General Arrangements to Borrow was contemplated; sales of special drawing rights; and issuance of U.S. Treasury securities denominated in foreign currencies. It was also announced that the Treasury would increase its sales of gold to at least 1½ million ounces monthly beginning in December.

As part of this program, on October 31 the Federal Open Market Committee voted to approve a delegation of authority to Chairman Miller to modify the domestic policy directive by raising the range for the Federal funds rate to 9½ to 9¾ per cent and by instructing the Manager, in deciding on the specific objective for the rate within that range, to be guided by developing conditions in domestic and international financial markets. The Chairman approved the modification of the directive on November 1, effective on that date.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Messrs. Gardner and Jackson.

2. Authorization for Foreign Currency Operations

On October 31 the Committee also voted to approve a delegation of authority to Chairman Miller to negotiate increases in the System's swap arrangements with the German Federal Bank, the Bank of Japan, and the Swiss National Bank. In addition, the Committee voted to approve a concurrent amendment to paragraph 2 of the authorization for foreign currency operations to raise correspondingly the amounts specified there for the swap arrangements with those central banks.

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On November 1 the Chairman approved increases of $2 billion, $3 billion, and $2.6 billion in the System's swap arrangements with the German Federal Bank, the Bank of Japan, and the Swiss National Bank, respectively. Accordingly paragraph 2 of the authorization was amended, effective on that date, to 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	6,000
Bank of Italy	3,000
Bank of Japan	5,000
Bank of Mexico	360
Netherlands Bank	500
Bank of Norway	250
Bank of Sweden	300
Swiss National Bank	4,000
Bank for International Settlements:	
Dollars against Swiss francs	600
Dollars against authorized European currencies other than Swiss francs	1,250

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Messrs. Gardner and Jackson.

Paragraph 1D of the Committee's authorization for foreign currency operations authorizes the Federal Reserve Bank of New York, for the System Open Market Account, to maintain an over-all open position in all foreign currencies not to exceed $1.0 billion, unless

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a larger position is expressly authorized by the Committee. On June 20, 1978, the Committee had authorized an over-all open position of $1.5 billion.

On October 27, 1978, the Committee authorized an increase in this limit to $2 billion in view of the scale of recent and potential Federal Reserve operations in the foreign exchange markets undertaken pursuant to the Committee's foreign currency directive.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Messrs. Gardner and Jackson.

On October 31 the Committee voted to approve a delegation of authority to Chairman Miller to authorize an open position of $5 billion. On November 1 the Chairman authorized an open position of that amount.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Messrs. Gardner and Jackson.

3. Authorization for Domestic Open Market Operations

On November 3, 1978, Committee members voted to increase from $3 billion to $5 billion the limit on changes between Committee meetings in System Account holdings of U.S. Government and Federal agency securities specified in paragraph 1(a) of the authorization for domestic open market operations, effective immediately, for the period ending with the close of business on November 21, 1978.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None. Absent and not voting: Messrs. Gardner and Jackson.

This action was taken on recommendation of the System Account Manager. The Manager had advised that large-scale sales of Treas-

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ury securities since the October meeting—required mainly to counter the effect on member bank reserves of a steep decline in Treasury balances at the Federal Reserve Banks and to accommodate substantial purchases of Treasury bills by foreign central banks—had reduced the leeway for further sales to $365 million. It now appeared likely that additional sales would be required as current projections indicated a need for further reserve-absorbing operations over the coming weeks.

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MEETING HELD ON NOVEMBER 21, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested that output of goods and services was continuing to grow at a moderate pace in the current quarter, following expansion at an annual rate of 3.4 per cent in the third quarter and a somewhat faster rate on the average over the first two quarters of the year. Average prices, as measured by the fixed-weight price index for gross domestic business product, appeared to be continuing their rapid rise, about in line with the annual rate of 7½ per cent estimated for the third quarter.

Staff projections of growth in output over the year ending in the third quarter of 1979 had been reduced from those of a month earlier. They now suggested a further slowing of expansion, in large part because of a reduction next year in the rise of business fixed investment and a decline in residential construction activity. The projections continued to suggest a rapid rise in average prices. The unemployment rate was expected to increase slightly from its October level.

In October the index of industrial production rose an estimated 0.5 per cent, the same as in September but somewhat below the average advance since last winter. Nonfarm payroll employment rose considerably in October following relatively small advances during the third quarter. In manufacturing, employment gains were the largest of the year and the average workweek edged up. The unemployment rate declined from 6.0 to 5.8 per cent.

Total private housing starts remained above an annual rate of 2 million units in September. However, sales of new units declined for the fourth consecutive month, and merchant-builder inventories of unsold single-family homes rose further. Sales of existing dwellings remained at an advanced level.

The dollar value of total retail sales declined somewhat in

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October following a sizable gain in August and a further advance in September. On balance, retail sales were modestly above their April level and slightly above their average in the third quarter. Unit sales of new automobiles increased in October but were still lower than in most other months since early spring.

The index of average hourly earnings of private nonfarm production workers increased at an annual rate of about 9 per cent in October; for the first 10 months of 1978 the advance was at a rate of 8.4 per cent, about 1 percentage point above the rise over 1977 as a whole. Total hourly compensation of nonfarm workers was estimated to have increased at an annual rate of nearly 10 per cent over the first three quarters of the year, about 1¾ percentage points faster than in 1977.

Average producer prices of finished goods rose substantially in October for the second consecutive month, reflecting in part a further large increase in producer prices of food products. In September the consumer price index rose at an annual rate of nearly 10 per cent following 2 months of somewhat smaller increases.

On October 24 the Government announced a new program aimed at moderating increases in prices and wages. The program included explicit numerical standards for price and wage increases, with voluntary compliance encouraged by a number of Government measures; procedures to minimize the inflationary impact of Government regulations; and a restrictive budget policy.

On November 1 a broad Government program was put in place to strengthen the dollar in foreign exchange markets and thereby to counter continuing domestic inflationary pressures. As part of this program the Federal Reserve announced the following actions: an increase in the discount rate from 8½ to 9½ per cent; establishment of a supplementary reserve requirement of 2 per cent against member bank time deposits in denominations of $100,000 or more; and increases in its reciprocal currency arrangements with the central banks of Germany, Japan, and Switzerland, and activation of the swap arrangement with the Bank of Japan. The U.S. Treasury announced related measures to mobilize key foreign currencies, including drawings on the U.S. reserve tranche in the International Monetary Fund; sales of special drawing rights; and issuance of foreign-currency-denominated securities. The Treasury also announced an increase in its monthly gold sales. The expanded

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availability of foreign currencies was to be used in a program of forceful intervention in exchange markets, coordinated with foreign central banks, to correct recent excessive exchange-rate movements.

In foreign exchange markets the trade-weighted value of the dollar against major foreign currencies declined substantially further during the last week of October, following large cumulative losses over recent months. After the announcement and initial implementation of the new support program on November 1, however, the dollar rose sharply—to a level somewhat above that in early October. The U.S. trade deficit in the third quarter was about unchanged from the second quarter.

In October the expansion of total credit at U.S. commercial banks slowed slightly from the pace in the third quarter. Bank loans other than security loans continued to grow rapidly, but bank investments were reduced somewhat. Outstanding commercial paper of nonfinancial businesses rose considerably in October, after having changed little on balance during the previous 2 months.

The narrowly defined money supply (*M*-1) grew at an annual rate of about 3¼ per cent in October, after having expanded at rates of about 8½ and 14 per cent in August and September, respectively; growth in *M*-2 and *M*-3 also moderated. Inflows of the interest-bearing deposits included in the broader aggregates slowed somewhat, although sales of 6-month money market certificates at both commercial banks and nonbank thrift institutions expanded sharply.

At its meeting on October 17, the Committee had agreed that early in the coming inter-meeting period operations should be directed toward a Federal funds rate of around 9 per cent, slightly above the rate of 8¾ per cent then prevailing. Subsequently, the objective for the Federal funds rate was to be raised or lowered in an orderly fashion within a range of 8¾ to 9¼ per cent. In setting a specific objective for the funds rate within that range, the Manager of the System Open Market Account was to be guided mainly by a range of tolerance of 5½ to 9½ per cent for the annual rate of growth in *M*-2 over the October–November period, provided that the rate of growth in *M*-1 over that period did not exceed 6½ per cent.

Immediately following the October 17 meeting the Manager began to seek reserve conditions consistent with a weekly average

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Federal funds rate of around 9 per cent. However, because a sizable short-term need for reserves coincided with temporary market scarcities of Treasury obligations for collateral behind System repurchase agreements, Federal funds traded at around 9¼ per cent. As October progressed, the Manager did not take aggressive action to exert downward pressure on the funds rate, in light of conditions in foreign exchange markets and of the Committee's related instruction to give due regard to such developments. Accordingly, Federal funds continued to trade at around 9¼ per cent in the days prior to November 1.

As part of the Government program announced on November 1, the Committee had voted on October 31 to delegate authority to Chairman Miller to modify the domestic policy directive by raising the range for the Federal funds rate to 9½ to 9¾ per cent and by instructing the Manager, in deciding on the specific objective for the rate within that range, to be guided by developing conditions in domestic and international financial markets; the Chairman approved the modification on November 1. During the first half of November, the Federal funds rate averaged in the upper half of that range. For several days immediately following the November 1 announcement, however, the rate was somewhat above the desired range as the Manager avoided aggressive action to reduce it during the initial stages of implementation of the new program.

The rise in the Federal funds rate during the inter-meeting period was accompanied by substantial increases in yields on most short-term market instruments. Advances in rates on Treasury bills were moderated, however, by large investments by foreign central banks of dollars obtained in currency support operations. Commercial banks increased the rate on loans to prime business borrowers from 10 per cent to 11 per cent during the period. Yields in bond markets advanced considerably during the second half of October, but a large portion of the increase was offset by sizable declines in early November. In mortgage markets, interest rates moved steadily higher over the inter-meeting period as demands for real estate credit remained strong. Residential mortgage lending apparently increased in October.

In the Committee's discussion of the economic situation and outlook, most members indicated that over the past month they

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had scaled down their expected rates of growth in real output of goods and services for the year ending in the third quarter of 1979. One or two members still anticipated moderate expansion over the period, but many projected slow growth, and some thought that a downturn in activity was likely or that the risks of an actual recession or a growth recession had increased. It was emphasized, however, that the uncertainties associated with any forecast of real output had increased significantly.

Most members expected that, over the year ending in the third quarter of 1979, the unemployment rate either would change little or would increase from the average level in the third quarter of 1978. All members continued to anticipate a rapid rise in average prices of goods and services.

The recent rise in short-term interest rates—specifically, its impact on the cost and possibly on the availability of mortgage credit—in addition to recent indications of a slowing next year in the rise of business fixed investment, was cited as one reason for reducing anticipated rates of growth in real output over the period ahead. On the other hand, the view was also expressed that the new program to strengthen the dollar and to counter inflationary pressures could have favorable effects on expectations, especially on those for inflation, and thereby could encourage spending. In this connection, it was noted that long-term bond yields had declined immediately after the announcement on November 1.

A difference in emphasis also existed with respect to Federal tax policy. Thus, it was suggested that prospects for sustaining the expansion in output had been improved by the recent enactment of reductions in income taxes. But it was also observed that the reductions would be largely offset by substantial increases in social security taxes in 1979.

Some skepticism was expressed, as it had been at the October meeting, that growth in output could be tapered down to a relatively slow rate without bringing on a recession, especially in view of the rapid inflation. It was stressed, on the other hand, that economic conditions in this period differed from those in other business expansions in ways that made it reasonable to expect a reduction in the rate of growth and a concomitant decrease in the rate of inflation without a slide into recession.

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At its meeting in October the Committee had agreed that from the third quarter of 1978 to the third quarter of 1979 growth of *M*-2 and *M*-3 within ranges of 6½ to 9 per cent and 7½ to 10 per cent, respectively, appeared to be consistent with broad economic aims. *M*-1 was expected to grow over that period within a range of 2 to 6 per cent, depending in part on the speed and extent of transfers from demand to savings deposits resulting from the introduction of the automatic transfer service (ATS). The associated range for the rate of growth in commercial bank credit was 8½ to 11½ per cent. The Committee had also decided that growth of *M*-1+ within a range of 5 to 7½ per cent appeared to be generally consistent with the ranges of growth for the other monetary aggregates. It had been agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings.

In the discussion of policy for the period immediately ahead, the members of the Committee agreed that, in seeking to achieve bank reserve and money market conditions broadly consistent with the longer-run ranges for monetary growth cited above, due regard should be given to the program for supporting the foreign exchange value of the dollar as well as to developing conditions in domestic financial markets and to uncertainties associated with the November 1 introduction of ATS. Against that background, the members differed somewhat in their views as to whether, and to what degree, additional firming in money market conditions should be sought during the next few weeks; no sentiment was expressed for easing money market conditions. As they had at the October meeting, moreover, most members favored giving greater weight than usual to money market conditions in the conduct of operations in the period before the next meeting, although some sentiment was expressed for a return to basing decisions for open market operations primarily on the behavior of the monetary aggregates.

The members favored directing open market operations early in the period before the next regular meeting toward maintaining the weekly-average Federal funds rate at 9¾ per cent, the upper end of the 9½ to 9¾ per cent range specified as of November 1, or slightly higher. With respect to the range in which the funds rate might be varied if growth in the aggregates appeared to approach

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or move beyond their specified limits, most members favored an upper limit of 10 per cent for the range; 10⅛ and 10¼ per cent were also proposed. Lower limits from 9½ to 9¾ per cent were suggested.

With respect to the monetary aggregates, almost all members proposed that the Committee take account of the unusual uncertainties associated with the introduction of ATS in the same way that it had at the October meeting—namely, by giving primary emphasis to growth of *M*-2 and by specifying only an upper limit, rather than a range, for growth of *M*-1. For the annual rate of growth in *M*-2 over the November–December period, most members favored a range with a lower limit of 6 per cent and an upper limit of 9 to 10 per cent. Almost all members proposed 5 or 5½ per cent for the ceiling on growth of *M*-1 over the 2-month period.

At the conclusion of the discussion the Committee agreed to instruct the Manager to seek a Federal funds rate of around 9⅞ per cent early in the period before the next regular meeting and subsequently to maintain the rate within a narrow band of 9¾ to 10 per cent. With regard to the specific objective for the rate within that range, the Committee instructed the Manager to be guided mainly by a range of tolerance for the annual rate of growth in *M*-2 over the November–December period of 6 to 9½ per cent, provided that the rate of growth in *M*-1 over that period did not exceed 5 per cent. 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 objectives.

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

> The information reviewed at this meeting suggests that in the current quarter real output of goods and services is continuing to grow moderately. In October industrial production expanded further, nonfarm payroll employment rose considerably, and the unemployment rate declined from 6.0 to 5.8 per cent. Following 2 months of gains, the dollar value of total retail sales declined somewhat to a level slightly above the average in the third quarter. Average producer prices of finished goods rose substantially in October, as in September, in part because of further large increases in prices of foods. The advance in the index of average hourly earnings has

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been somewhat faster so far in 1978 than it was on the average during 1977. In late October the Government announced a new program aimed at moderating increases in prices and wages.

On November 1 a broad program to strengthen the dollar in foreign exchange markets and thereby to counter continuing domestic inflationary pressures was announced. The program included an increase in Federal Reserve discount rates from 8½ to 9½ per cent, establishment of a supplementary reserve requirement of 2 per cent against member bank time deposits in denominations of $100,000 or more, increases in Federal Reserve reciprocal currency arrangements with certain central banks, and other measures to mobilize key foreign currencies.

The trade-weighted value of the dollar against major foreign currencies declined rapidly during the last week of October, but following the actions taken to strengthen the dollar, it rose sharply to a level somewhat above that in early October. The U.S. trade deficit was about the same in the third quarter as in the second quarter.

Growth in *M*-1, which had been rapid in August and September, slowed markedly in October, and growth in *M*-2 and *M*-3 also moderated. Inflows of the interest-bearing deposits included in the broader aggregates slowed somewhat, although sales of 6-month money market certificates at both commercial banks and nonbank thrift institutions expanded to record levels. Short-term market interest rates have risen substantially further since mid-October. Bond rates also have increased on balance, although they have declined appreciably since November 1; mortgage interest rates have continued to rise.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster monetary and financial conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions. At its meeting on October 17, 1978, in setting ranges for the monetary aggregates, the Committee recognized the uncertainties concerning the effects that the November 1 introduction of the automatic transfer service (ATS) would have on measures of the money supply, especially *M*-1. Against that background, the Committee agreed that appropriate monetary and financial conditions would be furthered by growth of *M*-2 and *M*-3 from the third quarter of 1978 to the third quarter of 1979 within ranges of 6½ to 9 per cent and 7½ to 10 per cent, respectively. The narrowly defined money supply (*M*-1) was expected to grow within a range of 2 to 6 per cent over the

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period, depending in part on the speed and extent of transfers from demand to savings deposits resulting from the introduction of ATS. The associated range for bank credit is 8½ to 11½ per cent. Growth of *M*-1+ (*M*-1 plus savings deposits at commercial banks and NOW accounts) in a range of 5 to 7½ per cent was thought to be generally consistent with the ranges of growth for the foregoing aggregates. These ranges are subject to reconsideration at any time as conditions warrant.

In the short run, the Committee seeks to achieve bank reserve and money market conditions that are broadly consistent with the longer-run ranges for monetary aggregates cited above, while giving due regard to the program for supporting the foreign exchange value of the dollar, to developing conditions in domestic financial markets, and to uncertainties associated with the introduction of ATS. Early in the period before the next regular meeting, System open market operations are to be directed at attaining a weekly average Federal funds rate slightly above the current level. Subsequently, operations shall be directed at maintaining the weekly average Federal funds rate within the range of 9¾ to 10 per cent. In deciding on the specific objective for the Federal funds rate, the Manager is to be guided mainly by a range of tolerance for the annual rate of growth over the November–December period of 6 to 9½ per cent in *M*-2, provided that the rate of growth in *M*-1 does not appear to exceed 5 per cent.

The objective for the funds rate is to be raised or lowered within its range if the rate of growth of *M*-2 appears to be close to or beyond the upper or lower limit of its range. Weight is to be given to *M*-1 if it appears to be growing at a rate close to or above its limit.

If the rates of growth in the aggregates appear to be falling outside the limits of the indicated ranges at a time when the objective for the funds rate has already been moved to the corresponding limit of its range, the Manager will promptly notify the Chairman, who will then decide whether the situation calls for supplementary instructions from the Committee.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None.

Subsequent to the meeting, on December 8, nearly final estimates indicated that in November *M*-1 had declined and *M*-2 had ex-

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panded at a slow pace. For the November–December period, staff projections suggested that the annual rates of growth in *M*-1 and *M*-2 would be about ¼ per cent and 6¼ per cent, respectively; for *M*-2, the projected rate was close to the lower limit of the 6 to 9½ per cent range specified by the Committee. During recent weeks the Federal funds rate had averaged about 9⅞ per cent. In light of the behavior of the aggregates, the Manager might, under normal circumstances, have sought to reduce the funds rate to about the 9¾ per cent lower limit of its specified range. Given current circumstances, however, Chairman Miller recommended that the Manager be instructed to continue to aim for a Federal funds rate of about 9⅞ per cent during the period before the next regular meeting of the Committee, unless growth of the aggregates appeared to weaken significantly further.

On December 8, 1978, the Committee modified the domestic policy directive adopted at its meeting of November 21, 1978, to call for open market operations directed at maintaining the Federal funds rate at about the prevailing level of 9⅞ per cent during the period before the next meeting unless growth of the aggregates appeared to weaken significantly further.

Votes for this action: Messrs. Miller, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, Winn, and Timlen. Votes against this action: None. Absent and not voting: Mr. Volcker. (Mr. Timlen voted as alternate for Mr. Volcker.)

2. Authorization for Foreign Currency Operations

At its meeting of March 21, 1978, the Committee had reaffirmed an agreement with the Treasury under which the Federal Reserve would undertake to ''warehouse'' foreign currencies held by the Exchange Stabilization Fund (ESF)—that is, to make spot purchases of foreign currencies from the ESF and simultaneously to make forward sales of the same currencies at the same exchange rate to the ESF—if that should prove necessary to enable the ESF to deal with potential liquidity strains. Specifically, the Committee had agreed that the Federal Reserve would be prepared, if requested by the Treasury, to warehouse up to $1½ billion of eligible foreign

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currencies, of which half would be for periods of up to 12 months and half for periods of up to 6 months.

On December 14, 1978, the Committee amended paragraph 1A of the authorization for foreign currency operations to provide for transactions in foreign currencies directly with the U.S. Treasury as well as with the ESF. Concurrently, the Committee agreed to raise the amount of eligible foreign currencies that the Federal Reserve would be prepared to warehouse to $1¾ billion at this time. These actions were taken in view of the first issuance of Treasury securities denominated in foreign currencies as one of the measures announced on November 1 in implementation of the broad program to strengthen the dollar and thereby to counter continuing domestic inflationary pressures. The Treasury was scheduled to receive payment of somewhat more than $1½ billion equivalent of German marks on December 15, 1978.

As amended, paragraph 1A read as follows:

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, for System Open Market Account, to the extent necessary to carry out the Committee's foreign currency directive and express authorizations by the Committee pursuant thereto, and in conformity with such procedural instructions as the Committee may issue from time to time:

A. To purchase and sell the following foreign currencies in the form of cable transfers through spot or forward transactions on the open market at home and abroad, including transactions with the U.S. Treasury, with the U.S. Exchange Stabilization Fund established by Section 10 of the Gold Reserve Act of 1934, with foreign monetary authorities, with the Bank for International Settlements, and with other international financial institutions:

Austrian schillings	Italian lire
Belgian francs	Japanese yen
Canadian dollars	Mexican pesos
Danish kroner	Netherlands guilders
Pounds sterling	Norwegian kroner
French francs	Swedish kronor
German marks	Swiss francs

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None.

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MEETING HELD ON DECEMBER 19, 1978

1. Domestic Policy Directive

The information reviewed at this meeting suggested greater strength in economic activity than had been evident at the time of the Committee's meeting a month earlier; growth in output of goods and services in the current quarter now appeared to be somewhat faster than the annual rate of 3.4 per cent indicated for the third quarter by preliminary estimates of the Commerce Department. The rise in average prices, as measured by the fixed-weight price index for gross domestic business product, appeared to be close to the annual rate of 8.2 per cent estimated for the third quarter.

Staff projections for the year ahead differed little from those prepared a month earlier. They continued to suggest a gradual slowing in the growth of economic activity as the year progressed. The rise in average prices was projected to remain rapid during 1979 and the rate of unemployment to rise marginally.

In November, the index of industrial production advanced an estimated 0.7 per cent, somewhat more than the gains in the preceding 2 months but close to the average monthly increase since the beginning of the year. Nonfarm payroll employment grew substantially in November for the second consecutive month. In manufacturing also, a large increase in employment was registered for the second month in a row and the average workweek rose somewhat further. The unemployment rate was unchanged at 5.8 per cent, close to its low for the year.

The dollar value of total retail sales expanded substantially in November and revised data indicated a sizable advance for October as well. Unit sales of new automobiles declined somewhat in November.

Total housing starts were at an annual rate of 2.1 million units in both October and November. Sales of new and existing single-family houses rose to new highs in October.

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The latest Department of Commerce survey of business plans, taken in late October and November, suggested that spending for plant and equipment would expand at an annual rate of nearly 16 per cent in the current quarter but at the markedly lower rate of about 8 per cent in the first half of 1979. The survey also indicated that in 1978 as a whole fixed investment outlays would be 12.7 per cent greater than in 1977. Manufacturers' new orders for nondefense capital goods advanced sharply in October, following sizable increases in other recent months.

The index of average hourly earnings of private nonfarm production workers increased at an annual rate of 8.3 per cent over the first 11 months of 1978, nearly 1 percentage point above the rise during 1977. Average producer prices of finished goods rose substantially in November for the third consecutive month despite more moderate increases in producer prices of food products than in the two earlier months. In October, the consumer price index advanced at an annual rate of 9 per cent, and the rate of increase for the year to date—about 9½ per cent—was nearly 3 percentage points above that during 1977.

In foreign exchange markets the trade-weighted value of the dollar against major foreign currencies fell sharply following the OPEC announcement on December 17 of a larger-than-anticipated increase in oil prices for 1979. Over the previous few weeks the dollar had declined slightly on balance. Nevertheless, at the time of this meeting it was still about 7 per cent above its low reached just prior to the November 1 announcement of the new program to strengthen the dollar. The U.S. trade deficit in October remained close to the annual rate recorded in the second and third quarters but well below that in the previous two quarters.

The growth of total credit at U.S. commercial banks was appreciably slower in November than in September and October. However, bank loans other than security loans continued to expand rapidly. To finance this expansion banks liquidated a sizable amount of security holdings and issued a substantial volume of large-denomination time deposits. Outstanding commercial paper of nonfinancial businesses rose considerably in November for the second consecutive month.

The narrowly defined money supply (*M*-1) declined at an annual rate of about 4½ per cent in November. The contraction reflected,

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among other things, the shifts of funds from demand deposits to savings deposits associated with the introduction of the automatic transfer service (ATS) and effects of the substantial rise in short-term market interest rates since April. Meanwhile, growth of *M*-2 and *M*-3 slackened further. Sales of 6-month money market certificates at commercial banks and nonbank thrift institutions continued strong in November, but savings deposits and time deposits subject to interest rate ceilings contracted at commercial banks. Total inflows of funds to nonbank thrift institutions slowed in November after growing rapidly in the preceding 3 months; the rate of expansion was still considerably above that in the first half of the year. Over the first 11 months of the year, *M*-1, *M*-2, and *M*-3 grew at annual rates of about 7¼, 8¼, and 9¼ per cent, respectively.

At its meeting on November 21, the Committee had agreed that early in the inter-meeting period System open market operations should be directed toward attaining a weekly-average Federal funds rate of about 9⅞ per cent, slightly above the level prevailing at that time. Subsequently, the objective for the Federal funds rate was to be raised or lowered within the range of 9¾ to 10 per cent. In setting a specific objective for the funds rate, the Manager of the System Open Market Account was to be guided mainly by a range of tolerance of 6 to 9½ per cent for the annual rate of growth in *M*-2 over the November–December period, provided that the rate of growth in *M*-1 over the same period did not appear to exceed 5 per cent.

Immediately following the November 21 meeting the Manager began to seek bank reserve conditions consistent with an increase in the weekly-average Federal funds rate to around 9⅞ per cent. Incoming data during the inter-meeting period suggested initially that growth in *M*-2 would be well within the range specified by the Committee and that growth in *M*-1 would be below 5 per cent. In subsequent weeks, newly available data led to progressively lower estimates of growth, and by the end of the first week in December the projections might, under normal circumstances, have called for a reduction in the objective for the Federal funds rate to 9¾ per cent. On December 8, however, the Committee approved a recommendation by the Chairman to instruct the Manager to continue aiming for a Federal funds rate of 9⅞ per cent during

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the period before the next regular meeting of the Committee, unless growth of the aggregates should appear to weaken significantly further.

Most market interest rates rose further during the inter-meeting period, as financial markets seemed to react to indications of continued strength in business conditions, added evidence of intense inflationary pressures, and the OPEC announcement of a large increase in oil prices. Commercial banks raised the loan rate to prime business borrowers from 11 per cent to 11½ per cent during the period. In mortgage markets interest rates continued to rise.

In the Committee's discussion of the economic situation and outlook, most members expressed little or no disagreement with the staff projection of a gradual slowing of the expansion during 1979 and of a slight rise in the unemployment rate. At the same time, however, the observation was made that the latest information provided contradictory indications of underlying trends in economic activity, and some members commented on the prospects for alternative courses of activity. The members continued to anticipate that average prices of goods and services would rise rapidly, and it was observed that the outlook for inflation had been worsened by the recent OPEC announcement of a substantial rise in oil prices during 1979.

With respect to some of the economic information that had become available recently, it was suggested that the retail sales and employment statistics—and the apparent rate of growth in GNP in the current quarter—indicated underlying strength, while the behavior of the monetary aggregates so far in the fourth quarter could be symptomatic of current or near-term weakness in demands for goods and services. Similarly, the latest data on new orders for nondefense capital goods and on construction contract awards were strong, but according to the Commerce Department's survey of business plans, plant and equipment expenditures in the first half of 1979 would be weak.

Concerning the over-all situation, it was suggested on the one hand that the current and prospective pace of growth in activity was too rapid, that output was beginning to press against the limits of capacity, and that inflationary pressures—which for a long time had been greater than generally projected—were still increasing. An alternative appraisal of the latest data was that the strength

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in the current quarter, especially in consumer spending, most likely was an aberration—similar to others during the past few years—and that economic activity was remarkably well balanced for the present stage of the expansion. It was also suggested, however, that the strength in demands and activity, although possibly persisting for a quarter or two, might culminate in a recession in the second half of 1979.

At its meeting in October the Committee had agreed that from the third quarter of 1978 to the third quarter of 1979 growth of *M*-2 and *M*-3 within ranges of 6½ to 9 per cent and 7½ to 10 per cent, respectively, appeared to be consistent with broad economic aims. *M*-1 was expected to grow over that period within a range of 2 to 6 per cent, depending in part on the speed and extent of transfers from demand to savings deposits resulting from the introduction of ATS. The associated range for the rate of growth in commercial bank credit was 8½ to 11½ per cent. The Committee had also decided that growth of *M*-1+ within a range of 5 to 7½ per cent appeared to be generally consistent with the ranges of growth for the other monetary aggregates. It had been agreed that the longer-run ranges, as well as the particular aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings.

In the discussion of policy for the period immediately ahead, most members of the Committee advocated some additional firming in money market conditions. A few members preferred to direct operations toward maintaining the money market conditions currently prevailing. No member recommended an easing in money market conditions per se, but one suggested that whether money market conditions were firmed or eased be determined altogether on the basis of the incoming evidence on the behavior of the monetary aggregates.

Several reasons were advanced for some additional firming in money market conditions. Available economic data suggested that growth of output had not yet been slowed and that inflationary pressures remained intense. The strength of demands for bank loans and other credit seemed to provide a more reliable indication of underlying economic conditions than did the recent weakness of growth in the monetary aggregates. In any case, it was observed, weakness in monetary expansion following a long period of strong

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growth could be accepted for a time. Some additional firming in money market conditions, moreover, would help to maintain public confidence in the program to moderate inflation and to support the foreign exchange value of the dollar.

In support of the preference for maintaining prevailing money market conditions, rather than firming, it was observed that over the preceding 2 months the Committee had increased monetary restraint substantially. Because the evidence on current and prospective economic developments was conflicting, the Committee ought to pause and evaluate the effects of its recent actions before contemplating additional firming; if the unexpected shortfall in monetary expansion persisted, it might contribute to a recession. The uncertainties in the current situation also provided the grounds for the proposal to base the Committee's objective for money market conditions altogether on the incoming evidence on the behavior of the monetary aggregates: It was suggested that whether fundamental economic conditions were strong or weak would inevitably become evident in renewal of rapid monetary expansion or in continuation of sluggish expansion, leading in either case to appropriate objectives for money market conditions.

At the conclusion of the discussion the Committee agreed to instruct the Manager to direct open market operations toward raising the Federal funds rate to 10 per cent or slightly higher early in the period before the next regular meeting and subsequently to maintain the rate within a range of 9¾ to 10½ per cent. With regard to the objective for the rate within that range, the Committee instructed the Manager to be guided by ranges of tolerance for the annual rates of growth of *M*-1 and *M*-2 of 2 to 6 per cent and 5 to 9 per cent, respectively. Thus, after a 2-month interruption, the Committee agreed to return to its practice of specifying a range rather than only an upper limit for *M*-1 and of instructing the Manager to give approximately equal weight to the behavior of *M*-1 and *M*-2 in assessing the behavior of the aggregates; it did so because recent experience had suggested that the impact of ATS on the annual rate of growth of *M*-1 could be estimated within fairly narrow limits. However, the Committee decided that the Manager should respond more quickly to relatively high than to relatively low rates of growth in the aggregates. Specifically, the objective for the funds rate was to be raised in an orderly fashion

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within its range if the 2-month growth rates of *M*-1 and *M*-2 appeared to be significantly above the midpoints of the indicated ranges. On the other hand, the objective was to be lowered in an orderly fashion only if the 2-month growth rates appeared to be approaching the lower limits of the indicated ranges.

The next regular meeting of the Committee was scheduled for February 6, 1979, but it was understood that a telephone conference would be held in mid-January to consider whether supplementary instructions were needed. It was also understood that the Chairman would call upon the Committee to consider the need for supplementary instructions if significant inconsistencies appeared to be developing among the Committee's objectives or if, before mid-January, the behavior of the monetary aggregates appeared to call for a reduction in the objective for the Federal funds rate toward the lower limit of its range.

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

The information reviewed at this meeting suggests that in the current quarter real output of goods and services has picked up somewhat from the rate in the third quarter. In November, as in October, the dollar value of total retail sales expanded substantially. Industrial production and nonfarm payroll employment rose considerably further, and the unemployment rate remained at 5.8 per cent. Over recent months, broad measures of prices and the index of average hourly earnings have risen rapidly.

The trade-weighted value of the dollar against major foreign currencies declined sharply following OPEC's announcement on December 17 of increased oil prices for 1979, after having declined slightly over the previous few weeks, but it remains substantially above the low reached just prior to the actions taken on November 1 to strengthen the dollar. The U.S. trade deficit in October was at about the rate recorded in the second and third quarters.

M-1 declined in November, only in part because of shifts of funds from demand deposits to savings deposits after the introduction of the automatic transfer service (ATS) at the beginning of the month. Over the first 11 months of 1978, *M*-1 grew at an annual rate of about 7¼ per cent. Growth of *M*-2 and *M*-3 slackened further in November; they grew at rates of about 8¼ and 9¼ per cent, respectively, over the first 11 months of the year. Inflows of deposits to nonbank thrift institutions slowed in November, after having

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grown rapidly in the preceding 3 months. Market interest rates in general have risen further in recent weeks.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster monetary and financial conditions that will resist inflationary pressures while encouraging continued moderate economic expansion and contributing to a sustainable pattern of international transactions. At its meeting on October 17, 1978, in setting ranges for the monetary aggregates, the Committee recognized the uncertainties concerning the effects that the November 1 introduction of ATS would have on measures of the money supply, especially *M*-1. Against that background, the Committee agreed that appropriate monetary and financial conditions would be furthered by growth of *M*-2 and *M*-3 from the third quarter of 1978 to the third quarter of 1979 within ranges of 6½ to 9 per cent and 7½ to 10 per cent, respectively. The narrowly defined money supply (*M*-1) was expected to grow within a range of 2 to 6 per cent over the period, depending in part on the speed and extent of transfers from demand to savings deposits resulting from the introduction of ATS. The associated range for bank credit is 8½ to 11½ per cent. Growth of *M*-1+ (*M*-1 plus savings deposits at commercial banks and NOW accounts) in a range of 5 to 7½ per cent was thought to be generally consistent with the ranges of growth for the foregoing aggregates. These ranges are subject to reconsideration at any time as conditions warrant.

In the short run, the Committee seeks to achieve bank reserve and money market conditions that are broadly consistent with the longer-run ranges for monetary aggregates cited above, while giving due regard to the program for supporting the foreign exchange value of the dollar, to developing conditions in domestic financial markets, and to uncertainties associated with the introduction of ATS. Early in the period before the next regular meeting, System open market operations are to be directed at attaining a weekly average Federal funds rate slightly above the current level. Subsequently, operations shall be directed at maintaining the weekly average Federal funds rate within the range of 9¾ to 10½ per cent. In deciding on the specific objective for the Federal funds rate the Manager shall be guided mainly by the relationship between the latest estimates of annual rates of growth in the December–January period of *M*-1 and *M*-2 and the following ranges of tolerance: 2 to 6 per cent for *M*-1 and 5 to 9 per cent for *M*-2. If, giving approximately equal weight to *M*-1 and *M*-2, their rates of growth appear to be significantly above the midpoints of the indicated ranges, the objective for the funds rate shall be raised in an orderly fashion within its

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range; if their rates of growth appear to be approaching the lower limits of the indicated ranges, the funds rate shall be lowered in an orderly fashion within its range.

If the rates of growth in the aggregates appear to be falling outside the limits of the indicated ranges at a time when the objective for the funds rate has already been moved to the corresponding limit of its range, the Manager will promptly notify the Chairman, who will then decide whether the situation calls for supplementary instructions from the Committee.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Willes, and Winn. Votes against this action: Mrs. Teeters and Mr. Wallich.

Mrs. Teeters dissented from this action because she believed that for the time being open market operations should be directed toward maintaining the money market conditions currently prevailing. In her view, the Committee should wait to evaluate the effects of the substantial firming in money market conditions of the past 2 months before contemplating any additional firming.

Mr. Wallich dissented from this action because he favored a somewhat more restrictive policy posture than that adopted by the Committee. In his opinion, the underlying economic situation was still strong and the strength of demands was adding to inflationary pressures and expectations while interest rates were not high in real terms and were not exerting strong restraint.

Subsequent to the meeting, on December 29, 1978, projections of growth in the monetary aggregates suggested that for the December–January period *M*-2 would grow at an annual rate well below the lower limit of the 5 to 9 per cent range specified by the Committee and that *M*-1 would grow at a rate in the lower portion of its range of 2 to 6 per cent. Since the meeting of the Committee on December 19 the Manager had been aiming for a Federal funds rate of about 10 per cent or slightly above, although Federal funds had been trading at higher levels in response to exceptional demands for excess bank reserves near the end of the year. The behavior of the aggregates would have called for a reduction in the objective for the funds rate toward the 9¾ per cent lower limit of its specified range. However, in view of uncertainties about the interpretation of the behavior of the aggre-

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gates at this time, and against the background of domestic and international economic and market conditions, Chairman Miller recommended that the Manager be instructed to continue to aim for a Federal funds rate of 10 per cent or slightly above, pending a review of the situation in the telephone conference, tentatively planned for January 12.

> On December 29, 1978, the Committee modified the domestic policy directive adopted at its meeting of December 19, 1978, to call for open market operations directed at maintaining the weekly-average Federal funds rate at about 10 per cent or slightly above.
>
> > Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None.

On January 12 the Committee held a telephone conference to review the situation and to consider whether supplementary instructions were needed. However, no change was made in the instruction to the Manager to continue to direct open market operations toward maintaining the weekly-average Federal funds rate at about 10 per cent or slightly above.

2. Authorization for Foreign Currency Operations

Paragraph ID of the Committee's authorization for foreign currency operations authorizes the Federal Reserve Bank of New York, for the System Open Market Account, to maintain an over-all open position in all foreign currencies not to exceed $1.0 billion, unless a larger position is expressly authorized by the Committee. On November 1, 1978, an open position of $5 billion had been authorized. At the meeting on December 19, 1978, the Committee authorized an increase in this limit to $8 billion to provide further flexibility for Federal Reserve operations in the foreign exchange markets undertaken pursuant to the Committee's foreign currency directive.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None.

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Pursuant to an agreement with the Treasury under which the Federal Reserve would undertake to "warehouse" foreign currencies—that is, to make spot purchases of foreign currencies and simultaneously to make forward sales of the same currencies at the same exchange rate—the Committee had agreed on December 14, 1978, to raise the amount that the Federal Reserve would be prepared to warehouse from $1½ billion to $1¾ billion equivalent of such foreign currencies. That action had been taken in view of the impending receipt by the Treasury of somewhat more than $1½ billion dollars equivalent of German marks resulting from its first issuance of securities denominated in foreign currencies as one of the measures of the broad program announced on November 1 to strengthen the dollar.

At this meeting the Committee agreed to raise the amount of eligible foreign currencies that the Federal Reserve would be prepared to warehouse to $5 billion. The Committee also agreed to warehouse such currencies for periods of up to 12 months; previously the agreement had provided that half of the authorized amount would be for periods of up to 6 months and half for periods of 12 months. These actions were taken in view of additional Treasury offerings of securities denominated in foreign currencies in prospect for early 1979.

Votes for these actions: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against these actions: None.

3. Authorization for Domestic Open Market Operations

On January 15, 1979, Committee members voted to increase from $3 billion to $5 billion the limit on changes between Committee meetings in System Account holdings of U.S. Government and Federal agency securities specified in paragraph 1(a) of the authorization for domestic open market operations, effective immediately, for the period ending with the close of business on February 6, 1979.

Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs.

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> Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None.

This action was taken on recommendation of the System Account Manager. The Manager had advised that large-scale sales of securities since the December meeting—required primarily to counter the effect on member bank reserves of an unusually and unexpectedly high level of float—had reduced the leeway for further sales to about $100 million. It appeared likely that additional sales would be required because current projections indicated a need for further reserve-absorbing operations over the coming weeks.

Subsequently, Committee members voted to increase the limit specified in paragraph 1(a) by an additional $1 billion, to $6 billion, effective immediately, for the period ending with the close of business on February 6, 1979.

> Votes for this action: Messrs. Miller, Volcker, Baughman, Coldwell, Eastburn, Partee, Mrs. Teeters, Messrs. Wallich, Willes, and Winn. Votes against this action: None.

This action was taken on recommendation of the Manager. On January 26 he had advised that, despite the Committee's action on January 15 to raise the inter-meeting limit to $5 billion, the leeway available for further sales would be only about $350 million as of the close of business on January 26. Since January 15, required reserves had been weaker than had been expected, and a decline of currency in circulation had provided reserves while float had remained high.

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Federal Reserve Operations in Foreign Currencies

The Federal Reserve, along with the U.S. Treasury, intervened in foreign exchange markets many times throughout 1978 to counter disorderly market conditions. As part of the measures announced on November 1, the System intervened actively to correct disorderly conditions and limit further the excessive depreciation of the dollar. In addition, the System at times acquired foreign currencies to repay swap indebtedness. Gross sales by the System of foreign currencies during the year totaled $7,315 million equivalent, and gross purchases totaled $3,304 million equivalent. Most sales of foreign currency occurred in the first and fourth quarters, while purchases were concentrated in the second and third quarters.

The dollar was under downward pressure during most of the year as the U.S. trade and current accounts continued in large deficit and U.S. inflation accelerated. Foreign central banks purchased large amounts of dollars, particularly in the first and fourth quarters when pressure on the dollar was especially severe. From the end of September 1977 to April 3, 1978, there was a 10 per cent drop in the dollar's trade-weighted value against 10 major foreign currencies. During a brief respite in the spring the dollar index rose by 4 per cent. Then from mid-May to the end of October, the dollar fell by more than 15 per cent despite some evidence of improvement in fundamental economic conditions beginning in the summer. The periods of decline were frequently characterized by exchange market disorder, as evidenced by wide bid–ask spreads and large and abrupt variations in exchange rates. On several occasions, the dollar's average value changed by more than 1 per cent in a day.

As part of a broad program to strengthen the dollar announced on November 1, the Federal Reserve increased its swap facilities with the central banks of West Germany, Switzerland, and Japan by $7.6 billion to a new total of $15 billion. The immediate market response to the program was a sharp appreciation in the value of the dollar. Periods of pressure on the dollar after the initiation

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of the support package were met with forceful intervention by the System in German marks, Swiss francs, and Japanese yen, and by the U.S. Treasury in German marks and Japanese yen.

The Federal Reserve's intervention for the account of the System in 1978 was conducted mostly in German marks. The System's gross sales of marks totaled $6,045 million equivalent, $5,356 million of which was financed by swap drawings on the German Federal Bank with the remainder coming from System balances. The System's gross purchases of marks totaled $2,274 million equivalent, most of which was bought during the second and third quarters in order to repay swap debts or to accumulate mark balances. A total of $1,722 million in mark-denominated swap drawings was repaid during the year.

The System's gross sales of Swiss francs during the year totaled $1,081 million equivalent. Most of the sales occurred in the fourth quarter, and most were financed by swap drawings. Gross purchases of Swiss francs totaling $942 million equivalent were made to repay outstanding swap debts. The purchases included $652 million equivalent that were acquired on a regular basis to repay Swiss franc liabilities incurred before August 15, 1971. The System purchased the required Swiss francs directly from the Swiss National Bank against dollars, German marks, and French francs. After repayments in 1978, there remained Swiss franc liabilities incurred by the System before August 1971 of $328 million equivalent, valued at the market exchange rate on December 29, 1978.

The System began operating in Japanese yen on November 1. Gross sales amounted to $158 million equivalent, nearly all of which was financed by swap drawings. Gross purchases totaled $57 million equivalent, which were used to liquidate swap debt and to accumulate a small yen balance.

The System's total outstanding swap debt at the end of the year was $5,752 million equivalent. The System had losses of $506 million on foreign exchange operations in 1978; that figure includes realized losses of $297 million and unrealized losses of $209 million resulting from the revaluation of foreign exchange holdings and outstanding commitments at current exchange rates. Of these amounts, $264 million and $150 million, respectively, reflect realized and unrealized losses associated with Swiss franc commitments

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Federal Reserve Purchases and Sales (−) of Foreign Currencies, 1978

Millions of dollars equivalent

Currency	Q1	Q2	Q3	Q4	Year
German marks	112	946	732	484	2,274
	−1,115	−93	−454	−4,383	−6,045
Swiss francs	162	237	192	351	942
	−69	−6	−155	−851	−1,081
Japanese yen	....	....	....	57	57
	....	....	....	−158	−158
French francs	31	....	....	....	31
	−31	....	....	....	−31
Total	**305**	**1,183**	**924**	**892**	**3,304**
	−1,215	−99	−609	−5,392	−7,315

NOTE. Purchases of $652 million equivalent of Swiss francs to repay pre-1971 swap debt are included. Of that amount, $195 million was against German marks and $31 million against French francs, which were acquired simultaneously with the Swiss francs in the market.

entered into before August 15, 1971. The total unrealized net loss was calculated using market exchange rates of December 29, 1978, to value the System's foreign currency holdings and foreign currency commitments; liquidation or payment may actually take place at exchange rates that differ from these rates. There were no swap drawings on the Federal Reserve by foreign central banks during 1978.

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Consumer Affairs

INTRODUCTION

Acting in concert with other Federal regulators of banks and thrift institutions, the Board of Governors took a number of actions in 1978 supporting and assuring the protection of consumers' rights. Regulations, hearings, and educational efforts for consumers, creditors, and financial institutions were the main focus of the efforts.

To fulfill its congressional mandate, the Board held nationwide hearings, offered two sets of proposals, and then issued final regulations implementing the Community Reinvestment Act of 1977.[1] It also proposed regulations for consumer protection under the Electronic Fund Transfer Act. These regulations are described in detail below.

In two other major actions, the five Federal regulators of financial institutions issued uniform guidelines for the enforcement of the Truth in Lending Act and proposed guidelines for the enforcement of the Equal Credit Opportunity Act, its implementing Regulation B, and the Fair Housing Act.[2]

During the year, the Federal Reserve System pursued a broad educational program in connection with the consumer credit protection laws.

First, in an effort to assist State member banks in complying with the new Fair Debt Collection Practices Act, the Board issued a fact sheet and a set of questions and answers describing the responsibilities of banks under the law. The act makes abusive and deceptive debt collection practices illegal for those it defines as debt collectors—generally, anyone who regularly tries, directly or indirectly, to collect consumer debt for someone else. The Board invited anyone who believes a bank has violated the act to lodge a complaint with the near-

[1] The Federal Reserve Board joined the Comptroller of the Currency, the Federal Deposit Insurance Corporation (FDIC), and the Federal Home Loan Bank Board (FHLBB) in issuing common CRA rules, known as the Community Reinvestment Act Regulations (12 C.F.R. Part 228 for the Federal Reserve System).

[2] In these instances the regulators listed in note 1 above were joined by the National Credit Union Administration.

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est Federal Reserve Bank or with the Board, and said the Federal Reserve would follow up on all such complaints (or refer them to the appropriate Federal regulator if the complaint does not concern a State member bank). Federal Reserve Bank examiners were given special instructions to watch for evidence of violations of this act.

Second, the Board published several new pamphlets explaining consumer rights and protections under Federal consumer credit protection laws and other pamphlets of interest to consumers. These were: *Consumer Handbook to Credit Protection Laws; How to File a Consumer Credit Complaint; If You Use a Credit Card; Truth in Leasing; The Equal Credit Opportunity Act and Credit Rights in Housing; Government in the Sunshine—A Guide to Meetings of the Board of Governors of the Federal Reserve System;* and *Guide to Federal Reserve Regulations.* At the end of 1978, 11 consumer education pamphlets were available to the public without charge.

Demand for the *Consumer Handbook,* which was published near the end of 1978, was unusually heavy. The *Handbook* summarizes the main provisions of seven major consumer credit protection laws: Truth in Lending, Truth in Leasing, the Real Estate Settlement Procedures Act, the Equal Credit Opportunity Act, the Home Mortgage Disclosure Act, the Fair Credit Reporting Act, and the Fair Credit Billing Act. The *Handbook* also contains a glossary of technical terms used in credit transactions and in the consumer credit protection laws and regulations.

The *Handbook* explains how to shop for the least costly credit, the meaning of key terms such as finance charge and annual percentage rate, consumer protections under Truth in Leasing and what to look for when leasing personal property, how to apply for credit, and the types of information creditors may and may not request in considering credit applications. It explains the "Three C's"—capacity (to repay), character, and collateral—that creditors rely on in determining creditworthiness. One section deals with discrimination against women in the granting of credit and summarizes the defenses the new legislation provides: ". . . you may not be denied credit just because you are a woman or just because you are married, single, widowed, divorced or separated." The procedures for determining whether a consumer has been discriminated against when credit is denied, and for correcting errors in a credit history, are described, as

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well as what the consumer can do, under the Fair Credit Billing Act, when defective merchandise is delivered.

In addition to the Board's efforts, the Federal Reserve Banks have also been active in advising consumers of their protections and rights. In 1978 the Federal Reserve Bank of Philadelphia produced a film on the antidiscrimination provisions of the Equal Credit Opportunity Act, "To Your Credit," available to all on loan. The Federal Reserve Bank of San Francisco developed a series of spot TV announcements highlighting System consumer education pamphlets and citing the San Francisco Bank as a source of consumer credit protection information.

At the end of the year, plans were being made with professional educational organizations for the development of teaching aids, study units, and a curriculum package on the consumer credit laws. In response to the Board's encouragement of the private sector, textbook publishers have indicated interest in conducting, with the help of Federal consumer offices, programs to inform educational publishers on changes in consumer laws and regulations and to identify gaps in curriculum materials.

Community Reinvestment Act Regulations

In October 1977, the Congress passed the Community Reinvestment Act of 1977 as Title VIII of the Housing and Community Development Act of 1977 (12 U.S.C. 2901).

The CRA requires each appropriate Federal financial supervisory agency to use its authority to encourage the institutions it examines to help meet the credit needs of the communities in which they are chartered, consistent with their own safe and sound operation. Further, the act calls for regulators to consider a lender's performance in helping to meet the credit needs of its community when that lender applies for a branch, a merger, a charter, or Federal deposit insurance. Past performance may be grounds for denial.

Early in 1978, the Board, the Comptroller, the FDIC, and the FHLBB decided that the objectives of the CRA could be accomplished more effectively and efficiently if the agencies developed substantively identical regulations and procedures. Also, because of broad public interest, the agencies felt it would be desirable at the outset to obtain the views of a wide spectrum of the public and financial institutions. Accordingly, the agencies requested public comment

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on 26 questions relating to how the agencies could best encourage the financial institutions they supervise to help meet the credit needs of their communities, including low- and moderate-income neighborhoods, consistent with safe and sound operation. Public hearings were held at the Federal Reserve Board in Washington, D.C., and in Boston, Atlanta, Dallas, Chicago, New York, and San Francisco in the spring of 1978. The written and oral comments received during these hearings were extremely helpful to the agencies in developing the regulations. In addition, on several occasions the Board staff discussed regulatory approaches with the Consumer Advisory Council.

On June 30, 1978, the four agencies published for comment proposed regulations to implement the CRA. Again, the comments that were received greatly assisted in clarifying the proposed regulations. On October 10, 1978, the agencies published their final, substantively identical CRA regulations, to be effective November 6.

On November 22, the agencies made public the procedures that had been developed by an interagency task force for the examination of financial institutions covered by the CRA. Both the regulations and the examination procedures emphasize that financial institutions can use a variety of means to help meet the credit needs of their local communities and to enhance communication with members of their communities regarding these needs.

All examinations for consumer affairs compliance of State member banks conducted by the Federal Reserve Board on or after November 6, 1978, have included an assessment of the performance of the banks in helping to meet the credit needs of their communities. In addition, all decisions by the Federal Reserve System since November 6 on applications covered by the CRA have included an evaluation of an applicant's performance in helping to meet those credit needs.

The four agencies have also adopted joint minimum procedures for notifying the public regarding the filing of applications with the agencies that are covered by the CRA. These procedures became effective on November 6.

Each Federal Reserve Bank has designated a member of its staff as a Community Reinvestment Act Officer to assist the public and financial institutions on matters pertaining to the CRA.

The agencies have agreed that an interagency staff task force on the CRA will continue to monitor the implementation of the regulations and the conduct of examinations, and to guide the public and

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financial institutions on questions relating to the CRA. The Board believes that as the agencies gain experience in implementing the CRA, they will be able to refine their examination procedures and strengthen their ability to encourage the financial institutions they supervise to help meet the credit needs of their communities.

In November 1978 the four Federal agencies with CRA enforcement responsibilities announced that they had developed common procedures for the examination of affected financial institutions under the requirements of the CRA.[3]

Electronic Funds Transfer Regulations

On December 26, 1978, pursuant to the Electronic Fund Transfer Act, the Board issued and invited comment on an initial set of regulations relating to sections of the act due to become effective February 8, 1979. These sections limit a consumer's liability for unauthorized use of an EFT card and restrict unsolicited issuance of EFT cards.

The Board's proposals, pending at the year-end, included a set of transitional disclosure rules—transitional because restraints on issuance of unsolicited EFT cards were to be effective in February 1979 while other provisions of the act were not to become effective until May 1980—that required disclosure of the following: consumer liability for unauthorized use of an EFT card; the way to report lost or stolen cards; the kind of electronic funds transfers the consumer may make and the charges involved; the circumstances under which the EFT card issuer will disclose information about the customer's account to others; the right of the consumer to stop payment on an EFT transaction and to receive a record of transactions; a summary of error-resolution procedures or a statement of the lack of such procedures; and a statement of the liability that the financial institution will assume for failure to make transfers.

Since the EFT Act permits unsolicited issuance of credit cards, which is prohibited under Truth in Lending, the Board proposed that the EFT Act should not be regarded as nullifying that prohibition and that Truth in Lending should govern the issuance of combined EFT–credit cards.

[3] In accordance with Section 805 of the act, the above paragraphs describe the steps taken by the Board, in conjunction with the three other financial supervisory agencies, to develop regulations and procedures to implement the CRA.

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The Board proposed that the consumer's liability for unauthorized use of EFT cards be governed by the kind of transaction—EFT or credit card—made. Under this proposal and the terms of the EFT Act, the consumer's liability for an unauthorized EFT shift of funds out of an account would be $50 if the consumer reported loss of the card within two business days of learning of it. Under some other circumstances, losses would be limited to $500; and they would be unlimited if the consumer failed to report the loss of a card within 60 days.

Early in 1979, Governor Nancy H. Teeters, on behalf of the Board, suggested to the Congress changes in the EFT, Fair Credit Billing, and Truth in Lending Acts to coordinate their provisions. In particular, the Board suggested that maximum consumer liability for unauthorized use of an EFT card might be limited to $50.

Consumer Advisory Council

During 1978 the Board met four times with its Consumer Advisory Council. On December 28, William D. Warren, Dean of the School of Law of the University of California at Los Angeles, was named Chairman, and Marcia A. Hakala of the University of Nebraska at Omaha was named Vice Chairman. Dr. Warren succeeded Leonor K. Sullivan, St. Louis, Missouri, a former member of the Congress who specialized in the development of consumer credit protection laws. Mrs. Sullivan had chaired the Council since its inception. The Board also selected eight new members of the Council from a roster of hundreds of names submitted at its invitation by the public to replace members whose terms expired.

The Council advises the Board on its responsibilities in the field of consumer credit protection laws. It was established in 1976 by the Congress, at the suggestion of the Board, as a statutory part of the Federal Reserve System. Members come from all parts of the Nation and include a broad representation of consumer and creditor interests.

Reports on Consumer Affairs

Following this introduction are the 1978 reports to the Congress by the Federal Reserve Board on Truth in Lending and Regulation Z; Equal Credit Opportunity and Regulation B; and Section 18(f)

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of the Federal Trade Commission Act (unfair and deceptive practices) and Regulation AA. These reports describe the Federal Reserve's activities during the year in promulgating rules and in securing compliance under these laws and regulations.

The final guidelines for the enforcement of Truth in Lending and Regulation Z and compliance guidelines proposed for enforcement of the Equal Credit Opportunity Act and Regulation B are discussed in these annual reports, along with other Federal Reserve actions during 1978 in these fields:

Amendment of Regulation B to define adverse action in a credit transaction at the point of sale.

A Board proposal to tighten the provisions of Regulation B to bring arrangers, as well as extenders, of credit within the scope of the regulation and to eliminate certain exemptions applying to business transactions.

Revision of the Board's procedures for issuing official staff interpretations under Regulation B and Regulation Z designed to give greater opportunity for public participation.

The annual report concerning the Board's responsibilities under Section 18(f) of the FTC Act describes the results of a special bank survey, growing out of a 1977 survey, which indicated that a low percentage of banks adequately described the conditions governing their checking accounts and that more than half of the advertised descriptions of "free" checking accounts were inaccurate. The report includes a statistical review of the 3,230 complaints against banks received from the public during 1978 resulting from the Board's invitation to the public in its Regulation AA. Nearly half of all complaints were not identifiable under specific consumer credit laws. These "other" complaints are discussed in the text of the report. At year-end the Federal Reserve had dealt with 1,489 of these complaints by referral to other agencies and had completed action in 1,613 cases, leaving 128 still unresolved.

TRUTH IN LENDING

This tenth Annual Report on the Truth in Lending Act (dated January 3, 1979) substantiates the continuing commitment of the Board of Governors of the Federal Reserve System to provide consumers

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with meaningful cost disclosures and to promote creditor compliance with the act. It presents the findings of the 1977 survey of consumer awareness, which obtained information about the impact of the Truth in Lending Act on the views of consumers; data supporting the need for Truth in Lending simplification; and evaluations of the effectiveness of the Fair Credit Billing Act. This report also discusses the uniform guidelines established jointly by the financial institution regulatory agencies for enforcing Regulation Z, assesses the extent to which compliance with the act is being achieved, and summarizes the Board's administration of its functions under the act.

This report does not contain recommendations of the Board for statutory amendments. Such recommendations, if any, will be made in the Board's ANNUAL REPORT to the Congress.

Simplification of Truth in Lending

Amendments to the Truth in Lending Act, and interpretations by the courts, have made compliance increasingly difficult. Also, Regulation Z, in providing detailed guidance to creditors, has introduced its own complexity to Truth in Lending. Concerns have arisen about the intelligibility and usefulness of current Truth in Lending disclosures to the average consumer, as well as about the possibility that excessive complexity is indirectly increasing the cost of credit to consumers.

In an effort to make the Truth in Lending disclosures more meaningful to consumers and to ease the burden of compliance on creditors, the Board in 1977 proposed to the Senate Committee on Banking, Housing and Urban Affairs a simplified version of the Truth in Lending Act that would have provided for disclosure of only the most important credit terms. That same year the Board proposed four simplifying revisions to Regulation Z concerning itemization of the finance charge, of the downpayment, and of certain fees to exclude them from the finance charge, and identification of the method of computing unearned finance charges upon prepayment. In April 1978 the Board decided to defer final action on these proposals because of pending congressional efforts to simplify the act. Nearly a month later the Senate passed a simplification measure, but the Congress in October 1978 adjourned without taking further action.

In June 1978 the Board announced a comprehensive review of all its regulations, including Regulation Z, to determine whether they needed modernization or improvement. The style and format of

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existing regulations are receiving special attention in an attempt to reduce, subject to legal and regulatory responsibilities, the burden of compliance. The Federal Reserve Bank of Atlanta was assigned responsibility for Regulation Z and is expected to submit its recommendations to the Board by the end of 1978. Pending completion of this regulatory review, the Board decided to defer any further amendments to Regulation Z, except those that are essential. While the Board still favors legislative simplification, it decided not to postpone further simplification of the regulation.

Information on Effectiveness

Consumer Awareness Survey

The Board recently published an analysis of the results of a survey of consumer awareness that was conducted in the summer of 1977 by the Survey Research Center of the University of Michigan under the joint sponsorship of the Board, the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency.[4] The survey, which was based on interviews with a nationwide sample of 2,563 consumers, provided information about consumers' recognition, comprehension, attitudes, and behavior regarding the regulation of credit use. Several areas of the survey that are relevant to the Truth in Lending Act and to Regulation Z are discussed below; the figures quoted have been revised and are in final form. A comparison of these findings with those of two earlier surveys conducted for the Board in 1969 and 1970 may be useful in identifying the effects of the Truth in Lending Act in the past and in suggesting directions that protection of consumer credit use should take.

Awareness of annual percentage rates (APR's). The results of the 1969 and 1970 surveys indicated substantial increases in the awareness of rates by consumers during the first 15 months after the Truth in Lending Act became effective. As the 1977 survey demonstrates, awareness has continued to grow, although more slowly, during the years 1970–77. In 1977, 54.5 per cent of consumers were classified as aware of APR's on recent credit transactions involving closed-end credit; 64.7 per cent for retail revolving credit; and 71.3 per cent for

[4] Thomas A. Durkin and Gregory Elliehausen, *1977 Consumer Credit Survey* (Board of Governors of the Federal Reserve System, 1978).

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1. Respondents' Agreement with Observations about Truth in Lending Disclosure Statements

Observation	Total	Agree strongly	Agree somewhat	Disagree somewhat	Disagree strongly	Do not know
Most people read their Truth in Lending statements carefully						
Number	2,563	201	501	839	789	224
Per cent	100.0	7.8	19.5	32.7	31.1	8.7
Truth in Lending statements are complicated						
Number	2,563	975	887	227	118	316
Per cent	100.0	38.0	34.6	10.8	4.6	12.3
Some information on the Truth in Lending statements is not very useful						
Number	2,563	502	1,007	401	139	514
Per cent	100.0	19.6	39.3	15.6	5.4	20.0

bank credit cards—increases of 16.2, 9.2, and 7.9 percentage points, respectively, since 1970.[5]

Data supporting simplification. Proponents of simplification in Truth in Lending contend that the act and its implementing regulation now require too many disclosures, which may actually overwhelm and confuse some borrowers. These observers advocate the elimination of all unnecessary information from the disclosure statements, leaving only the most meaningful cost disclosures. The 1977 survey questioned consumers about the complexity of Truth in Lending disclosures and gathered data about the credit terms that they regarded as important.

a. Usefulness of Disclosure Statements. Nearly two-thirds of those interviewed believed that Truth in Lending statements are not read carefully, and almost three-quarters agreed that disclosure statements are complicated (Table 1). Almost 60 per cent of the respondents indicated that some information on the Truth in Lending statements is not very useful.

Respondents who had less education or lower incomes, who were 50 years of age and older, and who were unaware of APR's or without current closed-end debts were more likely to express no opinions concerning these three observations (Table 2). Probably, people with those characteristics are less familiar with the Truth in Lending Act and have had little or no recent contact with disclosure statements.

[5] These findings were discussed in more detail in the Board's ANNUAL REPORT for 1977.

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Thus, the survey findings tend to support the idea that Truth in Lending statements present too much information and that streamlined statements might be read more carefully by consumers.

b. Important Credit Terms. As shown by the numbers in Table 3, over 75 per cent of those surveyed mentioned rate as an important credit term; of these, over 80 per cent regarded it as the most important disclosure. This result is noteworthy since payment size has been traditionally viewed as the most significant credit term. In this sur-

2. Respondents' Agreement with Observations about Truth in Lending Disclosure Statements, by Characteristics of Respondents

Percentage distribution

Group	Number[1]	Total	Strongly agree	Agree somewhat	Disagree somewhat	Strongly disagree	Do not know
	A. Most people read their Truth in Lending statements carefully						
All respondents	2,563	100.0	7.8	19.5	32.7	31.1	8.7
Education							
Some high school or less	842	100.0	11.9	18.4	27.9	24.9	16.9
High school	781	100.0	7.3	21.6	34.6	30.8	5.5
Some college or more	925	100.0	4.8	19.1	35.7	37.2	3.2
Age (years)							
Under 35	822	100.0	7.2	22.5	33.3	32.2	4.7
35–49	612	100.0	6.2	19.4	35.1	35.4	3.8
50 and over	1,111	100.0	9.3	17.2	31.2	27.9	14.4
Income (dollars)							
Less than 7,500	565	100.0	10.8	19.1	27.2	24.8	18.0
7,500–12,499	459	100.0	8.5	21.1	34.0	29.2	7.2
12,500–17,499	403	100.0	7.7	19.8	34.5	33.0	5.0
17,500 and more	793	100.0	4.4	19.2	35.8	36.9	3.6
Aware of APR[2]	1,421	100.0	6.3	18.8	35.7	35.2	3.9
Unaware of APR[3]	1,108	100.0	9.6	20.5	29.4	26.2	14.2
Those using closed-end credit now[4]	1,198	100.0	6.3	19.7	33.9	35.0	5.0
Those not using closed-end credit now	1,365	100.0	9.2	19.4	31.7	27.7	12.0
	B. Truth in Lending statements are complicated						
All respondents	2,563	100.0	38.0	34.6	10.8	4.6	12.3
Education							
Some high school or less	842	100.0	37.6	28.6	8.1	4.4	21.2
High school	781	100.0	39.9	35.7	10.6	4.5	9.2
Some college or more	925	100.0	37.0	39.4	13.5	5.0	5.1
Age (years)							
Under 35	822	100.0	38.4	37.6	12.2	4.6	7.2
35–49	612	100.0	39.0	36.1	13.1	5.7	6.0
50 and over	1,111	100.0	37.1	31.8	8.5	4.0	18.6
Income (dollars)							
Less than 7,500	565	100.0	36.8	26.7	8.5	4.1	23.9
7,500–12,499	459	100.0	41.2	36.4	8.3	3.7	10.4
12,500–17,499	403	100.0	37.5	40.4	10.4	4.5	7.2
17,500 and more	793	100.0	38.0	36.9	15.1	5.7	4.3
Aware of APR[2]	1,421	100.0	41.2	35.7	12.2	4.9	6.0
Unaware of APR[3]	1,108	100.0	34.5	33.3	9.4	4.0	18.9
Those using closed-end credit now[4]	1,198	100.0	39.6	36.8	12.3	4.8	6.6
Those not using closed-end credit now	1,365	100.0	36.7	32.7	9.5	4.5	16.6

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2.—Continued

Group	Number [1]	Total	Strongly agree	Agree somewhat	Disagree somewhat	Strongly disagree	Do not know
	C. Some information on Truth in Lending statements is not very useful						
All respondents	2,563	100.0	19.6	39.3	15.6	5.4	20.0
Education							
Some high school or less	842	100.0	21.5	32.2	11.3	5.8	29.2
High school	781	100.0	20.4	41.6	15.7	4.9	17.4
Some college or more	925	100.0	17.3	44.1	19.7	5.6	13.3
Age (years)							
Under 35	822	100.0	16.2	43.8	23.0	4.7	12.3
35–49	612	100.0	22.5	41.8	13.9	6.9	14.9
50 and over	1,111	100.0	20.4	34.6	11.0	5.2	28.7
Income (dollars)							
Less than 7,500	565	100.0	18.8	32.0	12.6	6.4	30.3
7,500–12,499	459	100.0	19.6	40.1	17.6	4.1	18.5
12,500–17,499	403	100.0	19.4	45.9	15.1	4.5	15.1
17,500 and more	793	100.0	20.2	41.9	17.9	6.4	13.6
Aware of APR [2]	1,421	100.0	20.6	42.1	16.2	6.2	14.8
Unaware of APR [3]	1,108	100.0	18.2	36.2	15.3	4.5	25.7
Those using closed-end credit now [4]	1,198	100.0	20.3	42.6	17.0	6.2	13.9
Those not using closed-end credit now	1,365	100.0	19.0	36.4	14.4	4.8	25.4

[1] A few respondents were excluded in calculating the percentages because their characteristics were not ascertained.

[2] Those responding with rates of 12 per cent or more to a hypothetical question about the annual percentage rate on a purchase of furniture.

[3] Those responding with rates below 12 per cent or "do not know" to hypothetical question about annual percentage rate on purchase of furniture.

[4] Respondents using credit from institutional sources.

vey, that term ranked second behind rate information by a significant amount—followed by the dollar amount of finance charge, penalties for late payment, and the handling of early payoffs.

These findings are significant since they support past legislative proposals for simplifying Truth in Lending by highlighting on the disclosure statement the credit terms consistently mentioned by consumers.

Credit-card billing errors. The 1977 survey explored consumers' knowledge, perceptions, and use of procedures for the resolution of billing disputes required under the Fair Credit Billing Act.

The overwhelming majority of respondents (82.8 per cent) either did not know whether any Federal legislation or regulation concerning credit-card billing errors existed or believed that there was none (Table 4). Even among cardholders who receive frequent notices about the act and consumers who have experienced a billing error, only about one in four was aware of the law.

Nearly 15 per cent of all cardholders had experienced at least one

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3. Automobile Credit Terms Respondent Would Want To Know

Term	Number of responses by rank				
	First	Second	Third	Fourth	Most important
Credit costs/terms					
Interest rates, annual rates	1,592	277	58	11	1,335
Interest dollars/finance charges	202	114	70	23	194
Fees other than interest	28	65	24	15	31
Amount of downpayment	23	32	26	7	9
Size of monthly payments	240	360	178	28	293
Variations in payment size/balloon payments	4	12	9	5	6
Length, maturity of contract	144	559	202	21	79
Ease of obtaining credit/credit availability	7	12	17	7	6
Availability/cost of credit insurance	11	84	60	30	24
Whether credit insurance is required	1	9	17	3	1
Rebates for prepayment	16	106	90	28	22
Handling of penalty for late payments	10	83	80	30	30
Willingness to defer payments	5	16	29	6	9
Garnishment procedures	0	0	0	0	0
Repossession conditions	2	11	7	10	4
Willingness to allow cosigning	0	0	1	0	0
Credit limit	8	9	6	3	6
Other terms/costs	29	64	43	17	22
Characteristics of institution					
Reputation	18	44	48	20	48
Amount/clarity of information given	4	13	19	3	12
Who the holder of the contract will be	4	6	17	7	8
All other	3	17	20	10	18
All else					
"Nothing"	4	0	0	0	3
"Everything"	3	1	0	0	1
Not known or not ascertained	205	1	0	0	402
No second, (third), (fourth) response	0	668	1,543	2,277	0
Total	**2,563**	**2,563**	**2,563**	**2,563**	**2,563**

billing error during the year prior to the interview. The most frequently cited errors involved incorrect charges, followed by the failure to credit payments or incorrect credits (Table 5). Three-quarters of the errors involved $100 or less and nearly one-third of these were less than $10 (Table 6).

The main response of consumers faced with billing errors was complaint to the creditor, and satisfactory outcomes were reported in most cases (Tables 7 and 8). These findings indicate that even without invoking Federal protection of their billing rights, of which most are unaware, consumers generally find creditors responsive to billing problems and complaints.

Inquiry on Rights under the Fair Credit Billing Act

In November 1977 the Board surveyed eight large creditors to determine the extent to which consumers exercise certain rights under the Fair Credit Billing Act.

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According to the Board's findings, which were published in May 1978, a substantial number of credit customers questioned their billing statements each month. The increase in the number of inquiries since the credit billing provisions were incorporated into Regulation Z is not known, but the proportions of statements questioned ranged

4. Responses to Question about Existence of Federal Law Dealing with Credit-Card Billing Errors

Type of respondent and response	Number	Per cent
All respondents		
Yes (there is a law)	421	16.4
No	622	24.3
Do not know	1,500	58.5
Not ascertained	20	.8
Total	**2,563**	**100.0**
Cardholders		
Yes (there is a law)	373	23.2
No	423	26.3
Do not know	808	50.2
Not ascertained	5	.3
Total	**1,609**	**100.0**
Those who experienced a billing error		
Yes (there is a law)	61	26.9
No	66	29.1
Do not know	100	44.0
Not ascertained	0	*
Total	**227**	**100.0**

* Less than 0.5 per cent.

5. Credit-Card Billing Errors by Type and Card

Item	Errors	
	Number	Per cent
Type of error		
Charged for another's purchase	46	17.6
Charged twice, charged for item not purchased, incorrect charge	118	45.2
Return item or refund not credited	19	7.3
Payment not credited or credited incorrectly	57	21.8
Other	16	6.1
Not ascertained	5	1.9
Total	**261**	**100.0**
Type of card		
Gasoline	38	14.6
Bank credit	64	24.5
General purpose (travel and entertainment)	12	4.6
Retail credit	134	51.3
Other or not ascertained	13	5.0
Total	**261**	**100.0**

6. Credit-Card Billing Errors by Dollar Amount

Amount of error (dollars)	Number	Per cent
1–10	63	24.1
11–25	59	22.6
26–50	49	18.8
51–100	29	11.1
101–250	19	7.3
251 and more	15	5.7
No money involved	5	1.9
Not known or not ascertained	22	8.4
Total	**261**	**100.0**

7. Consumers' Responses to Credit-Card Billing Errors

Response	Number	Per cent
Complaint to creditor	216	81.5
Complaint to attorney	1	.4
Complaint to Better Business Bureau	1	.4
Paid off debt	3	1.1
Refused to pay	4	1.5
All other	2	.8
No action taken	27	10.2
Not known or not ascertained	11	4.2
Total	**265**	**100.0**

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8. Responses to Questions on Credit-Card Billing

Response	Number	Per cent
Was the error corrected to your satisfaction?		
Yes	206	88.0
No	24	10.3
Not known or not ascertained	4	1.7
Total	**234**	**100.0**
Are there any *billing* practices of credit-card companies that you would like to see changed?		
Yes	326	20.3
No	1,247	77.5
Not known or not ascertained	36	2.2
Total	**1,609**	**100.0**

from less than 1 per cent to somewhat more than 6 per cent for the eight reporting creditors. While only a few of these inquiries followed the formal procedures provided by Regulation Z, most of the companies reported treating informal questions just as they do the formal ones.

Uniform Guidelines for Enforcing Regulation Z

The Board and four other agencies that enforce the act for financial institutions—the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board (FHLBB), and the National Credit Union Administration (NCUA)—have agreed on uniform enforcement guidelines for the Truth in Lending Act and Regulation Z. The guidelines are expected to go into effect by the end of 1978.

The guidelines, which were first issued for public comment in October 1977, are intended to provide standard criteria for the enforcement of the Truth in Lending Act when violations are discovered in examinations of financial institutions, and to emphasize to creditors the need for compliance. Reimbursement to individual consumers will be required for five types of violations resulting in payment of charges higher than those disclosed under the act. To correct the two most important violations, that remedy will be applied when the disclosed APR understates the true cost of credit by more than one-eighth of 1 percentage point, and when the disclosed finance charge understates the true charge by more than $100 or 1 per cent of the true charge, whichever is lower. Reimbursement will normally not be required for overcharges of less than $1 per individual account.

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Compliance

During the past year the Federal Reserve System and other Federal enforcement agencies continued to promote compliance with the act and regulation through a variety of methods. Many compliance programs feature specialized examinations conducted by examiners extensively trained in consumer law and regulations. By year-end Federal Reserve examiners had conducted approximately 800 such examinations under comprehensive procedures adopted by the Board in early 1977. This practice emphasizes to bank personnel the Board's commitment to achieving compliance with the consumer regulations.

In 1978 the education of examiners remained a high priority among the agencies enforcing the act by means of an examination process. The Comptroller of the Currency, for example, held six 2-week schools to train 300 of its examiners in consumer regulations, and joined the FDIC and the Board in conducting a 1-week seminar for supervisors and senior examiners. In addition to a training program, the NCUA distributed specially programmed calculators to all examiners, which, it reports, have greatly aided the examination function.

Most of the enforcement agencies and the appropriate offices of the exempt States—Connecticut, Maine, Massachusetts, Oklahoma, and Wyoming—have mechanisms for resolving consumer complaints. In the first 9 months of 1978, the Federal Reserve System received 381 consumer complaints relating to the act and regulation; of these, 82 involved State member banks. By far the two largest categories of complaints concerned fair credit billing and disclosure—a pattern also noted by the FDIC, the Comptroller, and the NCUA. During 1978, 67 complaints about State member banks warranted investigation by the Federal Reserve System; in 38 cases (57 per cent) the matter was resolved in favor of the consumer.

In view of increased enforcement activities, especially the adoption of uniform enforcement guidelines for Regulation Z, the staff of the Board's Division of Consumer Affairs has undertaken an extensive review of provisions relating to the computation and disclosure of the APR. The regulation currently permits numerous computation methods that often produce varying APR's and finance charges on a given transaction. The Board will publish for comment alternative solutions to the problems identified.

As part of its enforcement function under the Consumer Leasing

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Act, the Federal Trade Commission (FTC) surveyed 17 of the largest automobile lessors during the past year. An unexpected finding was that many of the lessors restrict their activities to commercial leasing. The Commission also recently began several preliminary investigations of consumer lessors for possible advertising violations.

The agencies and exempt States responsible for enforcing the Truth in Lending Act have reported varying assessments of the extent to which creditors are complying with the act's requirements. Several Federal agencies, including the FHLBB, and all of the exempt States found a high level of creditor compliance with the substantive provisions of the act and noted that most violations are nonsubstantive. Authorities from the exempt States of Massachusetts and Connecticut believe that the vast majority of creditors subject to their jurisdiction have a basic understanding of the law, attempt to conform to statutory and regulatory requirements, and fall short only when applying the more technical concepts. The FTC, while reporting apparently high substantial compliance, nonetheless initiated in September 1978 an industrywide investigation to better determine whether creditors are correctly disclosing to consumers the actual cost of credit and otherwise complying with the act.

The Comptroller of the Currency reported that the proportion of national banks not complying with the act has remained substantially the same as in 1977 when approximately 88 per cent were in violation, most of which was technical, and pointed out that since October 1976, national banks have made voluntary reimbursements approximating $2.5 million. Three other agencies reported significant increases in 1978 in the number of violations found. The per cent of examination reports reviewed by the FDIC that indicated apparent violations jumped from 36.2 per cent in 1977 to 81.6 per cent in 1978. Reasons frequently cited for noncompliance include misunderstanding the law, clerical error, oversight, and carelessness. The Board estimates that 85 per cent of State member banks are still not fully complying with Regulation Z—an increase of 13 percentage points since 1977; while the NCUA reports that the proportion of Federal credit unions that were not complying more than doubled in 1978, from 27 per cent a year earlier to 59 per cent. Again, for both kinds of institutions, most violations were nonsubstantive. All three agencies attribute the increase in reported violations to better training of their staffs and improved examination techniques rather than to

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a higher incidence of noncompliance. However, the NCUA believes that unique characteristics of credit unions continue to hinder enforcement efforts. Their cooperative nature, their prevalent use of payroll deductions, and their reliance on volunteers, it is felt, all create serious problems.

Thus, the 1978 examination reports of the Comptroller of the Currency, the FDIC, the Board, and the NCUA revealed high proportions of institutions still not fully complying with Regulation Z. However, this continued discovery of relatively high numbers of violations does not necessarily represent a deteriorating incidence of creditor compliance. Instead, it is thought that recently expanded formal training of examiners, development of more thorough and intensive examination procedures, and increased over-all efficiency of the examination staffs have all contributed to an improved ability to detect violations that may have been overlooked in the past.

During 1978 the FDIC, the FHLBB, and Oklahoma, an exempt State, all issued cease-and-desist orders. In addition, the FDIC referred four cases to the Department of Justice for possible criminal prosecution.

In 1977 the FTC instituted five civil penalty cases under a pilot enforcement program concerning the advertising requirements of Regulation Z. Since that time all five cases have been settled; civil penalties of $10,000 were assessed in four cases and $15,000 in the remaining case. The Commission is currently considering application of this enforcement mechanism to other types of Truth in Lending violations. During 1978 the FTC entered or provisionally accepted ten consent orders, obtained one final order, and issued one complaint. A variety of both Truth in Lending issues and types of creditors were involved.

Each enforcement agency and exempt State has estimated the annual cost of its compliance effort in connection with the Truth in Lending Act. While these figures are not strictly comparable, the total estimated expenditures for the nine Federal enforcement agencies exceeded $8.5 million in 1978, with the largest expenditures reported by the FDIC, the Comptroller of the Currency, and the Board. The five exempt States reported combined expenditures in excess of $1 million. Several agencies also anticipated substantial increases in their expenditures in 1979 due to the adoption of the uniform guidelines for enforcing Regulation Z.

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Legislative Recommendations

Although the Board is not making legislative recommendations in this report, several of the other Federal enforcement agencies have suggestions for amending the Truth in Lending Act. The Federal Trade Commission cited four problem areas needing special congressional attention: the increasing use of open-end credit disclosures in what would traditionally have been other than open-end credit transactions; unfair or deceptive insurance sales practices; obstacles to the right of rescission; and the forfeiture of credit balances. In addition, the FTC has urged the Congress to permit enforcement of Regulation Z as if it were a trade regulation rule; to minimize civil liabilities for "technical" violations; to extend the statute of limitations in civil actions; to codify the right to raise Truth in Lending claims as a recoupment after the statute of limitations has run; and to provide for earlier disclosure.

Suggestions from other agencies include eliminating the special exceptions from the general rule on what constitutes a finance charge; simplifying disclosures; permitting a tolerance of one-eighth percentage point for the APR; instructing the Board to issue model forms; exempting lending activities of farm credit institutions and agricultural loans from the act; and restricting rescission rights to indirect paper and home solicitation sales.

Consumer Advisory Council

Established in 1976 to advise the Board on consumer-related matters, the Consumer Advisory Council includes representatives of both consumers and creditors. During 1978 its discussions and suggestions in the area of Truth in Lending focused primarily on the uniform enforcement guidelines proposed by the five Federal financial institution regulatory agencies and proposals for simplifying the disclosure requirements under the Truth in Lending Act and Regulation Z.

In addition, the Council reviewed the efforts of the Federal Reserve Banks in examining and achieving member bank compliance and explored the role the Board should take in consumer education. Throughout the year the Council was briefed on legislative and regulatory developments and provided the Board with helpful advice. In December 1978 it recommended that the Board ask the Congress to exempt agricultural credit from the requirements of the act.

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Administrative Functions

Amendments and Interpretations of Regulation Z

Descriptive billing of nonsale transactions. In January 1978 the Board revised the provision of Regulation Z that specifies the date to be used on descriptive billing statements to identify certain nonsale credit transactions such as cash-advance check transactions. This amendment, which became effective March 28, 1978, permits a creditor to use the date on which a transaction is debited to the customer's account in lieu of the date on which the transaction occurred or the date appearing on the check or other credit instrument.

The amendment, prompted by the operational difficulties experienced by creditors in ascertaining the transaction date or the date appearing on the credit document, is intended to facilitate compliance with the descriptive billing provisions of Regulation Z.

However, the debiting date, if used, must be identified as such on the descriptive billing statement. In addition, a creditor using the date of debiting must, as an added protection to the customer, treat a subsequent inquiry about the transaction as if it were an inquiry about a billing error and as an erroneous billing under the provisions of the Fair Credit Billing Act, and the creditor must supply documentary evidence of the transaction to the customer, without charge, whether or not it is requested. Furthermore, any finance charge or other charge imposed as a result of the use of the debiting date must be credited to the customer's account if such an inquiry is made.

Revised procedures for issuance of official staff interpretations. In April 1978 the Board amended Regulation Z to revise the procedure for issuing official staff interpretations. Under this new procedure, official staff interpretations are issued with an effective date 30 days after publication in the *Federal Register,* which enables the public to review them before they become effective and permits interested parties to request the opportunity for public comment. If a request is received, the effective date of the interpretation is suspended and its text republished for public comment together with the letter requesting a comment period or a summary of the arguments presented in such a letter. After the comments are reviewed, a final interpretation is issued.

Preservation of evidence of compliance. In May 1978 the Board amended Regulation Z to change its record-retention requirements for creditors under the jurisdiction of the Comptroller of the Currency,

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the FDIC, the FHLBB, the Board, and the NCUA. Previously, all creditors had been permitted to dispose of records demonstrating compliance with Regulation Z 2 years after the date when disclosures were required to be made. This amendment, however, requires creditors and lessors subject to the five agencies to retain any credit-transaction records in their possession, even those in which more than 2 years have elapsed from the required disclosures.

This action was taken to avoid the destruction of records evidencing violations that would be subject to reimbursement under the uniform guidelines for enforcement of Regulation Z proposed by the five agencies in October 1977. Once the guidelines are in effect, creditors may dispose of records more than 2 years old after those records have been examined and found to be in compliance.

Rescission in open-end credit. In June 1978 the Board amended Regulation Z to create an exception to the right of rescission for individual transactions under certain open-end credit accounts secured by interests in consumers' homes. In lieu of notification of the right to cancel each individual transaction under such accounts, creditors must provide specified disclosures of a customer's rights at certain times: upon the opening of the account; prior to any increase in the credit limit; at the time a security interest in a home is added to an existing open-end credit arrangement; prior to any change in the terms of the account; and annually. Under the amendment, creditors may not change the terms of such accounts without allowing customers to pay off the balance according to the existing terms. However, if customers refuse the change in terms, creditors need not extend further credit on the accounts. The Board has also issued an interpretation (Section 226.904 of Regulation Z) that provides three sample disclosure notices that creditors may use to achieve compliance with certain of the amendment's requirements.

The major effect of this ruling is to facilitate the offering of credit plans that enable consumers to tap their largest illiquid asset—the equity in their homes—and, by controlling the payments, to minimize the amount of finance charge paid. In October 1978 the Board received from the FTC and Senators William Proxmire and Donald W. Riegle, Jr., requests to reconsider this ruling under which, it was felt, consumers might be tempted to overextend themselves and risk losing their homes. In a November letter to the two senators, Chairman Miller, while reiterating the Board's position that these accounts offer major benefits for consumers, promised to monitor developments

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closely. In addition, the Chairman indicated that a revision to the amendment, whereby creditors offering such open-end accounts would have to submit a notification of intent to the Board, was under consideration in an effort to aid the Board's monitoring activity. Consumers Union has filed a suit in the U.S. District Court for the District of Columbia asking that the court declare the amendment void.

Disclosure of schedule of variable payments. In August 1978 the Board amended Section 226.8(a) of Regulation Z to permit the disclosure of a complete payment schedule on as many pages as necessary in any transaction in which the payment amounts vary. Previously, all disclosures had to appear on one side of a single page. This alternative provides flexibility for creditors in a simple disclosure format, while insuring that customers receive meaningful information about their credit transactions.

Expansion of provision on minor irregularities. In August 1978 the Board amended an interpretation (Section 226.503 of Regulation Z) to facilitate the computation of APR's in long-term credit transactions involving irregular payment amounts, such as graduated-payment mortgages. This amendment permits first-payment periods of up to 62 days to be treated as if they were regular when calculating APR's on all transactions that have a scheduled term of 10 years or more and that are payable monthly, whether or not the monthly instalments are equal. This action permitted use of APR tables prepared by HUD for homes bought under its FHA graduated-payment mortgage program.

Disclosure of interest reduction. In August 1978 the Board proposed for comment an interpretation providing that in cases in which the interest rate on a time deposit securing a loan must be reduced in order to comply with State and Federal laws, such a reduction must be disclosed under Truth in Lending. Although the amount of the interest reduction would not need to be disclosed as part of the finance charge, the creditor would have to disclose the loss of interest. The comment period ended September 29, 1978.

State Exemptions

No new exemptions from the requirements of Chapter 2 of the Truth in Lending Act were granted to States in 1978, but one existing exemption was expanded. In October 1978 the Board approved an application by Massachusetts to expand the State's existing exemption to include Federal credit unions. This expansion was granted after

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an enforcement agreement was entered into between the Massachusetts Commissioner of Banks and the NCUA. The arrangement authorizes the Commissioner to examine Federal credit unions in the State for compliance with Massachusetts' Truth in Lending law and thereby ensures uniform enforcement of the State's law.

In May 1978 the Board adopted a supplement to Regulation Z (Supplement VI) setting out the procedures to be followed by a State seeking an exemption under Chapter 5 of the act (Consumer Leases) or a Board determination regarding whether a State law is inconsistent with the Consumer Leasing Act.

Education

An important aspect of the enforcement function is education. In 1978 the agencies responsible for Truth in Lending initiated a variety of educational activities designed for both consumers and creditors. Consumer-oriented efforts included speeches and presentations as well as the publication of explanatory brochures. The Board's *Consumer Handbook to Credit Protection Laws* is a comprehensive compilation of information about consumers' rights under credit laws and regulations. It is expected to be available for distribution by the end of 1978. During the year the Board also developed a pamphlet explaining what a consumer should do when experiencing a problem with a bank, which includes a complaint form addressed to the Federal Reserve. The Comptroller of the Currency and the FDIC have issued similar pamphlets for complaints about their respective institutions. The FTC has been developing a pocket-size *Credit Shopping Guide* in both English and Spanish that includes general information on shopping for credit and three sets of APR tables to facilitate cost comparison in transactions such as automobile, mobile home, and mortgage loans.

Efforts to familiarize creditors with the provisions of the act and regulation range from general guidance in individual cases to the more formalized Federal Reserve System program of advisory visits to State member banks and national banks. In the past year, over 450 such visits, generally lasting from ½ day to 1½ days, were made by System staff. Several new publications have been developed for creditors in 1978. The Federal Reserve Bank of New York has published *Consumer Regulations Checklist,* which highlights provisions of consumer regulations that have been identified by examiners as warranting closer attention by lenders. The NCUA issued the looseleaf

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Manual of Laws Affecting Federal Credit Unions and provided a free copy to all 13,000 Federal credit unions, and the Office of the State Examiner in Wyoming developed a looseleaf booklet that provides guidance to all Wyoming creditors on a variety of problems. The staff of the FHLBB attempts to monitor for accuracy information relating to Truth in Lending that is disseminated by the various national trade organizations.

EQUAL CREDIT OPPORTUNITY

The third Annual Report on the Equal Credit Opportunity Act (ECOA) describes the enforcement of the act and Regulation B by the Board of Governors of the Federal Reserve System and the other Federal enforcement agencies. It presents the findings of a major survey of consumers, which gathered information about consumer perceptions, and a smaller inquiry of creditors, which sought data on the use by consumers of consumer credit legislation. This report also discusses the uniform guidelines proposed jointly by the financial regulatory agencies for enforcing Regulation B, assesses the extent to which compliance with the act is being achieved, and outlines the Board's administration of its functions under the act.

This report does not contain recommendations of the Board for statutory amendments. Such recommendations, if any, will be made in the Board's ANNUAL REPORT to the Congress.

Special Civil Rights Enforcement Efforts

A preliminary review by the Board's staff at the end of 1977 of the special consumer affairs enforcement program that was established earlier in that year showed that although examinations frequently revealed procedural violations, they had not been as successful in uncovering evidence of banks engaging in substantive violations of Regulation B and the Fair Housing Act. The question arose whether existing procedures and training were adequate to enable examiners to detect unlawful discrimination readily.

To supplement research conducted by the staff on this question, the Board engaged a consultant to study the Board's procedures and materials for enforcing the ECOA and Fair Housing Act and to make recommendations for changes. The consultant's report, which was published in May 1978, suggested a redirection of emphasis in the System's enforcement efforts with respect to credit discrimina-

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tion. On the basis of this report and independent research, a task force of Board and Reserve Bank staff redrafted examiner manuals and examination procedures for Regulation B and the Fair Housing Act. In light of the field test results, the manuals and procedures are being revised. The staff expects to present the revised civil rights enforcement program to the Board early in 1979.

Meanwhile, in August 1978 the Division of Consumer Affairs augmented its compliance staff by designating three members of its legal staff as civil rights specialists. These persons, in conjunction with the compliance staff, were primarily responsible for drafting new examiner manuals and examination procedures. Each Federal Reserve Bank also appointed a member of its staff to assume primary civil rights responsibilities.

The Board's civil rights specialists conferred with the staff of the Department of Justice on recent developments in civil rights enforcement, and in September 1978 the Board's staff arranged for the Department of Justice to conduct a special 1-day seminar for all staff in the Division of Consumer Affairs and for the Reserve Bank civil rights specialists. The Board also conducted a 3-day training seminar for 12 examiners and 8 Board staff members on the subject of civil rights enforcement.

Three other Federal agencies reported special activities in the area of civil rights. The Federal Deposit Insurance Corporation (FDIC) established a Civil Rights Branch within its Office of Consumer Affairs and Civil Rights to provide leadership in administering the FDIC's enforcement of civil rights laws and regulations. The Federal Home Loan Bank Board (FHLBB) adopted a new Nondiscrimination Regulation effective July 1, 1978, which enhances Regulation B by prohibiting discrimination in housing lending on all of the bases prohibited by the ECOA as well as on two additional bases—age and location of the dwelling. The Federal Trade Commission (FTC) commissioned a report concerning discrimination in real estate finance, which reviews the FTC's enforcement options and provides recommendations about litigation strategies and possible rulemaking proceedings.

Compliance

During the past year the Federal Reserve System and other Federal enforcement agencies continued to enforce the Equal Credit Oppor-

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tunity Act and Regulation B through a variety of methods. This section summarizes the compliance activities in 1978 of the Federal Reserve System and the compliance reports of the other Federal enforcement agencies.

Many compliance efforts feature specialized examinations conducted by examiners versed in consumer law and regulations. In the past year Federal Reserve System examiners have conducted special examinations of approximately 800 State member banks to determine compliance with consumer credit regulations, including equal credit opportunity.

Training of examiners remains a major activity among those agencies that enforce the act by means of an examination process. The Comptroller of the Currency, for example, held six 2-week schools to train 300 of its examiners in consumer regulations, and joined the FDIC and the Board in conducting a 1-week seminar for supervisors and senior examiners.

Most of the enforcement agencies handle consumer complaints by investigating creditors and resolving complaints. During the first 10 months of 1978 the Federal Reserve System received 304 complaints relating to the act or Regulation B against State member banks. Of these, 260 charged unfair denial, termination, or change in terms of credit. Over half of these (138 complaints) claimed discrimination on a basis the act does not define as discriminatory, such as credit history, level of income, and length of employment. On the other hand, 28 complainants felt that marital status or sex was the reason for the creditor's adverse action, 11 charged discrimination because of age, and 11 because of race, color, or national origin.

With respect to the 304 complaints regarding State member banks, 168 investigations have been completed, 60 are still under investigation, and 76 were handled by furnishing information or an explanation. In the 168 completed investigations, the bank was found to be legally correct in 139 cases (in 36 of which it nevertheless reached an accommodation with the complainant); to have made an error, which has since been corrected, in 19 cases; to be in possible violation in 8 cases, 7 of which have since been resolved and 1 of which remains unresolved. In two cases, the credit applicant was in error.

For this same 10-month period, the Office of the Comptroller reported 625 consumer complaints received, 280 of which alleged discrimination on the basis of sex or marital status. In addition, 58

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complainants felt that they had been discriminated against due to race, color, or national origin; 30 cited age as the perceived reason for denial; and 16 charged discrimination due to receipt of public assistance and 2 because of religion.

The FHLBB noted 211 complaints received during this period. Over 25 per cent of these (56 complaints) alleged discrimination on the basis of sex or marital status and nearly 25 per cent more (52 complaints) charged redlining. Complainants also charged discrimination due to race, color, or national origin in 34 cases, age in 16 cases, and religion in 1 case.

During fiscal year 1978 the FDIC reported receiving 215 complaints and 17 inquiries concerning equal credit opportunity. Of these, approximately 30 per cent involved the notice of adverse action, 28 per cent alleged discrimination on the basis of sex or marital status, and 8 per cent cited race or age.

The National Credit Union Administration (NCUA) stated that during this same period it received 91 complaints about discrimination, the largest number of which (30 complaints) alleged discrimination on the basis of race, color, or national origin. Sex or marital status was considered the reason for discrimination in 20 instances, age in 4 instances, and receipt of public assistance in 3 instances.

During fiscal year 1978 the Federal Trade Commission responded to over 11,000 consumers with complaints or inquiries pertaining to the ECOA, an increase of approximately 4,000 from 1977. The FTC staff stated that it continues to rely heavily on information provided by consumers in identifying suspected violators of the act for ECOA enforcement actions. For this reason, the FTC staff is developing a computerized system—similar to those currently used by the Board, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, and the National Credit Union Administration—to aid in the retrieval of information about consumer complaints.

The Farm Credit Administration (FCA) reported receipt of 7 complaints of discrimination on the basis of race, color, or national origin, and 5 on the basis of sex or marital status. No complaints involving farm credit lending institutions are known to have resulted in litigation. However, the Department of Justice is investigating, under the ECOA, practices of a Federal Land Bank and a Federal Land Bank Association due to a complaint that the FCA explored.

The Civil Aeronautics Board (CAB) reported that it received

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approximately 150 complaints from the public involving the ECOA and Regulation B. The CAB indicated that virtually all of these complaints have been processed informally by contacting the carrier or supplying information to the complainant, and that several major investigations of consumer credit practices in the airline industry have been initiated as a result of the complaints.

During fiscal year 1978, 44 complaints of discrimination based on race, national origin, or sex were made against Small Business Administration (SBA) program offices and recipients, but SBA investigations found no violations.

Neither the Securities and Exchange Commission nor the Agricultural Marketing Service (Packers and Stockyards) received complaints alleging discrimination under the ECOA during 1978.

The agencies responsible for enforcing the Equal Credit Opportunity Act have reported varying assessments of the extent to which creditors are complying with the act. During the past year, two agencies noted substantial increases in levels of creditor noncompliance. NCUA's preliminary results show that 63 per cent of the credit unions examined were not in compliance, more than double the 28 per cent for 1977. Many of the violations involved noncomplying forms. Similarly, the proportion of FDIC examination reports indicating apparent violations rose from 26.6 per cent in fiscal year 1977 to 51.3 per cent in fiscal year 1978. These reported violations related primarily to failures to provide notifications in the event of adverse action and improper requests for the signature of a spouse. Both agencies attributed the reports of increased noncompliance to the additional staff training and improved examination techniques that followed special emphasis on civil rights enforcement.

Since many creditors supervised by the NCUA were found to be using improper forms, the NCUA has developed a set of model loan application forms written in plain English and designed to meet the special needs of credit unions. After the forms are reviewed, their optional use by credit unions should result in a decrease in this kind of violation.

From July 1977 through June 1978, 89 per cent of national banks examined by the Comptroller of the Currency were found to be in violation of the regulation compared with 97 per cent during the previous report period. Patterns of substantive violations of the regulation were reported for 66 per cent of banks examined. Roughly two-thirds of these involved requests for and subsequent considera-

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tion of certain prohibited information with regard to applicants, and 30 per cent concerned requests for signature of a spouse or other person. When a national bank is alleged to be discriminating on a prohibited basis, the Comptroller conducts a special investigation. Such an investigation, which may be triggered by a consumer complaint or by preliminary evidence discovered in the examination, entails use of a larger sample of loan files and provides for a detailed review of appraisal practices and other data.

The Comptroller's office said it believes that substantial compliance with the act is achieved by national banks after such a consumer examination and the required corrective action is taken. It noted the following three enforcement problems: the lack of uniform guidelines for required corrective action for banks found to be in violation; the difficulty of detecting illegal discouragement of credit applications by a review of loan application files; and the lack of written lending policies in banks, which can be overcome only partially by interviews with loan officers and bank management.

The Federal Reserve System's first round of special consumer examinations revealed approximately 78 per cent of State member banks in noncompliance with the regulation. Of those banks undergoing a second consumer examination, 28 per cent repeated violations previously cited although 73 per cent continued to have violations of one kind or another. The overwhelming majority of violations continue to relate to the use of noncomplying application forms, while other frequent violations involve the notification requirements of Regulation B and failure to request information for monitoring purposes.

The Federal Home Loan Bank Board reported that violations were found in 53 per cent of institutions examined from July 1977 through June 1978. Major concentrations of violations concerned improper requests for information on marital status, failure to notify about adverse action, and failure to obtain monitoring information.

The FHLBB said that enforcement of the ECOA was complicated by the difficulty of identifying and correcting practices that are neutral on their face but have the effect of discriminating against a protected class. The legal theory under which such practices are identified holds that practices having a greater negative impact on some protected classes may, if not justified by business necessity, be illegal because of their discriminatory effect, even though they are not intentionally discriminatory and are applied equally to all credit

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applicants. The FHLBB further indicated that, without clearer standards and guidance from the Congress or the courts, determinations as to how business necessity and discrimination relate to mortgage lending will remain extremely difficult to make.

The Federal Trade Commission stated that the level of compliance with the ECOA varies greatly among creditors subject to its jurisdiction. Although many violations are apparently confined to narrow segments of an industry, certain unlawful practices appear to occur more frequently. Such practices include requesting information about an applicant's spouse, and obtaining the signature of the spouse or other person on a promissory note; disregarding or treating less favorably income derived from sources other than employment, such as alimony, child support, pension, and public assistance payments; relying on ZIP codes as criteria of creditworthiness; misusing the Statement of Credit Denial, Termination, or Change sample form in Regulation B; failing to disclose that sensitive factors, such as age, are considered by the creditor; and providing vague, rather than specific, reasons for rejecting applicants.

The FTC described four enforcement problems encountered in fiscal year 1978 as significant: failure of creditors to provide the principal specific reasons for adverse action; difficulties in detecting and remedying racial steering in real estate financing; difficulties in documenting business credit discrimination; and difficulties in dealing with discriminatory telephone and mail solicitation techniques.

During the past year the FTC issued two final Commission Interpretations of the Fair Credit Reporting Act, designed to reconcile the goals of that statute with the goals of the ECOA. Interpretation 600.7 facilitates access to credit by women while preserving the privacy of their spouses. Interpretation 600.8 permits creditors to obtain reports on the nonapplicant spouse in certain circumstances. These interpretations are statements of FTC enforcement policy for all creditors subject to FTC jurisdiction.

The agencies enforcing the ECOA and Regulation B reported that they have taken the following formal administrative actions: During fiscal year 1978 the FDIC initiated one cease-and-desist order, made final four previously issued orders, and terminated three outstanding orders. In the same period, the FTC accepted one consent order and obtained one consent judgment. The FHLBB and the CAB each issued one cease-and-desist order during 1978.

Each enforcement agency, with the exception of the Securities and

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Exchange Commission (SEC) and the Interstate Commerce Commission (ICC), submitted a cost estimate of its compliance effort in connection with the Equal Credit Opportunity Act. While these figures are not strictly comparable, the total estimated expenditure was approximately $7.6 million in 1978.

Legislative Recommendations

Although the Board is not making legislative recommendations in this report, two of the other enforcement agencies made suggestions for amending the Equal Credit Opportunity Act. The Small Business Administration requested that the Congress transfer to it (from the FTC) the responsibility for monitoring Regulation B and the ECOA in its programs. SBA said it believes that would avoid duplicative administrative hearings when certain violations are alleged. The Office of Equal Opportunity within the Department of Agriculture recommends that discrimination because of a handicap be included among the prohibited bases under the ECOA.

Uniform Guidelines for Enforcing Regulation B

The five Federal agencies that supervise Federally insured financial institutions—the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, the Federal Reserve Board, and the National Credit Union Administration—have jointly proposed uniform guidelines for enforcement of the Equal Credit Opportunity Act, its implementing Regulation B, and the Fair Housing Act. The guidelines were issued for public comment in June 1978. They are intended to promote improved and uniform enforcement of the equal credit opportunity and fair housing laws among Federally regulated financial institutions by requiring corrective action for violations discovered during examinations and through investigation of complaints.

The enforcing agencies would encourage voluntary correction and compliance, and take the actions noted in the guidelines to correct violations. These violations include discouraging applications on a prohibited basis, using discriminatory elements in credit evaluation systems, charging a higher rate of interest on a prohibited basis or requiring insurance in violation of fair housing or equal credit opportunity laws, requiring a cosigner on a prohibited basis, failing to provide notices of adverse action, failing to maintain and report

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separate credit histories where required, failing to collect information for monitoring purposes, and terminating or changing the terms of accounts on a prohibited basis. In each case, the circumstances would be considered in determining the suitability of the remedy provided in the uniform guidelines. If violations remain uncorrected, the enforcing agencies would take administrative actions to ensure correction. The agencies have reviewed the comments received and are working toward final guidelines.

Comprehensive Review of Regulation B

In June 1978 the Board announced that it was embarking on a comprehensive review of all its regulations to determine whether they needed modernization or improvement. The style and format of existing regulations are receiving special attention in any attempt to make Federal Reserve regulations more understandable and to reduce the burden of compliance. The Federal Reserve Bank of Philadelphia, which was assigned responsibility for reviewing Regulation B, submitted its report to the Board at the end of 1978. The Board's staff will review the report and make recommendations to the Board.

New Information

During the past year the Board published the results of two studies—a major survey of consumers and a less extensive collection of data from creditors.[6] Both inquiries were undertaken to learn more about credit use and consumer needs and to provide information about consumer awareness and use of consumer credit legislation.

Consumer Awareness Survey

In the summer of 1977 the Survey Research Center of the University of Michigan conducted a survey of consumer awareness under the joint sponsorship of the Board, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency. The survey, which involved interviews with a nationwide sample of 2,563 consumers, included several questions pertaining to the act and Regulation B.

[6] Thomas A. Durkin and Gregory Elliehausen, *1977 Consumer Credit Survey* (Board of Governors of the Federal Reserve System, 1978); "Exercise of Consumer Rights under the Equal Credit Opportunity and Fair Credit Billing Acts," *Federal Reserve Bulletin,* vol. 64 (May 1978), pp. 363–66.

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Nearly one-quarter of the consumers surveyed experienced problems or treatment they considered unfair in their credit transactions; 622 respondents mentioned 947 problems. However, relatively few of them considered credit discrimination to be among their problems. They reported only 26 problems because of sex or marital status, 8 because of age, 3 because of race, and 6 because of other personal characteristics—a total of only 4.4 per cent of all problems (see Table 9).

The survey asked respondents what information they thought creditors use in deciding whether to make a loan. As shown in Table 10, 9.6 per cent of the responses related to personal characteristics such as age or race, while the rest related to credit history or financial characteristics. In response to a question that focused on personal characteristics protected by the ECOA, personal factors were mentioned very infrequently (Table 11), even by minority, female, elderly, and nonmarried respondents (Table 12).

9. Type of Credit Problem Considered Unfair

Problem [1]	Number of mentions	Per cent	
		Problems mentioned	Respondents
Credit refusals, limits	172	18.2	6.7
Reason for refusal not given	1	.1	0
High rates, charges	128	13.5	5.0
Other terms poor, short maturities, etc.	54	5.7	2.1
Contract sale to other creditor	27	2.8	1.0
Prepayment penalty	21	2.2	.8
Insufficient information about credit terms	35	3.7	1.4
Dunning, garnishment, embarrassment over bills	94	9.9	3.7
Repossession	25	2.6	1.0
Problem with handling of defective merchandise	54	5.7	2.1
Billing errors	70	7.4	2.7
Improper identification (another's purchase, former spouse, stolen credit card)	10	1.0	.4
Other mistakes, incorrect information, incompetence	66	7.0	2.6
Rudeness, unfriendliness	8	.8	.3
Family background or size, and credit	2	.2	.1
Sex, marital status, and credit	26	2.7	1.0
Age and credit	8	.8	.3
Race and credit	3	.3	.1
Other personal characteristics and credit	6	.6	.2
Lack of: assets, security, savings account, downpayment	13	1.4	.5
Insufficient credit history	17	1.8	.7
Credit-rating problem	33	3.5	1.3
Requirement of certain financial characteristics, residence, or job	33	3.5	1.3
All other mentions	25	2.6	1.0
Do not know or not ascertained	16	1.7	.6
Total	**947**	**100.0**	...

[1] The 947 problems were mentioned by 622 respondents, or by 24.3 per cent of the 2,563 total respondents.

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The survey did not attempt to measure consumers' awareness of the ECOA directly because at the time of the interviews the law had only recently taken effect. Survey research with respect to other credit laws indicates that public awareness of them tended to develop very slowly.

10. Consumer Perceptions of Credit Criteria Used by Creditors, Open-Ended Question

Criterion	Mentions	
	Number	Per cent
Personal		
Family size	68	1.1
Marital status	69	1.1
Sex	27	.4
Age	110	1.8
Race	12	.2
Personal character reputation	228	3.8
Other	73	1.2
Credit		
Credit history, credit rating, credit bureau reports	1,583	26.4
Assets, collateral, security	556	9.3
Amount of other debt	646	10.8
Other	40	.7
Financial		
Type of employment, security of employment, time on job	1,033	17.2
Homeownership	94	1.6
Time of current address	102	1.7
Amount of income	1,089	18.1
Other	34	.6
Other		
Other responses	45	.7
Do not know or not ascertained	193	3.2
Total	**6,002**	**100.0**

11. Consumer Responses to Closed-End Question about Credit Criteria Used by Creditors, by Criterion

Criterion	Number of mentions	Per cent of respondents (N=2,563)
Length of time on present job	1,478	57.7
Length of time at present address	358	14.0
Race	57	2.2
Having a checking account or not	251	9.8
Homeownership (own or rent)	726	28.3
Sex	74	2.9
Amount of other monthly payments (including rent or mortgage)	1,022	39.9
Age	219	8.5
Income	1,592	62.1
Marital status (married, single, separated, divorced)	143	5.6
Size of family	77	3.0
Previous credit experience	1,634	63.8

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12. Distribution of Responses by Consumers with Selected Characteristics about Use by Creditors of that Characteristic as Criterion

Group	Per cent of respondents	
	Mentioning	Not mentioning
Race		
Caucasian	1.9	98.1
Non-Caucasian	4.5	95.5
All	2.2	97.8
Sex		
Male	2.2	97.8
Female	4.3	95.7
All	2.9	97.1
Age		
Under 50 years	5.4	94.6
50 years and over	12.4	87.6
All	8.5	91.5
Marital status		
Married	5.0	95.0
Separated	2.4	97.6
Divorced	9.4	90.6
Widowed	7.9	92.1
Single, never married	4.8	95.2
All	5.6	94.4

Inquiry on Exercise of Rights under the Equal Credit Opportunity Act

In November 1977 the Board surveyed eight large creditors to determine the extent to which consumers exercise certain rights under the ECOA and the cost to creditors of complying with this law. Two areas covered in the inquiry were the right to a separate credit history for married persons and notification by creditors of specific reasons for denial of credit.

Creditors enclosed with billing statements the initial notices regarding the right to a separate credit history. Approximately 11 per cent of customers requested the maintenance of separate credit histories. The average cost to the creditors of printing and processing each notice in such a mailing was less than 1 cent, and the average cost of processing the return requests and initially reporting the new information to the credit-reporting agencies was about 9 cents per request.

A substantial proportion of rejected credit applicants requested the reasons for denial if they had not been given reasons at the time of rejection; many applicants subsequently provided additional information sufficient to warrant the granting of credit. Similarly, many applicants who were initially given reasons for credit denial supplied more information, and a high proportion of these were then granted credit. The cost of providing reasons for the denial of credit to the

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rejected applicants varied widely—ranging from 22 cents to $5.25 per account.

Consumer Advisory Council

The Consumer Advisory Council, whose members include a broad representation of consumer and creditor interests, was established in late 1976 to advise on the Board's responsibilities in the field of consumer credit protection laws. During 1978 the Council met four times and discussed various issues, including the uniform guidelines for enforcing Regulation B. In addition, the Council reviewed the efforts of the Federal Reserve in achieving member bank compliance with the ECOA and Fair Housing Act and explored approaches the Board should consider in its consumer education efforts.

In February 1978 the Board expanded the Council membership to 28 by appointing 2 additional members. In December, 8 new members were appointed to the Council for terms of 3 years to replace those whose terms expired at the end of 1978. A list of members currently serving on the Council, and their terms, is shown in the section "Federal Reserve Directories and Meetings."

Administrative Functions

Amendments and Interpretations of Regulation B during 1978

Over the course of 1978 the Board made a number of amendments and interpretations of Regulation B.

Occurrence of adverse action at point of sale. Under Regulation B, in each instance of adverse action, a creditor must either give a written explanation to the customer of the reason for such action or inform the customer of the right to receive an explanation upon request. In March 1978 the Board amended its definition to exclude most point-of-sale or loan denials from the adverse-action requirements. Under the revised definition a refusal to authorize a point-of-sale or loan transaction is *not* adverse action unless a creditor unfavorably changes the terms of an account, such as by lowering the customer's credit limit; closes an account; or turns down an application to increase the credit of an account made in accordance with the creditor's procedures at the point of sale. The amendment superseded Official Staff Interpretation EC-0008, which was rescinded.

Revised procedures for issuance of official staff interpretations. In April 1978 the Board amended Regulation B to revise the pro-

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cedure for issuing official staff interpretations. Under the new procedure, official staff interpretations are issued with an effective date 30 days after publication in the *Federal Register,* which enables the public to review them before they become effective and permits interested parties to request the opportunity for public comment. If a request is received, the effective date of the interpretation is suspended and its text republished for public comment together with the request for a comment period or a summary of the arguments presented in the request. After the comments have been reviewed, a final interpretation is issued.

Proposed amendments to Regulation B. In response to certain recommendations from the staff of the Federal Trade Commission and the President's Task Force on Women Business Owners, the Board, in October 1978, proposed for comment several changes to Regulation B that would broaden its scope. The proposed amendments would (1) bring under the regulation arrangers of credit—for example, real estate brokers who choose the creditors with which a credit application willl be filed; (2) eliminate the exemption of business credit from the record-keeping and notification requirements in certain transactions under $100,000; and (3) eliminate the exemption of business credit from the general bar against asking for an applicant's marital status. The proposed amendment regarding business credit incorporates Official Staff Interpretation EC-0009, which requires creditors to give applicants for business credit written or oral notice of action taken on an application or an existing account within a reasonable time. The comment period ended December 26, 1978.

Official staff interpretations. During 1978 the staff issued three official staff interpretations of Regulation B and withdrew two previously issued. In March 1978 the Board instructed its staff to withdraw Official Staff Interpretation EC-0007 dealing with the collection, for marketing purposes, of information otherwise prohibited under the regulation, and to issue a new interpretation, EC-0010, limiting the applicability of the interpretation. Official Staff Interpretation EC-0008, which concerned whether adverse action can occur at the point of sale, was superseded by the March 1978 amendment to the regulation.

The remaining two official staff interpretations, EC-0011 and EC-0012, deal, respectively, with the applicability of Regulation B to certain lending operations conducted outside the United States, and

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with the revised application forms for residential mortgage loans prepared by the Federal Home Loan Mortgage Association and the Federal National Mortgage Association. Both were issued under the revised procedures but were not challenged.

Education

An integral part of any enforcement program is educating both creditors and consumers as to their rights and responsibilities. During the past year the enforcement agencies participated in a number of educational efforts, including speeches and seminars involving consumers, creditors, school groups, professional associations, and others.

Explanatory pamphlets remain a popular method of consumer education. This past year the Federal Reserve Board announced two new brochures, one of which, *The Equal Credit Opportunity Act and . . . Credit Rights in Housing,* provides information about how the major provisions of the ECOA affect mortgage lending. Another, the Board's *Consumer Handbook to Credit Protection Laws,* is a compilation of consumers' rights under credit laws and regulations. The Small Business Administration reports that pamphlets concerning its "Women in Business Program" are available for distribution in all SBA program offices.

The Federal Reserve Bank of Philadelphia has recently produced a film entitled "To Your Credit." The film is being distributed to various consumer and civic groups. It depicts common problems faced by consumers in credit transactions and offers solutions by informing consumers of their rights under the many consumer credit protection laws. The FTC and the Federal Reserve Bank of San Francisco have each developed public service announcements for television and radio.

Education of creditors often occurs during the examination process. Most agencies report that this procedure enables one-to-one guidance in the areas in which it is most needed. As a supplement to this on-site education, the Federal Reserve System continued its program of advisory visits to member banks with approximately 450 visits during 1978. In addition, several new publications have been developed for creditors in 1978, such as the Federal Reserve Bank of New York's *Consumer Regulations Checklist* and the NCUA's *Manual of Laws Affecting Federal Credit Unions.*

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FEDERAL TRADE COMMISSION ACT

This is the fourth Annual Report describing the activities of the Board of Governors of the Federal Reserve System in fulfilling its responsibilities under Section 18(f) of the Federal Trade Commission Act. Those responsibilities are (1) to identify unfair or deceptive banking practices and to adopt regulations prohibiting them; (2) to receive and take appropriate action upon complaints against State member banks; and (3) within 60 days after rules prescribed by the Federal Trade Commission (FTC) take effect, to promulgate substantially similar regulations applicable to banks (unless certain exceptions apply).

This report also presents the findings of a survey that was undertaken to help determine whether certain bank practices warrant regulatory or other action by the Board. It discusses the Board's handling of consumer complaints throughout the year and summarizes the status of three rules proposed by the Federal Trade Commission that may require parallel Board action.

Initiation of Regulations by the Board

In carrying out its responsibilities to identify unfair or deceptive banking practices, the Board in early 1977 asked approximately 400 State agencies and legal-service organizations across the country to pinpoint banking acts or practices that appeared to be prevalent and problematical. From nearly 100 responses and subsequent discussions with representatives from other Federal bank regulatory agencies, the Board identified six banking practices for consideration:

1. Failing to disclose in a meaningful way to new depositors the contract terms governing use of their accounts, or failing to give reasonable advance notice to depositors of any change in terms.
2. Describing checking account services as "free" when in fact there are charges, or preconditions for no-cost checking.
3. Attaching, freezing, or closing a depositor's account without promptly notifying the depositor.
4. Imposing, as a matter of policy, an unnecessarily long "hold" on customers' funds deposited in the form of checks because of the type of check or the location of the bank on which it is drawn.
5. Describing interest paid on savings accounts as the "highest allowed by law."
6. Indicating in writing to a loan applicant that credit life or

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disability insurance is optional, but implying or stating that its acquisition is necessary for favorable consideration of the applicant's loan request.

To provide additional information about the first four practices, the Board, in conjunction with the Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency, designed a bank survey questionnaire. Examiners from all three bank regulatory agencies incorporated the questionnaire into their scheduled consumer examinations from February 1 through March 15, 1978; 846 commercial banks were surveyed. The major findings are discussed below.

Disclosure of Deposit Account Terms

Only 26 per cent of the banks surveyed disclosed on a single document the principal terms governing the checking accounts they offer. The majority of the remaining banks either did not disclose their account terms at all or made oral disclosures. In the case of savings accounts, 51 per cent of banks made comparable written disclosures.

Of the banks surveyed, 40 per cent reported that in the last 2 years they had changed the principal terms of checking accounts that affected existing customers. Of these, 62 per cent indicated that their customers were notified of the changes before they went into effect, largely through statement stuffers and separately mailed notices. While fewer banks reported similar changes in savings account terms, the percentage reporting advance notification of existing customers was approximately the same as that for checking accounts.

Advertisement of "Free" Checking Accounts

Half of the banks surveyed that advertise their checking accounts reported using "free," "no-cost," or similar wording in their advertisements. Of this group, only 43 per cent actually offered free checking accounts; the remainder offered accounts with preconditions, such as minimum balances in checking or savings accounts, or required lines of credit. However, 90 per cent of advertisements of "free" checking mentioned the preconditions.

Notification of Attached or Frozen Funds, or Set-Offs

About 97 per cent of banks responding to this question indicated an attempt to notify their account holders of attachment orders. Notification was given in advance by 16 per cent of these banks, simultaneously by 72 per cent, and after the attachment by 12 per cent. In addition, 81 per cent of banks that communicated with their

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customers about attachment orders informed them of the balances remaining in the accounts that had been frozen or attached.

Of the banks surveyed, 68 per cent indicated that they informed their customers when they have exercised the right of set-off (the right some States grant to apply funds from a customer's personal account to delinquent obligations owed the bank); 2 per cent did not notify customers of such actions; and the remaining 30 per cent either did not have the right of set-off or had not exercised it. Nearly 66 per cent of banks that notified their customers did so at the time of the set-off, 20 per cent after the action, and 14 per cent in advance.

Delayed Funds Availability

Thirty-eight per cent of banks surveyed delayed the availability of funds because of the type of check (such as personal, cashier's or bank, money order, or private payroll), or the geographical location of the bank on which the check was drawn (whether same-city, out-of-city, out-of-county, or out-of-State). More than 30 per cent of these banks delayed funds availability more than 3 days on personal checks from banks in the same city; more than 65 per cent delayed availability on personal checks on out-of-State banks more than 6 days; and more than 30 per cent delayed availability on out-of-State cashier's checks more than 3 days.

Using an analysis of the survey results, the Board will consider what regulatory or other action may be appropriate.

Consumer Complaints

During 1978, the Federal Reserve System continued to reply to complaints and inquiries about many areas of consumer activity. Responses ranged from providing consumers with information or explanations to investigating and resolving complaints against State member banks. In keeping with the Board's special civil rights enforcement efforts, separate procedures have been developed for handling complaints involving possible credit discrimination. Complaints that involved creditors or businesses not under the Board's supervisory jurisdiction and that required more than information were forwarded to the appropriate enforcement agency.

To help consumers report complaints against State member banks, the Board published a pamphlet, *How to File a Consumer Complaint.* The pamphlet explains what a consumer should do when experiencing a problem with a bank, and includes a com-

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plaint form addressed to the Board, which solicits specific information about the problem. As of January 31, 1979, nearly 740,000 pamphlets had been distributed.

Table 13 summarizes all consumer complaints received by the Board as of December 31, 1978. The following discussion focuses on the "other" complaints, which include allegations of unfair or deceptive practices not currently regulated.

The three most common types of "other" complaints involved discrepancies in account balances and disagreements over the amount of a deposit made to an account, which together represented 15 per cent of the total, and tactics used by creditors or businesses in collecting debts, which accounted for 6.5 per cent of the total.

Of the 1,543 "other" complaints, 835 were referred to other agencies and 708 were handled by the Federal Reserve System. Of the complaints handled by the System, 253 have been investigated,

13. Consumer Complaints Received by the Federal Reserve System, 1978

Subject area	*Number*
Regulation B (Equal Credit Opportunity)	824
Regulation C (Home Mortgage Disclosure)	8
Regulation Q (Interest on Deposits)	132
Regulation T (Securities Credit)	2
Regulation Z (Truth in Lending)	528
Regulation BB (Community Reinvestment)	1
Fair Credit Reporting	139
Fair Debt Collection Practices	14
Title VIII, Civil Rights	7
Transfer agents	12
Holder in due course	19
Municipal securities dealer regulation	1
Other[1]	3,230
Total	3,230
Disposition	
Cases completed by type of creditor involved	
State member banks, and processed by System staff	792
Other than State member banks	
Referred	1,489
Response provided by System staff	821
Cases pending as of December 31 by type of creditor involved	
State member banks	113
Other than State member banks	15
Total	3,230

[1] "Other" refers primarily to complaints that did not fall under identifiable consumer credit legislation administered by the Board, and includes complaints against business entities as well as financial institutions.

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61 are still under investigation, and 39 have been deferred pending receipt of additional information from the complainant. The remaining 355 complaints (approximately 50 per cent) were handled by providing information or an explanation about the acts or practices that prompted the complaints.

In the 253 completed investigations, the bank was found to be legally correct in 159 cases (in 40 of which it gave the complainant a special concession as an indication of good faith and intentions); to have made an error, which has since been corrected, in 66 cases; and to have possibly made an error in 7 cases, 4 since corrected and 3 still unresolved. The remaining 21 cases concerned factual disputes, and consumers have been advised of the legal remedies available to them.

In an ongoing effort to monitor the effectiveness of the System's efforts to resolve consumer complaints, the Federal Reserve Board sent followup letters to individuals who had contacted the Board during the year about a problem with a State member bank. Of the 45 per cent of complainants who responded to the letter, the majority expressed satisfaction with the promptness and courtesy afforded them. Although only 51 per cent of those were satisfied with the resolution of their problems, more than 84 per cent indicated that they would contact the Federal Reserve in the event of future problems.

Issuance of Substantially Similar Regulations

During 1978, no new rules were proposed by the FTC under the Federal Trade Commission Act. There were, however, further developments during 1978 on some proposals made in earlier years.

Preservation of Consumers' Claims and Defenses

The FTC proposed in November 1975 an amendment to its "holder-in-due-course rule" that would require creditors to insert a notice in certain consumer credit contracts to preserve a consumer's right to assert against a lender claims or defenses that would have been assertable against a seller of defective goods or services. In February 1976 the Board published for comment a substantially similar version of the proposed rule; a revised draft prepared by the Board's staff was transmitted by the Board to the FTC in early 1978.

During April 1976 the FTC held hearings on its proposed creditor

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amendment to the holder rule; in February 1978 it published the report of the presiding officer, and in September 1978 the FTC staff issued a report. The Board's staff commented on the FTC's staff report in January 1979; the Board is awaiting further action by the FTC before proceeding with its proposed rule, which would, if adopted, impose substantially similar requirements on banks.

Credit-Practices Rule

This rule, first proposed by the FTC in April 1975, would ban specified terms used in consumer credit contracts and specified practices used in collecting unpaid debts. The rule would also require creditors to deliver disclosures to cosigners informing them of their responsibilities and potential liability. A virtually identical rule was published for comment by the Board later in that month.

During the latter half of 1977 the FTC held hearings on its proposals; on December 20, 1977, an attorney on the Board's staff appeared and presented an analysis of the comments received by the Board and a discussion of possible technical problems concerning the proposed rule. In August 1978 the report of the presiding officer was published by the FTC. The Board is awaiting the FTC staff report on this proposal before acting further.

Sale of Used Motor Vehicles

In December 1975 the FTC proposed for comment a rule that would require used-vehicle dealers to make certain disclosures. The proposal also would cover those banks that sell used motor vehicles—for example, after repossession or expiration of leases. In May 1976 the FTC published amendments to its proposed rule, and it received written comments (including those submitted by the Board staff) through October of that year. Regional hearings were conducted through May 1977, and in late May 1978 the FTC published the report of the presiding officer. The FTC staff issued its report in mid-November 1978, and the Board staff offered further comments in December 1978. The Board is awaiting final action by the FTC before proceeding with its responsibilities under the act.

HOME MORTGAGE DISCLOSURE

Enforcement of the Home Mortgage Disclosure Act

The Board of Governors of the Federal Reserve System enforces the Home Mortgage Disclosure Act (HMDA) and its implementing Reg-

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ulation C for State member banks. Special consumer affairs examinations of State member banks covered under the HMDA continue to indicate a high level of compliance with the act.

Exemptions from the HMDA

During 1978 the Board approved one application for exemption from the disclosure requirements of the HMDA and annulled one exemption that had been granted previously.

In April 1978 the Connecticut Bank Commissioner, on behalf of the State of Connecticut, requested an exemption on the ground that Connecticut law and implementing State regulations call for disclosures substantially similar to those imposed by the HMDA and include adequate enforcement provisions. The Board received two comments on the application from the Federal Reserve Banks of Boston and New York, recommending approval of the exemption application. On August 2, 1978, the Board granted the exemption for all Connecticut-chartered depositary institutions that are subject to the Connecticut act.

On July 26, 1978, the Board annulled the exemption granted in December 1976 that applied to all Illinois-chartered depositary institutions covered by the Illinois Financial Institutions Disclosure Act. The continuation of the exemption had been contingent upon developments in litigation that had challenged the constitutionality of the Illinois law. On May 26, 1978, the Illinois Supreme Court decided that the Illinois act was unconstitutional in part and therefore void, thus removing the basis for the Illinois exemption. The State of Illinois requested that the U.S. Supreme Court review the State court decision, but the request was denied.

Section 308 Study

Under Section 308 of the HMDA, the Board, in consultation with the U.S. Department of Housing and Urban Development, was directed to study the feasibility and utility of extending the disclosure requirements of the act to depositary institutions located outside standard metropolitan statistical areas. The results of the study were submitted to the Congress in January 1979.

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Securities Acts Amendments of 1975

Pursuant to the Securities Acts Amendments of 1975 (Public Law 94–29), the Board of Governors is designated "the appropriate regulatory agency" with respect to State member banks and bank holding companies that act as municipal securities dealers or as clearing agencies. As of December 31, 1978, 50 State member banks, or separately identifiable departments or divisions of such banks, were registered as municipal securities dealers; 48 were examined in 1978.

As of December 31, 1978, four registered clearing agencies were members of the Federal Reserve System; all were examined during 1978. These examinations are designed to determine whether the clearing agency's activities are conducted in accordance with safe and sound banking practices and, if they are not, to evaluate the impact of the agency's over-all condition and to recommend and enforce appropriate corrective action.

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Government in the Sunshine

Under the Government in the Sunshine Act (Public Law 94–409, which became effective March 12, 1977), the Board opened more than a third of its meetings in 1978 to public observation, either entirely or in part. Items considered in closed sessions under exemptions in the act related primarily to monetary policy (premature disclosure of which could cause financial speculation) and to supervision of banks and bank holding companies (discussions of which generally involve information from bank examination reports or confidential commercial and financial information). To illustrate, more than half the agenda items since March 1977 involved applications by individual banks and bank holding companies; in these discussions the Board is required by law to consider financial and managerial information, which it obtains chiefly from bank examination reports.

To aid the public in obtaining the maximum possible benefit from the Board's open meetings, copies of most staff memoranda considered by the Board at open meetings are made available to the public and an agenda summarizing the issues to be discussed is provided at each meeting. A pamphlet has been prepared explaining the applicability of the act to the Board's proceedings. Photographs of Board members and seating charts are available in the Board Room. For those unable to attend, a recording of the discussion is retained in cassette form in the Board's Freedom of Information Office; copies may also be purchased at a nominal fee.

The Board maintains a Sunshine mailing list to ensure that interested members of the public learn of meetings in a timely manner. Besides announcements in the *Federal Register,* notices of meetings are made available at the Board's Freedom of Information and Public Affairs Offices and at the Treasury Department's press room.

A record, including either minutes or recordings, of each closed meeting is provided in the Freedom of Information Office, unless the Board has voted to withhold part or all of the discussion under the act's exemptions. This material is released when the exemptions no longer apply.

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Legislative Recommendations

The Board of Governors has made the following recommendations for legislation to the Congress of the United States.

MONETARY IMPROVEMENT PROGRAM

Confronting rapid change in the financial system of the Nation and increasingly intense competition among depositary institutions, many banks have become less willing in recent years to bear the high cost of uncompensated cash reserve requirements associated with membership in the Federal Reserve System. Consequently, there has been a steady and, indeed, accelerating decline in the proportion of bank deposits subject to Federal reserve requirements. At the end of 1978, member banks held less than 71 per cent of total commercial bank deposits, down more than 9 percentage points since 1970. At present, more than one-fourth of commercial bank deposits—and over three-fifths of all banks—are outside the Federal Reserve System.

The attrition in deposits subject to reserve requirements set by the Federal Reserve weakens the linkage between member bank reserves and the monetary aggregates and makes the relationship less predictable. It is essential that the Federal Reserve maintain adequate control over the monetary aggregates if the Nation is to succeed in curbing inflation, sustaining economic growth, and maintaining the value of the dollar in international exchange markets.

Moreover, because of the attrition in membership and the growth of transactions balances at nonbank depositary institutions, the proportion of the financial system with direct access to the discount window on a day-to-day basis has shrunk. The growth of transactions balances at institutions that do not have access to Federal Reserve clearing services also could lead to a deterioration of the quality of the Nation's payments system.

In sum, the major functions of the Federal Reserve System—to conduct monetary policy in the public interest, to provide back-up liquidity and flexibility to the financial system, and to assure a safe and efficient payments mechanism—all have been undermined by attrition in Federal Reserve membership.

The basic reason for the decline in membership is the financial

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burden that membership entails. Member banks must keep their required reserves entirely in nonearning form and thus are at a competitive disadvantage compared with nonmember banks and other depositary institutions, which do not face similar requirements. Using 1977 data, the Board's staff estimates that the aggregate burden to member banks of Federal Reserve membership exceeds $650 million annually, or about 9 per cent of the profits of member banks before taxes.

To facilitate the implementation of monetary policy and to promote competitive equality among all depositary institutions, the Board suggests legislation that would establish universal reserve requirements applicable to all deposits at commercial banks and to transactions balances at thrift institutions. Reserve ratios would be reduced from present-day levels. Under this proposal, small institutions would be exempt from holding any reserves at all. The proposed exclusion would apply to the first $10 million of transactions deposits at all institutions, and $10 million of other deposits at commercial banks. The reserves against deposits above the $10 million exclusion and up to $50 million would be held in an "earnings participation account" at the Federal Reserve, on which the earnings would be equivalent to the average return on the Federal Reserve's portfolio. The proposal would greatly increase the proportion of transactions deposits at commercial banks controlled by the Federal Reserve—from 70.8 per cent to 94 per cent—thereby enhancing the implementation of monetary policy.

The proposal also contemplates giving all commercial banks and thrift institutions with transactions accounts access to the Federal Reserve discount window. The Federal Reserve could then act as a lender of last resort to a broad class of depositary institutions, thereby providing greater safety and soundness to the depositary system. All depositary institutions would also be given access to Federal Reserve services; under an appropriate pricing schedule, this action should improve the efficiency of the payments mechanism that underlies all of the Nation's economic transactions.

FINANCIAL TRANSACTIONS WITH AFFILIATES

During 1976 and 1977 the Board conducted a major review of Section 23A of the Federal Reserve Act. Section 23A is designed to protect member banks from abuse by restricting non-arm's-length

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financial transactions between these banks and affiliated companies. The Board's review of this statute was prompted in part by the discovery that several relatively large banks had been adversely affected by transactions with their affiliates.

One of the Board's major conclusions is that bank transactions with affiliates within the statutory limits have not produced substantial instability in the banking system. At the same time, the Board finds some flaws in the present statute: (1) it is inordinately complex; (2) it contains some potentially troublesome loopholes; and (3) it appears to be unduly restrictive in several ways.

The Board has recommended amendments to Section 23A to correct these flaws. Principal among its recommendations are those (1) to allow a holding company greater freedom to transfer funds among its sister subsidiary banks but prohibit a bank from purchasing low-quality assets from a sister bank subsidiary; (2) to broaden the definition of "affiliate" to include real estate investment trusts and other financial organizations that are sponsored and advised by a banking organization; and (3) to expand the types of collateral permitted on bank loans and extensions of credit to affiliates while requiring that these new types of collateral have a high value relative to the loan.

LENDING AUTHORITY OF FEDERAL RESERVE BANKS

The Board again urges enactment of legislation to permit member banks to borrow from their Reserve Banks on the security of any sound assets without paying a penalty rate of interest whenever paper ineligible for discount by Federal Reserve Banks is presented as collateral.

Under Section 13 of the Federal Reserve Act, Federal Reserve Banks may extend credit at the basic discount rate to member banks on promissory notes that are secured by obligations eligible either for purchase or for discount by the Reserve Banks.

Under Section 10(b) the Reserve Banks are authorized to extend to member banks credit on promissory notes secured to the satisfaction of the Reserve Banks. However, Section 10(b) also provides that such credit extensions "shall bear interest at a rate not less than one-half of 1 per centum per annum higher than the highest discount rate in effect" at the Reserve Bank making the loan, except when the loan is secured by mortgages on 1- to 4-family homes. The result is that many sound member-bank loans cannot qualify as security for

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Federal Reserve advances except at this penalty rate of interest, even though their quality may be equal to that of currently "eligible" paper. Elimination of the penalty rate means that obligations such as commercial paper with maturities in excess of 90 days could be used as collateral for advances at the basic discount rate.

EXPANSION OF CLASS C DIRECTORS

The Board has submitted to the Congress draft legislation to increase the number of Class C directors at each Federal Reserve Bank from three to six. The proposal aims to diversify further the backgrounds and interests represented on the Reserve Bank boards of directors as a way of accomplishing one of the objectives of the Federal Reserve Reform Act of 1977. That act provides for the representation of the interests of consumers, labor, and services, in addition to agriculture, commerce, and industry, on the boards of directors of the Reserve Banks.

TERM OF CHAIRMAN OF THE BOARD OF GOVERNORS

Proposals to align the term of the Chairman of the Federal Reserve with the term of the President of the United States have been under consideration in various forms for some years. The Board has recommended legislation making the 4-year term of the Chairman begin 1 year following the inauguration of the President, believing that this arrangement would contribute to the coordination of monetary, fiscal, and other economic policy-making without undermining the independence of the Federal Reserve System.

The bill also would authorize the Vice Chairman to act as Chairman in the event of (1) the temporary absence and unavailability or incapacity of the Chairman; or (2) the death, resignation, or permanent incapacity of the Chairman, pending appointment and confirmation of a successor. In addition, it would clarify that the Chairman and Vice Chairman continue to serve in those capacities after expiration of their terms until a successor is designated and confirmed.

LOANS TO EXAMINERS

Section 212 of the U.S. Criminal Code prohibits loans to a bank examiner by any bank that the examiner is authorized to examine. As a result, Federal Reserve examiners are greatly limited in their

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sources of credit because they are authorized to examine not only State member banks but also national banks and any insured nonmember bank that is an affiliate of either a member bank or a registered bank holding company. The growth of the bank holding company movement has increasingly narrowed the remaining sources of credit for System examiners. The Board recommends enactment of an amendment that would authorize an insured bank to make loans to an examiner under regulations prescribed by the Federal agency that employs the examiner, provided that the examiner does not examine that institution.

AUTHORITY FOR BANK HOLDING COMPANIES TO ACQUIRE BANKS ACROSS STATE LINES IN EMERGENCY AND FAILING-BANK SITUATIONS

The Board again recommends that the Congress give the Federal Reserve authority in certain emergency and failing-bank situations to approve the acquisition by an out-of-State bank holding company of a large bank that is in severe financial difficulty. The purpose of the legislation is to avoid an adverse potential impact when the failing bank is one of the largest in the State and the public interest would best be served by such an acquisition.

The authority would be limited to cases involving a bank that has assets in excess of $500 million or a bank that is one of the three largest in the State. The authority would be used only in cases in which few or no purchasers could be found within the State and in which the size or other special characteristics of the problem bank and the probability of widespread financial effects of its failure warrant an exception to the general restrictions on out-of-State bank acquisitions by a bank holding company.

SIMPLIFICATION OF TRUTH IN LENDING ACT

As a result of widespread concern about the complexity of Truth in Lending, the Board has made recommendations to the Congress to improve and simplify the statute. Creditors acting in good faith have experienced difficulty in complying with Truth in Lending. Likewise, the complexity of the disclosures appears to have diminished their usefulness to consumers.

The Board's proposal has several major elements. It is designed

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to inform consumers better and to emphasize the cost disclosures most needed in shopping for credit—the annual percentage rate, the finance charge, and the payments schedule. The 1977 Consumer Credit Survey, which was initiated by the Board in cooperation with the Comptroller of the Currency and the Federal Deposit Insurance Corporation and conducted by the University of Michigan's Survey Research Center, shows that these disclosures are far more important to consumers than those of other terms. The proposal reduces the detail of the disclosures—for example, eliminating the itemization of the components of the finance charge and of the amount financed. Significant information that is less important for shopping purposes, such as whether the obligation is secured, would be summarized, but the details would be relegated to the contract.

Under the proposal the disclosures required by Federal law would be segregated from other matters in the contract and from other disclosures required by State law so that the Truth in Lending disclosures would not be lost among other provisions.

In addition, the credit-cost terminology would be explained in plain English; and the Board would develop and publish model forms and clauses that, if properly completed, would protect creditors from civil liability under the act. The proposal also contains extensive technical clarifications.

UNIFORM RULES FOR CREDIT AND EFT TRANSACTIONS

When the Ninety-Fifth Congress enacted the Electronic Fund Transfer Act to regulate the consumer aspects of electronic funds transfers, the Board was assigned the responsibility of writing regulations to implement the act. In doing so, the Board has become concerned that consumers will encounter unnecessary difficulty in understanding the rules provided by the new act, and will confuse them with the rules under the Truth in Lending and Fair Credit Billing Acts.

Confusion may arise particularly when a single card will perform multiple functions and be subject at one time to the rules of the Truth in Lending and Fair Credit Billing Acts, as in the case of a credit purchase, and at another time to the different rules of the EFT Act, as in the case of a cash withdrawal. Even apart from the multiple-function card, the Board believes consumers should not have to learn one set of rules for a credit card and another for an EFT card. In order to minimize confusion, the Board recommends

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that the act be amended to provide a single set of rules governing credit and EFT transactions.

Among its proposals to unify the requirements, the Board has made the following specific recommendations:

To establish a uniform dollar limit governing liability for unauthorized use. Now, the Truth in Lending Act imposes a $50 limit on the liability of a credit-card holder each time a card is lost or stolen; the EFT Act has a $50, $500, and unlimited-liability structure.

To provide that oral notice to the creditor be sufficient to take advantage of the rules on the resolution of disputes under the Fair Credit Billing Act. Now, a consumer must write to the creditor under that act, whereas the EFT Act permits oral notice.

To establish parallel timing requirements for correction of errors under the EFT and Fair Credit Billing Acts. Under both acts, within 10 days of a customer's notifying a creditor of an error, the customer would be given either notice that a correction had been made or, if the creditor believes that no error occurred, an explanation of the transaction. As an alternative, a written notice that the customer's account had been provisionally recredited would be required for EFT transactions; and a written notice that amounts in dispute need not be paid would be required for credit transactions. Also, the EFT Act would be amended to conform to the Fair Credit Billing Act's requirement for resolution of a dispute within 90 calendar days.

To eliminate the annual notice of rights under the EFT Act and the semiannual notice of rights under the Fair Credit Billing Act, and in their place to require that periodic statements contain a summary notice setting out the rights and the way to obtain a complete explanation.

To permit the unsolicited issuance of unvalidated credit cards. At present, the Truth in Lending Act prohibits the unsolicited issuance of credit cards, while the EFT Act permits the unsolicited issuance of cards provided they are not validated.

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Litigation

During 1978 the Board of Governors was named in 22 lawsuits, compared with 15 filed in 1977 and 22 in 1976. Of the actions filed in 1978, 17 raise questions under the Bank Holding Company Act; 9 such actions were filed in 1977. As of December 31, 1978, 33 cases remained pending, 24 of which raise questions under the Bank Holding Company Act. A brief description of each case that is still pending or that was disposed of in 1978 follows.

BANK HOLDING COMPANIES—ANTITRUST ACTION

In 1978 the U.S. Department of Justice filed no challenges under the antitrust laws of the United States to acquisitions by registered bank holding companies or bank mergers that had been previously approved by the Board, and no such cases are pending from previous years.

BANK HOLDING COMPANIES—REVIEW OF BOARD ACTIONS

In *Bankers Trust New York Corporation* v. *Board of Governors,* No. 73–1805 (2d Cir., filed May 25, 1973), petitioner requested the court to review and set aside a Board order (*Federal Reserve Bulletin,* volume 59, May 1973, page 364) denying petitioner's application to engage in investment advisory activities through a newly formed subsidiary corporation in Palm Beach, Florida. In October 1973 the court granted petitioner's request for a delay in the proceedings pending the outcome, on appeal, of a suit in U.S. District Court for the Northern District of Florida challenging the constitutionality of a Florida statute prohibiting out-of-State banking organizations from performing investment advisory services in Florida, upon which the Board had based its order. On April 14, 1975, the U.S. Supreme Court vacated the district court judgment in that suit, finding the suit inappropriate for a three-judge court, and sent the case back to the district court (421 U.S. 901). The district court, on December 15, 1978, ruled that the Florida statute violated the commerce clause of

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the U.S. Constitution, thus leaving the petitioner's suit against the Board pending.

In *Investment Company Institute* v. *Board of Governors,* No. 77–1862 (D.C. Cir., filed on September 23, 1977), petitioner sought judicial review of a Board order, dated August 31, 1977 (*Federal Reserve Bulletin,* volume 63, September 1977, page 856), denying its petition for reconsideration and rescission of a portion of the Board's January 1972 amendment to Regulation Y (*Federal Register,* volume 37, 1972, page 1463). Petitioner challenged the validity, under the Glass-Steagall Act, of the Board's amendment, which permits bank holding companies to act as investment adviser to an investment company that is registered under the Investment Company Act of 1940. Oral argument has been heard by the court, and the case is pending.

In *Alabama Association of Insurance Agents, Inc.* v. *Board of Governors,* No. 74–2981 (5th Cir., filed July 26, 1974), and *Georgia Association of Independent Insurance Agents* v. *Board of Governors,* No. 74–3544 (5th Cir., filed October 3, 1974), petitioners challenged the Board's orders (*Federal Reserve Bulletin,* volume 60, August 1974, page 596, and *Federal Register,* volume 39, 1974, page 33414) permitting Southern Bancorporation, Birmingham, Alabama, and First National Holding Company, Atlanta, Georgia, to engage in certain insurance agency activities. On June 10, 1976, the court issued a decision upholding the Board's findings that the sale of property and casualty insurance by a bank holding company, when related to an extension of credit, is closely related to banking within the meaning of Section 4(c)(8) of the Bank Holding Company Act and of Section 225.4(a) of the Board's Regulation Y, and that the applications in question could reasonably be expected to have public benefits that outweight possible adverse effects. The court, however, determined that the sale of insurance for the holding company and its nonbanking subsidiaries, the sale of insurance as a convenience for the purchaser, and general insurance agency activities in towns of fewer than 5,000 inhabitants are not activities closely related to banking and therefore are not permissible for bank holding companies (533 F.2d 244).

On petitions for rehearing by the parties, the court, by order dated September 1, 1977 (558 F.2d 729), rejected petitioners' contentions that the sale of property and casualty insurance in connection with extensions of credit and other financial services should be restricted

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to sales by bank subsidiaries of bank holding companies. The court also remanded to the Board the question of whether general insurance agency activities in towns of fewer than 5,000 inhabitants are closely related to banking. A petition for certiorari filed by petitioners in the U.S. Supreme Court was denied on February 2, 1978 (46 U.S.L.W. 3541).

In *Florida Association of Insurance Agents, Inc.* v. *Board of Governors,* Nos. 75–3151 to 3153 (5th Cir., filed August 12, 1975), petitioner sought judicial review of three Board orders (*Federal Register,* volume 40, 1975, pages 30869, 30872, 30876) approving the applications of four bank holding companies to engage in certain insurance agency activities in Florida to the extent permitted by State law. These cases were consolidated in the Fifth Circuit with the claims brought in *National Association of Insurance Agents, Inc.* v. *Board of Governors,* Nos. 75–3342, 75–3343, and 75–3358 (D.C. Cir.), in which the petitioner challenged the same Board orders. These cases were argued on September 12, 1978, and are pending before the court.

In *BankAmerica Corporation* v. *Board of Governors,* No. C77–1005 SW (N.D. Cal., filed May 13, 1977), petitioner sought a declaratory judgment that its proposal to expand geographically and to continue to engage in data processing activities through its subsidiary, the Decimus Corporation, within a 500-mile radius of Piscataway, New Jersey, had been approved because the Board failed to act on the proposal within the 91-day period required for Board action under 12 U.S.C. 1843(c). On July 29, 1977, the district court ruled in favor of BankAmerica Corporation. The Board has appealed this decision (No. 77–3485, 9th Cir.).

In a second case, *BankAmerica Corporation* v. *Board of Governors*, No. 77–2173 (9th Cir., filed May 25, 1977), BankAmerica sought judicial review of a Board order, dated May 20, 1977 (*Federal Register*, volume 42, 1977, page 27293), providing for a hearing with respect to its application to engage in data processing activities through the Decimus Corporation. Both actions have been consolidated and are pending in the Court of Appeals for the Ninth Circuit.

In *First Lincolnwood Corporation* v. *Board of Governors,* No. 76–1114 (7th Cir., filed February 5, 1976), petitioner asked the court to review the Board's order of January 9, 1976 (*Federal Reserve Bulletin*, volume 62, February 1976, page 153), denying, on the grounds

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of inadequate financial resources, petitioner's application to become a bank holding company through acquisition of the First National Bank of Lincolnwood, Lincolnwood, Illinois. In a decision dated December 7, 1976 (546 F.2d 718), a panel of the court affirmed the Board's order, holding that substantial evidence supported the Board's findings; that the Board's order was issued within 91 days from the submission of the complete record; and that the Board complied with its own regulations governing applications to form a bank holding company.

On petitioner's request for rehearing, the court *en banc,* in a decision dated July 13, 1977 (560 F.2d 258), set aside the Board's order, holding that under the Bank Holding Company Act the Board's authority to deny, for financial reasons, an application to form a bank holding company is limited to cases in which the formation would cause or worsen adverse financial conditions in the proposed subsidiary bank. The court found that the restructuring of bank ownership from individuals to a corporation owned by the same individuals was not likely to have such a result and that the Board improperly denied approval to First Lincolnwood.

The Board filed a petition for a writ of certiorari by the U.S. Supreme Court for review, which was granted (No. 77–832). The Supreme Court held that the Board has authority under the Bank Holding Company Act to disapprove formation of a bank holding company solely on grounds of pre-existing financial or managerial unsoundness, regardless of whether the unsoundness would be caused or enhanced by the formation. The Court reversed the decision of the Seventh Circuit (47 U.S.L.W. 4048, December 12, 1978).

In *Memphis Trust Company* v. *Board of Governors,* No. C76–64 (W.D. Tenn., filed February 19, 1976), plaintiff requested that the Board's order of April 10, 1975 (*Federal Reserve Bulletin*, volume 61, May 1975, page 327), denying plaintiff's application to acquire Home Owners Savings and Loan Association, Collierville, Tennessee, be set aside. In a decision on June 4, 1976, the court held that plaintiff's application had been approved by operation of law because the Board had not acted on the application within 91 days after the submission of the complete record to the Board. The district court further held that it had jurisdiction over plantiff's suit.

The Board appealed the decision to the U.S. Court of Appeals for the Sixth Circuit (No. 76–2183). The Court held, on September 22,

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1978, that the district court lacked subject matter jurisdiction, reversed the district court, and remanded the case for dismissal without prejudice to petitioner's right to request the Board to reconsider its order of April 10, 1975.

In *Central Wisconsin Bankshares, Inc.* v. *Board of Governors*, No. 76–1603 (7th Cir., filed June 25, 1976), petitioner requested the court to review and set aside an order of the Board dated May 26, 1976 (*Federal Reserve Bulletin,* volume 62, June 1976, page 538), denying petitioner's application to acquire Central National Bank of Wausau, Wausau, Wisconsin. Petitioner argued that the application was approved by operation of law because the Board failed to act on the application within the 91-day period required for Board action by 12 U.S.C. 1842(b). On July 14, 1978, the court upheld the Board's order, finding that the Board had met the 91-day statutory requirement for processing the application.

In *National Automobile Dealers Association, Inc.* v. *Board of Governors,* No. 76–2021 (D.C. Cir., filed November 12, 1976), petitioner challenged a Board order dated October 13, 1976 (*Federal Reserve Bulletin,* volume 62, November 1976, page 930), in which the Board determined that automobile leasing is closely related to banking and made a general determination that automobile leasing is a proper incident to banking. The Board concluded that bank holding companies may continue to conduct automobile leasing activities consistent with the Board's personal-property leasing regulation and amended its Regulation Y to provide that such leases be on a nonoperating basis. The court upheld the Board's order on February 21, 1978, and the NADA petition for a writ of certiorari to the U.S. Supreme Court was denied on October 3, 1978 (42 U.S.L.W. 3225).

In *First State Bank of Abilene, Texas* v. *Board of Governors*, No. 77–1703 (D.C. Cir., filed August 5, 1977), petitioner asked the court to set aside the Board's order of July 7, 1977 (*Federal Reserve Bulletin,* volume 63, August 1977, page 744), approving the application of First International Bancshares, Inc., Dallas, Texas, to acquire the Texas State Bank, Abilene, Texas, a proposed new bank. The court dismissed the action on February 15, 1978, pursuant to a motion filed by First International Bancshares.

In *Plaza Bank of West Port* v. *Board of Governors*, No. 77–1730 (8th Cir., filed September 14, 1977), petitioner sought judicial review of a Board order dated August 15, 1977 (*Federal Reserve Bulletin,*

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volume 63, September 1977, page 848), approving the application of Manchester Financial Corporation, St. Louis, Missouri, to acquire Manchester Bank West County, Maryland Heights, Missouri, a proposed new bank. The court, on May 15, 1978, upheld the Board's order (575 F.2d 1248).

In *Central Bank* v. *Board of Governors,* No. 77–1937 (D.C. Cir., filed October 17, 1977), petitioner asked the court to review a September 13, 1977, determination by the Board denying petitioner's request for a determination that the individual organizers of the Tri-City National Bank of West Allis, West Allis, Wisconsin, constitute a company under the Bank Holding Company Act. The court remanded the case to the Board for further proceedings on November 21, 1978. The Board petitioned the court for rehearing on December 12, 1978.

In *Vickars–Henry Corporation* v. *Board of Governors,* No. 77–3890 (9th Cir., filed December 13, 1977), petitioner challenged a Board letter determination, dated November 15, 1977, that petitioner is not a bank holding company for purposes of the Bank Holding Company Tax Act of 1976. The case is awaiting oral argument.

In *Gelfand* v. *Board of Governors,* No. 77–3473 (5th Cir., filed December 19, 1977), petitioner sought to overturn a November 22, 1977, decision by the Federal Reserve Bank of Chicago to extend, pursuant to Section 4(c)(2) of the Bank Holding Company Act, for 1 year the time within which First Chicago Corporation, Chicago, Illinois, must divest shares of Beacon Hill Corporation acquired by First Chicago in the course of securing or collecting a debt previously contracted in good faith. The court granted, on May 25, 1978, the Board's motion to dismiss for lack of standing.

In *Wisconsin Bankers Association* v. *Board of Governors,* No. 78–1083 (D.C. Cir., filed January 31, 1978), petitioner sought judicial review of the Board's order, dated December 30, 1977 (*Federal Reserve Bulletin*, volume 64, January 1978, page 40), approving the application of WISCUB, Inc., Milwaukee, Wisconsin, to become a bank holding company through the acquisition of Cleveland State Bank, Cleveland, Wisconsin. On October 27, 1978, the court remanded the case to the Board for further development of the record.

In *Michigan National Corporation* v. *Board of Governors,* No. 78–3057 (6th Cir., filed February 1, 1978), petitioner sought judicial review of the Board's order, dated January 31, 1978 (*Federal Reserve Bulletin*, volume 64, February 1978, page 127), approving petitioner's

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application to acquire Michigan National Bank–Sterling, Sterling Heights, Michigan, a proposed new bank, on the condition that petitioner discontinue the "accommodation transaction services" offered at its subsidiary banks. The court granted, on April 21, 1978, petitioner's motion to consolidate the case with two others that petitioner has appealed from Federal district court. The case is awaiting oral argument.

In *Security Bancorp* v. *Board of Governors,* Nos. 78–1581 and 78–2031 (9th Cir., filed March 17 and May 12, 1978), petitioners challenged the Board's action in denying Security Bancorp's application to become a bank holding company through the acquisition of Security National Bank, Walnut Creek, California (*Federal Reserve Bulletin,* volume 64, May 1978, page 405). The cases are awaiting oral argument.

In *Citicorp* v. *Board of Governors,* No. 78–4039 (2d Cir., filed March 23, 1978), petitioner sought judicial review of a Board order, dated March 13, 1978 (*Federal Reserve Bulletin,* volume 64, April 1978, page 321), denying petitioner's application to retain Advance Mortgage Corporation, Southfield, Michigan. On January 2, 1978, the court upheld the Board's order, holding that the Board's decision was supported by substantial evidence and that the Board had met the 91-day statutory requirement for processing the application.

In *Dakota Bankshares, Inc.* v. *Board of Governors,* No. 78–1257 (8th Cir., filed April 4, 1978), petitioner sought judicial review of the Board's order, dated March 9, 1978 (*Federal Reserve Bulletin*, volume 64, April 1978, page 310), denying the application by petitioner to become a bank holding company through the acquisition of The Dakota National Bank and Trust Company of Fargo, Fargo, North Dakota. The case was dismissed by the court on August 7, 1978, pursuant to petitioner's motion, after the Board granted reconsideration of its order and approved petitioner's application.

In *Hawkeye Bancorporation* v. *Board of Governors,* No. 78–1247 (8th Cir., filed April 5, 1978), petitioner sought judicial review of the Board's order, dated March 7, 1978 (*Federal Reserve Bulletin*, volume 64, April 1978, page 315), denying petitioner's application to acquire Second National Bank, Eldora, Iowa. The court remanded the case to the Board on September 21, 1978, pursuant to petitioner's motion, to enable the Board to consider petitioner's request for reconsideration of the Board's denial. The Board granted recon-

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sideration and approved the acquisition on November 3, 1978. On November 27, 1978, the court dismissed the case pursuant to petitioner's motion.

In *Ellis Banking Corporation* v. *Board of Governors,* No. 78–2098 (5th Cir., filed May 22, 1978), petitioner sought judicial review of the Board's order, dated April 24, 1978 (*Federal Reserve Bulletin,* volume 64, May 1978, page 400), denying petitioner's application to acquire Madeira Beach Bank, Madeira Beach, Florida, and First Gulf Beach Bank and Trust Company, St. Petersburg Beach, Florida. The court dismissed petitioner's appeal on November 29, 1978, pursuant to a motion by petitioner.

In *NCNB Corporation* v. *Board of Governors,* No. 78–1363 (4th Cir., filed June 8, 1978), petitioner sought review of the Board's order, dated May 10, 1978 (*Federal Reserve Bulletin,* volume 64, June 1978, page 506), refusing to publish for comment a proposal to engage in the underwriting of property and casualty insurance, adjusting insurance claims, and appraising and valuing property in connection with those activities. Petitioner claims that the Board failed to act on the application within the 91-day period required for Board action by 12 U.S.C. 1842(b) and that the Board acted arbitrarily and capriciously in declining to publish for comment petitioner's proposal. The case is awaiting oral argument.

In *NCNB Corporation* v. *Board of Governors,* No. 78–1364 (4th Cir., filed June 8, 1978), petitioner sought judicial review of a Board order, dated May 11, 1978 (*Federal Reserve Bulletin,* volume 64, June 1978, page 504), denying petitioner's application to retain TranSouth Financial Corporation and its subsidiary, TranSouth Mortgage Corporation, both of Florence, South Carolina. The court entered a consent order on August 1, 1978, remanding the case to the Board for consideration of an amended application by NCNB. The Board approved NCNB's amended application by order dated October 27, 1978 (*Federal Reserve Bulletin,* volume 64, November 1978, page 904). The court dismissed the case on December 7, 1978, pursuant to petitioner's motion to dismiss.

In *Mid-Nebraska Bancshares, Inc.* v. *Board of Governors,* No. 78–1658 (D.C. Cir., filed July 14, 1978), the petitioner sought judicial review of a Board order, dated June 16, 1978 (*Federal Reserve Bulletin,* volume 64, July 1978, page 589), denying the application by Mid-Nebraska Bancshares, Inc., Ord, Nebraska, to become a bank

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holding company through the acquisition of Nebraska State Bank, Ord, Nebraska. Petitioner claims that the Board's order was not supported by substantial evidence and was in excess of the Board's authority under the Bank Holding Company Act.

In *Manchester-Tower Grove Community Organization/ACORN* v. *Board of Governors, No.* 78–1898 (D.C. Cir., filed September 12, 1978), petitioner sought judicial review of the Board's order of June 16, 1978 (*Federal Reserve Bulletin,* volume 64, July 1978, page 576), approving the merger of Manchester Financial Corporation, St. Louis, Missouri, into Commerce Bancshares, Inc., Kansas City, Missouri. On December 1, 1978, the court denied petitioner's motion for a stay of the approved merger. Petitioner claims the Board failed to comply with the recently enacted Community Reinvestment Act in approving the merger. The case is pending.

In *Metro North State Bank* v. *Board of Governors,* No. 78–1786 (8th Cir., filed October 30, 1978), petitioner sought judicial review of the Board's order, dated September 27, 1978 (*Federal Reserve Bulletin,* volume 64, October 1978, page 803), approving the acquisition of the Commerce Bank of Clay County, N.A., Kansas City, by Commerce Bancshares, Inc., Kansas City. The case is pending.

In *United Bank Corporation of New York* v. *Board of Governors,* No. 78–4172 (2d Cir., filed November 1, 1978), petitioner challenged the Board's order, dated October 3, 1978 (*Federal Reserve Bulletin,* volume 64, November 1978, page 894), denying petitioner's application to acquire the Schenectady Trust Co., Albany, New York. The case has been dismissed, pursuant to stipulation, pending submission by petitioner of a petition to the Board for reconsideration of an amended application.

In *Jackson* v. *Board of Governors,* No. 78–3476 (5th Cir., filed November 13, 1978), petitioners sought judicial review of the Board's order, dated November 1, 1978 (*Federal Reserve Bulletin,* volume 64, December 1978, page 982), approving the application of Texas American Bancshares, Inc., Fort Worth, Texas, to acquire additional shares of Bank of Fort Worth, Fort Worth, Texas. The case is pending.

In *Commercial National Bank* v. *Board of Governors,* No. 78–2238 (D.C. Cir., filed December 4, 1978), petitioners sought judicial review of the Board's order, dated November 3, 1978 (*Federal Reserve Bulletin,* volume 64, December 1978, page 964), approving

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indirect retention by First Arkansas Bankstock Corporation, Little Rock, Arkansas, of First National Bank in Mena, Mena, Arkansas. Petitioner filed a motion to dismiss on January 12, 1979.

In *Hunter Holding Company* v. *Board of Governors,* No. 78–1907 (8th Cir., filed December 28, 1978), petitioner sought judicial review of a Board order, dated November 29, 1978 (*Federal Reserve Bulletin,* volume 64, December 1978, page 976), denying petitioner's application to become a bank holding company by acquiring Security State Bank of Hunter, Hunter, North Dakota. The case is pending.

In *California Life Corporation* v. *Board of Governors,* No. 79–1013 (D.C. Cir., filed January 4, 1979), petitioner sought judicial review of a December 7, 1978, letter of the Federal Reserve Bank of Kansas City regarding the proposed acquisition by Baldwin-United Corporation, Cincinanti, Ohio, pursuant to 12 U.S.C. 1843(c)(12) and 12 C.F.R. 225.4(d), of College/University Corporation, Indianapolis, Indiana. The case is pending.

OTHER LITIGATION INVOLVING CHALLENGES TO BOARD PROCEDURES AND REGULATIONS

In *Roussel* v. *Board of Governors,* No. 75–1044 (E.D. La., filed April 5, 1975), plaintiff sought damages and an injunction against a removal action instituted against plaintiff by the Board under the Financial Institutions Supervisory Act—12 U.S.C. 1818(e)(2) and (4). The court dismissed the request for injunctive relief following plaintiff's resignation from the board of directors of the National American Bank of New Orleans, New Orleans, Louisiana, and the entry of a consent order of prohibition concerning his participation in the affairs of that institution. The court dismissed the case with prejudice on March 14, 1978, pursuant to a stipulation between the parties.

In a case related to the failure of the United States National Bank, San Diego, California, *Roberts Farms, Inc.* v. *Comptroller of the Currency,* No. 75–0268 (S.D. Cal., filed November 20, 1975), plaintiff sought damages on the grounds that the Federal bank regulatory agencies negligently supervised the bank. The case has been stayed indefinitely pending the outcome of similar suits.

In *Merrill* v. *Federal Open Market Committee,* No. 75–0736 (D.D.C., filed May 8, 1975), plaintiff brought suit under the Freedom

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of Information Act to compel the Committee to disclose immediately records of its policy actions and memoranda of discussion at its meetings in January and February 1975. By order of March 9, 1976 (413 F. Supp. 494), the court ruled that the records of the Committee's policy actions must be made available to the public upon adoption and that reasonably segregable factual portions of the memoranda of discussions must also be disclosed. The Committee appealed to the U.S. Court of Appeals for the District of Columbia Circuit the ruling on policy actions (No. 76–1379). The Court of Appeals, on November 10, 1977 (565 F.2d 778), affirmed the ruling of the district court that the Committee's monthly policy actions, including its Domestic Policy Directives and tolerance ranges for the money supply and the Federal funds rate, must be publicly released upon adoption by the Committee. The Board filed a petition for a writ of certiorari by the Supreme Court for review of the decision of the court of appeals (46 U.S.L.W. 3722, May 23, 1978), which was granted. The case was argued before the Supreme Court on December 6, 1978, and is pending.

In Re: Franklin National Bank Securities Litigation, MDL No. 196 (cases consolidated on April 22, 1977), consolidated several actions for damages brought against various defendants who were connected with the Franklin National Bank, New York, New York, which was declared insolvent by the Comptroller of the Currency on October 8, 1974. Several defendants in these actions—the insurers and auditors of Franklin National Bank and its parent holding company—filed, or sought to file, third-party actions against the United States based on the alleged negligence of the banking regulatory agencies, including the Board and the Federal Reserve Bank of New York, in the supervision of the bank. In an opinion dated January 17, 1978, the court declined to dismiss completely the Government's motion to dismiss the third-party actions. The court held that in certain circumstances the United States may be liable for alleged negligent supervision by bank regulatory agencies if their activities with respect to the bank substituted their decisions for those of the bank's management to the bank's detriment. The case is pending.

In a related case, *Corbin* v. *Federal Reserve Bank of New York,* No. 77–C4896 (S.D.N.Y., filed October 6, 1977), plaintiff, the trustee in bankruptcy of Franklin National Bank's parent holding

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company, alleges that certain provisions in the agreement under which the Federal Deposit Insurance Corporation assumed the obligation to repay Franklin National Bank's indebtedness to the Federal Reserve Bank of New York are inequitable and unjust. On October 6, 1978, the court dismissed the suit as to the Board.

In *National Urban League* v. *Office of the Comptroller of the Currency,* No. 76–0718 (D.D.C., filed April 26, 1976), plaintiffs (nine civil rights organizations and the National Association of Real Estate Brokers) filed suit against the Board, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Federal Home Loan Bank Board, alleging that those agencies failed to establish regulations and otherwise to enforce the provisions of Title VIII of the Civil Rights Act of 1968, which prohibits discrimination in home mortgage lending. The complaint was dismissed with respect to the Federal agency defendants other than the Board after these agencies entered into settlement agreements with the plaintiffs. Defendant's motion for summary judgment for lack of standing was granted, and the case was dismissed on May 3, 1978 (78 F.R.D. 543).

In *Reuss* v. *Balles,* No. 76–1142, (D.D.C., filed June 22, 1976), plaintiff, a member of the U.S. House of Representatives, alleged that the provisions of the Federal Reserve Act governing the appointment of members of the Federal Open Market Committee violate the appointments clause of the Constitution, Article II, Section 2, Clause 2. On December 22, 1976, the court dismissed the complaint for lack of standing (73 F.R.D. 90). Plaintiff appealed from the dismissal of the complaint (No. 77–1012, D.C. Cir.), and, on July 7, 1978, the U.S. Court of Appeals for the District of Columbia affirmed the district court's dismissal. On July 21, 1978, Representative Reuss' petition for rehearing *en banc* was denied by the Court of Appeals. His petition for a writ of certiorari to the U.S. Supreme Court was denied on November 28, 1978 (47 U.S.L.W. 3369).

In *Department of Revenue of the State of Illinois* v. *Olympic Savings and Loan Association,* No. 77–L–8824 (Circuit Court of Cook County, Illinois, filed July 7, 1977), the Board of Governors was named as defendant in a third-party action that challenged the constitutionality of the Federal Internal Revenue Code and the issuance of Federal Reserve notes. On December 8, 1977, the court dismissed the third-party complaint against the Board.

In *Hansen* v. *The National Commission on Observance of Inter-*

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national Women's Year, No. 77–1158 (D. Ida., filed September 21, 1977), plaintiff, a U.S. Congressman, brought suit against the National Commission on Observance of International Women's Year and various Federal officials, including the Chairman of the Board of Governors, to prevent the expenditure of Federal funds in connection with the activities of the Commission. Defendants' motion to dismiss for lack of standing is pending.

In *Consumers Union* v. *Board of Governors,* No. 77–1800 (D.D.C., filed October 17, 1977), plaintiff sought to compel the Board to provide access under the Government in the Sunshine Act to internal memoranda and other materials to be discussed at public meetings of the Board. Access to the memoranda sought by Consumers Union had been granted under the Freedom of Information Act. The parties filed a stipulation of dismissal with prejudice on January 19, 1978.

In *Emch* v. *United States,* No. 77–C–677 (E.D. Wis., filed November 18, 1977), plaintiff, a shareholder of the parent company of the American City Bank & Trust Co., N.A., Milwaukee, Wisconsin, a failed bank, alleged that the Board and other bank regulatory agencies were negligent in supervising and examining the bank. A motion to dismiss is pending.

Two cases were pending in 1978 involving challenges to the Board's employment practices. On June 29, 1977, the complaint in *Hilliard* v. *Burns,* No. 76–1655 (D.D.C., filed December 8, 1976), was dismissed. Plaintiff has filed a notice of appeal from that decision (No. 77–1700, D.C. Cir.), and the case is pending. In *Hadigian* v. *Board of Governors,* No. 76–1694 (D.D.C., filed September 17, 1976), the court granted, on December 6, 1978, the Board's motion for summary judgment. The court held that the Board's action was neither arbitrary nor capricious.

In *Waller* v. *First National Bank of Maryland,* No. 78–0193 (D.D.C., filed February 3, 1978), the petitioner challenged the Board's refusal to help petitioner recover funds that the petitioner alleged had been converted by First National Bank of Maryland, Baltimore, Maryland. The court dismissed the case on August 21, 1978, pursuant to the defendants' motion to dismiss.

In *U.S. League of Savings Associations* v. *Board of Governors,* No. 78–0878 (D.D.C., filed May 16, 1978), the plaintiff challenged the Board's May 1, 1978, decision to amend Regulation Q, effective November 1, 1978, to permit individual bank customers to transfer

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funds automatically from their savings to their checking accounts. The court granted the Board's motion for summary judgment on October 31, 1978. The plaintiff has appealed the decision to the U.S. Court of Appeals for the District of Columbia, where the case is pending.

In *Independent Bankers Association of Texas* v. *First National Bank in Dallas,* No. CA 3–78–0918–F (N.D. Tex., filed July 26, 1978), the plaintiff alleged that the Board and the Federal Reserve Bank of Dallas are unlawfully permitting the collection of share drafts drawn on Federal credit unions. The Federal defendants have moved to dismiss.

In *Beckley* v. *Board of Governors,* No. 78–C–2955 (N.D. Ill., filed July 27, 1978), petitioner challenged the Board's withholding of certain raw data used to compile reports. A stipulation between petitioner and the Board for dismissal of the case is currently pending.

In *Consumers Union of United States, Inc.* v. *Miller,* No. 78–2188 (D.D.C., filed November 21, 1978), the plaintiff seeks declaratory and injunctive relief, alleging that the Board exceeded its authority and acted arbitrarily in amending Regulation Z (see *Federal Register,* volume 42, 1977, page 62146) to provide certain exceptions to the right of rescission for credit secured by a consumer's residence. The case is pending.

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Legislation Enacted

INTERNATIONAL BANKING ACT

Public Law 95–369, the International Banking Act (IBA), approved September 17, 1978, contains the following provisions:

1. Authorizes the Comptroller of the Currency to waive the requirement that all of the directors of a national bank be U.S. citizens.

2. Removes the requirement in the Edge Act—Section 25(a) of the Federal Reserve Act—that all of the directors of an Edge corporation be U.S. citizens. Similarly, the Edge Act is amended to permit one or more foreign banks to own 50 per cent or more of the shares of an Edge corporation with the prior approval of the Board. Previously, the Edge Act required, without exception, that a majority of the shares of an Edge corporation be owned by U.S. citizens.

3. Requires the Board to revise its regulation dealing with Edge corporations within 270 days of enactment of the IBA. In doing so, the Board is required to implement several congressional purposes for Edge corporations including affording Edge corporations powers sufficiently broad to enable them to compete in the United States and abroad with similar foreign-owned institutions. Edge corporations are also to serve as a means of financing international trade, particularly exports. The minimum 10 per cent reserve requirement on the U.S. deposits of Edge corporations is eliminated, and the Board is authorized to impose the same reserve requirements on the corporations as on member banks. The IBA removes the statutory limitation on the issuance by Edge corporations of debentures, bonds, and promissory notes. The Board is required to report to the Congress the effects of these amendments on the capitalization and activities of Edge corporations, banks, and the banking system. This report is printed in the section on Bank and Bank Holding Company Supervision and Regulation by the Federal Reserve System of this ANNUAL REPORT.

4. Authorizes the Comptroller of the Currency to license and supervise one or more Federal branches or agencies of a foreign bank in States that do not prohibit the establishment of branches or agencies by foreign banks.

5. Prohibits a foreign bank from establishing and operating branches outside its "home" State unless the foreign bank enters into

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an agreement or undertaking with the Board that it will receive only such deposits at the out-of-State offices as are permissible for an Edge corporation. Offices of foreign banks that were established, or for which an application had been filed, prior to June 27, 1978, are exempt from this prohibition.

6. Requires Federal deposit insurance for branches of foreign banks that receive deposits of less than $100,000. Requires Federal deposit insurance for Federal branches wherever located and for State branches in States that require deposit insurance for State-chartered banks.

7. Authorizes the Federal banking agencies to examine U.S. offices of foreign banks and in appropriate circumstances to institute cease-and-desist proceedings against them.

8. Imposes reserve requirements and interest rate limitations on Federal branches and agencies of large foreign banks in the same manner and to the same extent as on member banks. The Board is authorized to impose the same requirements and limitations on State branches and State agencies after consultation and in cooperation with State bank supervisory authorities. Subject to the Board's regulations, branches and agencies that maintain reserves would have access to System facilities.

9. Subjects a foreign bank that has a branch, agency, or commercial lending company in the United States to most provisions of the Bank Holding Company Act in the same manner and to the same extent as bank holding companies. Nonbanking activities engaged in or applied for by July 26, 1978, are exempt under a grandfather clause. Otherwise, a foreign bank may not engage directly or indirectly in nonbanking activities in the United States other than those permissible to bank holding companies.

10. Requires that joint studies and reports be undertaken by the President with respect to the McFadden Act; the Secretary of the Treasury with respect to the treatment of U.S. banks abroad; and the Board with respect to Edge corporations becoming members of the Federal Reserve System.

FULL EMPLOYMENT AND BALANCED GROWTH ACT

Public Law 95–523, approved October 27, 1978, has the following provisions, among others:

1. Finds that an effective policy to promote full employment and

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production, increased real income, balanced growth, a balanced Federal budget, adequate productivity growth, proper attention to national priorities, achievement of an improved trade balance, and reasonable price stability should be based on the development of explicit economic goals and policies involving the President, the Congress, and the Board of Governors of the Federal Reserve System, with maximum reliance on the resources and ingenuity of the private sector of the economy.

2. Provides that the Economic Report of the President set forth short-term numerical goals and programs and policies that the President deems necessary to achieve prescribed medium-term goals and a balanced Federal budget, and to achieve reasonable price stability as rapidly as feasible. The medium-term goals in the first three Economic Reports, subject to revision and modification, are to include interim numerical goals for reducing the rate of unemployment to not more than 3 per cent among individuals aged 20 and over, and 4 per cent among individuals aged 16 and over, within a 5-year period, and for reducing the rate of inflation to not more than 3 per cent within the same period. Policies and programs for reducing the rate of inflation, however, are to be designed so as not to impede achievements of the goals and timetables for reduction of unemployment.

3. States that the means of achieving the goals for unemployment and reasonable price stability should be mutually reinforcing to the extent practicable.

4. Provides that the Board of Governors transmit to the Congress, not later than February 20 and July 20 of each year, independent written reviews and analyses of recent developments affecting economic trends, the objectives and the plans of the Board of Governors and the Federal Open Market Committee with respect to the ranges of growth of the monetary and credit aggregates for the calendar year, and the relation of such objectives and plans to the short-term goals set forth in the most recent Economic Report of the President and to any short-term goals approved by the Congress. The July 20 report is also to include a statement of objectives and plans with respect to the ranges of growth of the monetary and credit aggregates for the next calendar year. The Board is to consult with the appropriate committees, which will then submit their views and recommendations with respect to the Board's intended policies.

While nothing in the act requires the Board to fulfill its plans for

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the monetary and credit aggregates set out in its reports if the Board and the Federal Open Market Committee determine that the plans cannot or should not be achieved because of changing conditions, the act does require the Board to explain any revision of that kind in subsequent consultations.

FINANCIAL INSTITUTIONS REGULATORY AND INTEREST RATE CONTROL ACT

On November 10, 1978, the President approved the Financial Institutions Regulatory and Interest Rate Control Act of 1978 (Public Law 95–630).

Title I, Supervisory Authority Over Depository Institutions, effective 120 days after enactment, does the following, among others:

1. Provides for civil penalties for violations of Section 22 (loans to executive officers and transactions with directors) and 23A (loans to affiliates) of the Federal Reserve Act, to be assessed by the Board of Governors or the Comptroller of the Currency; for violations of Section 19 of the Federal Reserve Act (reserve requirements and interest rate ceilings), to be assessed by the Board of Governors; and for violations of the National Bank Act, to be assessed by the Comptroller of the Currency.

2. Amends Section 22 of the Federal Reserve Act to limit loans to executive officers or 10 per cent stockholders or their controlled entities (18 per cent stockholders in towns of less than 30,000 population) to 10 per cent of capital and surplus. Loans to any executive officer, director, or 10 per cent stockholder must be made on substantially the same terms as those prevailing for comparable transactions with others and be without more than normal risk; if the aggregate of such loans to any such person and his controlled entities is more than $25,000, advance approval of a majority of the directors, with the interested party abstaining, is required.

3. Prohibits payment of an overdraft on the account of an executive officer or director.

4. Authorizes the Board to require a holding company to divest a nonbank subsidiary or terminate a nonbank activity if there is reasonable cause to believe that continuation of such activity or control constitutes a serious risk to the financial safety, soundness, or stability of a subsidiary bank.

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5. Provides for civil penalties for violation of the Bank Holding Company Act to be assessed by the Board, and authorizes the Board to issue subpoenas and exercise other procedural authority in connection with hearings or investigations under the Bank Holding Company Act.

6. Provides for cease-and-desist actions directly against directors, officers, employees, agents, or other persons participating in the affairs of a bank and not merely against the bank itself, and against any bank holding company or subsidiary of a bank holding company and against Edge Act and agreement corporations; however, only the Board of Governors may initiate such proceedings against bank holding companies.

7. Authorizes the Federal banking agencies to remove an officer, director, or other person participating in the affairs of a bank in the case of a violation that involves personal dishonesty *or* a willful or continuing disregard for the bank's safety and soundness.

8. Provides for civil penalties for violation of cease-and-desist orders to be assessed by the Federal banking agencies.

9. Amends Section 22(g) of the Federal Reserve Act to double the dollar limitation on loans that may be made to executive officers and thus permits a loan of $60,000 for the purchase of a home; $20,000 to finance the education of children; and $10,000 for any other purpose.

10. Provides a standard for suspension or removal of an officer, director, or other person participating in the affairs of a bank because of his indictment for or conviction of a felony involving dishonesty or breach of trust.

11. Repeals the Bank Holding Company Act exemption for labor, agricultural, or horticultural organizations, but includes a grandfather clause for those in existence on January 4, 1977.

12. Authorizes obligations that are fully guaranteed as to principal and interest by the United States or any of its agencies to be eligible collateral for Federal Reserve notes.

Title II (the Depository Institution Management Interlocks Act), effective 120 days after enactment, has the following provisions, among others:

1. Prohibits interlocks between management officials of nonaffiliated depositor institutions (banks, thrift institutions, industrial banks, and credit unions) or holding companies in the same Standard

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Metropolitan Statistical Area or in the same or contiguous or adjacent city, town, or village, except that in the case of depositary institutions with less than $20 million in assets, the SMSA test does not apply.

2. Prohibits interlocks of this kind between an institution with more than $1 billion in assets and another with more than $500 million in assets without geographic limit.

3. Excludes from coverage as affiliates holding companies and their subsidiaries; corporations with 50 per cent or more common ownership; insured State banks that are engaged primarily in providing banking services for other banks and not the public whose voting securities are held by other banks or officers of banks; and interlocks between mutual savings banks and existing trust companies owned by mutual savings banks.

4. Exempts a number of organizations, including Edge and agreement corporations, a credit union being served by a management official of another credit union, an organization that does no business in the United States except as an incident to its foreign activities, a State-chartered savings and loan guaranty corporation, and a Federal home loan bank or other bank organized specifically to serve depositary institutions.

5. Applies a grandfather clause for a 10-year period to existing interlocks not in violation of Section 8 of the Clayton Act.

6. Divides administrative, enforcement, regulatory, and rulemaking authority among the five Federal supervisory agencies for depositary institutions.

Title III (Foreign Branching), effective 120 days after enactment, does the following, among other things:

1. Provides that State nonmember insured banks must have the written consent of the Federal Deposit Insurance Corporation to establish foreign branches or to invest in foreign banks.

2. Reduces from three to two the number of directors needed to attest to the correctness of reports of condition.

3. Makes it a Federal offense to kill an employee of the Federal financial regulatory agencies (including the Federal Reserve Banks) when he is in pursuit of his official duties.

4. Amends the International Banking Act of 1978 to apply to operations in the United States of foreign banks, branches, and controlled lending companies the Federal and State nondiscrimination laws applicable to national or State banks; and requires that nondis-

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crimination be agreed to in any Federal or State branch or agency application.

Title IV (American Arts Gold Medallions), effective October 1, 1979, directs the Treasury to strike and sell to the general public each year, over a 5-year period, gold medallions containing in the aggregate not less than 1 million troy ounces of fine gold and commemorating outstanding individuals in the American arts.

Title V (Credit Union Restructuring), effective on the effective date of the act, establishes a National Credit Union Administration as an independent agency in the executive branch to be managed by a new three-member National Credit Union Administration Board, appointed by the President for 6-year terms, with the advice and consent of the Senate.

Title VI (Change in Bank Control Act), effective 120 days after enactment, makes the following changes, among others:

1. Provides that no person shall acquire control of any insured bank unless the appropriate Federal banking agency has been given 60 days' prior written notice and does not disapprove within that time period or any authorized extension.

2. Except as otherwise provided by regulation, requires the applicant to furnish the agency with a personal history, information on business background, pending legal or administrative proceedings, criminal indictments or convictions, financial statements, the terms and conditions of the proposed acquisition, the source of funds, and any plans to liquidate, sell, or merge the bank or make major changes in its business or management.

3. Authorizes Federal banking agencies to disapprove on anticompetitive grounds; because the financial condition of the acquiring person might jeopardize the financial stability of the bank; because the competence, experience, or integrity of an acquiring person or proposed management personnel indicates that the acquisition would be contrary to the interest of the bank; or because any acquiring person fails to furnish all information required.

4. Requires an insured bank to report all loans that it makes that are secured by 25 per cent or more of the stock of another insured bank.

5. Requires the acquired bank to report any changes in its chief executive officer or any director during the year following acquisition.

6. Provides for civil penalties for violations.

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Title VII (Change in Savings and Loan Control Act), effective 120 days after the date of enactment, provides that no person shall acquire control of any insured savings and loan association (or any savings and loan holding company) unless the Federal Savings and Loan Insurance Corporation has been given 60 days' prior written notice and does not disapprove of the proposed acquisition within that time period or any authorized extension.

Other provisions, including criteria for disapproval, are virtually identical to those applicable to insured banks under Title VI.

Title VIII (Correspondent Accounts), effective 120 days after the date of enactment, does the following, among other things:

1. Prohibits a correspondent bank from extending credit to an executive officer, director, or 10 per cent stockholder of a respondent bank, or from opening a correspondent account for another bank while it has outstanding an extension of credit to an officer, director, or 10 per cent stockholder of that bank, unless that credit is granted on substantially the same terms as those prevailing for comparable transactions with other persons and does not involve more than normal risks.
2. Establishes the same prohibitions for similar transactions initiated by a respondent bank with respect to correspondent banks.
3. Requires each executive officer or 10 per cent stockholder of record to make a written report to the board of directors of that bank for any year during which he has outstanding an extension of credit from a correspondent bank; such reports are to be compiled and forwarded to the appropriate Federal banking agency.
4. Requires each insured bank to file a report listing by name the executive officers or 10 per cent stockholders of record who file such reports, together with the aggregate amount of all extensions of credit by correspondent banks to such officers, directors, and their controlled entities.
5. Provides for civil penalties for violations.

Title IX (Disclosure of Material Facts), effective 120 days after the date of enactment, among other things, requires an insured bank to file an annual report with the appropriate Federal banking agency listing each executive officer or 10 per cent stockholder of record of the bank and listing the aggregate amount of all extensions of credit by the bank during the preceding calendar year to them, or their controlled entities.

Title X (Federal Financial Institutions Examination Council Act

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of 1978), effective 120 days after enactment, has the following provisions, among others:

1. Establishes a Federal Financial Institutions Examination Council consisting of the Comptroller of the Currency, the Chairman of the Federal Deposit Insurance Corporation, a Governor of the Federal Reserve Board to be designated by the Chairman of the Board, the Chairman of the Federal Home Loan Bank Board, and the Chairman of the National Credit Union Administration.

2. Provides that the Council shall establish uniform principles and standards and report forms for the examination of financial institutions to be applied by the agencies; make recommendations for uniformity on other matters, such as classifying loans subject to country risk, identifying institutions in need of special supervisory attention, and evaluating large loans shared by two or more institutions; make recommendations regarding the adequacy of supervisory tools for determining the impact of holding company operations on subsidiary financial institutions; and consider the ability of supervisory agencies to discover possible fraud or questionable and illegal payments and practices of financial institutions or their holding companies.

3. Provides that when a recommendation of the Council is unacceptable to an agency, the agency shall submit to the Council a written statement of its reasons.

4. Provides that the Council shall conduct schools for examiners to be open to employees of State supervisory agencies.

5. Establishes a liaison committee composed of five representatives of State supervisory agencies to encourage the application of uniform examination principles and standards by State and Federal agencies.

6. Subjects the Council to audit by the General Accounting Office.

Title XI (Right to Financial Privacy Act of 1978), effective 120 days after enactment, except where otherwise provided, does the following:

1. Prohibits a government authority from having access to, information from, or copies of a financial institution's customer records, unless obtained pursuant to written consent of the customer, administrative subpoena or summons, search warrant, judicial subpoena, or formal written request (procedures and requirements for each method of obtaining information are specified in detail).

2. Prohibits financial institutions from providing any government

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authority access to, information from, or copies of any customer's financial records until the government authority certifies in writing that it has complied with the provisions of Title XI.

3. Requires financial institutions promptly to notify all of their customers of their financial privacy rights and provides that the Board of Governors of the Federal Reserve System shall prepare a statement of customers' rights; and provides that any financial institution that provides its customers a statement of customers' rights as prepared by the Board shall be deemed to be in compliance with the customer notice requirement. (On March 7, 1979, this section of the act was repealed.)

4. Exempts from the procedures of Title XI examination by or disclosure to any supervisory agency of financial records or information in the exercise of its supervisory, regulatory, or monetary functions with respect to a financial institution, in accordance with procedures authorized by the Internal Revenue Code, when disclosure is required by Federal statute or regulation, in connection with criminal or civil litigation to which the Government and the customer are parties, and in connection with an official proceeding, investigation, examination, or inspection directed at the financial institution itself.

5. Provides exemptions for the Secret Service or a Government authority authorized to conduct foreign intelligence activities and exempts the Securities and Exchange Commission for 2 years.

6. Effective October 1, 1979, generally requires a government authority to reimburse the financial institution for the cost incurred due to its request, subject to regulations of the Board of Governors establishing the rate and conditions of reimbursement.

7. Provides for civil penalties for violations by a Federal agency or department or a financial institution.

8. Provides that financial institutions making disclosure in good-faith reliance on a certificate of a government agency are not liable to the customer for such disclosure.

9. Establishes certain reporting requirements for the Administrative Office of the U.S. courts and each Government authority requesting financial institution records during the year.

Title XII (Charters for Thrift Institutions), effective 120 days after enactment, does the following, among other things:

1. Authorizes the Federal Home Loan Bank Board to establish rules and regulations for the organization, examination, and opera-

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tion of Federal mutual savings banks (State mutual savings banks that have converted from State charters where conversion is not prohibited by State law).

2. Prohibits conversion from the State mutual to the stock form of ownership.

3. Subjects State mutuals converting to Federal charters to the branching limitations of State law, except as to any numerical limits and except that the Federal Home Loan Bank Board may permit branches in the converted bank's Standard Metropolitan Statistical Area or county, or within 35 miles of its home office, but only in its State of domicile.

4. Provides that the Federal Savings and Loan Insurance Corporation shall insure the accounts of Federal mutual savings banks.

Title XIII (NOW [Negotiable Orders of Withdrawal] Accounts), effective on the date of enactment, adds New York to the States that are authorized to issue NOW accounts.

Title XIV (Insurance of IRA [Individual Retirement Accounts] and Keogh Accounts), effective on the date of enactment, increases Federal deposit insurance for IRA and Keogh accounts to $100,000 per account at insured banks, savings and loan associations, and credit unions.

Title XV (Miscellaneous Provisions), effective upon enactment, has the following provisions:

1. Extends until February 27, 1981, the prohibition on the imposition of surcharges for use of a credit card and restrictions of cash discounts by credit-card issuers.

2. For purposes of the Community Reinvestment Act, permits a financial institution serving predominantly military personnel to define its entire community to include its entire customer base without regard to geographic location.

3. Exempts graduated-payment mortgages insured by the Department of Housing and Urban Development from State requirements for a minimum amortization of principal.

4. Enables the Comptroller of the Currency to charter a national bank whose powers are limited to trust activities.

Title XVI (Interest Rate Control), effective upon the date of enactment, extends the authority to set flexible deposit interest rates (Regulation Q) to December 15, 1980, and eliminates the differential for interest rate ceilings on automatic transfer accounts offered by

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thrift institutions. The maximum rate on such accounts is the commercial bank rate.

Title XVII (Federal Savings and Loan Investment Authority), effective on enactment, amends the investment authority of savings and loan associations in the following ways:

1. Permits investment in community development areas.
2. Increases the authority to invest in loans for property alteration, repair, or improvements.
3. Expands the authority to invest in obligations issued by State or local governments for the purpose of rehabilitation, financing, or construction of residential real property.
4. Places in the unlimited-investment category the authority to invest in or lend to State housing corporations provided that the obligations are secured by real estate insured by the Federal Housing Administration.

Title XVIII (National Credit Union Central Liquidity Facility Act), effective October 1, 1979, does the following, among others:

1. Establishes a Central Liquidity Facility, with voluntary membership, within the National Credit Union Administration. The purpose of the Facility is to improve the general financial stability of credit unions by meeting their liquidity needs, defined to include seasonal, short-term adjustment, and longer-term emergency or unusual credit requirements.
2. Prohibits the Facility from extending credit to expand credit union portfolios.
3. Authorizes the NCUA, acting in the interest of the Facility, to borrow from any source provided that the total value of these obligations not exceed 12 times the subscribed capital stock and surplus of the Facility, from the National Credit Union Share Insurance Fund up to $500,000 to defray initial organizational and operating expenses, and from the Treasury up to $500 million in the event that the NCUA certifies that the Facility does not have sufficient funds to meet the liquidity needs of credit unions.

Title XX (Electronic Fund Transfer Act), which is effective 18 months after enactment (except for the provisions on consumer liability and unsolicited-card distribution, effective 90 days after enactment), has these provisions, among others:

1. Requires disclosure of the terms and conditions of electronic

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funds transfers (defined to exclude, among other things, wire transfers of funds, telephone transfers not pursuant to an agreement, and transfers made pursuant to an automatic transfer service program) at the time the consumer contracts for an electronic funds transfer service.

2. Requires that the consumer be afforded written documentation for each funds transfer made from an electronic terminal, notice as to whether pre-authorized transfers were completed, and a periodic statement of account.

3. Requires financial institutions to establish procedures for correcting errors for electronic funds transfers.

4. Provides limitations on the maximum liability of a consumer for unauthorized transfers from his or her account subject, in part, to whether the consumer reports to the financial institution within prescribed time periods either unauthorized transfers appearing on the periodic account statement, or the loss or theft of an electronic funds transfer card.

5. Imposes liability on the financial institution under certain circumstances for all damages proximately caused by the institution's failure to make an electronic funds transfer or failure to stop payment of a pre-authorized transfer when instructed to do so in accordance with the terms and conditions of the accounts.

6. Permits unsolicited distribution only for unvalidated debit cards.

7. Provides that Title XX does not annul, alter, or affect the laws of any State relating to electronic funds transfers, except to the extent that those laws are inconsistent with Title XX.

8. Authorizes the Board to exempt from coverage electronic funds transfers within any State that imposes requirements "substantially similar" to Title XX.

9. In connection with promulgating regulations to carry out the act, requires the Board to prepare a statement on economic impact, to issue model clauses to facilitate compliance, and, if necessary, to modify its regulations to ease the compliance burden on small financial institutions.

SECURITIES INVESTOR PROTECTION ACT AMENDMENTS

Public Law 95–283, approved May 21, 1978, has the following provisions, among others:

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1. Increases from $50,000 to $100,000 the maximum amount that the Securities Investor Protection Corporation can reimburse customers of insolvent securities firms.

2. Increases the maximum reimbursement from $20,000 to $40,000 for cash in customers' accounts.

3. Increases the maximum amount of securities issues exempt from the registration requirements of the Securities Act of 1933 from $500,000 to $1.5 million.

FEDERAL BANKING AGENCY AUDIT ACT

Public Law 95–320, approved July 21, 1978, has the following provisions, among others:

1. Provides for General Accounting Office audit of the Federal Reserve Board, the Federal Reserve Banks and their branches and facilities, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency.

2. Exempts from General Accounting Office audit of the Federal Reserve transactions conducted on behalf of or with foreign central banks, foreign governments, and nonprivate international financial organizations; deliberations, decisions, and actions on monetary policy matters, including discount window operations, reserves of member banks, securities credit, interest on deposits, and open market operations; transactions made under the direction of the Federal Open Market Committee; and System communications and discussions regarding the foregoing matters.

3. Generally prohibits the General Accounting Office or any of its employees or officers from disclosing information that would identify a specific customer of any bank or bank holding company, or a specific operating bank or bank holding company.

4. Limits General Accounting Office access to bank examination materials in the custody of audited agencies to statistically meaningful samples, as determined by that Office.

5. Provides that, as frequently as practicable, the Comptroller General make reports to the Congress on the results of audit work after an advance copy of the report has been made available to the agency concerned with 30 days for agency comments.

6. Imposes criminal penalties on General Accounting Office per-

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sonnel for disclosure of specified confidential material from examination reports.

DEBT CEILING INCREASE

Public Law 95–333, approved August 3, 1978, increases the temporary debt limit to $798 billion through March 31, 1979. An earlier authorization (Public Law 95–252) had extended the temporary debt limit of $752 billion from March 31, 1978, to July 31, 1978. Public Law 95–333 also increases from $27 billion to $32 billion the amount of long-term U.S. Government bonds that may be issued with interest rates above the 4.25 per cent statutory ceiling.

NEW YORK CITY LOAN GUARANTEES

Public Law 95–339, approved August 8, 1978, has the following provisions, among others:

1. Authorizes the Secretary of the Treasury to guarantee New York City obligations with an aggregate principal amount outstanding not to exceed $1.65 billion at any one time, in accordance with a specified time schedule and conditions and limitations, including a determination by the Secretary that there is a reasonable prospect of repayment, that credit is effectively unavailable to the city elsewhere, and that the interest rate is reasonable.
2. Specifies independent auditing procedures to precede and follow extension of guarantees.
3. Specifies that the city shall offer to sell its term notes in 1980, 1981, and 1982 and its long-term bonds in 1981 and 1982, unless the Secretary determines that any such offer would be inconsistent with the financial interests of the city.
4. Requires the city to establish a Productivity Council to develop means to enhance the productivity of city employees.
5. Provides that interest on guaranteed obligations be taxable.

The authority to guarantee new obligations terminates on June 30, 1982.

Public Law 95–415, approved October 5, 1978, authorizes the Secretary of the Treasury to guarantee the payment of princi-

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pal and interest on loans in accordance with the provisions of the New York City Loan Guarantee Act of 1978 in amounts not to exceed $1.65 billion in principal outstanding at any time, and appropriates, effective October 1, 1978, amounts necessary for payment of principal and interest on loans in default and guaranteed pursuant to the Guarantee Act, to remain available until September 30, 1998.

NATIONAL CONSUMER COOPERATIVE BANK

Public Law 95–351, approved August 20, 1978, among other things, provides the following:

1. Establishes a National Consumer Cooperative Bank, to be privately owned after a period of joint Federal and private ownership, to provide credit and technical assistance to consumer cooperatives.
2. Establishes within the Bank an Office of Self-Help Development and Technical Assistance authorized to make capital investment advances to cooperatives serving low-income persons.
3. Authorizes the Secretary of the Treasury, over the first 5 years, to purchase up to $300 million of stock of the Bank to be retired as soon as practicable.

FUTURES TRADING ACT

Public Law 95–405, approved September 30, 1978, amends the Commodity Exchange Act to require the Commodity Futures Trading Commission to do the following, among other things:

1. Keep the Treasury, the Board of Governors of the Federal Reserve System, and the Securities and Exchange Commission fully informed of Commission activities relating to the responsibilities of those agencies, in order to seek their views on such activities, and to consider the relationships between the volume and nature of investment and trading in commodity futures and in securities and financial instruments under the jurisdiction of those agencies.
2. Deliver to the Treasury and the Board of Governors a copy of any application by a Board of Trade to be designated as a contract market involving transactions for future delivery of any security issued or guaranteed by the United States or any of its agencies with

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a 45-day opportunity for comment; to consider all comments it receives from the Treasury and the Board of Governors; and consider the effect that any such designation, suspension, revocation, or emergency action may have on the debt financing requirements of the U.S. Government and the continued efficiency and integrity of the underlying market for government securities.

BRETTON WOODS AGREEMENTS ACT AMENDMENTS

Public Law 95-435, approved October 10, 1978, has three provisions of special interest:

1. Authorizes the appropriation of an amount of dollars equivalent to 1.45 billion Special Drawing Rights for the participation of the United States in the Supplementary Financing Facility (the "Witteveen Facility") of the International Monetary Fund.
2. Provides that the Secretary of the Treasury shall instruct the U.S. Executive Director of the International Monetary Fund to seek to assure that no decision on the use of the facility undermines or departs from U.S. policy regarding comparability of treatment of public and private creditors in cases of debt rescheduling in which official U.S. credits are involved.
3. Provides that the budget of the Federal Government shall be balanced beginning with fiscal year 1981.

SUSAN B. ANTHONY DOLLAR COIN ACT

Public Law 95-447, approved October 10, 1978, among other things provides for the issuance of a new $1 coin, bearing on one side the likeness of Susan B. Anthony, and on the other a design of the symbolic eagle of the Apollo 11 landing on the moon; and modifies the size and weight specifications for $1 coins so that the new coins will be smaller and lighter than those previously minted.

ETHICS IN GOVERNMENT ACT

Public Law 95-521, approved October 26, 1978, among other things, provides for annual financial disclosure statements that will be avail-

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able to the public by members of the Congress, the President, the Vice President, and high-level officials of the legislative, executive, and judicial branches of the Federal Government; establishment of an Office of Government Ethics within the Office of Personnel Management; and limitations on the activities of officers and employees after they leave the Federal Government.

RENEWAL OF FEDERAL RESERVE BANKS' DIRECT PURCHASE AUTHORITY

Public Law 95–534, approved October 27, 1978, amends Section 14(b) of the Federal Reserve Act to renew through May 1, 1979, the authority of Federal Reserve Banks to purchase U.S. obligations directly from the Treasury. The previous authority had expired on April 30, 1978.

HOUSING AND COMMUNITY DEVELOPMENT AMENDMENTS

Public Law 95–557, approved October 31, 1978, amends and extends certain Federal laws relating to housing, and community development and preservation. Title III has the following provisions, among others:

1. Authorizes direct sales and servicing access to the Federal Home Loan Mortgage Corporation by mortgage bankers.

2. Authorizes the Federal Housing Administration to insure, under Section 203(k) of the National Housing Act, mortgages to purchase and rehabilitate one- to four-family structures, which could then be purchased by the Government National Mortgage Association.

3. Authorizes the FHA to insure mortgages on one-family condominium units in existing non-FHA-insured multifamily projects containing 12 or more units.

4. Reduces paperwork by consolidating and simplifying mortgage forms of the Department of Housing and Urban Development and the Veterans Administration.

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5. Establishes a procedure for legislative review of proposed rules and regulations of HUD.

Title VI has the following provisions, among others:

1. States the finding by the Congress that the neighborhood housing service of the Urban Reinvestment Task Force is a successful program to revitalize older urban neighborhoods by mobilizing public, private, and community resources at the neighborhood level. The demand for neighborhood housing services programs in cities throughout the United States warrants the creation of a public corporation to institutionalize and expand that program.

2. Establishes the National Neighborhood Reinvestment Corporation to continue the efforts of the Federal financial supervisory agencies and the Department of Housing and Urban Development to promote reinvestment in older neighborhoods by local financial institutions cooperating with community people and local government. The board of directors of the corporation consists of the Chairman of the Federal Home Loan Bank Board, as chairman of the board of directors for the first 2 years, the Secretary of Housing and Urban Development, a member of the Board of Governors of the Federal Reserve System to be designated by the Chairman of that Board, the Chairman of the Federal Deposit Insurance Corporation, the Comptroller of the Currency, and the Administrator of the National Credit Union Administration.

3. Sets out the duties of the corporation to include (a) establishing neighborhood housing services and providing them with grants and technical assistance; (b) identifying, monitoring, evaluating, and providing grants and technical assistance to selected neighborhood preservation projects that promise to reverse neighborhood decline; (c) experimentally replicating successful neighborhood preservation projects; and (d) supporting Neighborhood Housing Services of America with technical assistance and grants to expand its national loan purchase pool. An appropriation to the corporation not to exceed $12.5 million is authorized for fiscal year 1979.

REVENUE ACT

Public Law 95–600, approved November 6, 1978, includes the following:

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1. Liberalizes personal income tax provisions.

2. Provides for a five-step schedule for corporate tax rates with a maximum tax rate of 46 per cent and makes the investment tax credit of 10 per cent permanent.

3. Reduces the effective rate on individual capital gains.

4. States the intention of the tax-writing committees of the Congress to report legislation providing significant tax reductions for individuals when certain goals for Federal expenditures are met and when justified in the light of prevailing and expected economic conditions over the next 4 years.

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Bank and Bank Holding Company Supervision and Regulation by the Federal Reserve System

DOMESTIC ACTIVITIES AND APPLICATIONS

Bank Holding Companies

The System meets its supervisory and regulatory responsibilities with regard to bank holding companies through two primary functions:

1. Monitoring the operations and performance of bank holding companies, mainly by "on-site" inspections and evaluations of reports and other information obtained from such companies.
2. Action on applications to form or expand bank holding companies.

The Board of Governors' Division of Banking Supervision and Regulation is organized along functional lines in order to provide effective staff monitoring of financial institutions and efficient processing of applications. Individual responsibilities within the Division are sharply defined with regard to bank holding company, bank merger, and international applications; surveillance; trust activities; legally oriented activities; research and policy matters; regulatory compliance; and supervision of financial institutions.

A new standardized Report of Bank Holding Company Inspection, which became effective on January 1, 1978, has intensified the supervision of bank holding companies. As a result, approximately 85 per cent of all bank holding company assets will be subject to Federal Reserve review each year. The report is to be used in conjunction with the annual inspection of (1) bank holding companies with consolidated assets of more than $300 million; (2) bank holding companies with consolidated assets of less than $300 million that control significant credit-extending nonbank subsidiaries; and (3) any other bank holding company at the discretion of a Federal Reserve Bank.

Most bank holding companies that are exempt under the new inspection procedures will continue to be subject to inspection at least

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once every 3 years. For these holding companies, all of which will have less than $300 million in consolidated assets and no significant credit-extending nonbank subsidiaries, a new standardized report has been developed and will be implemented in early 1979. To aid in on-site inspections and report preparation, a System task force is drafting a new manual for inspections of bank holding companies, which is expected to be completed during 1979.

For the calendar year 1977, annual reports were obtained from all registered bank holding companies, pursuant to the provision of Section 5(c) of the Bank Holding Company Act. At the end of 1978, 2,222 bank holding companies were in operation.

Each action by the Board on an application to form a bank holding company or to expand an existing company through acquisition of a bank or an existing nonbank company is effected by an order. Orders set forth the action taken, the voting record of the Board members participating, the essential facts, and the basis for the action.

Whether issued by the Board or by Reserve Banks acting under delegated authority, orders are released immediately to the public and press. Copies are available from the Board's offices, and the System's actions are reported in Board publications, including the *Federal Reserve Bulletin* and the weekly H.2 statistical release. The numbers of proposals acted on during 1978 by the Board, and under delegated authority by the Secretary's Office and the Federal Reserve Banks, are shown in the accompanying table.

Although the number of applications processed in 1978 increased by 12 per cent over 1977, the System again processed more than

Section	Direct action		Delegated authority			Total
	Board		Secretary's Office	Reserve Banks		
	Approved	Denied	Approved	Approved	Permitted	
3(a)(1)	68	14	41	150	0	273
3(a)(3)	77	6	13	57	0	153
3(a)(5)	4	0	0	0	0	4
4(c)(8)	58	4	3	28	494	587
4(c)(12)	2	0	0	0	28	30
Total	209	24	57	235	522	1,047

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90 per cent within 90 days of the filing of a legally and informationally sufficient application, as the table below indicates. This standard, it should be noted, is self-imposed and is considerably more difficult to meet than the period referred to in the Bank Holding Company Act of 1956 as amended.

Item	1977					1978				
	Q1	Q2	Q3	Q4	Year	Q1	Q2	Q3	Q4	Year
Number processed......	205	226	241	259	931	269	257	270	251	1,047
Per cent processed within 90 days........	84	89	90	94	90	90	90	95	94	92

Late in the year the Federal financial regulatory agencies adopted regulations implementing the Community Reinvestment Act. This statute provides that an agency, in acting upon an expansion proposal involving depositary financial institutions, must consider an applicant's record in meeting the credit needs of its community. Beginning November 6, 1978, all applications to acquire a bank had to disccuss the applicant's performance in this respect.

On December 28, 1978, the Board issued a policy statement concerning grandfather rights that expire on December 31, 1980. This statement built on earlier ones dated February 15, 1977, which provided general divestiture guidelines, and October 13, 1977, which established a voluntary filing date of June 30, 1978, for those facing the December 31, 1980, deadline.

The Board established September 30, 1979, as the date by which affected bank holding companies should have filed either retention applications or divestiture plans with their respective Reserve Banks. The Board pointed out that the failure to do so could lead to forced sales and that there were a number of possible obstacles that could delay expeditious processing of applications, especially those filed in a tardy manner.

Of particular concern to the Board was the number of bank holding companies and subsidiaries that remain to comply fully with the December 31, 1980, deadline and the insubstantial progress made

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to date. As the table shows, several hundred filings have yet to be made, and only 2 years remain for all requisite clearances to be obtained.

Date	Number of bank holding companies	Number of bank holding company subsidiaries [1]			
		Total	Permissible [2]	Impermissible [2]	General insurance agencies [3]
October 1977	353	497	175	171	151
December 1978	313	404	136	123	145

[1] This includes parent companies engaging directly in nonbanking activities.
[2] This is based on preliminary review.
[3] The Board has yet to determine the permissibility of operating a general insurance agency in a town of less than 5,000 population.

Member Banks

Each State member bank is subject to examination, made by direction of the Board of Governors or of the Federal Reserve Bank of the district in which it is located, by examiners selected or approved by the Board. The general policy is for the Bank to conduct at least one regular examination of each State member bank in its district during each calendar year and to prepare a complete examination report. However, banks that clearly exhibit no major unsatisfactory features in operations and financial condition, and that have been operated prudently over time, may receive an examination of limited scope in 1 year, with a brief report, and a full examination the following year. Banks with severe problems are examined fully at least once in each calendar year and more often when necessary. In some States concurrent examinations are made in cooperation with the State banking authorities; in others, the examinations are independent.[1] All but 27 of the 1,015 State member banks subject to examination during 1978 were examined.

The Board makes its reports of examination of State member

[1] In the Federal Reserve District of Chicago, one examiner is assigned to accompany a full contingent of State examiners at each annual examination of State member banks in that portion of Indiana located in the Chicago Reserve District. The State examination report of these banks is accepted in lieu of a Federal Reserve report.

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banks available to the Comptroller and to the Federal Deposit Insurance Corporation (FDIC). Also, upon request, the FDIC provides its reports of insured nonmember State banks to the Board.

In its supervision of State member banks, the Board analyzes reports of examination of State member banks and coordinates and evaluates the examination and supervisory functions of the System. Similar oversight is exercised with respect to bank holding companies, for which the Board has sole supervisory responsibility.

National banks, all of which are members of the Federal Reserve System, are subject to examination by direction of the Board or of the Federal Reserve Banks. As a matter of practice, they are not examined by either because the law charges the Comptroller of the Currency directly with that responsibility. The Comptroller provides reports of examination of national banks to the Board upon request, and each Federal Reserve Bank purchases from the Comptroller copies of those reports.

The Board passes on applications for admission of State banks to membership in the System; administers the public-disclosure requirements of the Securities Exchange Act of 1934, as amended, with respect to equity securities of State member banks within its jurisdiction under the 1934 act, and regulates certain security credit transactions; and under provisions of the Federal Reserve Act and other statutes, passes on applications of member banks for permission to (1) merge banks, (2) establish domestic and foreign branches, (3) exercise expanded powers to create bank acceptances, (4) establish foreign banking and financing corporations, and (5) invest in bank premises an amount in excess of 100 per cent of the bank's capital stock.

By Public Law 88–593, approved September 12, 1964, insured banks must inform the appropriate Federal banking agency of any changes in control of management, and of any loans by them secured by 25 per cent or more of the voting stock of any insured bank. In 1978, 10 changes in ownership of the outstanding voting stock of State member banks were reported to the Federal Reserve Banks as changes in control. Arrangements continue among the three Federal supervisory agencies for appropriate exchanges of reports received pursuant to the act. The Reserve Banks send copies of all reports received to the appropriate district office of the FDIC, the Regional

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Administrator of National Banks (Comptroller of the Currency), and the State bank supervisor.

The Reserve Banks are under instructions to forward promptly to the Board reports involving changes in control of State member banks, with a statement (1) that the new owner and management are known and acceptable to the Reserve Bank, or (2) if they are not known, that an investigation is being made; its findings, and the conclusions of the Reserve Bank, are to be forwarded to the Board.

By Public Law 90–44, approved July 3, 1967, each member bank of the Federal Reserve System must include with each report of condition a list of all loans to its executive officers since its previous report. Data submitted by member banks during 1978 appear, as required by law, below.

Period covered (condition report dates)	Total loans to executive officers		Range of interest rates charged (per cent)
	Number	Amount (dollars)	
July 1, 1977–Sept. 30, 1977	7,322	30,120,828	1–18
Oct. 1, 1977–Dec. 31, 1977	8,138	34,967,924	1–19
Jan. 1, 1978–Mar. 31, 1978	8,030	32,383,601	1–18
Apr. 1, 1978–June 30, 1978	8,038	34,198,118	1–18
July 1, 1978–Sept. 30, 1978	7,866	32,884,172	1–23
Oct. 1, 1978–Dec. 31, 1978	[1]	[1]	[1]

[1] Compilation of data for condition reports of December 31, 1978, has not been completed.

Federal Reserve Membership

As of December 31, 1978, member banks accounted for 38 per cent of the number of all commercial banks in the United States and for 58 per cent of all commercial banking offices, and they held approximately 72 per cent of the total deposits in such banks—almost the same percentages as at the end of 1977. State member banks accounted for 11 per cent of the number of all State commercial banks in the United States and for 27 per cent of the banking offices, and they held approximately 39 per cent of total deposits in State commercial banks.

Of the 5,564 banks that were members of the Federal Reserve System at the end of 1978, there were 4,564 national banks and 1,000 State banks. During the year there were net declines of 91

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national and 14 State member banks. The decline in State member banks was offset in part by the organization of 37 new national banks and by the conversion of 3 nonmember banks to national banks. The decrease in State member banks reflected mainly 37 withdrawals from membership and 13 conversions to branches incident to mergers and absorptions.

At the end of 1978, member banks were operating 22,830 branches, facilities, and additional offices, 643 more than at the close of 1977. During the year member banks established 1,044 *de novo* branches.

Detailed figures on changes in the banking structure during 1978 are shown in Table 19 in the Statistical Tables section of this REPORT.

Bank Mergers

Under Section 18(c) of the Federal Deposit Insurance Act, 12 U.S.C. 1828(c), the prior written consent of the Board of Governors must be obtained before a bank may merge, consolidate, or acquire the assets and assume the liabilities of another bank if the resulting bank is to be a State member bank.

In deciding whether to approve an application, the Board is required by Section 18(c) to consider the impact of the proposed transaction on competition, the financial and managerial resources and prospects of the existing and proposed institutions, and the convenience and needs of the community to be served. The Board is precluded from approving "any proposed merger transaction which would result in a monopoly, or which would be in furtherance of any combination or conspiracy to monopolize or to attempt to monopolize the business of banking in any part of the United States." A proposed transaction "whose effect in any section of the country may be substantially to lessen competition, or to tend to create a monopoly, or which in any other manner would be in restraint of trade" may be approved only if the Board is able to find that the anticompetitive effects of the transaction would be clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served.

Before acting on each application the Board must request reports from the Attorney General, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation on the competitive factors

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involved in each transaction. The Board in turn responds to requests by the Comptroller or the FDIC for reports on competitive factors involved when the resulting bank is to be a national bank or an insured nonmember State bank.

During 1978 the Board approved 3 merger applications and submitted 84 reports on competitive factors to the Comptroller of the Currency and 78 to the FDIC. In addition, the Federal Reserve Banks approved 19 merger applications on behalf of the Board pursuant to delegated authority. As required by Section 18(c), a description of each of the 22 applications approved by the Board or the Reserve Banks, with other pertinent information, is shown in Table 21.

Orders of the Board with respect to all bank merger applications, whether approved or disapproved, are released immediately to the press and the public. These orders set forth the factors considered, the conclusions reached, and the vote of each member of the Board present.

Miscellaneous Actions under Delegated Authority

In addition to delegating action on certain applications concerning bank holding companies and bank mergers, the Board of Governors has delegated to the Reserve Banks, along with other things, authority to approve, on behalf of the Board, certain applications of State member banks to establish domestic branches, to invest in bank premises, and to grant or deny a waiver of 6 months' notice by a bank of its intention to withdraw from membership in the Federal Reserve System.

The Board has also delegated authority to the Director of the Division of Banking Supervision and Regulation for, among other things, furnishing to the Comptroller of the Currency and the Federal Deposit Insurance Corporation certain reports on competitive factors under Section 18(c)(4) of the Federal Deposit Insurance Act, 12 U.S.C. 1828(c)(4). The Director may furnish the reports if each of the appropriate departments or divisions of the Federal Reserve Bank and the Board believe that the competitive effects of the proposed merger would be at worst only slightly adverse, and if no member of the Board has objected prior to the forwarding of the

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report. Under this authority 151 reports on competitive factors were furnished.

INTERNATIONAL ACTIVITIES AND APPLICATIONS

Foreign Activities of Member Banks

Under provisions of the Federal Reserve Act (Section 25 for national banks and Sections 9 and 25 for State member banks) and Regulation M, member banks may establish branches or subsidiaries in foreign countries and invest in foreign banks, usually subject to prior Board approval. In reviewing proposed transactions, the Board considers regulatory limitations, the condition of the bank, and the bank's existing foreign operations. In 1978 the Board approved 74 applications for the establishment of branches in foreign countries and 27 applications by member banks for investments in banks in various countries.

At the end of 1978, member banks had in active operation 761 branches in foreign countries and overseas areas of the United States: 105 national banks were operating 649 of these branches, and 32 State member banks were operating 112 branches. The growth in the number and total assets of foreign branches is shown in the table below.

Year	Number		Total assets (billions of dollars)	
	Foreign branches	Sections 25 and 25(a) corporations	Foreign branches [1]	Sections 25 and 25(a) corporations
1971	577	85	55.1	5.5
1972	627	92	72.1	6.1
1973	699	103	108.8	6.9
1974	732	117	127.3	10.1
1975	762	116	145.3	9.1
1976	731 [2]	117	174.5	11.1
1977	738	122	205.0	13.4
1978	761	124	270.0 [e]	15.5 [e]

[e] Estimated.

[1] These data are derived from reports of condition that were filed at the end of the year with the Comptroller of the Currency and the Federal Reserve System, and they differ in certain respects from other statistical reports on overseas branch operations. The amounts shown are net of claims on other foreign branches of the same bank.

[2] This decrease from 1975 is due primarily to the conversion of 30 branches in Colombia into subsidiaries to conform with Colombian banking laws.

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International Financial Corporations

Under provisions of Sections 25 and 25(a) of the Federal Reserve Act and Regulation K, corporations ("Edge Act" or "agreement" corporations) may be established to engage in international banking or foreign financial transactions. These corporations are generally of three types: banking corporations that are owned by large banks and located in U.S. commercial centers other than the location of their parent banks, and that engage in international banking; investment companies owned by banks of large or medium size that invest in foreign financial institutions, such as consumer or mortgage finance corporations or leasing companies; and corporations that invest in foreign commercial banking institutions.

In 1978 the Board acted on 164 applications, in accordance with Sections 25 and 25(a) of the Federal Reserve Act, and with Section 4(c)(13) of the Bank Holding Company Act, which included requests for investments in such activities as commercial banking in Egypt, Nigeria, Malaysia, and Australia; equipment leasing in Korea, Brazil, and Belgium; investment banking in the Philippines, France, England, and Korea; and consumer finance in Japan and Chile. At the end of 1978, 124 of these corporations were in existence, and during that year all but one were examined by examiners for the Board.

Under the provisions of Section 25(a) of the Federal Reserve Act, the Board issued two final permits during 1978 for corporations to engage in international or foreign financial operations. In addition, the Articles of Association were approved and preliminary permits were issued for the formation of two other corporations.

Growth in the number of Section 25 and 25(a) corporations is given in the table on the previous page.

Timely Processing of Applications

As in the domestic area, the System measures its performance in the timely processing of international applications against a 90-day standard. In 1978 the number of international applications processed increased from 233 to 287, or 23 per cent. Nine out of ten of the applications were processed within 90 days in 1977, compared with 86 per cent in 1978, as the following tabulation shows.

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Year	Q1		Q2		Q3		Q4		Year	
	Number	Per cent	Number	Per cent	Number	Per cent	Number	Per cent	Number	Per cent
1977	36	81	76	92	57	100	64	84	233	90
1978	47	89	67	82	75	84	98	89	287	86

Capitalization and Activities of Edge Corporations, Banks, and the Banking System

The International Banking Act of 1978 (IBA) (Public Law 95–369), amended the Edge Act—Section 25(a) of the Federal Reserve Act—in several respects. One amendment removed the provision in the Edge Act that limited an Edge corporation's liabilities on account of debentures, bonds, and promissory notes to ten times the corporation's capital and surplus. Another removed the statutory minimum 10 per cent reserve requirement on the U.S. deposits of an Edge corporation. Section 3(h) of the IBA requires the Board, as part of its ANNUAL REPORT, to assess the effects of these amendments on the capitalization and activities of Edge corporations, banks, and the banking system.

The Board of Governors has amended its regulation governing Edge corporations to conform to the elimination of the statutory minimum reserve requirement. In addition, the Board has conducted a general review of its regulation and, as required by the IBA, has issued for comment proposed amendments to the regulation. Amendments to the regulation will become effective in mid-1979. Particular attention has been given to the regulatory requirement that an Edge corporation's aggregate liabilities (including liabilities on account of debentures, bonds, and promissory notes) be limited to ten times the corporation's capital and surplus.

Because the IBA only recently became effective and requires further Board action for its implementation, it is not possible to assess at this time its effects on Edge corporations, banks, or the banking system. Information available to the Board during the coming year should permit an assessment in the next ANNUAL REPORT of the Board.

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SCHOOLS

In 1978 the Bank Examination School of the Board of Governors conducted two sessions of the School for Examiners, three sessions of the School for Assistant Examiners, one session of the School for Trust Examiners, two sessions of the Bank Holding Company School, and one session of the International School. A Senior Trust Seminar was held in 1978 jointly with the Comptroller of the Currency and the Federal Deposit Insurance Corporation.

Since the establishment of this program, 6,220 persons have attended the various sessions, including representatives of the Federal bank supervisory agencies; the State Banking Departments of 36 States; the Treasury Department of the Commonwealth of Puerto Rico; the Division of Banking and Insurance, the Virgin Islands; and 29 foreign countries.

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Condition of the Banking System

Throughout 1978 the American banking system continued to make a good recovery from the problems that it encountered during the 1974–75 recession. Seven banks failed during the year, fewer then half the 1975–76 average, and the number of problem banks continued to decline. The continuation of the economic expansion that began in 1975 made a major contribution to this improvement by its favorable impact on the financial condition of many borrowers and the consequent reduction in problem loans of most banks.

At the end of 1978 the banking system was in good condition. Nevertheless, as banks entered 1979 they faced significant challenges. These included a likely slowdown in the economy, particularly in housing, a high rate of inflation with its consequent distortions, an intensified competitive environment, and a need to arrest the decline in bank capital ratios and bank liquidity.

TRENDS IN INDEXES OF BANK SOUNDNESS

Appraisals of the condition of the banking system are typically based on an analysis of trends in the major indexes of bank soundness: asset quality, capital, liquidity, and earnings.

Asset Quality

Between 1973 and 1976 the classified assets of member banks almost quadrupled, rising from $9 billion to $35 billion.[1] During 1977, however, asset quality improved, and classified assets declined more than 11 per cent to $31 billion. Moreover, the amount of assets classified as "doubtful" and "loss"—the two most serious classifications—fell about 20 per cent. This trend continued in 1978. For example, at midyear nonperforming assets were 12.2 per cent below their level at the end of 1977, according to a recent analysis of the nonperforming assets of slightly more than 100 large banking organizations. The ratio of such assets to loans was down to 2.6 per cent at midyear 1978, compared with 3.2 per cent,

[1] Classified assets are loans or securities that have been identified by bank examiners as having significant potential for loss.

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4.5 per cent, and 4.3 per cent at the end of 1977, 1976, and 1975, respectively.

Real estate loans, particularly construction loans and loans to real estate investment trusts, remain the major problem in bank loan portfolios. Most of these problem loans were made during the real estate boom of the early 1970's, when far more projects were undertaken than the market could digest. In the last several years real estate markets have improved significantly, as has the financial condition of many real estate borrowers. As a result, some problem loans have been repaid, and banks have been able to liquidate at more favorable prices property acquired in foreclosure.

Capital

In the several decades ending in 1975, bank capital ratios had declined almost steadily, a trend that had accelerated as a consequence of the rapid bank growth of the early 1970's. With the marked slowing of bank growth during 1975–76, capital ratios improved significantly. In 1977 and 1978, however, capital ratios resumed their secular decline as a result of relatively rapid asset growth—on average, about 13 per cent per year. In June 1978 the aggregate ratio of equity capital to total assets for banks stood at 5.96 per cent, compared with 6.11 per cent at the end of 1976.

In recent years banks have been building up their equity capital at a fairly steady annual rate of about 10 per cent. They have relied principally on retained earnings for these additions to capital and are now retaining about two-thirds of their earnings. Because prices of bank stocks have been depressed since 1974, banks have largely avoided new equity issues. At present, the stock prices of most of the major banking organizations are hovering between five and seven times earnings, and many stocks are selling below book value. Discussions with banks and investment bankers indicate, however, that many banking organizations desire to come in to the equity market whenever bank stock prices improve.

Liquidity

After having run their liquidity down sharply during the rapid growth of the early 1970's, banks considerably restored their liquidity positions during 1975–76. The decline was resumed in 1977, how-

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ever, and accelerated last year. For example, between mid-1977 and mid-1978 bank holdings of U.S. Treasury and agency securities with a maturity of less than 1 year fell from $45 billion to $36 billion. Meanwhile, on the other side of the balance sheet, volatile liabilities of banks increased sharply. Time deposits exceeding $100,000 rose from $136 billion to $180 billion, and Federal funds purchased rose from $76 billion to $90 billion.

Earnings

During the last 2 years, bank earnings have been unusually strong. In 1977 earnings of insured banks rose more than 13 per cent. Moreover, current estimates suggest that earnings for 1978 were approximately 25 per cent ahead of 1977, which would be the largest gain in several decades.

A primary reason for the unusually strong earnings performance in 1978 was the rapid growth of bank assets and loans, which were up an estimated 14 per cent and 16 per cent, respectively. A second factor was a slight improvement in net interest margins because of a rise in the general level of interest rates, fewer nonaccruing loans, and a shift in portfolios toward higher-yielding assets.[2] The improvement in net interest margins in 1978 was greater at the large regional banks than at the money center banks. It is worth noting that loan-loss provisions did not have a positive effect on bank earnings in 1978 as they did in 1977. Actually, responding to rapid loan growth, banks began to increase their loan-loss provisions in 1978 (even though charge-offs were still declining) in order to maintain their ratios of valuation reserves to loans.

INTERNATIONAL ACTIVITIES

While data for the end of 1978 are not yet available, the growth in foreign assets held by U.S. banks in 1978 apparently was below the 17 per cent growth rate in 1977 and an even higher rate of growth in the previous year. Factors contributing to the slower rate were an increase in loan demand in the United States and declining spreads on Euro-currency credits.

In spite of slower asset growth and lower spreads on some new

[2] A bank's net interest margin is equal to the difference between the interest earned and the interest paid by the bank divided by the bank's average earning assets.

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business, international earnings in 1978 appear to have remained strong, and international earnings continue to account for a substantial part of the total earnings of the largest U.S. banks. Loan-loss experience on international credits also remained good.

Most foreign countries in which U.S. banks make loans improved their economic performance and balance of payments in 1978. However, several of these countries continued to experience serious economic and financial problems and to have difficulty servicing their external debt promptly. In the past, actual default by countries on external debt has been rare. Assuming a continuation of past trends, the risk to banks from the failure of countries to service their external borrowings on schedule would be a temporary reduction in liquidity and lower income rather than loan charge-offs.

SUPERVISORY IMPROVEMENTS

During 1978 the Federal Reserve took new steps and continued past initiatives to improve its policies and procedures for supervising State member banks and bank holding companies. Some of these changes resulted from problems that had become evident in recent years. Others represented efforts to anticipate banking problems and to enable the Federal Reserve to respond quickly as circumstances change. Two key underlying objectives have been to enhance the effectiveness and efficiency of the supervisory process and, in cooperation with other Federal banking agencies and the Interagency Coordinating Committee, to ensure uniform treatment of significant banking practices.

Last year the Federal Reserve and the other banking agencies developed a new examination system for dealing with country risks in international lending by banks. Under this system, to be implemented in 1979, concentrations of credit that might have a significant impact on a bank's condition in the event of problems in a particular country will get special attention. The year also saw a continuation of efforts to increase cooperation among central banks and the regulatory authorities of the major countries.

During 1978 the Federal Reserve put into practice an expanded program for inspecting bank holding companies. The program calls for a standardized report form for use in examining, on an annual basis, most holding companies with consolidated assets in excess of $300 million. This initiative has served to focus attention on nonbank assets, holding company debt, and the financial condition of the con-

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solidated corporation. To further enhance the supervision of holding companies, a framework is being developed for evaluating and rating the performance and financial condition of bank holding companies. In conjunction with the inspection program, the rating system will ensure that institutions are reviewed on a timely basis and that supervisory resources are directed to those companies most in need of supervisory attention.

In the interests of uniformity in the supervision of commercial banks, the Federal Reserve and the other two Federal banking agencies have adopted a new uniform bank-rating system. The system will expand the number of financial factors considered in rating banks, set forth the principal relationships that must be analyzed, and identify more precisely those banks with significant operating or financial difficulties. The Federal regulatory agencies have also adopted uniform systems and procedures for evaluating trust departments and electronic data-processing centers and for appraising the audit and control functions of commercial banks.

The Federal Reserve reinforced these strengthened supervisory programs during 1978 with continued emphasis upon examiner training. In addition, the Federal Reserve has continued to treat examiners as specialists in fields such as consumer compliance and international banking. Moreover, significant resources have been allocated to the development of examination procedures and staffs to ensure compliance with the Community Reinvestment Act. In addition, a standardized report form for use in examining Edge corporations has been developed as a means for ascertaining the impact of the international operations of Edge subsidiaries on the parent bank. Finally, the Federal Reserve has maintained its efforts to improve surveillance and data collection, and to reduce the reporting burden by streamlining the process.

CONCLUSION

The financial condition of the banking system has improved significantly in the last several years, and the system was in good condition at year-end 1978. During 1978 the quality of bank portfolios continued to improve and banks experienced their fastest earnings growth in many years, although bank capital ratios and bank liquidity declined.

At the end of 1978 it appeared likely that banks would have to

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operate in 1979 in an economy marked by higher inflation and slower growth than was true of the previous several years. If expectations are borne out, this development will come at a time when banks still have a relatively high, though declining, level of problem loans.

Further, the competitive environment in which banks operate is becoming steadily more rigorous. First, domestic banks are expanding their entry into each other's markets in a variety of activities. Second, foreign banks are steadily increasing their presence in the U.S. market, and are competing more and more aggressively in foreign markets in which American banks have played a major role. Finally, the new powers of thrift institutions are blurring the distinctions between them and banks and consequently making them more formidable competitors.

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Regulatory Improvement Project

PROJECT PLAN

In June 1978 the Board of Governors formally adopted a plan to improve all Federal Reserve regulations and rulemaking procedures, including its internal rules and procedures. The scope of the Regulatory Improvement Project is broad and encompasses a number of separate but related phases, each with assignments and deadlines designed to produce the desired result by early 1980.

Phase I focuses on (1) improving the organizational scheme and framework of the regulations, and (2) broadening access to Board regulatory materials by creating a new, publicly distributed regulatory service that will contain all formal regulations, underlying statutes, published and unpublished Board interpretations, previously uncirculated Board and staff rulings and opinions, and other regulatory materials.

Phase II involves a substantive zero-base review of each Federal Reserve regulation to determine (1) fundamental objectives and the extent to which the regulation is meeting current policy goals, (2) costs and benefits of the regulation, (3) any unnecessary burdens imposed by the regulation that could be eliminated, (4) clarity and readability of the regulation, and (5) nonregulatory alternatives that would accomplish the same objectives.

Another phase of the project focuses on improving the Board's Rules of Procedure and the quality of its regulations, and enhancing public participation in and understanding of the regulatory process, in compliance with the spirit and intent of Executive Order 12044 (Improving Government Regulations).

The final phase contemplates creation of a system that will preserve the integrity of the improved regulatory structure and content and the adoption of procedures for reviewing each regulation at least once every 5 years.

IMPLEMENTATION

Each Federal Reserve Bank is actively involved in the Regulatory Improvement Project and has accepted responsibility for one or

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more regulations, sometimes in conjunction with another Bank or with the Board's staff. Guidelines have been established for analysis of the regulations, development of policy issues warranting review by the Board, and drafting of the regulations.

Reports on each regulation usually are prepared by the staff of a Reserve Bank and are accompanied by comments of the Board's staff. These reports and comments are reviewed by committees made up of Board members. The staff proposals, modified as necessary, are then sent to the Board of Governors for review and approval. Once the Board approves the proposals, any contemplated regulatory changes ordinarily are sent out for public comments. After consideration of the comments and any modification of the proposals, final rules may be adopted.

ACCOMPLISHMENTS

Considerable work on various phases of the Regulatory Improvement Project has been completed since June 1978.

The main issues involved in Phase I of the project were resolved in December 1978. An Options Paper concerning changes to the structure and format of regulations, interpretations, orders, and other regulatory documents was distributed to Federal Reserve Banks and outside users for their comments. Project staff analyzed the responses and prepared a report on recommendations and detailed procedures for organizing regulatory materials, which was approved by the Board. The Phase I proposal for a new, publicly distributed regulatory service was also approved by the Board. The regulatory service, to be published in early 1980, will make publicly available a wide range of regulatory materials, including regulations, previously unpublished interpretations, rulings, and other documents along the lines recommended in the Phase I report.

Work on Phase II also progressed rapidly in 1978. The majority of the reports received from 10 Reserve Banks, together with comments of the Board's staff, were reviewed by appropriate Board committees. In addition, the full Board issued revised versions of Regulations O (Loans to Executive Officers) and V (Loan Guarantees for Defense Production) for comment, and completed the review of Regulations C (Home Mortgage Disclosure) and E (Warrants), in the last case rescinding the regulation. Proposals regard-

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ing several other regulations are in advanced stages of development.

Another part of the project was completed in early 1979, when the Board adopted a Statement of Policy Regarding Expanded Rulemaking Procedures. The Board's policy is to improve the quality and minimize the burdens of its regulations by encouraging maximum public participation in their development, by carefully considering an analysis of proposals before they are published for comment, and by informing the public of the reasons for the Board's regulatory actions. The new procedures will apply to all major regulatory proposals, except for those in which speed is necessary or beneficial to the public, such as when regulations or amendments are adopted to implement monetary policy, to relieve undue regulatory burdens, or to meet statutory deadlines.

Finally, preliminary planning for the final phase—creating a system for the future review of regulations—was begun, and additional review procedures for the drafting of regulations were recommended.

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Federal Reserve Banks

PAYMENTS MECHANISM DEVELOPMENTS

In 1978 the Federal Reserve successfully linked together the 36 automated clearing houses (ACH's) into a nationwide network. This action, along with operational improvements planned for 1979, will substantially increase the attractiveness of the ACH as an alternative to the check-clearing system. During 1978 retirement payments of the Navy Department and the Central Intelligence Agency were added to the Direct Deposit of Federal Recurring Payments Program, increasing the activity in that program to 104.5 million items, a gain of 25 per cent over 1977. At the end of 1978, the Treasury Department began to test the feasibility of paying salaries to Federal employees through ACH's.

During 1978 the 48 Federal Reserve offices that process checks handled more than 14.1 billion items, an increase of 6 per cent over the previous year.

The Treasury Check Truncation Program, a new procedure to expedite reconciliation of U.S. Treasury checks by the Treasury Department, was implemented during the year. Treasury checks received for payment by the Federal Reserve Banks are microfilmed, and the data required by the Treasury Department to reconcile its accounts are put on magnetic tape. The magnetic tape and microfilm are then sent to the Treasury in order to speed the processing of inquiries from check recipients and to avoid the issuance of duplicate checks.

In November 1978 the Board sent to the Congress a preliminary schedule of prices for Federal Reserve check collection and for ACH services as part of a comprehensive plan to promote greater competitive equality among financial institutions. Pricing may be implemented when steps have been taken to alleviate the burden of membership in the Federal Reserve System.

EXAMINATION

The Board's Division of Federal Reserve Bank Examinations and Budgets examined the 12 Federal Reserve Banks and their 25

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branches during 1978, as required by Section 21 of the Federal Reserve Act.

In conjunction with the examination of the Federal Reserve Bank of New York, the Board's examiners audited the accounts and holdings related to the System Open Market Account and the foreign currency operations conducted by that Bank in accordance with policies formulated by the Federal Open Market Committee, and furnished copies of these reports to the Committee. The procedures followed by the Board's examiners were surveyed and appraised by a private firm of certified public accountants, pursuant to the policy of having such reviews made on an annual basis.

EARNINGS AND EXPENSES

The accompanying table summarizes the earnings, expenses, and distribution of net earnings of the Federal Reserve Banks for 1978 and 1977.

Current earnings of $8,455 million in 1978 were 23 per cent higher than in 1977. The principal changes in earnings were increases of $1,546 million on U.S. Government securities and $40 million on loans, and a decrease of $25 million on all other earnings.

Current expenses were $653 million, or 4.6 per cent more than in 1977. Assessment for expenditures of the Board of Governors amounted to $53 million.

The profit and loss account showed a $633 million net deduction, primarily because of net losses of $130 million on sales of U.S. Government securities and of $506 million on foreign exchange operations. The loss on foreign exchange operations includes realized losses of $297 million and unrealized losses of $209 million resulting from the revaluation of foreign exchange holdings and outstanding commitments at current exchange rates. Of these amounts, $264 million and $150 million, respectively, reflect realized and unrealized losses associated with Swiss franc commitments entered into before August 15, 1971. The total unrealized net loss was calculated in accordance with generally accepted accounting principles (Financial Accounting Standards Board Statement No. 8), using market exchange rates of December 29, 1978. Previously, foreign exchange holdings and outstanding commitments were valued at historical rates.

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Statutory dividends to member banks totaled $63 million, $3 million more than in 1977. This rise reflected an increase in the capital and surplus of member banks and a consequent increase in the paid-in capital stock of the Federal Reserve Banks.

Payments to the Treasury as interest on Federal Reserve notes totaled $7,006 million, compared with $5,937 million in 1977. This sum consists of all net earnings after dividends and the amount necessary to bring surplus to the level of paid-in capital.

Earnings, Expenses, and Distribution of Net Earnings of Federal Reserve Banks, 1978 and 1977

Thousands of dollars

Item	1978	1977
Current earnings	8,455,390	6,891,318
Current expenses	652,617	623,860
Current net earnings	7,802,773	6,267,458
Net deduction from current net earnings	633,123	177,034
Assessment for expenditures of Board of Governors	53,322	47,366
Net earnings before payments to U.S. Treasury	7,116,328	6,043,058
Dividends paid	63,280	60,182
Payments to U.S. Treasury (interest on Federal Reserve notes)	7,005,780	5,937,148
Transferred to surplus	47,268	45,728

A detailed statement of earnings and expenses of each Federal Reserve Bank during 1978 is shown in Table 6 and a condensed historical statement in Table 7, in the Statistical Tables section of this REPORT. A detailed statement of assessments and expenditures of the Board of Governors appears in the section "Federal Reserve Directories and Meetings."

FEDERAL RESERVE BANK PREMISES

During 1978 the Board of Governors authorized construction of a new building for the Miami Branch. The Federal Reserve Bank of Richmond occupied its new quarters, and the vacated building and property were sold. With approval of the Board, property adjacent to the New Orleans Branch was acquired for future expansion.

Table 8 in the Statistical Tables section of this REPORT shows the cost and book value of bank premises owned and occupied by the

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Federal Reserve Banks and of real estate acquired for banking-house purposes.

HOLDINGS OF LOANS AND SECURITIES

The accompanying table shows holdings, earnings, and average interest rates on loans and securities of the Federal Reserve Banks during the past 3 years.

Average daily holdings of loans and securities during 1978 amounted to $115,291 million, an increase of $10,587 million over 1977. Holdings of U.S. Government securities increased $10,208 million, loans increased $411 million, and acceptances decreased $32 million.

The average rates of interest on holdings increased from 6.56 per cent to 7.33 per cent on U.S. Government securities, from 5.68 to 7.58 per cent on loans, and from 5.27 to 7.85 per cent on acceptances.

Loans and Securities of Reserve Banks, 1976–78

Item and year	Total	U.S. Govt. securities [1]	Loans	Acceptances
	Millions of dollars			
Average daily holdings [2]				
1976	97,523	96,834	85	604
1977	r 104,704	104,002	465	237
1978	115,291	114,210	876	205
Earnings				
1976	6,528.2	6,487.8	4.8	35.6
1977	6,859.0	6,820.1	26.4	12.5
1978	8,449.0	8,366.5	66.4	16.1
	Per cent			
Average rate of interest				
1976	6.69	6.70	5.65	5.89
1977	6.55	6.56	5.68	5.27
1978	7.33	7.33	7.58	7.85

r Revised.
[1] Includes Federal Agency obligations.
[2] Based on holdings at opening of business.

LOAN GUARANTEES FOR DEFENSE PRODUCTION

Under the Defense Production Act of 1950, the Departments of the Army, Navy, and Air Force; the Defense Logistics Agency of the

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Department of Defense; the Departments of Commerce, Interior, Agriculture, and Energy; the General Services Administration; the National Aeronautics and Space Administration; and the Nuclear Regulatory Commission are authorized to guarantee loans for defense production that are made by commercial banks and other private financing institutions. The Federal Reserve Banks act as fiscal agents of the guaranteeing agencies under the Board's Regulation V.

During 1978 the guaranteeing agencies did not authorize the issuance of any new guarantee agreements. Loan authorizations outstanding on December 31, 1978, totaled $2.9 million, all of which represented outstanding loans. Of total loans outstanding, less than 1 per cent on the average was guaranteed. During the year, no amounts were disbursed on the guaranteed loans.

Authority for the V-loan program will terminate on September 30, 1979.

Table 16 in the Statistical Tables section of this REPORT shows guarantee fees and maximum interest rates applicable to Regulation V loans.

VOLUME AND COST OF OPERATIONS

Table 9 in the Statistical Tables section of this REPORT shows the volume of operations in the principal departments of the Federal Reserve Banks for 1975–78, and Table 10 shows the cost of the larger operations of the Reserve Banks.

The Reserve Banks handled greater volume in 1978 than in 1977. The number of transfers of funds increased 16.6 per cent to 28.7 million, involving $50.5 trillion. The number of checks processed rose 5.5 per cent to 14.8 billion; the dollar amount rose to $7.6 trillion. Other significant volume increases were experienced in loans and in currency and coin.

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Board of Governors

FINANCIAL STATEMENTS

The accounts of the Board for the year 1978 were audited by Arthur Andersen & Co., independent public accountants.

AUDITORS' REPORT

Board of Governors of the
Federal Reserve System
Washington, D.C.

We have examined the balance sheet of the Board of Governors of the Federal Reserve System as of December 31, 1978, and the related statements of assessments and expenses and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. The financial statements of the Board of Governors of the Federal Reserve System for the year ended December 31, 1977, were examined by other auditors whose report dated February 10, 1978, expressed an unqualified opinion on those statements.

In our opinion, the accompanying financial statements present fairly the financial position of the Board of Governors of the Federal Reserve System as of December 31, 1978, and the results of its operations and the changes in its financial position for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Arthur Andersen & Co.

1666 K Street, N.W.
Washington, D.C.
February 9, 1979

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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

BALANCE SHEET

ASSETS	December 31 1978	December 31 1977
OPERATING FUND:		
Cash	$ 4,797,310	$ 4,897,185
Miscellaneous receivables and advances	360,095	847,867
Stockroom and cafeteria inventories, at lower of cost (first-in, first-out) or market	155,543	168,368
Total operating fund	5,312,948	5,913,420
PROPERTY FUND, at cost (Notes 1 and 4):		
Land and improvements	1,299,884	1,255,864
Buildings	59,223,136	49,860,720
Furniture and equipment	6,753,431	4,479,586
Computer equipment	3,476,832	3,342,122
Construction-in-progress	—	4,834,267
Total property fund	70,753,283	63,772,559
	$76,066,231	$69,685,979
LIABILITIES AND FUND BALANCES		
OPERATING FUND:		
Liabilities—		
Accounts payable	$ 2,872,392	$ 2,393,968
Accrued payroll and related taxes	1,562,912	1,330,114
	4,435,304	3,724,082
Commitments and contingencies (Notes 1, 2, and 4)		
Fund balance (Note 1)—		
Balance, beginning of year	2,189,338	2,234,625
Expenses in excess of assessments	(1,311,694)	(45,287)
Balance, end of year	877,644	2,189,338
Total operating fund	5,312,948	5,913,420
PROPERTY FUND (Note 1):		
Fund balance—		
Balance, beginning of year	63,772,559	60,377,404
Additions—at cost	8,688,619	7,556,266
Disposals—at cost	(1,707,895)	(4,161,111)
Total property fund	70,753,283	63,772,559
	$76,066,231	$69,685,979

The accompanying notes are an integral part of this balance sheet.

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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

STATEMENT OF ASSESSMENTS AND EXPENSES

	Year ended December 31	
	1978	1977
ASSESSMENTS LEVIED ON FEDERAL RESERVE BANKS (Note 1):		
For Board expenses and property additions	$ 53,321,700	$47,366,100
For expenditures made on behalf of the Federal Reserve Banks for printing, issuance and redemption of Federal Reserve notes	60,454,967	50,543,541
Total assessments	113,776,667	97,909,641
EXPENSES (Note 1):		
Board expenses—		
Salaries	31,212,936	29,021,842
Retirement and insurance contributions (Note 3)	6,313,145	5,383,462
Travel expenses	1,174,888	1,040,702
Professional fees	564,501	607,008
Contractual services	492,689	613,700
Printing and binding, net	1,117,575	1,088,676
Equipment, office space and other rentals (Note 2)	1,687,813	1,670,001
Telephone and telegraph	683,049	789,649
Postage	415,660	371,930
Stationery, office and other supplies	405,986	380,739
Heat, light, and power	877,116	836,954
Cafeteria operations, net	305,653	271,714
Repairs and maintenance	424,402	372,398
Books and subscriptions	130,318	119,764
Miscellaneous	227,395	188,179
	46,033,126	42,756,718
Board property additions, net of recoveries on disposals of $88,351 in 1978 and $2,901,597 in 1977 (Note 1)	8,600,268	4,654,669
	54,633,394	47,411,387
Expenditures for printing, issuance and redemption of Federal Reserve notes on behalf of the Federal Reserve Banks (Note 1)	60,454,967	50,543,541
Total expenses	115,088,361	97,954,928
EXPENSES IN EXCESS OF ASSESSMENTS	$ (1,311,694)	$ (45,287)

The accompanying notes are an integral part of this statement.

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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

STATEMENT OF CHANGES IN FINANCIAL POSITION

	Year ended December 31,	
	1978	1977
Sources of Funds:		
Assessments levied for Board expenses and property additions	$ 53,321,700	$ 47,366,100
Assessments levied for expenditures made on behalf of the Federal Reserve Banks	60,454,967	50,543,541
Recoveries from disposals of property	88,351	2,901,597
Decrease (increase) in miscellaneous receivables, advances and inventories	500,597	(500,067)
Increase in liabilities	711,222	1,275,638
Total sources	115,076,837	101,586,809
Applications of Funds:		
Board expenses	46,033,126	42,756,718
Expenditures for printing, issuance and redemption of Federal Reserve notes on behalf of the Federal Reserve Banks	60,454,967	50,543,541
Additions to property—		
Land and improvements	88,970	111,029
Buildings	6,511,319	158,826
Furniture and equipment	1,953,620	224,279
Computer	134,710	3,052,800
Construction-in-progress	—	4,009,332
	8,688,619	7,556,266
Total applications	115,176,712	100,856,525
Increase (Decrease) in Cash	(99,875)	730,284
Cash Balance, beginning of year	4,897,185	4,166,901
Cash Balance, end of year	$ 4,797,310	$ 4,897,185

The accompanying notes are an integral part of this statement.

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 1978 AND 1977

(1) Significant Accounting Policies

In preparing its financial statements, the Board has applied accounting principles which, in its opinion, best reflect its financial position and results of operations. These accounting principles include certain principles which are generally accepted for organizations in the private sector and also certain principles which are generally accepted for governmental units. A summary of significant accounting policies is shown below.

Accounting for Assessments, Board Expenses and Property Additions—Assessments made by the Board on the Federal Reserve Banks for Board expenses and additions to property are calculated based upon expected cash needs and are accrued when assessed. Board expenses and property additions are recorded on the accrual basis of accounting.

Accounting for Assessments and Expenditures Made on Behalf of the Federal Reserve Banks—Assessments and expenditures made on behalf of the Federal Reserve Banks for the printing, issuance, and redemption of Federal Reserve notes are recorded on the cash basis. This treatment produces results which are not materially different from those which would have been produced using the accrual basis of accounting.

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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

NOTES TO FINANCIAL STATEMENTS—CONTINUED

YEARS ENDED DECEMBER 31, 1978 AND 1977

Accounting for Property—The Board does not charge depreciation as an operating expense. Property additions are charged to expense in the Operating Fund in the year of acquisition; recoveries on the disposal of property are recorded as a reduction of expense in the Operating Fund in the year of disposal. When property is acquired or sold, the property accounts in the Property Fund are increased or reduced at cost, with a corresponding increase or decrease in the Property Fund balance.

Accounting for Employee Annual Leave—The Board does not accrue for salary expense related to employee annual leave that has been earned and would be paid if not taken prior to termination of employment. As of December 31, 1978, vested employee annual leave is approximately $1,830,000.

(2) Leases

The Board leases office and computer equipment and office and storage space under leases, which may generally be terminated within one year. At December 31, 1978, fixed future rental commitments are $495,000 for 1979.

(3) Retirement Plans

There are two major retirement programs for employees of the Board. Approximately 86 per cent of the employees are covered by the Federal Reserve Board Plan. All new members of the staff who do not come directly from a position in the government are covered by this Plan. The second Plan, the Civil Service Retirement Plan, covers all new employees who come directly from government service. Employee contributions are the same percentage of salary under both Plans, and benefits are similar, being based upon the Civil Service Plan.

Under the Civil Service Plan, Board contributions match employee payroll deductions while under the Federal Reserve Board Plan, Board contributions are actuarially determined.

Additionally, employees of the Board participate in the Federal Reserve System's Thrift Plan. Under this Plan, the Board adds a fixed percentage to allowable employee savings.

Board contributions to all retirement plans totaled approximately $5,691,000 in 1978 and $4,798,000 in 1977.

(4) Contingent Liabilities

The Board has been named as a defendant in litigation involving challenges to, or appeals from, actions or proposed actions of the Board pursuant to statutory requirement or authorization. Such lawsuits generally seek injunctive or declaratory relief against the Board rather than monetary awards. It is the opinion of Board counsel that lawsuits involving monetary awards do not represent a material liability to the Board.

The Board does not maintain insurance against loss of its buildings and furniture and equipment from fire or other casualties or employee fidelity bonding. Coverage for other customarily insured risks, such as worker's compensation insurance, builders risk and comprehensive general liability insurance, is carried by the Board.

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Statistical Tables

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1. Detailed Statement of Condition of All Federal Reserve Banks Combined, December 31, 1978

Thousands of dollars

ASSETS

Item				
Gold certificates on hand			1,278	
Gold certificates due from U.S. Treasury			11,669,796	
Total gold certificate account				11,671,074
Special Drawing Rights certificate account				1,300,000
Coin				273,667
Loans to member banks, by type of security				
U.S. Government and agency obligations		701,090		
Other eligible paper		210,217		
Other paper, Sec. 10(b)		262,712	1,174,019	
Loans to others				
Total loans			1,174,019	
Acceptances				
Bought outright				
Held under repurchase agreement			587,128	
Federal agency obligations				
Bought outright			7,895,553	
Held under repurchase agreement			133,000	
U.S. Government securities				
Bought outright				
Bills	42,158,660			
Notes	54,854,949			
Bonds	12,464,780			
Total bought outright		109,478,389		
Held under repurchase agreement		1,083,900		
Total U.S. Government securities			110,562,289	
Total loans and securities				120,351,989
Cash items in process of collection				
Transit items			12,799,471	
Exchanges for clearing house			275,733	
Other cash items			2,009,285	
Total cash items in process of collection				15,084,489
Bank premises				
Land			66,783	
Buildings (including vaults)		199,754		
Building machinery and equipment		99,330		
Construction account		166,791		
Total bank premises		465,875		
Less depreciation allowances		140,003	325,872	
Bank premises, net				392,655
Other assets				
Furniture and equipment		84,311		
Less depreciation		18,350		
Total furniture and equipment, net			65,961	
Denominated in foreign currencies [1]			1,605,611	
Interest accrued			1,573,366	
Premium on securities			123,563	
Real estate acquired for banking-house purposes			38,623	
Suspense account			606,087	
Overdrafts			19,801	
All other			115,596	
Total other assets				4,148,608
TOTAL ASSETS				153,222,482

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1.—Continued

LIABILITIES

Item			
Federal Reserve notes			
Outstanding (issued to Federal Reserve Banks)		112,836,414	
Less held by Federal Reserve Banks		9,508,930	
Total Federal Reserve notes, net			**103,327,484**
Deposits			
Member bank reserves		**31,223,365**	
U.S. Treasury—General account		**4,196,307**	
Foreign		**367,536**	
Other deposits			
Nonmember bank—Clearing accounts	1,444		
Officers' and certified checks	19,370		
Reserves of corporations doing foreign banking or financing	340,491		
International organizations	336,920		
Secretary of Treasury special account	29,161		
All other	528,822		
Total other deposits		**1,256,208**	
Total deposits			**37,043,416**
Deferred availability cash items			**8,578,921**
Other liabilities			
Exchange-translation account [2]		278,954	
Unearned discount		318	
Discount on securities		1,593,998	
Sundry items payable		17,450	
Suspense account		226,769	
All other		2,632	
Total other liabilities			**2,120,121**
TOTAL LIABILITIES			**151,069,942**

CAPITAL ACCOUNTS

Item	
Capital paid in	**1,076,270**
Surplus	**1,076,270**
Other capital accounts [3]	....
TOTAL LIABILITIES AND CAPITAL ACCOUNTS	**153,222,482**

[1] Valued at market exchange rates of Dec. 29, 1978.
[2] Of this amount, $150 million reflects revaluation of Swiss franc commitments entered into before Aug. 15, 1971.
[3] During the year, this item includes the net earnings, expenses, profit and loss items, and accrued dividends, which are closed out on Dec. 31: see Table 6 in the Statistical Tables section of this REPORT.

NOTE. Amounts in boldface type indicate items in the Board's weekly statement of condition of the Federal Reserve Banks.

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2. Statement of Condition of Each Federal Reserve Bank, December 31, 1978 and 1977

Millions of dollars

Item	Total		Boston		New York		Philadelphia		Cleveland		Richmond	
	1978	1977	1978	1977	1978	1977	1978	1977	1978	1977	1978	1977
ASSETS												
Gold certificate account	11,671	11,718	760	541	3,206	3,492	598	631	921	934	974	982
Special Drawing Rights certificate account	1,300	1,250	67	62	330	313	69	74	112	107	116	113
Coin	274	282	17	17	21	18	15	13	33	40	23	28
Loans												
Secured by U.S. Government and agency obligations	717	226	30	10	80	103	68	11	31	2	24	13
Other	455	40	....	....	231	....	10	4	....	....	24	....
Acceptances												
Bought outright	....	....	....	....	....	....	....	....	....	....	....	....
Held under repurchase agreement	587	954	....	....	587	954	....	....	....	....	....	....
Federal agency obligations												
Bought outright	7,896	8,004	367	374	1,921	1,889	395	427	657	670	647	655
Held under repurchase agreement	133	451	....	....	133	451	....	....	....	....	....	....
U.S. Government securities												
Bought outright [1]	109,478	100,918	5,095	4,715	26,632	23,819	5,483	5,384	9,111	8,448	8,965	8,250
Held under repurchase agreement	1,084	1,901	....	....	1,084	1,901	....	....	....	....	....	....
Total loans and securities	120,350	112,494	5,492	5,099	30,668	29,117	5,956	5,826	9,799	9,120	9,660	8,918
Cash items in process of collection	15,084	11,542	566	335	1,360	1,450	631	342	808	461	2,432	1,866
Bank premises	394	378	106	106	10	9	55	56	23	23	80	72
Other assets												
Denominated in foreign currencies [2]	1,606	18	50	1	416	4	69	1	136	1	87	1
All other	2,543	2,046	104	94	624	489	168	104	162	138	183	155
Interdistrict Settlement Account	....	....	*−525*	*−23*	*+854*	*−1,313*	*−637*	*−389*	*−438*	*−42*	*−262*	*+247*
TOTAL ASSETS	153,222	139,728	6,637	6,232	37,489	33,579	6,924	6,658	11,556	10,782	13,293	12,382

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LIABILITIES												
Federal Reserve notes	103,325	93,153	5,308	4,761	26,335	23,678	5,198	4,936	8,551	7,987	9,249	8,329
Deposits												
Member bank reserves	31,223	26,709	666	642	6,884	5,784	1,081	891	1,798	1,650	1,781	1,534
U.S. Treasury—General account	4,196	7,114	222	428	1,033	1,399	208	452	388	451	248	598
Foreign	368	379	6	10	217	174	9	12	17	24	11	15
All other	1,256	1,187	23	23	815	688	21	34	36	43	53	57
Total deposits	37,043	35,389	917	1,103	8,949	8,045	1,319	1,389	2,239	2,168	2,093	2,204
Deferred-availability cash items	8,579	7,894	270	249	920	991	234	183	446	361	1,680	1,625
Other liabilities and accrued dividends	2,119	1,234	76	55	725	331	85	62	136	92	157	114
TOTAL LIABILITIES	151,066	137,670	6,571	6,168	36,929	33,045	6,836	6,570	11,372	10,608	13,179	12,272
CAPITAL ACCOUNTS												
Capital paid in	1,078	1,029	33	32	280	267	44	44	92	87	57	55
Surplus	1,078	1,029	33	32	280	267	44	44	92	87	57	55
Other capital accounts	....	....	....	....	....	....	....	....	....	....	....	....
TOTAL LIABILITIES AND CAPITAL ACCOUNTS	153,222	139,728	6,637	6,232	37,489	33,579	6,924	6,658	11,556	10,782	13,293	12,382
FEDERAL RESERVE NOTE STATEMENT												
Federal Reserve notes												
Issued to Federal Reserve Bank by Federal Reserve Agent and outstanding	112,836	100,534	6,068	4,977	28,269	25,038	6,165	5,383	9,077	8,360	9,925	8,897
Less held by issuing Bank, and forwarded for redemption	9,511	7,381	760	216	1,934	1,360	967	447	526	373	676	568
Federal Reserve notes, net [3]	103,325	93,153	5,308	4,761	26,335	23,678	5,198	4,936	8,551	7,987	9,249	8,329
Collateral held by Federal Reserve Agent for notes issued to Bank												
Gold certificate account	11,671	11,713	760	541	3,206	3,491	598	631	921	933	974	982
Special Drawing Rights certificate account	1,300	880	67	62	330	313	69	....	112	107	116	109
Eligible paper	907	....	30	....	175	....	71	....	31	....	44	....
U.S. Government securities	98,958	89,675	[4] 5,211	4,400	24,558	21,550	5,427	4,800	8,013	7,500	8,791	7,950
TOTAL COLLATERAL	112,836	102,268	6,068	5,003	28,269	25,354	6,165	5,431	9,077	8,540	9,925	9,041

For notes see end of table.

2. Statement of Condition of Each Federal Reserve Bank, December 31, 1978 and 1977—Continued

Millions of dollars

Item	Atlanta		Chicago		St. Louis		Minneapolis		Kansas City		Dallas		San Francisco	
	1978	1977	1978	1977	1978	1977	1978	1977	1978	1977	1978	1977	1978	1977
ASSETS														
Gold certificate account	518	560	1,763	1,736	466	469	231	225	425	393	509	456	1,300	1,299
Special Drawing Rights certificate account	51	64	215	198	55	53	28	25	48	44	57	48	152	149
Coin	32	28	14	24	22	20	11	9	38	43	17	12	31	30
Loans														
Secured by U.S. Government and agency obligations	104	....	59	40	32	7	8	1	20	11	46	23	215	5
Other	50	7	8	2	30	....	2	....	15	1	47	1	38	25
Acceptances														
Bought outright	....	....	....	....	....	....	....	....	....	....	....	....	....	....
Held under repurchase agreement	....	....	....	....	....	....	....	....	....	....	....	....	....	....
Federal agency obligations														
Bought outright	357	395	1,259	1,282	322	340	190	196	324	321	410	400	1,047	1,055
Held under repurchase agreement	....	....	....	....	....	....	....	....	....	....	....	....	....	....
U.S. Government securities														
Bought outright [1]	4,952	4,982	17,460	16,166	4,470	4,283	2,627	2,471	4,486	4,049	5,683	5,046	[5] 14,514	13,305
Held under repurchase agreement	....	....	....	....	....	....	....	....	....	....	....	....	....	....
Total loans and securities	5,463	5,384	18,786	17,490	4,854	4,630	2,827	2,668	4,845	4,382	6,186	5,470	15,814	14,390
Cash items in process of collection	1,879	1,127	1,630	1,367	583	565	802	573	1,292	924	1,066	887	2,035	1,645
Bank premises	22	14	16	16	13	13	29	30	19	18	12	12	9	9
Other assets														
Denominated in foreign currencies [2]	120	1	246	3	50	1	48	1	68	1	91	1	225	2
All other	190	151	337	259	105	74	56	46	83	75	126	96	405	365
Interdistrict Settlement Account	*−740*	*−277*	*+184*	*+89*	*+68*	*−115*	*−434*	*+13*	*+385*	*+362*	*+439*	*+290*	*+1,106*	*+1,158*
TOTAL ASSETS	7,535	7,052	23,191	21,182	6,216	5,710	3,598	3,590	7,203	6,242	8,503	7,272	21,077	19,047

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LIABILITIES														
Federal Reserve notes	3,682	3,669	17,190	15,428	4,540	3,912	1,854	1,999	4,321	3,461	4,964	4,071	12,133	10,922
Deposits														
Member bank reserves	2,099	1,952	4,091	3,591	888	817	866	720	1,485	1,156	2,481	1,922	7,103	6,050
U.S. Treasury—General account	229	511	428	705	246	474	183	276	255	637	162	453	594	730
Foreign	15	21	31	41	6	9	6	8	9	12	12	15	29	38
All other	57	77	107	90	20	23	8	13	18	22	34	34	64	83
Total deposits	2,400	2,561	4,657	4,427	1,160	1,323	1,063	1,017	1,767	1,827	2,689	2,424	7,790	6,901
Deferred-availability cash items	1,184	602	758	834	380	363	560	483	945	822	643	603	559	778
Other liabilities and accrued dividends	107	64	260	179	70	48	53	29	78	46	81	58	291	156
TOTAL LIABILITIES	7,373	6,896	22,865	20,868	6,150	5,646	3,530	3,528	7,111	6,156	8,377	7,156	20,773	18,757
CAPITAL ACCOUNTS														
Capital paid in	81	78	163	157	33	32	34	31	46	43	63	58	152	145
Surplus	81	78	163	157	33	32	34	31	46	43	63	58	152	145
Other capital accounts	....	....	....	....	....	....	....	....	....	....	....	....	....	....
TOTAL LIABILITIES AND CAPITAL ACCOUNTS	7,535	7,052	23,191	21,182	6,216	5,710	3,598	3,590	7,203	6,242	8,503	7,272	21,077	19,047
FEDERAL RESERVE NOTE STATEMENT														
Federal Reserve notes														
Issued to Federal Reserve Bank by Federal Reserve Agent and outstanding	4,736	4,524	17,722	16,111	4,891	4,329	2,313	2,143	4,780	4,030	5,683	4,888	13,207	11,854
Less held by issuing Bank, and forwarded for redemption	1,054	855	532	683	351	417	459	144	459	569	719	817	1,074	932
Federal Reserve notes, net [3]	3,682	3,669	17,190	15,428	4,540	3,912	1,854	1,999	4,321	3,461	4,964	4,071	12,133	10,922
Collateral held by Federal Reserve Agent for notes issued to Bank														
Gold certificate account	518	559	1,763	1,736	466	468	231	225	425	393	509	456	1,300	1,298
Special Drawing Rights certificate account	51	62	215	....	55	53	28	25	48	42	57	48	152	59
Eligible paper	128	....	59	....	46	....	8	....	26	....	75	....	214	....
U.S. Government securities	4,039	4,000	15,685	14,500	4,324	3,850	2,046	2,010	4,281	3,700	5,042	4,415	11,541	11,000
TOTAL COLLATERAL	4,736	4,621	17,722	16,236	4,891	4,371	2,313	2,260	4,780	4,135	5,683	4,919	13,207	12,357

[1] Includes securities loaned—fully guaranteed by U.S. Government securities pledged with Federal Reserve Banks—and excludes any securities sold and scheduled to be bought back under matched sale-purchase transactions.
[2] Beginning Dec. 29, 1978, such assets are revalued monthly at market exchange rates.
[3] Includes Federal Reserve notes held by U.S. Treasury and by Federal Reserve Banks other than the issuing Bank.
[4] Includes securities borrowed from other Federal Reserve Banks.
[5] Includes securities loaned to other Federal Reserve Banks.

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3. Federal Reserve Bank Holdings of U.S. Government and Federal Agency Securities, December 31, 1976–78

Millions of dollars

Description of issue	Coupon (per cent)	December 31			Increase or decrease (−)	
		1978	1977	1976	1978	1977
U.S. Government securities—Total	...	**110,562**	**102,819**	**97,021**	**7,743**	**5,798**
Held outright [1]						
Treasury bills—Total	...	42,159	41,560	38,572	598	2,989
Within 3 months	...	20,661	20,106	19,529	555	577
3–6 months	...	14,911	15,690	14,277	−779	1,413
After 6 months	...	6,586	5,765	4,765	821	1,000
Treasury notes—Total	...	54,855	50,509	47,972	4,346	2,537
Feb. 15, 1977—A	8	...	...	2,481	...	−2,481
Feb. 28, 1977—F	6	...	...	150	...	−150
Mar. 31, 1977—G	6½	...	...	516	...	−516
Apr. 30, 1977—H	7⅜	...	...	84	...	−84
May 15, 1977—C	6⅞	...	...	525	...	−525
—D	9	...	...	2,994	...	−2,994
May 31, 1977—I	6¾	...	...	171	...	−171
June 30, 1977—J	6½	...	...	260	...	−260
July 31, 1977—K	7½	...	...	59	...	−59
Aug. 15, 1977—B	7¾	...	...	848	...	−848
Aug. 31, 1977—L	8¼	...	...	120	...	−120
Sept. 30, 1977—M	8⅜	...	...	48	...	−48
Oct. 31, 1977—N	7½	...	...	166	...	−166
Nov. 15, 1977—E	7¾	...	...	1,231	...	−1,231
Nov. 30, 1977—Q	6⅝	...	...	81	...	−81
Dec. 31, 1977—P	7¼	...	328	259	−328	69
Jan. 31, 1978—J	6⅜	...	272	250	−272	22
Feb. 15, 1978—A	6¼	...	2,650	2,628	−2,650	22
Feb. 28, 1978—G	8	...	53	35	−53	18
Mar. 31, 1978—K	6¾	...	312	241	−312	71
Apr. 30, 1978—L	6½	...	391	360	−391	31
May 15, 1978—D	7⅛	...	953	921	−953	32
—F	7⅞	...	1,539	1,503	−1,539	36
May 31, 1978—M	7⅛	...	175	152	−175	23
June 30, 1978—N	6⅞	...	771	723	−771	48
July 31, 1978—P	6⅞	...	259	208	−259	51
Aug. 15, 1978—C	8¾	...	633	629	−633	4
—E	7⅝	...	2,571	2,549	−2,571	22
Aug. 31, 1978—Q	6⅝	...	173	145	−173	28
Sept. 30, 1978—R	6¼	...	415	346	−415	69
Oct. 31, 1978—S	5⅞	...	192	117	−192	75
Nov. 15, 1978—B	6	...	2,468	2,448	−2,468	20
Nov. 30, 1978—T	5¾	...	234	143	−234	91
Dec. 31, 1978—H	8⅛	244	177	140	67	37
—U	5¼	643	446	352	197	94
Jan. 31, 1979—L	5⅞	151	88	...	63	88
Feb. 15, 1979—H	7	1,731	1,724	1,700	7	24
Feb. 28, 1979—M	5⅞	368	308	...	60	308
Mar. 31, 1979—N	6	640	570	...	70	570
Apt. 30, 1979—P	5⅞	159	118	...	41	118
May 15, 1979—D	7⅞	550	538	491	12	47
May 31, 1979—Q	6⅛	239	209	...	30	209
June 30, 1979—E	7¾	157	119	70	38	49
—R	6⅛	291	265	...	26	265
July 31, 1979—S	6¼	159	111	...	48	111
Aug. 15, 1979—A	6¼	669	630	599	39	31
—J	6⅞	880	838	814	42	24
Aug. 31, 1979—T	6⅝	440	210	...	230	210
Sept. 30, 1979—F	8½	230	222	210	8	12
—U	6⅝	333	248	...	85	248
Oct. 31, 1979—V	7¼	455	248	...	207	248
Nov. 15, 1979—B	6⅝	890	890	875	...	15
—K	6¼	250	228	121	22	107
—C	7	366	362	351	4	11
Nov. 30, 1979—W	7⅛	475	261	...	214	261
Dec. 31, 1979—G	7½	137	107	92	30	15
—X	7⅛	568	...	...	568	...
Jan. 31, 1980—K	7½	365	...	...	365	...
Feb. 15, 1980—G	6½	1,461	1,452	...	9	1,452
Feb. 29, 1980—L	7⅝	334	...	...	334	...
Mar. 31, 1980—C	7½	724	167	111	557	56
Apr. 30, 1980—N	7¾	437	...	...	437	...
May 15, 1980—A	6⅞	5,272	5,267	5,264	5	3
May 31, 1980—P	8	177	...	...	177	...
June 30, 1980—D	7⅝	294	288	231	6	57
—Q	8¼	858	...	...	858	...
July 31, 1980—R	8½	699	...	...	699	...
Aug. 15, 1980—B	9	2,435	2,427	2,422	8	5
—H	6¾	657	489	...	168	489

For notes see end of table.

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3.—Continued

Description of issue	Coupon (per cent)	December 31			Increase or decrease (−)	
		1978	1977	1976	1978	1977
Treasury notes—Cont.						
Aug. 31, 1980—S	8⅜	416	...	...	416	...
Sept. 30, 1980—E	6⅞	153	141	33	12	108
—T	8⅜	686	...	...	686	...
Oct. 31, 1980—U	8⅞	309	...	...	309	...
Nov. 15, 1980—J	7⅛	693	658	...	35	658
Nov. 30, 1980—V	9¼	250	...	...	250	...
Dec. 31, 1980—F	5⅞	33	33	8	...	25
Feb. 15, 1981—A	7	351	349	338	2	11
—C	7⅜	1,007	914	826	93	88
Mar. 31, 1981—H	6⅞	203	55	...	148	55
May 15, 1981—D	7⅜	182	175	109	7	66
—M	7½	1,034	...	...	1,034	...
June 30, 1981—J	6¾	70	67	...	3	67
Aug. 15, 1981—F	7⅝	297	241	129	56	112
—N	8⅜	1,297	...	...	1,297	...
Sept. 30, 1981—K	6¾	72	48	...	24	48
Nov. 15, 1981—B	7¾	1,597	1,591	1,554	6	37
—G	7	113	83	14	30	69
Dec. 31, 1981—L	7¼	124	13	...	111	13
Feb. 15, 1982—D	6⅛	56	35	...	21	35
Mar. 31, 1982—G	7⅞	235	...	...	235	...
May 15, 1982—A	8	1,444	1,439	1,421	5	18
—E	7	30	14	...	16	14
—K	9¼	1,018	...	...	1,018	...
June 30, 1982—H	8¼	93	...	...	93	...
Aug. 15, 1982—B	8⅛	1,161	1,110	1,065	51	45
Sept. 30, 1982—J	8⅜	62	...	...	62	...
Nov. 15, 1982—C	7⅞	754	715	633	39	82
—F	7⅛	209	4	...	205	4
Feb. 15, 1983—A	8	2,136	2,101	2,075	35	26
May 15, 1983—C	7⅞	89	...	...	89	...
Nov. 15, 1983—B	7	95	95	81	...	14
Feb. 15, 1984—A	7¼	3,900	3,659	...	241	3,659
Aug. 15, 1984—B	7¼	372	337	...	35	337
Feb. 15, 1985—A	8	1,448	...	...	1,448	...
Aug. 15, 1985—B	8¼	1,618	...	...	1,618	...
May 15, 1986—A	7⅞	1,086	852	695	234	157
Aug. 15, 1986—B	8	1,978	1,941	1,757	37	184
Nov. 15, 1987—A	7⅝	616	448	...	168	448
May 15, 1988—A	8¼	1,744	...	...	1,744	...
Nov. 15, 1988—B	8¾	1,087	...	...	1,087	...
Treasury bonds—Total	...	12,465	8,848	6,725	3,617	2,123
1975–85	4¼	156	156	156	...	...
1978–83	3¼	87	87	87	...	...
1980—Feb.	4	266	266	261	...	5
Nov.	3½	74	74	74	...	...
1981—Aug.	7	123	123	123	...	...
1982—Feb.	6⅜	371	364	364	7	...
1984—Aug.	6⅜	355	355	355	...	...
1985—May	3¼	47	47	47	...	...
1986—Nov.	6⅛	310	310	310	...	...
1987–92	4¼	509	509	509	...	...
1988–93	4	24	24	24	...	...
	7½	380	380	352	...	28
1989–94	4⅛	77	77	77	...	...
1990—Feb.	3½	84	84	84	...	...
May	8¼	342	285	240	56	45
1992—Aug.	7¼	91	76	...	15	76
1993—Feb.	6¾	70	70	70	...	...
	7⅞	127	...	...	127	...
Aug.	8⅝	61	...	...	61	...
Nov.	8⅝	121	...	...	121	...
1993–98	7	157	157	157	...	...
1994–99	8½	999	955	900	44	55
1995—Feb.	3	2	2	2	...	...
1995–2000	7⅞	562	517	455	45	62
	8⅜	2,004	902	842	1,102	60
1996–2001	8	480	430	341	50	89
1998—Nov.	3½	31	31	31	...	...
2000–05	8¼	1,493	950	864	543	86
2002–07	7⅝	1,389	1,379	...	10	1,379
	7⅞	265	240	...	25	240
2003–08	8⅜	747	...	...	747	...
	8¾	661	...	...	661	...
Held under RP's	...	1,084	1,901	3,753	−817	−1,852

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3. Federal Reserve Bank Holdings of U.S. Government and Federal Agency Securities, December 31, 1976–78—Continued

Millions of dollars

Description of issue	December 31			Increase or decrease (−)	
	1978	1977	1976	1978	1977
U.S. Government securities—Total	**110,562**	**102,819**	**97,021**	**7,743**	**5,798**
Within 90 days	24,097	25,309	26,429	−1,212	−1,120
91 days to 1 year	29,465	32,539	25,889	−3,074	6,650
1–5 years	31,608	27,516	30,710	4,092	−3,194
5–10 years	14,717	10,388	9,045	4,329	1,343
Over 10 years	10,675	7,067	4,949	3,608	2,118
Federal agency obligations					
Held outright—Total	7,896	8,004	6,794	−108	1,210
Banks for Cooperatives	85	112	78	−27	34
Export-Import Bank	69	106	118	−37	−12
Federal Farm Credit Banks	68	58	....	10	58
Federal Home Loan Banks	2,189	2,151	1,786	38	365
Federal Intermediate Credit Banks	466	465	414	1	51
Federal Land Banks	1,377	1,352	946	25	406
Farmers Home Administration	196	238	295	−42	−57
Federal National Mortgage Association	3,196	3,266	2,899	−70	367
Government National Mortgage Association—PC's	83	87	90	−4	−3
U.S. Postal Service	37	37	37	0	0
Washington Metropolitan Area Transit Authority	117	117	117	0	0
General Services Administration	14	14	14	0	0
Held under RP's	133	451	278	−318	173

[1] Excludes securities sold under matched sale-purchase agreements, and securities held under repurchase agreements.

NOTE. Details may not add to totals because of rounding.

4. Federal Reserve Bank Holdings of Special Short-Term Treasury Certificates Purchased Directly from the United States, 1971–78

Millions of dollars

Date	Amount	Date	Amount	Date	Amount	Date	Amount
1971		1973		1975		1975	
June 8	79	Aug. 15	351	Mar. 11	626	Aug. 13	399
9	582	Sept. 7	73	12	1,043	15	481
10	610	8	73	13	315		
11	593	9[1]	73	14	820	1976	0
12	593	10	42	15	820		
13[1]	593	11	485	16[1]	820	1977	
14	243	12	169	17	832	Sept. 30	2,500
15	588	14	319			Oct. 1	2,500
16	349	15	319	Aug. 5	656	2[1]	2,500
		16[1]	319	6	965	3	2,500
				7	474		
1972		1974		11	204		
Sept. 12	38	Nov. 6	131	12	543	1978	0

[1] Sunday or holiday.

NOTE. Under authority of Section 14(b) of the Federal Reserve Act.

Throughout the period shown the interest rate paid on such securities was ¼ per cent below the prevailing discount rate of the Federal Reserve Bank of New York. For data for earlier years, beginning with 1942, see previous ANNUAL REPORTS.

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5. Open Market Transactions of the Federal Reserve System, 1978

Millions of dollars

Month	Outright transactions in U.S. Government securities, by maturity (excluding matched sale–purchase transactions): Treasury bills			Others within 1 year			1–5 years		
	Gross purchases	Gross sales	Redemptions	Gross purchases	Gross sales	Exch., maturity shifts, or redemptions	Gross purchases	Gross sales	Exch. or maturity shifts
January	696	1,323	...	56	...	−511	311	...	511
February	379	1,974	1,100	...	...	−653	...	...	1,109
March	748	50	31	288	...	261	813	...	−261
April	1,670	...	...	100	...	136	235	...	−136
May	416	737	300	53	...	−2,343	290	...	−79
June	4,395	...	...	135	...	−380	631	...	467
July	701	466	...	...	...	−241	...	...	241
August	972	689	...	171	...	−1,544	424	...	−490
September	2,635	...	...	168	...	563	350	...	−563
October	1,978	2,148	...	73	...	−385	507	...	385
November	2,039	3,587	603	139	...	−778	628	...	−657
December	...	2,751	...	...	...	705	...	...	−705
TOTAL	16,628	13,725	2,033	1,184	...	−5,170	4,188	...	−178

Month	Outright transactions (continued): 5–10 years			Over 10 years			Total			Matched sale–purchase transactions (U.S. Government securities)	
	Gross purchases	Gross sales	Exch. or maturity shifts	Gross purchases	Gross sales	Exch. or maturity shifts	Gross purchases	Gross sales	Redemptions	Gross sales	Gross purchases
January	89	...	...	100	...	...	1,252	1,323	...	54,859	51,016
February	...	...	−906	...	...	450	379	1,974	1,100	40,128	44,270
March	370	...	...	147	...	...	2,367	50	31	44,976	44,129
April	191	...	...	145	...	...	2,341	...	...	42,262	42,799
May	101	...	1,526	74	...	895	935	737	300	40,634	40,362
June	176	...	−87	115	...	...	5,451	...	...	52,544	52,557
July	...	...	...	...	...	...	701	466	...	44,657	44,712
August	238	...	1,434	113	...	600	1,919	689	...	29,162	29,641
September	110	...	...	122	...	...	3,386	...	...	33,346	33,130
October	87	...	...	139	...	...	2,785	2,148	...	35,112	36,106
November	163	...	835	108	...	600	3,075	3,587	603	40,785	40,546
December	...	...	...	...	...	...	...	2,751	...	52,661	51,586
TOTAL	1,526	...	2,803	1,063	...	2,545	24,591	13,725	2,033	511,126	510,854

Month	Repurchase agreements (U.S. Government securities)		Net change in U.S. Government securities	Federal agency obligations: Outright		Federal agency obligations: Repurchase agreements, net	Bankers acceptances, net		Net change [1]
	Gross purchases	Gross sales		Gross purchases	Sales or redemptions		Outright	Repurchase agreements	
January	10,229	12,130	−5,815	...	*	−451	...	−954	−7,220
February	16,057	16,057	1,447	...	22	...	...	...	1,425
March	13,155	11,468	3,127	...	53	264	...	770	4,107
April	8,044	8,999	1,923	...	...	−128	...	−480	1,315
May	11,517	11,819	−674	...	34	−110	...	−17	−834
June	14,956	13,100	7,320	301	28	333	...	747	8,673
July	15,822	17,374	−1,261	...	4	−288	...	−753	−2,305
August	16,286	15,140	2,854	...	186	48	...	28	2,744
September	10,724	10,353	3,540	...	28	528	...	419	4,460
October	18,976	20,565	43	...	12	−521	...	−479	−969
November	7,719	8,383	−2,017	...	39	−127	...	−236	−2,419
December	8,133	7,049	−2,743	...	3	133	...	587	−2,026
TOTAL	151,618	152,436	7,743	301	409	−318	...	−366	6,951

[1] Net change in U.S. Government securities, Federal agency obligations, and bankers acceptances.
* Less than $500,000.

NOTE. Sales, redemptions, and negative figures reduce System holdings; all other figures increase them. Details may not add to totals because of rounding.

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Earnings and Expenses of Federal Reserve Banks during 1978

Dollars

Item	Total	Boston	New York	Philadelphia	Cleveland	Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
CURRENT EARNINGS													
Loans	66,432,544	3,245,915	9,505,085	4,540,535	2,808,745	7,617,868	7,351,144	8,002,815	4,379,601	2,379,465	4,626,585	8,079,987	3,894,799
Acceptances	16,143,824	....	16,143,824	....	....	....	....	....	....	....	....	....	....
U.S. Government securities	8,366,526,794	386,649,265	2,079,456,103	420,301,803	691,795,139	679,295,907	384,595,104	1,325,212,566	342,463,451	200,242,758	338,156,854	426,605,079	1,091,752,765
Foreign currencies	1,941,592	60,676	502,812	83,524	165,279	104,982	145,774	297,496	60,400	58,181	81,582	110,626	270,260
All other	4,345,647	159,728	3,071,930	20,775	45,080	51,256	114,519	247,834	114,748	318,625	88,150	60,489	52,513
TOTAL	8,455,390,401	390,115,584	2,108,679,754	424,946,637	694,814,243	687,070,013	392,206,541	1,333,760,711	347,018,200	202,999,029	342,953,171	434,856,181	1,095,970,337
CURRENT EXPENSES													
Salaries	328,005,818	21,916,219	77,095,640	15,843,596	20,125,859	25,613,957	30,521,132	40,934,900	16,885,253	13,056,958	21,031,226	15,798,212	29,182,866
Retirement and other benefits	89,828,248	6,170,811	19,745,485	4,676,623	5,722,567	6,939,376	7,828,091	11,724,781	4,927,587	3,242,429	5,814,665	4,431,156	8,604,677
Fees—Directors and others	4,553,267	361,886	1,350,579	297,948	215,747	434,473	151,513	280,821	200,363	196,552	173,461	124,940	764,984
Travel	8,420,713	510,537	1,372,752	273,216	717,420	663,603	881,833	927,940	375,496	419,643	704,029	510,303	1,063,941
Postage	12,269,928	625,889	1,977,393	459,742	726,178	1,006,258	909,737	1,252,553	887,402	881,342	1,408,394	605,317	1,529,723
Expressage	61,310,547	3,380,612	8,054,214	2,419,367	6,141,406	6,915,912	7,288,212	7,997,364	4,171,905	2,253,532	3,574,443	3,193,479	5,920,101
Telephone and telegraph	11,986,632	764,144	2,724,113	466,799	720,935	1,068,921	1,057,741	1,524,726	472,721	584,607	867,087	685,461	1,049,377
Printing and supplies	26,064,366	1,845,530	4,941,294	1,234,245	1,476,533	2,331,118	2,887,246	3,585,735	1,355,101	944,551	1,858,129	1,261,749	2,343,135
Taxes on real estate	13,904,609	2,615,882	2,398,563	1,225,982	759,548	1,233,877	626,317	1,530,299	449,261	1,521,196	496,218	457,860	589,606
Bank premises													
Depreciation	8,292,381	2,121,742	211,017	1,432,376	618,413	1,038,620	291,461	390,433	371,155	873,458	453,935	175,039	314,732
Maintenance and repairs	6,034,478	276,122	760,117	774,083	311,559	365,260	381,164	1,512,018	293,950	300,532	303,805	425,862	330,006
Utilities	11,981,469	1,812,969	2,076,645	1,165,795	983,107	910,099	888,337	1,094,763	662,713	488,586	670,510	593,295	634,650
Rent	8,749,213	414,629	5,248,169	15,668	71,697	839,045	621,596	863,535	119,290	50,021	25,517	8,960	471,086
Furniture and equipment													
Rentals	41,631,171	2,849,597	5,884,570	1,761,696	2,990,844	5,262,923	4,044,331	6,532,985	1,873,780	1,114,566	3,472,809	2,422,256	3,420,814
Depreciation	8,061,885	623,534	1,937,930	760,275	435,208	309,525	546,591	337,719	598,775	340,716	564,706	547,692	1,059,214
Cost of Federal Reserve currency	60,059,365	3,402,235	10,887,074	3,282,514	3,870,545	6,130,502	5,798,774	8,412,192	2,668,073	992,134	3,350,331	4,084,786	7,180,205
All other	15,901,094	1,394,469	3,246,252	731,161	1,181,469	1,284,297	1,111,798	1,188,328	727,243	897,884	982,830	1,154,605	2,000,758
TOTAL [1]	714,700,652	51,086,807	149,911,807	36,821,086	47,069,035	[1] 59,993,234	65,835,874	90,091,092	37,040,068	28,158,707	45,752,095	36,480,972	66,459,875
Reimbursements and recoveries	62,084,267	4,258,295	14,365,677	3,066,594	5,107,141	4,057,603	6,542,458	7,307,401	3,283,020	1,942,398	3,964,376	2,145,140	6,044,164
Net expenses	652,616,385	46,828,512	135,546,130	33,754,492	41,961,894	55,935,631	59,293,416	82,783,691	33,757,048	26,216,309	41,787,719	34,335,832	60,415,711

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PROFIT AND LOSS

urrent net earnings........	7,802,773,195	343,287,072	1,973,133,624	391,192,145	652,851,614	631,136,273	332,913,125	1,250,977,078	313,259,116	176,782,720	301,165,452	400,520,350	1,035,554,626
dditions to current net earnings...............	4,940,734	304,048	361,442	13,212	22,756	2,700,179	234,819	234,909	13,774	86,607	153,057	130,832	685,099
eductions from current net earnings													
Losses on sales of U.S. Government securities.	130,299,594	6,066,725	31,579,498	6,578,886	10,852,014	10,667,112	5,961,247	20,792,235	5,346,810	3,134,776	5,324,859	6,733,067	17,262,365
Losses on foreign exchange transactions...	505,682,038	15,676,143	130,971,648	21,744,328	42,982,973	27,306,830	37,926,153	77,369,352	15,676,143	15,170,461	21,238,646	28,823,876	70,795,485
All other................	2,082,588	47,347	582,453	105,555	55,742	143,039	377,346	270,521	55,676	33,731	67,674	105,515	237,989
Total deductions...	638,064,220	21,790,215	163,133,599	28,428,769	53,890.729	38,116,981	44,264,746	98,432,108	21,078,629	18,338,968	26,631,179	35,662,458	88,295,839
let deductions from current net earnings...........	633,123,486	21,486,167	162,772,157	28,415,557	53,867,973	35,416,802	44,029,927	98,197,199	21,064,855	18,252,361	26,478,122	35,531,626	87,610,740
ssessment for expenditures of Board of Governors [2].	53,321,700	1,660,900	13,851,000	2,269,800	4,522,400	2,843,100	4,015,100	8,130,000	1,667,200	1,596,100	2,256,600	3,021,300	7,488,200
let earnings before payments to U.S. Treasury.	7,116,328,009	320,140,005	1,796,510,467	360,506,788	594,461,241	592,876,371	284,868,098	1,144,649,879	290,527,061	156,934,259	272,430,730	361,967,424	940,455,686
ividends paid............	63,280,312	1,946,584	16,518,453	2,634,130	5,408,170	3,343,867	4,750,650	9,602,654	1,974,615	1,920,399	2,681,174	3,618,601	8,881,015
ayments to U.S. Treasury (interest on F.R. notes)..	7,005,779,497	317,624,721	1,766,858,714	358,221,808	584,291,421	587,995,404	277,118,648	1,129,478,225	287,219,396	151,703,760	267,573,506	353,757,723	923,936,171
ransferred to surplus......	47,268,200	568,700	13,133,300	−349,150	4,761,650	1,537,100	2,998,800	5,569,000	1,333,050	3,310,100	2,176,050	4,591,100	7,638,500
urplus, January 1.........	1,029,001,850	32,222,500	266,708,950	44,148,400	87,018,650	55,093,750	77,609,550	157,032,950	32,136,900	30,730,200	43,479,200	58,222,650	144,598,150
urplus, December 31.......	1,076,270,050	32,791,200	279,842,250	43,799,250	91 780,300	56,630,850	80,608,350	162,601,950	33,469,950	34,040,300	45,655,250	62,813,750	152,236,650

[1] The total expense for Richmond has been adjusted to exclude $2,354,532, which as allocated to the expenses of other Federal Reserve Banks for operation of the Federal eserve Communications System.

[2] For additional details, see the last three pages of the section "Board of Governors, Income and Expenses."

NOTE. Details may not add to totals because of rounding.

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7. Earnings and Expenses of Federal Reserve Banks, 1914–78

Dollars

Period or Bank	Current earnings	Current expenses	Net additions or deductions (−)	Assessment for expenditures of Board of Governors	Dividends paid	Payments to U.S. Treasury			Transferred to surplus (Sec. 13b)	Transferred to surplus (Sec. 7)
						Franchise tax	Under Sec. 13b	Interest on Federal Reserve notes		
All Federal Reserve Banks										
1914–15	2,173,252	2,018,282	5,875	302,304	217,463	...	...	...	...	...
1916	5,217,998	2,081,722	−193,001	192,277	1,742,775	...	...	...	...	...
1917	16,128,339	4,921,932	−1,386,545	237,795	6,804,186	1,134,234	...	...	...	1,134,234
1918	67,584,417	10,576,892	−3,908,574	382,641	5,540,684	...	...	...	...	48,334,341
1919	102,380,583	18,744,815	−4,673,446	594,818	5,011,832	2,703,894	...	...	...	70,651,778
1920	181,296,711	27,548,505	−3,743,907	709,525	5,654,018	60,724,742	...	...	...	82,916,014
1921	122,865,866	33,722,409	−6,314,796	741,436	6,119,673	59,974,466	...	...	...	15,993,086
1922	50,498,699	28,836,504	−4,441,914	722,545	6,307,035	10,850,605	...	...	...	−659,904
1923	50,708,566	29,061,539	−8,233,107	702,634	6,552,717	3,613,056	...	...	...	2,545,513
1924	38,340,449	27,767,886	−6,191,143	663,240	6,682,496	113,646	...	...	...	−3,077,962
1925	41,800,706	26,818,664	−4,823,477	709,499	6,915,958	59,300	...	...	...	2,473,808
1926	47,599,595	26,628,458	−3,637,668	721,724	7,329,169	818,150	...	...	...	8,464,426
1927	43,024,484	26,739,327	−2,457,792	779,116	7,754,539	249,591	...	...	...	5,044,119
1928	64,052,860	26,207,133	−5,026,029	697,677	8,458,463	2,584,659	...	...	...	21,078,899
1929	70,955,496	28,909,469	−4,861,642	781,644	9,583,911	4,283,231	...	...	...	22,535,597
1930	36,424,044	27,533,141	−93,136	809,585	10,268,598	17,308	...	...	...	−2,297,724
1931	29,701,279	26,322,110	311,451	718,554	10,029,760	...	...	...	...	−7,057,694
1932	50,018,817	25,562,571	−1,413,192	728,810	9,282,244	2,011,418	...	...	...	11,020,582
1933	49,487,318	28,422,677	−12,307,074	800,160	8,874,262	...	...	...	...	−916,855
1934	48,902,813	27,869,374	−4,430,008	1,372,022	8,781,661	...	...	...	−60,323	6,510,071
1935	42,751,959	30,171,545	−1,736,758	1,405,898	8,504,974	...	297,667	...	27,695	607,422
1936	37,900,639	28,194,457	485,817	1,679,566	7,829,581	...	227,448	...	102,880	352,524
1937	41,233,135	27,052,234	−1,631,274	1,748,380	7,940,966	...	176,625	...	67,304	2,616,352
1938	36,261,428	27,186,684	2,232,134	1,724,924	8,019,137	...	119,524	...	−419,140	1,862,433
1939	38,500,665	27,025,391	2,389,555	1,621,464	8,110,462	...	24,579	...	−425,653	4,533,977
1940	43,537,805	27,461,466	11,487,697	1,704,011	8,214,971	...	82,152	...	−54,456	17,617,358
1941	41,380,095	31,123,609	720,636	1,839,541	8,429,936	...	141,465	...	−4,333	570,513
1942	52,662,704	36,877,718	−1,568,208	1,746,326	8,669,076	...	197,672	...	49,602	3,554,101
1943	69,305,715	41,129,934	23,768,282	2,415,630	8,911,342	...	244,726	...	135,003	40,237,362
1944	104,391,829	46,879,564	3,221,880	2,296,357	9,500,126	...	326,717	...	201,150	48,409,795
1945	142,209,546	46,376,762	−830,007	2,340,509	10,182,851	...	247,659	...	262,133	81,969,625
1946	150,385,033	54,975,323	−625,991	2,259,784	10,962,160	...	67,054	...	27,708	81,467,013
1947	158,655,566	62,753,308	1,973,001	2,639,667	11,523,047	...	35,605	75,223,818	86,772	8,366,350
1948	304,160,818	69,466,518	−34,317,947	3,243,670	11,919,809	...	...	166,690,356	...	18,522,518
1949	316,536,930	74,235,176	−12,122,274	3,242,500	12,329,373	...	...	193,145,837	...	21,461,770

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1950	275,838,994	77,138,071	36,294,117	3,433,700	13,082,992	...	...	196,628,858	...	21,849,490
1951	394,656,072	91,373,589	−2,127,889	4,095,497	13,864,750	...	...	254,873,588	...	28,320,759
1952	456,060,260	100,572,489	1,583,988	4,121,602	14,681,788	...	...	291,934,634	...	46,333,735
1953	513,037,237	109,415,220	−1,058,993	4,099,800	15,558,377	...	...	342,567,985	...	40,336,862
1954	438,486,040	105,558,331	−133,641	4,174,600	16,442,236	...	...	276,289,457	...	35,887,775
1955	412,487,931	105,865,923	−265,456	4,194,100	17,711,937	...	...	251,740,721	...	32,709,794
1956	595,649,092	115,842,696	−23,436	5,339,800	18,904,897	...	...	401,555,581	...	53,982,682
1957	763,347,530	124,306,103	−7,140,914	7,507,900	20,080,527	...	...	542,708,405	...	61,603,682
1958	742,068,150	131,804,455	124,175	5,917,200	21,197,452	...	...	524,058,650	...	59,214,569
1959	886,226,116	138,232,106	98,247,253	6,470,600	22,721,687	...	...	910,649,768	...	−93,600,791
1960	1,103,385,257	147,348,575	13,874,702	6,533,700	23,948,225	...	...	896,816,359	...	42,613,100
1961	941,648,170	155,009,475	3,481,628	6,265,100	25,569,541	...	...	687,393,382	...	70,892,300
1962	1,048,508,335	169,481,234	−55,779	6,654,900	27,412,241	...	...	799,365,981	...	45,538,200
1963	1,151,120,060	179,700,557	614,835	7,572,800	28,912,019	...	...	879,685,219	...	55,864,300
1964	1,343,747,303	188,740,689	725,948	8,655,200	30,781,548	...	...	1,582,118,614	...	−465,822,800
1965	1,559,484,027	195,713,790	1,021,614	8,576,396	32,351,602	...	...	1,296,810,053	...	27,053,800
1966	1,908,499,896	198,379,526	996,230	9,021,600	33,696,336	...	...	1,649,455,164	...	18,943,500
1967	2,190,403,752	209,351,250	2,093,876	10,769,596	35,027,312	...	...	1,907,498,270	...	29,851,200
1968	2,764,445,943	228,152,172	8,519,996	14,198,198	36,959,336	...	...	2,463,628,983	...	30,027,250
1969	3,373,360,559	259,953,236	−557,553	15,020,084	39,236,599	...	...	3,019,160,638	...	39,432,450
1970	3,877,218,444	300,145,586	11,441,829	21,227,800	41,136,551	...	...	3,493,570,636	...	32,579,700
1971	3,723,369,921	344,550,798	94,266,075	32,634,002	43,488,074	...	...	3,356,559,873	...	40,403,250
1972	3,792,334,523	379,371,852	−49,615,790	35,234,499	46,183,719	...	...	3,231,267,663	...	50,661,000
1973	5,016,769,328	450,705,676	−80,653,488	44,411,700	49,139,682	...	...	4,340,680,482	...	51,178,300
1974	6,280,090,965	506,424,874	−78,487,237	41,116,600	52,579,643	...	...	5,549,999,411	...	51,483,200
1975	6,257,936,784	551,488,714	−202,369,615	33,577,201	54,609,555	...	...	5,382,064,098	...	33,827,600
1976	6,623,220,383	606,948,264	7,310,500	41,827,700	57,351,487	...	...	5,870,463,382	...	53,940,050
1977	6,891,317,498	623,859,582	−177,033,463	47,366,100	60,182,278	...	...	5,937,148,425	...	45,727,650
1978	8,455,390,401	652,617,206	−633,123,486	53,321,700	63,280,312	...	...	7,005,779,497	...	47,268,200
TOTAL, 1914–78	76,479,145,130	8,535,255,138	−1,036,422,554	538,615,908	1,235,051,957	149,138,300	2,188,893	63,777,533,787	−3,657	1,204,942,249
Aggregate for each Federal Reserve Bank, 1914–78										
Boston	3,743,172,097	587,280,874	−35,167,577	24,457,386	61,629,903	7,111,395	280,843	2,984,222,683	135,411	42,886,025
New York	19,601,775,744	1,806,618,573	−268,397,272	144,742,986	352,598,874	68,006,262	369,116	16,644,377,253	−433,413	317,098,821
Philadelphia	4,139,612,960	468,178,654	−41,592,461	29,389,218	75,320,802	5,558,901	722,406	3,460,430,385	290,661	58,129,472
Cleveland	6,106,303,422	639,139,573	−90,198,197	48,068,290	114,173,080	4,842,447	82,930	5,104,794,718	−9,906	105,014,093
Richmond	5,596,259,955	666,076,056	−54,133,017	28,054,276	60,413,658	6,200,189	172,493	4,718,771,125	−71,517	62,510,658
Atlanta	3,989,307,324	665,623,614	−78,796,147	34,977,660	70,942,160	8,950,561	79,264	3,044,057,537	5,491	85,874,890
Chicago	12,174,189,654	1,142,070,018	−165,664,337	79,705,772	172,306,019	25,313,526	151,045	10,411,036,551	11,682	177,930,704
St. Louis	2,958,791,412	484,607,238	−34,819,927	18,291,672	41,929,758	2,755,629	7,464	2,337,816,661	−26,515	38,589,578
Minneapolis	1,676,000,596	334,102,448	−27,236,054	13,509,315	30,013,681	5,202,900	55,615	1,227,898,196	64,874	37,917,513
Kansas City	3,076,735,067	505,604,355	−41,786,560	22,129,309	49,578,844	6,939,100	64,213	2,400,846,160	−8,674	49,795,200
Dallas	3,430,539,847	429,497,593	−58,940,696	28,594,073	62,426,249	560,049	102,083	2,783,272,539	55,337	67,091,228
San Francisco	9,986,457,052	806,456,142	−139,690,311	66,695,951	143,718,929	7,697,341	101,421	8,660,009,979	−17,089	162,104,067
TOTAL	76,479,145,130	8,535,255,138	−1,036,422,554	538,615,908	1,235,051,957	149,138,300	2,188,893	63,777,533,787	−3,657	[1] 1,204,942,249

[1] The $1,204,942,249 transferred to surplus was reduced by direct charges of $500,000 for charge-off on Bank premises (1927), $139,299,557 for contributions to capital of the Federal Deposit Insurance Corporation (1934), and $3,657 net upon elimination of Sec. 13b surplus (1958), and was increased by $11,131,013 transferred from reserves for contingencies (1945), leaving a balance of $1,076,270,048 on Dec. 31, 1978.

NOTE. Details may not add to totals because of rounding.

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8. Bank Premises of Federal Reserve Banks and Branches, December 31, 1978

Dollars

Federal Reserve Bank or branch	Cost				Net book value	Other real estate [3]
	Land	Buildings (including vaults) [1]	Building machinery and equipment	Total [2]		
Boston	20,240,081	88,016,595	....	108,256,676	105,756,972	2,443,426
Annex	27,840	89,202	44,538	161,580	139,747	....
New York	3,436,277	11,065,009	12,128,539	26,629,825	7,070,178	9,439,872
Annex	477,863	1,136,219	716,471	2,330,553	477,862	....
Buffalo	673,076	2,768,584	1,610,759	5,052,419	2,417,112	....
Philadelphia	1,876,601	51,803,403	4,828,637	58,508,641	54,999,804	....
Cleveland	1,000,000	4,964,238	3,665,369	9,629,607	1,386,582	1,224,363
Cincinnati	1,980,331	13,541,023	7,521,727	23,043,081	17,407,921	....
Pittsburgh	1,658,376	4,510,657	2,937,674	9,106,707	4,342,637	....
Richmond	1,962,349	70,577,480	....	72,539,829	71,782,242	....
Annex	522,733	3,725,466	3,511,136	7,759,335	4,924,924	....
Baltimore	738,436	2,434,345	1,189,949	4,362,730	2,217,676	3,870,130
Charlotte	347,071	1,102,322	677,037	2,126,430	1,007,673	1,634,312
Atlanta	1,202,255	10,803,860	3,558,580	15,564,695	10,503,030	1,905,667
Birmingham	340,775	1,905,770	1,019,618	3,266,163	1,564,188	....
Jacksonville	164,004	1,706,794	749,369	2,620,167	987,426	....
Annex	107,925	76,236	15,842	200,003	161,925	....
Miami	1,667,108	....	....	1,667,108	1,667,108	....
Nashville	592,342	1,474,678	1,147,075	3,214,095	1,559,855	....
New Orleans	2,911,128	2,764,347	1,465,131	7,140,606	5,048,721	283,753
Chicago	4,511,942	14,473,333	10,891,182	29,876,457	12,721,687	....
Annex	50,000	302,248	93,916	446,164	404,197	....
Detroit	797,734	2,910,976	1,952,171	5,660,881	2,511,095	....
St. Louis	700,378	2,981,037	3,660,178	7,341,593	2,017,313	....
Little Rock	800,104	2,037,868	1,015,628	3,853,600	2,606,217	....
Louisville	700,075	2,945,104	1,159,753	4,804,932	2,508,746	....
Memphis	1,135,623	4,263,255	2,126,755	7,525,633	5,732,882	....
Minneapolis	1,394,384	23,606,389	10,928,091	35,928,864	28,409,784	....
Helena	65,681	101,000	61,906	228,587	94,942	139,735
Kansas City	1,338,737	8,691,064	4,302,234	14,332,035	7,413,924	....
Denver	2,997,746	3,209,227	2,336,576	8,543,549	5,872,347	....
Oklahoma City	646,385	2,428,550	1,477,170	4,552,105	3,765,969	....
Omaha	1,030,226	1,504,365	817,214	3,351,805	1,935,157	457,973
Dallas	3,687,482	4,664,970	3,570,804	11,923,256	6,199,767	....
El Paso	262,477	787,728	393,301	1,443,506	828,056	....
Houston	1,959,770	1,408,574	729,262	4,097,606	3,109,355	....
San Antonio	448,596	1,400,390	570,847	2,419,833	1,401,773	....
San Francisco	475,488	3,459,240	2,121,193	6,055,921	1,184,944	17,223,440
Annex	247,201	124,000	62,078	433,279	353,679	....
Los Angeles	644,238	5,062,628	1,756,471	7,463,337	3,288,503	....
Portland	207,380	1,682,683	649,432	2,539,495	1,561,386	....
Salt Lake City	480,222	2,129,722	724,434	3,334,378	1,982,812	....
Seattle	274,772	1,904,457	1,141,558	3,320,787	1,327,005	....
TOTAL	66,783,212	366,545,036	99,329,605	532,657,853	392,655,123	38,622,671

[1] Figures include expenditures for construction at some offices pending allocation to appropriate accounts.
[2] Figures exclude charge-offs of $17,698,968 prior to 1952.
[3] Figures include acquisitions for banking-house purposes, and premises formerly occupied by Federal Reserve Banks and being held pending sale.

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9. Volume of Operations in Principal Departments of Federal Reserve Banks, 1975–78

Operation	1978	1977	1976	1975
	Millions of pieces [1]			
Loans	(2)	(2)	(2)	(2)
Currency received and counted	8,537	8,186	r 8,061	7,666
Currency verified and destroyed	2,621	2,609	2,671	2,625
Coin received and counted	18,096	16,563	15,925	15,412
Checks handled				
U.S. Government checks	721	740	768	844
Postal money orders	125	139	169	176
All other [3]	14,107	13,312	12,287	11,410
Collection items handled				
U.S. Government coupons paid	5	6	8	9
All other	5	4	4	16
Issues, redemptions, and exchanges of U.S. Government securities	281	286	289	277
Transfers of funds	29	25	21	17
Food stamps redeemed	1,906	1,901	2,003	2,493
	Amounts (millions of dollars)			
Loans	138,928	77,511	17,697	39,822
Currency received and counted	81,175	75,933	71,011	66,065
Currency verified and destroyed	16,443	14,952	14,606	14,279
Coin received and counted	2,495	2,239	2,109	2,120
Checks handled				
U.S. Government checks	439,907	416,386	399,468	349,957
Postal money orders	5,534	5,661	6,305	8,524
All other [3]	7,111,254	5,499,856	4,645,069	4,256,924
Collection items handled				
U.S. Government coupons paid	2,028	3,276	4,748	6,175
All other	28,769	26,959	23,929	26,973
Issues, redemptions, and exchanges of U.S. Government securities	8,036,749	8,835,730	7,051,978	4,575,365
Transfers of funds	50,482,656	43,165,467	35,617,756	31,392,865
Food stamps redeemed	7,251	7,422	7,883	7,940

r Revised.
1 Packaged items handled as a single item are counted as one piece.
2 The number handled (in thousands) was as follows: 1978, 31; 1977, 12; 1976, 4; 1975, 6.
3 This is exclusive of checks drawn on Federal Reserve Banks.

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10. Principal Operations of Federal Reserve Banks—Expense, Ratio of Expense for Each Operation to Total Expenses, and Average Number of Employees, 1975–78

Expenses in thousands of dollars; number of employees in thousands; ratios in per cent

Operation and item	1978 [1]	1977 [1]	1976	1975
Check clearing operations [2]				
Expense	259,983	246,981	135,209	130,024
Ratio to total expenses	36.4	36.2	20.5	21.7
Average number of employees	6.3	6.5	6.3	7.1
Currency function				
Expense	187,864	182,875	114,036	99,306
Ratio to total expenses	26.3	26.8	17.3	16.6
Average number of employees	2.0	2.2	2.3	2.4
Fiscal agency operations				
Expense	76,837	73,002	48,158	45,307
Ratio to total expenses	10.7	10.7	7.3	7.6
Average number of employees	1.9	2.0	2.3	2.4
Bank supervision				
Expense	58,303	52,702	23,322	19,936
Ratio to total expenses	8.2	7.7	3.5	3.3
Average number of employees	1.3	1.3	1.1	1.0
Other operations [3]				
Expense	131,713	126,318	29,919	27,623
Ratio to total expenses	18.4	18.6	4.6	4.6
Average number of employees	2.2	2.2	1.4	1.5
General administration and support				
Expense	....	....	307,806	277,014
Ratio to total expenses	....	....	46.8	46.2
Average number of employees	9.8	10.1	11.1	11.3
Accounting	....	....	23,298	21,702
Auditing	....	....	8,050	7,289
Bank administration	....	....	38,519	33,226
Data processing	....	....	39,814	34,652
Occupancy	....	....	64,292	58,391
Personnel	....	....	27,219	26,449
Protection	....	....	24,501	22,255
Other	....	....	82,113	73,050
TOTAL EXPENSES	714,700	681,878	658,450	599,210
Less reimbursements	62,084	58,018	51,502	47,721
NET EXPENSES	652,616	623,860	606,948	551,489

[1] Under a new expense-accounting system, certain support activities were reclassified as operations and all general administration and support costs were allocated to operations beginning in 1977.
[2] Figures include automated clearinghouse and noncash collections.
[3] Figures include mainly economic research and statistics, foreign operations, and lending and credit.

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11. Number and Salaries of Officers and Employees of Federal Reserve Banks, December 31, 1978

Federal Reserve Bank (including branches)	President	Other officers		Employees			Total	
	Annual salary (dollars)	Number	Annual salaries (dollars)	Number: Full-time	Number: Part-time	Annual salaries (dollars)	Number	Annual salaries (dollars)
Boston	80,000	45	1,591,400	1,353	171	19,799,329	1,570	21,470,729
New York	110,000	131	5,758,050	4,334	99	66,550,269	4,565	72,418,319
Philadelphia	70,500	38	1,301,250	1,037	95	13,908,764	1,171	15,280,514
Cleveland	79,400	40	1,357,100	1,416	63	17,803,058	1,520	19,239,558
Richmond	69,450	63	2,169,600	1,928	76	23,320,479	2,068	25,559,529
Atlanta	83,000	64	2,133,150	2,271	36	26,992,363	2,372	29,208,513
Chicago	90,000	60	2,103,000	2,829	133	35,958,669	3,023	38,151,669
St. Louis	74,500	43	1,425,635	1,160	67	14,281,465	1,271	15,781,600
Minneapolis	57,700	32	1,151,600	843	7	10,825,900	883	12,035,200
Kansas City	60,700	53	1,635,000	1,566	73	18,560,843	1,693	20,256,543
Dallas	66,600	36	1,136,800	1,190	42	13,995,745	1,269	15,199,145
San Francisco	90,000	70	2,425,000	1,824	73	25,479,762	1,968	27,994,762
TOTAL	931,850	675	24,187,585	21,751	935	287,476,646	23,373	312,596,081

12. Federal Reserve Bank Interest Rates, December 31, 1978

Per cent per annum

Federal Reserve Bank	Loans to member banks: Under Secs. 13 and 13a [1]	Under Sec. 10(b) [2]: Regular rate	Under Sec. 10(b) [2]: Special rate [3]	Loans to all others under last paragraph of Sec. 13 [4]
Boston	9½	10	10½	12½
New York	↑	↑	↑	↑
Philadelphia				
Cleveland				
Richmond				
Atlanta				
Chicago				
St. Louis				
Minneapolis				
Kansas City				
Dallas	↓	↓	↓	↓
San Francisco	9½	10	10½	12½

[1] This rate applies to discounts of eligible paper and advances secured by such paper or by U.S. Government obligations or any other obligations eligible for purchase by a Federal Reserve Bank.

[2] This rate applies to advances secured to the satisfaction of the Federal Reserve Bank. Advances secured by mortgages on 1- to 4-family residential property are made at the Section 13 rate.

[3] The rate is applicable to special advances described in Section 201.2(e)(2) of Regulation A.

[4] This rate applies to advances to individuals, partnerships, or corporations other than member banks that are secured by direct obligations of, or obligations fully guaranteed as to principal and interest by, the U.S. Government or any of its agencies.

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13. Member Bank Reserve Requirements

Per cent of deposits

Through July 13, 1966

Effective date [1]	Net demand deposits [2]			Time deposits (all classes of banks)
	Central reserve city banks	Reserve city banks	Country banks	
1917—June 21	13	10	7	3
1936—Aug. 16	19½	15	10½	4½
1937—Mar. 1	22¾	17½	12¼	5¼
May 1	26	20	14	6
1938—Apr. 16	22¾	17½	12	5
1941—Nov. 1	26	20	14	6
1942—Aug. 20	24	...	...	...
Sept. 14	22	...	...	...
Oct. 3	20	...	...	...
1948—Feb. 27	22	...	...	...
June 11	24	...	...	...
Sept. 24, 16	26	22	16	7½
1949—May 5, 1	24	21	15	7
June 30, July 1	...	20	14	6
Aug. 1	...	...	13	...
Aug. 11, 16	23½	19½	12	5
Aug. 18	23	19	...	...
Aug. 25	22½	18½	...	...
Sept. 1	22	18	...	...
1951—Jan. 11, 16	23	19	13	6
Jan. 25, Feb. 1	24	20	14	...
1953—July 9, 1	22	19	13	...
1954—June 24, 16	21	...	...	5
July 29, Aug. 1	20	18	12	...
1958—Feb. 27, Mar. 1	19½	17½	11½	...
Mar. 20, Apr. 1	19	17	11	...
Apr. 17	18½	...	...	...
Apr. 24	18	16½	...	...
1960—Sept. 1	17½	...	...	...
Nov. 24	...	...	12	...
Dec. 1	16½	...	...	...
1962—July 28	[3]	...	...	...
Oct. 25, Nov. 1	...	...	...	4

July 14, 1966, through Nov. 8, 1972 (deposit intervals in millions of dollars)

Effective date [1]	Net demand deposits [2]				Time deposits [4] (all classes of banks)		
	Reserve city banks		Country banks		Savings	Other time	
	0–5	Over 5	0–5	Over 5		0–5	Over 5
1966—July 14, 21	[5] 16½		[5] 12		[5] 4	[5] 4	5
Sept. 8, 15	...		...		...	...	6
1967—Mar. 2	...		...		3½	3½	...
Mar. 16	...		...		3	3	...
1968—Jan. 11, 18	16½	17	12	12½	...	...	...
1969—Apr. 17	17	17½	12½	13	...	...	...
1970—Oct. 1	...	...	...	...	...	...	5

[1] Reserves required during the period from inception of the Federal Reserve System until June 20, 1917, were not strictly comparable with later requirements; they were based on aggregate amounts of deposits, and reserve balances with the Reserve Banks were increased in stages.

When two dates are shown, the first applies to the change at central reserve or reserve city banks and the second to the change at country banks.

[2] Demand deposits subject to reserve requirements, beginning Aug. 23, 1935, have been total demand deposits minus cash items in process of collection and demand balances due from domestic banks (also minus war loan and Series E bond accounts during the period Apr. 13, 1943–June 30, 1947).

All required reserves were held on deposit with Federal Reserve Banks from June 21, 1917, until late 1959. Since then, member banks have also been allowed to count vault cash as reserves, as follows: country banks—in excess of 4 and 2½ per cent of net demand deposits effective Dec. 1, 1959, and Aug.

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13.—Continued

Beginning Nov. 9, 1972 (deposit intervals in millions of dollars)

Effective date	Net demand deposits[2,6]					Time deposits[4]						
							Other time[7]					
							0–5, by time to maturity[8]			Over 5, by time to maturity[8]		
	0–2	2–10	10–100	100–400	Over 400	Savings	30–179 days	180 days to 4 yrs.	4 yrs. or more	30–179 days	180 days to 4 yrs.	4 yrs. or more
1972—Nov. 9	8	10	12	[9]16½	17½	[5]3	[5]3			[5]5		
Nov. 16				13								
1973—July 19		10½	12½	13½	18							
1974—Dec. 12					17½					6	3	
1975—Feb. 13	7½	10	12	13	16½							
Oct. 30							3		[10]1		3	[10]1
1976—Jan. 8							3	[10]2½			[10]2½	
Dec. 30	7	9½	11¾	12¾	16¼							
In effect Dec. 31, 1978	7	9½	11¾	12¾	16¼	3	3	[10]2½	[10]1	6	[10]2½	[10]1

Legal limits—Dec. 31, 1978	Minimum	Maximum
Net demand deposits		
Reserve city banks	10	22
Other banks	7	14
Time deposits	3	10

25, 1960, respectively; central reserve city and reserve city banks—in excess of 2 and 1 per cent effective Dec. 3, 1959, and Sept. 1, 1960, respectively; all member banks were allowed to count all vault cash as reserves effective Nov. 24, 1960.

[2] In graduated requirement schedules, each deposit interval applies to that part of the deposits of each bank. Beginning Oct. 16, 1969, Regulation M required reserves against (a) net balances due from domestic offices to their foreign branches and (b) foreign-branch loans to U.S. residents; Regulation D imposed a similar requirement against (c) borrowings from foreign banks by domestic offices of a member bank. Limited reserve-free base amounts were originally permitted under Regulation M but were eliminated for (b) effective June 21, 1973, and were lowered in steps for (a) and (c) until eliminated effective Mar. 14, 1974. Beginning June 21, 1973, loans aggregating $100,000 or less to any U.S. resident have been excluded from computations, as have total loans of a bank to U.S. residents if not exceeding $1 million. The applicable reserve percentage, which was originally 10 per cent, was increased to 20 per cent on Jan. 7, 1971; reduced to 8 per cent on June 21, 1973, to 4 per cent on May 22, 1975, and to zero on Aug. 24, 1978. Effective Dec. 1, 1977, the reserve required against deposits that foreign branches of U.S. banks use for lending to U.S. residents was reduced to 1 per cent, and on Aug. 24, 1978, it was reduced to zero. For details see Regulations D and M as described in "Record of Policy Actions of the Board of Governors," in previous Annual Reports.

[3] Authority of the Board of Governors to classify or reclassify cities as central reserve cities was terminated effective July 28, 1962.

[4] Time deposits such as Christmas and vacation club accounts became subject to the same requirements as savings deposits, effective Jan. 5, 1967. Negotiable orders of withdrawal (NOW) accounts were defined in the Board's Regulation Q as savings deposits beginning Jan. 1, 1974.

The last three paragraphs of note 2 above are also relevant to time deposits.

[5] This rate had been established in the earlier structure. It remained the same in the new structure established this date.

[6] Effective Nov. 9, 1972, a new criterion was adopted to designate reserve cities, and on the same date requirements for reserves against net demand deposits of member banks were restructured to provide that each member bank will maintain reserves related to the size of its net demand deposits. The new reserve city designations are as follows: A bank having net demand deposits of more than $400 million is considered to have the character of business of a reserve city bank, and the presence of the head office of such a bank constitutes designation of that place as a reserve city. Cities in which there are Federal Reserve Banks or branches are also reserve cities. Any bank, wherever located, having net demand deposits of $400 million or less is considered to have the character of business of banks outside of reserve cities and is permitted to maintain reserves at ratios set for banks not in reserve cities.

[7] Beginning Nov. 2, 1978, a supplementary reserve requirement of 2 per cent was added to the existing requirements for time deposits of $100,000 or more and for certain other liabilities.

[8] From June 21, 1973, through Dec. 11, 1974, member banks, except as noted below, were subject to a marginal reserve requirement against increases in the aggregate of the following types of obligations: (a) outstanding time deposits of $100,000 or more, (b) outstanding funds obtained by the bank through issuance by a bank's affiliate of obligations subject to the existing reserve requirements on time deposits, and (c) beginning July 12, 1973, funds from sales of finance bills. For the period June 21 through Aug. 29, 1973, (a) included only single-maturity time deposits. The requirement applied to balances above a specified base, but was not applicable to banks having obligations of these types aggregating less than $10 million. Including the basic requirement (5 per cent during the entire period), requirements were as follows: 8 per cent for (a) and (b) from June 21 through Oct. 3, 1973, and for (c) from July 12 through Oct. 3, 1973; 11 per cent from Oct. 4 through Dec. 26, 1973; and 8 per cent from Dec. 27, 1973, through Sept. 18, 1974. Beginning Sept. 19, the 8 per cent requirement applied only to those obligations in (a), (b), and (c) with initial maturities of less than 120 days, and effective Dec. 12, 1974, the remaining marginal reserve was removed on this type of obligation issued to mature in less than 4 months. For details, see "Record of Policy Actions of the Board of Governors" in 1973 and 1974 Annual Reports.

[9] The 16½ per cent requirement applied only for 1 week and solely to former reserve city banks. For other banks, the 13 per cent requirement was contintued in this deposit interval.

[10] The average of reserves on savings and other time deposits must be at least 3 per cent, the legal minimum.

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14. Maximum Interest Rates Payable on Time and Savings Deposits

Per cent per annum

Nov. 1, 1933–July 19, 1966

Type of deposit	Effective date							
	Nov. 1, 1933	Feb. 1, 1935	Jan. 1, 1936	Jan. 1, 1957	Jan. 1, 1962	July 17, 1963	Nov. 24, 1964	Dec. 6, 1965
Savings deposits								
12 months or more	} 3	2½	2½	3	4	4	} 4	4
Less than 12 months					3½	3½		
Postal savings deposits [1]								
12 months or more	} 3	2½	2½	3	4	4	} 4	4
Less than 12 months					3½	3½		
Other time deposits [2]								
12 months or more	} 3	2½	2½	3	4	} 4	4½	} 5½
6–12 months					3½			
90 days to 6 months	3	2½	2	2½	2½			
Less than 90 days (30–89 days)	3	2½	1	1	1	1	4	

July 20, 1966–June 30, 1973

Type of deposit	Effective date			
	July 20, 1966	Sept. 26, 1966	Apr. 19, 1968	Jan. 21, 1970
Savings deposits	4	4	4	4½
Other time deposits [2]				
Multiple maturity [3]				
30–89 days	4	4	4	4½
90 days to 1 year	} 5	5	5	5
1–2 years				5½
2 years or more				5¾
Single-maturity				
Less than $100,000				
30 days to 1 year	} 5½		5	5
1–2 years				5½
2 years or more				5¾
$100,000 or more				
30–59 days	} 5½	5½	5	(4)
60–89 days			5¾	(4)
90–179 days			6	(4)
180 days to 1 year			} 6¼	(4)
1 year or more				(4)

Beginning July 1, 1973

Type of deposit	Effective date					
	July 1, 1973	Nov. 1, 1973	Nov. 23, 1974	Dec. 23, 1974	July 6, 1977	June 1, 1978
Savings deposits	5	5	5	5	5	....
Other time deposits (multiple- and single-maturity) [2, 3]						
Less than $100,000						
30–89 days	5	5	5	5	5	....
90 days to 1 year	5½	5½	5½	5½	5½	....
1–2½ years	6	6	6	6	6	....
2½ years or more	6½	6½	6½	6½	6½	....
Minimum denomination of $1,000 [5]						
4–6 years	} (6)	7¼	7¼	7¼	7¼	....
6 years				7½	7½	....
8 years or more	....	....	....	....	....	7¾
Governmental units	(7)	(7)	7½	7¾	7¾	8
Individual retirement accounts and Keogh (H.R. 10) plans [8]	....	....	....	....	7¾	8
Money market time deposits [9]	....	....	....	....	....	(10)
$100,000 or more	(4)	(4)	(4)	(4)	(4)	....

[1] Closing date for the Postal Savings System was Mar. 28, 1966.

[2] For exceptions with respect to foreign time deposits, see ANNUAL REPORT for 1962, p. 129; 1965, p. 233; 1968, p. 69.

[3] Multiple-maturity time deposits include deposits that are automatically renewable at maturity without action by the depositor and deposits that are payable after written notice of withdrawal.

For additional notes see opposite page.

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15. Margin Requirements [1]

Per cent of market value

Effective date	For credit extended under Regulation T (brokers and dealers), U (banks), G (others than brokers, dealers, or banks), and X (borrowers)			
	Margin stocks	Convertible bonds	Short sales, T only	Writing options, T only [2]
11-01-37	40	....	50	....
2-05-45	50	....	50	....
7-05-45	75	....	75	....
1-21-46	100	....	100	....
2-01-47	75	....	75	....
3-03-49	50	....	50	....
1-17-51	75	....	75	....
2-20-53	50	....	50	....
1-04-55	60	....	60	....
4-23-55	70	....	70	....
1-16-58	50	....	50	....
8-05-58	70	....	70	....
10-16-58	90	....	90	....
7-28-60	70	....	70	....
7-10-62	50	....	50	....
11-06-63	70	....	70	....
3-11-68	70	50	70	....
6-08-68	80	60	80	....
5-06-70	65	50	65	....
12-06-71	55	50	55	....
11-24-72	65	50	65	....
1-03-74	50	50	50	....
1-01-77	50	50	50	30

[1] Regulations T, U, G, and X, adopted by the Board of Governors pursuant to the Securities Exchange Act of 1934, limit the amount of credit to purchase and carry "margin securities" and "margin stock" (as defined in the regulations) when such credit is collateralized by securities. Margin requirements are the difference between the market value (100 per cent) and the maximum loan value of collateral as prescribed by the Board. Regulation T was adopted effective Oct. 15, 1934; Regulation U, effective May 1, 1936; Regulation G, effective Mar. 11, 1968; and Regulation X, effective Nov. 1, 1971.

For earlier data, see *Banking and Monetary Statistics, 1914–1941*, 2nd printing (Part I only) (Board of Governors of the Federal Reserve System, August 1976), Table 145, p. 504.

[2] The margin is expressed as a per cent of the current market value of the stock underlying the option.

Notes to Table 14 on opposite page

[4] The limit on rates on single-maturity time deposits of $100,000 or more has been suspended. The maximum rates that became effective Jan. 21, 1970, and the dates when they were suspended are as follows:

30–59 days	6¼ per cent	June 24, 1970
60–89 days	6½ per cent	
90–179 days	6¾ per cent	
180 days to 1 year	7 per cent	May 16, 1973
1 year or more	7½ per cent	

Rates on multiple-maturity time deposits in denominations of $100,000 or more were suspended July 16, 1973, when the distinction between single- and multiple-maturity deposits was eliminated.

[5] The $1,000 minimum-denomination requirement does not apply to time deposits representing funds contributed to an individual retirement account established pursuant to 26 U.S.C. (I.R.C. 1954), Sec. 408, or to a Keogh (H.R. 10) plan established pursuant to 26 U.S.C. (I.R.C. 1954), Sec. 401. These exceptions were effective Dec. 4, 1975, and Nov. 8, 1976, respectively.

[6] Between July 1, and Oct. 31, 1973, there was no ceiling for certificates maturing in 4 years or more with minimum denominations of $1,000. The amount of such certificates that a bank could issue was limited to 5 per cent of its total time and savings deposits. Sales in excess of that amount were subject to the 6½ per cent ceiling that applies to time deposits maturing in 2½ years or more.

Effective Nov. 1, 1973, a ceiling rate of 7¼ per cent was imposed on certificates maturing in 4 years or more with minimum denominations of $1,000. There is no limitation on the amount of these certificates that banks may issue.

[7] Prior to Nov. 27, 1974, no distinction was made between the time deposits of governmental units and of other holders insofar as Regulation Q ceilings on rates payable were concerned. Effective Nov. 27, 1974, governmental units were permitted to hold savings deposits and could receive interest rates on time deposits with denominations under $100,000, irrespective of maturity, as high as the maximum rate permitted on such deposits at any Federally insured depositary institution. Effective June 1, 1978, the maximum rate on such governmental-unit time deposits was set as high as the maximum permitted on such deposits maturing in 6 months (26 weeks) or more at any Federally insured commercial bank, mutual savings bank, or savings and loan association.

[8] Three-year minimum maturity.

[9] These deposits must have a maturity of exactly 26 weeks and a minimum denomination of $10,000, and must be nonnegotiable.

[10] Commercial banks were authorized to offer money market time deposits effective June 1, 1978. The ceiling rate is the discount rate on most recently issued 6-month U.S. Treasury bills. The most recent rates and effective dates are published monthly in the *Federal Reserve Bulletin*, p. A10.

NOTE. Maximum rates that may be paid by member banks are established by the Board of Governors under provisions of Regulation Q; however, a member bank may not pay a rate in excess of the maximum rate payable by State banks or trust companies on like deposits under the laws of the State in which the member bank is located. Beginning Feb. 1, 1936, maximum rates that may be paid by nonmember insured commercial banks, as established by the Federal Deposit Insurance Corporation,

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16. Fees and Rates under Regulation V on Loans Guaranteed Pursuant to Defense Production Act of 1950, December 31, 1978

Fees payable to guaranteeing agency by financing institution on guaranteed portion of loan		
Percentage of loan guaranteed	Guarantee fee (percentage of interest payable by borrower)[1]	Percentage of any commitment fee charged borrower
70 or less	10	10
75	15	15
80	20	20
85	25	25
90	30	30
95	35	35
Over 95	40–50	40–50

Maximum rates financing institution may charge borrower (per cent per annum)[2]	
Interest rate	7½
Commitment rate	½

[1] In any case in which the rate of interest on the loan is in excess of 6 per cent, the guarantee fee shall be computed as though the interest rate were 6 per cent.

[2] The agency guaranteeing a particular loan may from time to time prescribe a higher rate if it determines that the loan is necessary in financing any contract or other operation that the agency deems essential to the national defense.

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17. Principal Assets and Liabilities, and Number of Insured Commercial Banks, by Class of Bank, September 30, 1978 and 1977 [1]

Asset and liability items shown in millions of dollars

Item	Insured commercial banks				Insured nonmember banks
	Total	Member banks			
		Total	National	State	
	September 30, 1978				
Loans and investments, total	981,029	714,082	553,558	160,523	266,946
Loans					
Gross	717,174	532,801	414,220	118,581	184,372
Net	692,724	515,552	400,334	115,218	177,171
Investments	263,855	181,280	139,337	41,942	82,574
U.S. Treasury securities	95,068	65,763	49,199	16,564	29,304
Other	168,787	115,516	90,138	25,378	53,269
Cash assets, total	158,379	134,955	91,224	43,730	23,424
Deposits, total	960,918	701,194	533,059	168,135	259,723
Interbank	58,004	55,364	28,796	26,567	2,639
Other demand	320,772	235,931	179,769	56,161	84,841
Other time	582,141	409,899	324,492	85,406	172,242
Total equity capital	85,540	63,174	48,288	14,885	22,365
Number of banks	14,390	5,593	4,596	997	8,797
	September 30, 1977				
Loans and investments, total	877,988	648,339	499,707	148,631	229,649
Loans					
Gross	623,299	468,683	362,752	105,930	154,615
Net	602,476	453,835	350,946	102,888	148,641
Investments	254,689	179,655	136,954	42,700	75,033
U.S. Treasury securities	98,633	70,746	51,984	18,762	27,886
Other	156,056	108,908	84,970	23,938	47,147
Cash assets, total	140,399	119,930	82,208	37,722	20,469
Deposits, total	861,846	636,761	483,958	152,803	225,085
Interbank	49,412	47,050	25,129	21,921	2,361
Other demand	292,795	219,629	166,481	53,147	73,165
Other time	519,639	370,081	292,346	77,734	149,558
Total equity capital	77,691	58,070	44,123	13,947	19,620
Number of banks	14,420	5,691	4,676	1,015	8,729

[1] All insured commercial banks in the United States.

NOTE. Details may not add to totals because of rounding.

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18. Member Bank Reserves, Federal Reserve Bank Credit, and Related Items—Year-end, 1918-78 and Month-end, 1978

Millions of dollars

Period	Factors supplying reserve funds										
	Federal Reserve Bank credit outstanding								Gold stock [4]	Special drawing rights certificate accounts	Treasury currency outstanding [5]
	U.S. Government securities			Loans	Float [1]	All other [2]	Other Federal Reserve assets [3]	Total			
	Total	Bought outright	Held under repurchase agreement								
1918...	239	239	......	1,766	199	294	......	2,498	2,873	......	1,795
1919...	300	300	......	2,215	201	575	......	3,292	2,707	......	1,707
1920...	287	287	......	2,687	119	262	......	3,355	2,639	......	1,709
1921...	234	234	......	1,144	40	146	......	1,563	3,373	......	1,842
1922...	436	436	......	618	78	273	......	1,405	3,642	......	1,958
1923...	134	80	54	723	27	355	......	1,238	3,957	......	2,009
1924...	540	536	4	320	52	390	......	1,302	4,212	......	2,025
1925...	375	367	8	643	63	378	......	1,459	4,112	......	1,977
1926...	315	312	3	637	45	384	......	1,381	4,205	......	1,991
1927...	617	560	57	582	63	393	......	1,655	4,092	......	2,006
1928...	228	197	31	1,056	24	500	......	1,809	3,854	......	2,012
1929...	511	488	23	632	34	405	......	1,583	3,997	......	2,022
1930...	729	686	43	251	21	372	......	1,373	4,306	......	2,027
1931...	817	775	42	638	20	378	......	1,853	4,173	......	2,035
1932...	1,855	1,851	4	235	14	41	......	2,145	4,226	......	2,204
1933...	2,437	2,435	2	98	15	137	......	2,688	4,036	......	2,303
1934...	2,430	2,430	......	7	5	21	......	2,463	8,238	......	2,511
1935...	2,431	2,430	1	5	12	38	......	2,486	10,125	......	2,476
1936...	2,430	2,430	......	3	39	28	......	2,500	11,258	......	2,532
1937...	2,564	2,564	......	10	19	19	......	2,612	12,760	......	2,637
1938...	2,564	2,564	......	4	17	16	......	2,601	14,512	......	2,798
1939...	2,484	2,484	......	7	91	11	......	2,593	17,644	......	2,963
1940...	2,184	2,184	......	3	80	8	......	2,274	21,995	......	3,087
1941...	2,254	2,254	......	3	94	10	......	2,361	22,737	......	3,247
1942...	6,189	6,189	......	6	471	14	......	6,679	22,726	......	3,648
1943...	11,543	11,543	......	5	681	10	......	12,239	21,938	......	4,094
1944...	18,846	18,846	......	80	815	4	......	19,745	20,619	......	4,131
1945...	24,262	24,262	......	249	578	2	......	25,091	20,065	......	4,339
1946...	23,350	23,350	......	163	580	1	......	24,093	20,529	......	4,562
1947...	22,559	22,559	......	85	535	1	......	23,181	22,754	......	4,562
1948...	23,333	23,333	......	223	541	1	......	24,097	24,244	......	4,589
1949...	18,885	18,885	......	78	534	2	......	19,499	24,427	......	4,598
1950...	20,778	20,725	53	67	1,368	3	......	22,216	22,706	......	4,636
1951...	23,801	23,605	196	19	1,184	5	......	25,009	22,695	......	4,709
1952...	24,697	24,034	663	156	967	4	......	25,825	23,187	......	4,812
1953...	25,916	25,318	598	28	935	2	......	26,880	22,030	......	4,894
1954...	24,932	24,888	44	143	808	1	......	25,885	21,713	......	4,985
1955...	24,785	24,391	394	108	1,585	29	......	26,507	21,690	......	5,008
1956...	24,915	24,610	305	50	1,665	70	......	26,699	21,949	......	5,066
1957...	24,238	23,719	519	55	1,424	66	......	25,784	22,781	......	5,146
1958...	26,347	26,252	95	64	1,296	49	......	27,755	20,534	......	5,234
1959...	26,648	26,607	41	458	1,590	75	......	28,771	19,456	......	5,311
1960...	27,384	26,984	400	33	1,847	74	......	29,338	17,767	......	5,398
1961...	28,881	28,722	159	130	2,300	51	......	31,362	16,889	......	5,585
1962...	30,820	30,478	342	38	2,903	110	......	33,871	15,978	......	5,567
1963...	33,593	33,582	11	63	2,600	162	......	36,418	15,513	......	5,578
1964...	37,044	36,506	538	186	2,606	94	......	39,930	15,388	......	5,405

For notes see last two pages of table.

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18.—Continued

Factors absorbing reserve funds										
Currency in circulation	Treasury cash holdings [6]	Deposits, other than member bank reserves, with Federal Reserve Banks			Other Federal Reserve accounts [3]	Other Federal Reserve liabilities and capital [3]	Member bank reserves			
		Treasury	Foreign	Other			With Federal Reserve Banks	Currency and coin [7]	Required [8]	Excess [8]
4,951	288	51	96	25	118	....	1,636	....	1,585	51
5,091	385	31	73	28	208	....	1,890	....	1,822	68
5,325	218	57	5	18	298	....	1,781	....	....	....
4,403	214	96	12	15	285	....	1,753	....	1,654	99
4,530	225	11	3	26	276	....	1,934	....	....	....
4,757	213	38	4	19	275	....	1,898	....	1,884	14
4,760	211	51	19	20	258	....	2,220	....	2,161	59
4,817	203	16	8	21	272	....	2,212	....	2,256	−44
4,808	201	17	46	19	293	....	2,194	....	2,250	−56
4,716	208	18	5	21	301	....	2,487	....	2,424	63
4,686	202	23	6	21	348	....	2,389	....	2,430	−41
4,578	216	29	6	24	393	....	2,355	....	2,428	−73
4,603	211	19	6	22	375	....	2,471	....	2,375	96
5,360	222	54	79	31	354	....	1,961	....	1,994	−33
5,388	272	8	19	24	355	....	2,509	....	1,933	576
5,519	284	3	4	128	360	....	2,729	....	1,870	859
5,536	3,029	121	20	169	241	....	4,096	....	2,282	1,814
5,882	2,566	544	29	226	253	....	5,587	....	2,743	2,844
6,543	2,376	244	99	160	261	....	6,606	....	4,622	1,984
6,550	3,619	142	172	235	263	....	7,027	....	5,815	1,212
6,856	2,706	923	199	242	260	....	8,724	....	5,519	3,205
7,598	2,409	634	397	256	251	....	11,653	....	6,444	5,209
8,732	2,213	368	1,133	599	284	....	14,026	....	7,411	6,615
11,160	2,215	867	774	586	291	....	12,450	....	9,365	3,085
15,410	2,193	799	793	485	256	....	13,117	....	11,129	1,988
20,449	2,303	579	1,360	356	339	....	12,886	....	11,650	1,236
25,307	2,375	440	1,204	394	402	....	14,373	....	12,748	1,625
28,515	2,287	977	862	446	495	....	15,915	....	14,457	1,458
28,952	2,272	393	508	314	607	....	16,139	....	15,577	562
28,868	1,336	870	392	569	563	....	17,899	....	16,400	1,499
28,224	1,325	1,123	642	547	590	....	20,479	....	19,277	1,202
27,600	1,312	821	767	750	706	....	16,568	....	15,550	1,018
27,741	1,293	668	895	565	714	....	17,681	....	16,509	1,172
29,206	1,270	247	526	363	746	....	20,056	....	19,667	389
30,433	1,270	389	550	455	777	....	19,950	....	20,520	−570
30,781	761	346	423	493	839	....	20,160	....	19,397	763
30,509	796	563	490	441	907	....	18,876	....	18,618	258
31,158	767	394	402	554	925	....	19,005	....	18,903	102
31,790	775	441	322	426	901	....	19,059	....	19,089	−30
31,834	761	481	356	246	998	....	19,034	....	19,091	−57
32,193	683	358	272	391	1,122	....	18,504	....	18,574	−70
32,591	391	504	345	694	841	....	18,174	310	18,619	−135
32,869	377	485	217	533	941	....	17,081	2,544	18,988	637
33,918	422	465	279	320	1,044	....	17,387	2,823	20,114	96
35,338	380	597	247	393	1,007	....	17,454	3,262	20,071	645
37,692	361	880	171	291	1,065	....	17,049	4,099	20,677	471
39,619	612	820	229	321	1,036	....	18,086	4,151	21,663	574

For notes see last two pages of table.

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18. Member Bank Reserves, Federal Reserve Bank Credit, and Related Items—Year-end, 1918–78 and Month-end, 1978—Continued

Millions of dollars

Period	Factors supplying reserve funds										
	Federal Reserve Bank credit outstanding								Gold stock [4]	Special drawing rights certificate accounts	Treasury currency outstanding [5]
	U.S. Government securities [9]			Loans	Float [1]	All other [2]	Other Federal Reserve assets [3]	Total			
	Total	Bought outright [10]	Held under repurchase agreement								
1965...	40,768	40,478	290	137	2,248	187	......	43,340	13,733	......	5,575
1966...	44,316	43,655	661	173	2,495	193	......	47,177	13,159	......	6,317
1967...	49,150	48,980	170	141	2,576	164	......	52,031	11,982	......	6,784
1968...	52,937	52,937	....	186	3,443	58	......	56,624	10,367	......	6,795
1969...	57,154	[10] 57,154	....	183	3,440	64	2,743	63,584	10,367	......	6,852
1970...	62,142	62,142	....	335	4,261	57	1,123	67,918	10,732	400	7,149
1971...	70,804	69,481	1,323	39	4,343	261	1,068	76,515	10,132	400	7,710
1972...	71,230	71,119	111	1,981	3,974	106	1,260	78,551	10,410	400	8,313
1973...	80,495	80,395	100	1,258	3,099	68	1,152	86,072	11,567	400	8,716
1974...	85,714	84,760	954	299	2,001	999	3,195	92,208	11,652	400	9,253
1975...	94,124	92,789	1,335	211	3,688	1,126	3,312	102,461	11,599	500	10,218
1976...	104,093	100,062	4,031	25	2,601	991	3,182	110,892	11,598	1,200	10,810
1977...	111,274	108,922	2,352	265	3,810	954	2,442	118,745	11,718	1,250	11,331
1978...	118,591	117,374	1,217	1,174	6,432	587	4,543	131,327	11,671	1,300	11,831
1978											
Jan...	105,008	105,008	....	758	4,083	....	2,939	112,788	11,718	1,250	11,380
Feb..	106,432	106,432	....	304	3,499	....	1,899	112,134	11,718	1,250	11,396
Mar..	109,770	107,819	1,951	332	2,732	770	2,328	115,932	11,718	1,250	11,441
Apr..	111,564	110,697	867	1,750	3,017	290	3,161	119,782	11,718	1,250	11,482
May .	110,747	110,290	457	1,167	4,419	274	2,586	119,193	11,718	1,250	11,526
June .	118,672	116,027	2,645	1,428	3,318	1,021	2,454	126,893	11,706	1,250	11,565
July..	117,120	116,313	807	1,127	5,092	268	2,902	126,509	11,693	1,250	11,592
Aug..	119,836	117,836	2,000	954	5,225	296	2,063	128,374	11,679	1,300	11,641
Sept..	123,876	120,977	2,899	1,365	3,719	715	2,439	132,114	11,668	1,300	11,683
Oct. .	123,387	122,597	790	1,207	4,436	236	2,756	132,022	11,655	1,300	11,731
Nov..	121,204	121,204	....	813	7,238	....	2,350	131,605	11,642	1,300	11,790
Dec..	118,591	117,374	1,217	1,174	6,432	587	4,543	131,327	11,671	1,300	11,831

[1] Beginning with 1960, figures reflect a minor change in concept; see *Federal Reserve Bulletin*, vol. 47 (Feb. 1961), p. 164.

[2] Data consist principally of acceptances and, until Aug. 21, 1959, industrial loans, authority for which expired on that date.

[3] Before Apr. 16, 1969, this category includes the total of Federal Reserve Bank capital paid in, surplus, other capital accounts, and other liabilities and accrued dividends less the sum of bank premises and other assets, and was reported as "Other Federal Reserve accounts"; thereafter, "Other Federal Reserve assets" and "Other Federal Reserve liabilities and capital" are shown separately.

[4] Before Jan. 30, 1934, data include gold held in Federal Reserve Banks and in circulation.

[5] These figures include currency and coin (other than gold) issued directly by the Treasury. The largest components are fractional and dollar coins. For details see the regular table, "Currency and Coin in Circulation," in the *Treasury Bulletin*.

[6] This category consists of the coin and paper currency held by the Treasury, as well as any gold in excess of the gold certificates issued to the Reserve Bank.

[7] Between Dec. 1, 1959, and Nov. 23, 1960, part of the amount was allowed as reserves; thereafter all was allowed.

[8] These figures are estimated through 1958. Before 1929, they were available only on call dates (in 1920 and 1922, the call dates were Dec. 29). Beginning Sept. 12, 1968, the amount is based on close-of-business figures for the reserve period 2 weeks previous to the report date.

[9] Beginning Dec. 1, 1966, these securities include Federal agency obligations held under repurchase agreements and beginning Sept. 29, 1971, Federal agency issues bought outright.

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18.—Continued

Factors absorbing reserve funds

Currency in circulation	Treasury cash holdings [6]	Deposits, other than member bank reserves, with Federal Reserve Banks			Other Federal Reserve accounts [3]	Other Federal Reserve liabilities and capital [3]	Member bank reserves			
		Treasury	Foreign	Other			With Federal Reserve Banks	Currency and coin [7]	Required [8]	Excess [8, 11]
42,056	760	668	150	355	211	....	18,447	4,163	22,848	−238
44,663	1,176	416	174	588	−147	....	19,779	4,310	24,321	−232
47,226	1,344	1,123	135	653	−773	....	21,092	4,631	25,905	−182
50,961	695	703	216	747	−1,353	....	21,818	4,921	27,439	−700
53,950	596	1,312	134	807	....	1,919	22,085	5,187	28,173	−901
57,093	431	1,156	148	1,233	....	1,986	24,150	5,423	30,033	−460
61,068	460	2,020	294	999	....	2,131	27,788	5,743	32,496	1,035
66,516	345	1,855	325	840	....	2,143	25,647	6,216	32,044	[11]98
72,497	317	2,542	251	[12]1,419	....	2,669	27,060	6,781	35,268	−1,360
79,743	185	3,113	418	[12]1,275	....	2,935	25,843	7,370	37,011	−3,798
86,547	483	7,285	353	1,090	....	2,968	26,052	8,036	35,197	[13]−1,103
93,717	460	10,393	352	1,357	....	3,063	25,158	8,628	35,461	−1,535
103,811	392	7,114	379	1,187	....	3,292	26,870	9,421	37,615	−1,265
114,645	240	4,196	368	1,256	....	4,275	31,152	10,538	42,694	−893
100,819	387	11,228	422	871	....	4,109	19,301	9,893	37,292	−8,020
101,369	388	3,615	445	698	....	3,933	26,047	9,085	36,012	−794
102,392	393	4,705	352	740	....	3,860	27,900	8,935	36,291	623
103,114	376	7,177	481	684	....	4,080	28,321	9,247	37,608	35
105,443	365	2,398	454	660	....	4,235	30,135	9,215	36,529	2,899
106,288	337	11,614	288	773	....	4,193	27,920	9,513	38,324	−817
106,577	313	10,331	347	771	....	4,247	28,461	9,881	37,705	713
107,588	299	12,068	309	691	....	4,329	27,705	9,578	37,295	63
107,663	299	16,647	325	628	....	4,372	26,830	9,904	38,746	−1,937
109,307	276	15,467	305	531	....	4,560	26,260	9,861	38,295	−2,095
112,072	267	6,587	379	567	....	4,545	31,919	10,056	41,138	918
114,645	240	4,196	368	1,256	....	4,275	31,152	10,538	42,694	−893

[10] *Includes*, beginning 1969, securities loaned—fully guaranteed by U.S. Government securities pledged with Federal Reserve Banks—and *excludes* (if any) securities sold and scheduled to be bought back under matched sale-purchase transactions.

[11] Beginning with the week ending Nov. 15, 1972, figures include $450 million of reserve deficiencies on which Federal Reserve Banks are allowed to waive penalties for a transition period in connection with bank adaptation to Regulation J as amended, effective Nov. 9, 1972. Allowable deficiencies (beginning with first statement week of quarter) included are (in millions): 1973—Q1, $279; Q2, $172; Q3, $112; Q4, $84; and 1974—Q1, $67, and Q2, $58. The transition period ended after the second quarter of 1974.

[12] Beginning July 1973, this item includes certain deposits of domestic nonmember banks and foreign-owned banking institutions held with member banks and redeposited in full with Federal Reserve Banks in connection with voluntary participation by nonmember institutions in the Federal Reserve System's program of credit restraint.

As of Dec. 12, 1974, the amount of voluntary nonmember bank and foreign-agency and branch deposits at Federal Reserve Banks that are associated with marginal reserves are no longer reported. However, two amounts are reported: (1) deposits voluntarily held as reserves by agencies and branches of foreign banks operating in the United States, and (2) Euro-dollar liabilities.

[13] Beginning with the week ending Nov. 19, 1975, figures are adjusted to include waivers of penalties for reserve deficiencies, in accordance with a change in Board policy that became effective Nov. 19, 1975.

NOTE. For a description of figures and discussion of their significance, see "Member Bank Reserves and Related Items," Section 10 of *Banking and Monetary Statistics, 1941–1970* (Board of Governors of the Federal Reserve System, September 1, 1976), pp. 507–23.

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19. Changes in Number of Banking Offices in the United States during 1978 [1]

Type of office and change	All banks	Commercial banks (including stock savings banks and nondeposit trust companies)						Mutual savings banks	
		Total	Member			Nonmember			
			Total	National	State	Insured	Noninsured	Insured	Noninsured
Banks, Dec. 31, 1977	**15,172**	**14,705**	**5,669**	**4,655**	**1,014**	**8,729**	**307**	**323**	**144**
Changes during 1978									
New banks	182	180	54	37	17	94	32	2	....
Placed in receivership	−1	−1	....	....	....	−1	....	....	....
Ceased banking operations	−1	−1	....	....	....	....	−1	....	....
Banks converted into branches	−158	−154	−67	−54	−13	−87	....	−1	−3
Other	−16	−16	−8	−8	....	−6	−2	....	....
Interclass changes									
Nonmember to national	....	....	3	3	....	−3	....	....	....
State member	....	....	12	....	12	−12	....	....	....
State member to nonmember	....	....	−37	....	−37	37	....	....	....
National to nonmember	−1	−1	−62	−62	....	61	....	....	....
National to State member	....	....	....	−7	7	....	....	....	....
Noninsured to insured	....	....	....	....	....	3	−3	....	....
Noninsured mutual to insured mutual	....	....	....	....	....	....	....	1	−1
Net change	5	7	−105	−91	−14	86	26	2	−4
Dec. 31, 1978	**15,177**	**14,712**	**5,564**	**4,564**	**1,000**	**8,815**	**[1]333**	**325**	**140**
Branches and additional offices, Dec. 31, 1977 [2]	**35,018**	**32,704**	**22,037**	**17,449**	**4,588**	**10,613**	**54**	**1,979**	**335**
Changes during 1978									
De novo	2,058	1,804	1,044	896	148	758	2	239	15
Banks converted	156	152	75	47	28	77	....	1	3
Discontinued	−310	−279	−219	−150	−69	−59	−1	−31	....
Sale of branch	−1	−1	−5	−4	−1	4	....	....	....
Interclass changes									
Nonmember to national	....	....	9	9	....	−9	....	....	....
Nonmember to State member	....	....	110	....	110	−110	....	....	....
State member to national	....	....	....	8	−8	....	....	....	....
State member to nonmember	....	....	−129	....	−129	129	....	....	....
National to State member	....	....	....	−37	37	....	....	....	....
National to nonmember	....	....	−241	−241	....	241	....	....	....
Noninsured mutual to insured mutual	....	....	....	....	....	....	....	4	−4
Noninsured to insured	....	....	....	....	....	4	−4	....	....
Facilities reclassified as branches	5	5	3	3	....	2	....	....	....
Other	4	5	1	−6	7	4	....	−1	....
Net change	1,912	1,686	648	525	123	1,041	−3	212	14
Dec. 31, 1978 [2]	**36,930**	**34,390**	**22,685**	**17,974**	**4,711**	**11,654**	**51**	**2,191**	**349**
Banking facilities, Dec. 31, 1977 [3]	**176**	**176**	**150**	**139**	**11**	**26**	....	....	....
Changes during 1978									
Discontinued	−3	−3	−2	−2	....	−1	....	....	....
Interclass changes									
Facilities reclassified as branches	−5	−5	−3	−3	....	−2	....	....	....
Net change	−8	−8	−5	−5	....	−3	....	....	....
Dec. 31, 1978 [3]	**168**	**168**	**145**	**134**	**11**	**23**	....	....	....

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20. Number of Par and Nonpar Banking Offices, December 31, 1978

Area	Total		Par						Nonpar (nonmember)	
			Total		Member		Nonmember			
	Banks	Branches and offices	Banks	Branches and offices	Banks	Branches and offices	Banks	Branches and offices	Banks	Branches and offices
	Federal Reserve district									
Boston	362	2,126	362	2,126	178	1,119	184	1,007	......	....
New York	458	4,791	458	4,791	245	4,022	213	769	......	....
Philadelphia	367	2,344	367	2,344	227	1,416	140	928	......	....
Cleveland	753	2,920	753	2,920	450	2,314	303	606	......	....
Richmond	759	4,685	759	4,685	394	2,861	365	1,824	......	....
Atlanta	1,872	3,663	1,855	3,643	595	1,919	1,260	1,724	17	20
Chicago	2,759	3,781	2,759	3,781	918	2,292	1,841	1,489	......	....
St. Louis	1,444	1,813	1,444	1,813	407	834	1,037	979	......	....
Minneapolis	1,419	627	1,419	627	512	343	907	284	......	....
Kansas City	2,262	1,039	2,262	1,039	796	632	1,466	407	......	....
Dallas	1,558	457	1,552	456	701	167	851	289	6	1
San Francisco	536	6,584	536	6,584	141	4,961	395	1,623	......	....
TOTAL	**14,549**	**34,830**	**14,526**	**34,809**	**5,564**	**22,880**	**8,962**	**11,929**	**23**	**21**
	State									
Alabama	312	552	312	552	122	374	190	178	......	....
Alaska	12	112	12	112	6	84	6	28	......	....
Arizona	20	484	20	484	3	320	17	164	......	....
Arkansas	260	372	260	372	75	194	185	178	......	....
California	229	3,897	229	3,897	60	3,073	169	[1] 824	......	....
Colorado	299	81	299	81	159	55	140	26	......	....
Connecticut	65	587	65	587	21	287	44	300	......	....
Delaware	17	147	17	147	5	5	12	142	......	....
District of Columbia	17	138	17	138	16	136	1	2	......	....
Florida	611	743	611	743	263	360	348	383	......	....
Georgia	440	786	440	786	73	427	367	359	......	....
Hawaii	8	157	8	157	2	11	6	146	......	....
Idaho	24	228	24	228	10	184	14	44	......	....
Illinois	1,270	394	1,270	394	486	211	784	183	......	....
Indiana	405	1,035	405	1,035	162	555	243	480	......	....
Iowa	656	500	656	500	143	183	513	317	......	....
Kansas	617	256	617	256	170	145	447	111	......	....
Kentucky	344	644	344	644	89	348	255	296	......	....
Louisiana	256	715	233	694	61	335	172	359	23	21
Maine	43	294	43	294	20	155	23	139	......	....
Maryland	106	855	106	855	40	462	66	393	......	....
Massachusetts	151	925	151	925	80	514	71	411	......	....
Michigan	365	1,793	365	1,793	208	1,354	157	439	......	....
Minnesota	759	176	759	176	237	87	522	89	......	....
Mississippi	184	635	184	635	42	268	142	367	......	....
Missouri	714	400	714	400	153	105	561	295	......	....
Montana	160	23	160	23	101	15	59	8	......	....
Nebraska	452	199	452	199	125	144	327	55	......	....
Nevada	9	130	9	130	5	108	4	22	......	....
New Hampshire	77	134	77	134	42	100	35	34	......	....
New Jersey	184	1,535	184	1,535	111	1,172	73	363	......	....
New Mexico	86	227	86	227	46	132	40	95	......	....
New York	292	3,316	292	3,316	171	3,086	121	[1] 230	......	....
North Carolina	88	1,683	88	1,683	29	810	59	873	......	....
North Dakota	172	117	172	117	46	47	126	70	......	....
Ohio	482	1,942	482	1,942	327	1,621	155	321	......	....
Oklahoma	483	216	483	216	207	170	276	46	......	....
Oregon	63	525	63	525	7	329	56	196	......	....
Pennsylvania	376	2,426	376	2,426	238	1,598	138	828	......	....
Rhode Island	16	226	16	226	5	115	11	111	......	....

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20. Number of Par and Nonpar Banking Offices, December 31, 1978—Cont.

Area	Total		Par: Total		Par: Member		Par: Nonmember		Nonpar (nonmember)	
	Banks	Branches and offices	Banks	Branches and offices	Banks	Branches and offices	Banks	Branches and offices	Banks	Branches and offices
	State—Continued									
South Carolina	87	661	87	661	25	340	62	321	......	....
South Dakota	155	149	155	149	60	107	95	42	......	....
Tennessee	349	953	349	953	82	460	267	493	......	....
Texas	1,401	202	1,401	202	649	52	752	150	......	....
Utah	66	253	66	253	23	203	43	50	......	....
Vermont	29	148	29	148	14	46	15	102	......	....
Virginia	262	1,303	262	1,303	167	1,086	95	217	......	....
Washington	102	785	102	785	25	644	77	141	......	....
West Virginia	230	56	230	56	135	34	95	22	......	....
Wisconsin	628	443	628	443	156	174	472	269	......	....
Wyoming	88	3	88	3	62	1	26	2	......	....
	Other area									
American Samoa [2]	......	1	......	1	......	....	......	1	......	....
Guam [2]	3	12	3	12	......	5	3	7	......	....
Puerto Rico [3]	19	232	19	232	......	25	19	207	......	....
Virgin Islands [3]	6	24	6	24	......	24	6	....	......	....

[1] Includes 1 Los Angeles branch and 19 New York City branches of 3 insured nonmember Puerto Rican banks.

[2] American Samoa and Guam assigned to the San Francisco District for check-clearing and collection purposes. All member branches in Guam are branches of California and New York banks.

[3] Puerto Rico and the Virgin Islands assigned to the New York District for check-clearing and collection purposes. All member branches in Puerto Rico are branches of banks located in California, New York, and Pennsylvania. Certain branches of Canadian banks (2 in Puerto Rico and 5 in the Virgin Islands) are included above as nonmember banks; and nonmember branches in Puerto Rico include 8 other branches of Canadian banks.

NOTE. Comprises all commercial banking offices on which checks are drawn, including 168 banking facilities. Number of banks and branches differs from that in Table 19 because this table includes banks in Guam, Puerto Rico, and the Virgin Islands but excludes banks and trust companies on which no checks are drawn.

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21. Mergers, Consolidations, Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors during 1978

Name of bank, type of transaction, and other banks involved [1]	Assets (millions of dollars)	Number of banking offices		Page for Attorney General's and Board's actions
		In operation	To be operated	
Apple Capital Bank, Mount Jackson, Va.	(2)	(2)	1	426
Merger				
The Stonewall Jackson Bank and Trust Company, Mount Jackson, Va.	2	1		
The Bank of Mid-Jersey, Bordentown Township, N.J.	128	7	10	425
Acquisition of assets and assumption of liabilities				
The Hamilton Bank, N.A., Hamilton Township, N.J.	25	3		
Bank of Utah, Ogden, Utah	124	13	15	430
Merger				
Bank of Brigham City, Brigham City, Utah	5	2		
Bank of Utah, Ogden, Utah	124	13	14	429
Merger				
Bank of Northern Utah, Clearfield, Utah	8	1		
Bank of Virginia—Richmond, Richmond, Va.	(2)	(2)	129	431
Merger				
Bank of Virginia, Richmond, Va.	691	40		
Bank of Virginia—Eastern, Norfolk, Va.	293	25		
Bank of Virginia—Eastern Shore, Hallwood, Va.	31	1		
Bank of Virginia—Loudoun, Sterling, Va.	7	1		
Bank of Virginia—Petersburg, Petersburg, Va.	48	3		
Bank of Virginia—Potomac, Falls Church, Va.	230	23		
Bank of Virginia—Shenandoah, Winchester, Va.	6	1		
Bank of Virginia—Southwest, Roanoke, Va.	330	33		
Bank of Virginia—Warren, Front Royal, Va.	32	2		
Chemical Bank, New York, N.Y.	30,576	255	272	428
Merger				
Chemical Bank of Binghamton, Binghamton, N.Y.	15	2		
Chemical Bank—Buffalo, Buffalo, N.Y.	21	3		
Chemical Bank—Eastern, N.A., Greenwich, N.Y.	16	4		
Chemical Bank of Rochester, Hilton, N.Y.	34	4		
Chemical Bank of Syracuse, Syracuse, N.Y.	15	4		
The Connecticut Bank and Trust Company, Hartford, Conn.	1,981	83	86	428
Merger				
The Connecticut Bank and Trust Company, N.A., Norwalk, Conn.	16	3		

For notes see p. 423.

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21. Mergers, Consolidations, Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors during 1978—Cont.

Name of bank, type of transaction, and other banks involved [1]	Assets (millions of dollars)	Number of banking offices		Page for Attorney General's and Board's actions
		In operation	To be operated	
The Connecticut Bank and Trust Company, Hartford, Conn.	1,981	83	86	432
Merger				
Liberty National Bank, Stamford, Conn.	29	3		
The Conway Trust Company, Conway, N.H.	(2)	(2)	4	428
Merger				
The Carroll County Trust Company, Conway, N.H.	35	4		
The F.B.G. Bank of Mount Sterling, Mount Sterling, Ohio	(2)	(2)	1	430
Merger				
The Sterling State Bank, Mount Sterling, Ohio	17	1		
Fidelity American Bank, Virginia Beach, Va.	65	7	27	427
Merger				
Fidelity American Bank, N.A., Tidewater, Portsmouth, Va.	130	12		
Fidelity American Bank, Hampton Roads, Newport News, Va.	48	7		
Fidelity American Bank, Williamsburg, Va.	4	1		
First State Bank of Miami, Miami, Fla.	143	1	6	431
Merger				
Hialeah—Miami Springs First State Bank, Hialeah, Fla.	113	1		
North Hialeah First State Bank, Hialeah, Fla.	35	1		
Airport First State Bank, Miami, Fla.	25	1		
Miami Lakes First State Bank, Hialeah, Fla.	26	1		
North Miami First State Bank, North Miami, Fla.	8	1		
First Virginia Bank, Falls Church, Va.	527	49	59	434
Merger				
First Virginia Bank/Manassas National, Manassas, Va.	39	10		
First Virginia Bank—Eastern, Warrenton, Va.	(2)	(2)	2	429
Merger				
Bank of Warrenton, Warrenton, Va.	3	2		

For notes see opposite page.

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21.—Continued

Name of bank, type of transaction, and other banks involved [1]	Assets (millions of dollars)	Number of banking offices		Page for Attorney General's and Board's actions
		In operation	To be operated	
Flagship Bank of Tampa, Tampa, Fla.	143	1	4	427
Merger				
Flagship Bank of Town 'N Country, Tampa, Fla.	20	1		
Flagship Bank of Tampa—East, Tampa, Fla.	18	1		
Flagship Bank of Lutz, Lutz, Fla.	9	1		
Hamilton Bank and Trust Company, Bailey's Crossroads, Va.	40	5	7	424
Merger				
The Bank of Arlington, Arlington, Va.	15	2		
Metropolitan Bank and Trust Company, Tampa, Fla.	149	2	3	425
Merger				
American Guaranty Bank, Tampa, Fla.	16	1		
Nova Bank and Trust Company, Newport News, Va.	(2)	(2)	4	433
Merger				
First City Bank of Newport News, Newport News, Va.	20	4		
Savannah Interim Bank, Savannah, Ga.	(2)	(2)	11	424
Merger				
Savannah Bank and Trust Company of Savannah, Savannah, Ga.	225	11		
Southern Bank and Trust Company, Richmond, Va.	231	11	15	426
Merger				
The Bank of Chesterfield, Chesterfield County, Va.	17	4		
Southern Bank and Trust Company, Richmond, Va.	231	14	16	431
Merger				
Williamsburg National Bank, Williamsburg, Va.	16	2		
Walker Bank & Trust Company, Salt Lake City, Utah	641	28	29	424
Merger				
American Bank of Commerce, Cedar City, Utah	5	1		

[1] Each proposed transaction was to be effected under the charter of the first-named bank. This table is in alphabetical order; the notes appear in chronological order of approval.
[2] This is a newly organized bank, not in operation.

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21. Mergers, Consolidations, Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors during 1978—Cont.

Walker Bank & Trust Company, Salt Lake City, Utah, ***to merge with*** **American Bank of Commerce, Cedar City, Utah**

SUMMARY REPORT BY THE ATTORNEY GENERAL (12-29-77)

We have reviewed this proposed transaction and conclude that it would not have a substantial competitive impact.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (2-6-78)

The sole office of the American Bank of Commerce (American Bank) is more than 200 miles from an office of Walker Bank & Trust Company (Applicant), and, under Utah law, Applicant could not open a *de novo* branch in Cedar City. Aside from American Bank, Cedar City is served by a bank with deposits of about $17 million and a branch of First Security Bank of Utah, N.A., Ogden, which has total deposits of $1 billion. American Bank holds about 7 per cent of the deposits in the Cedar City banking market. The proposed merger would have no adverse competitive effects.

American Bank was established in 1974 and has experienced numerous problems. Financial factors thus weigh in favor of approval of the application. The resulting bank will offer expanded banking services to present customers of American Bank, and the convenience and needs factor weighs in favor of approval.

Savannah Interim Bank, Savannah, Ga., ***to merge with*** **Savannah Bank and Trust Company of Savannah, Savannah, Ga.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (1-30-78)

The proposed merger is part of a plan through which Savannah Bank and Trust Company of Savannah would become a subsidiary of SBT Corporation, a proposed bank holding company. The instant merger, however, would merely combine an existing bank with a nonoperating institution [Savannah Interim Bank]; as such, and without regard to the acquisition of the surviving bank by SBT Corporation, it would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (2-7-78)

The proposal is a transaction to facilitate the acquisition of Savannah Bank and Trust Company of Savannah by SBT Corporation, a proposed bank holding company.

The proposed merger would, in itself, have no adverse competitive effects. The financial and convenience and needs factors are consistent with approval of the application.

Hamilton Bank and Trust Company, Bailey's Crossroads, Va., ***to merge with*** **The Bank of Arlington, Arlington, Va.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (2-24-78)

The merging banks are both wholly owned subsidiaries of the same bank holding company. As such, their proposed merger is essentially a corporate reorganization and would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (3-16-78)

Both banks are wholly owned subsidiaries of Central National Corporation, both having been acquired by that bank holding company in November 1974. The merger would result in no change in the corporation's relative position in

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21.—Continued

the State or in the banking markets involved, and would have no adverse effects upon competition in the area.

The financial and managerial resources and prospects of the banks proposing to merge and of the resulting institution are considered consistent with approval of the application. Considerations relating to the convenience and needs of the community to be served are likewise consistent with approval to the extent that a pooling of resources within the merging banks and a reduction of duplicated services should result in more efficient operations.

The Bank of Mid-Jersey, Bordentown Township, N.J., ***to acquire the assets and assume the liabilities of*** **The Hamilton Bank, N.A., Hamilton Township, N.J.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (3-14-78)

We have reviewed this proposed transaction and conclude that it would not have a substantial competitive impact.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (3-29-78)

The Bank of Mid-Jersey (Applicant) is requesting approval to acquire The Hamilton Bank, N.A. (Hamilton Bank). Applicant operates 6 offices in Burlington County and 1 in Ocean County, while Hamilton Bank has 3 offices, all in Mercer County. All offices of the 2 banks are located in the Trenton banking market; Applicant holds 4.1 per cent of the market deposits and Hamilton Bank 1.6 per cent. Although the nearest offices of the 2 banks are 3½ miles apart, in view of the condition of Hamilton Bank, as discussed below, this bank cannot be considered competitive within the market. Moreover, because numerous banking facilities will still remain in the Trenton banking market if this proposal is approved, it is concluded that the competitive effects of the proposed merger would not be adverse.

Although the general condition of Applicant is satisfactory, Hamilton Bank, which was established in 1970, has been considered a problem bank since 1974. This bank has never shown an operating profit, and its capital funds have declined almost $400,000 from 1974 to September 1977.

The condition of the resulting bank, which plans to increase its capital funds by the sale of $1.5 million in capital notes, is expected to be generally satisfactory. In addition, the range and quality of banking services provided to customers of Hamilton Bank would be increased.

Banking factors and the convenience and needs factor support approval of the application, and the proposal would not have adverse competitive effects.

Metropolitan Bank and Trust Company, Tampa, Fla., ***to merge with*** **American Guaranty Bank, Tampa, Fla.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (2-24-78)

We have reviewed this proposed transaction and conclude that it would not have a substantial competitive impact.

BASIS FOR APPROVAL BY BOARD OF GOVERNORS (4-27-78)

Metropolitan Bank and Trust Company (Applicant) is the 4th largest bank in the Tampa banking market and holds 5.6 per cent of the total deposits of commercial banks in that market: American Guaranty Bank (American Bank) is the 20th largest and holds 0.8 per cent of the total deposits.

Consummation of the proposed merger would increase Applicant's share of bank deposits in Florida and in the Tampa banking market by less than 1 per

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21. Mergers, Consolidations, Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors during 1978—Cont.

cent, and would not change its rank among banking organizations in the State or in the same market. It would, however, eliminate some direct competition between Applicant and American Bank, but apparently not by a significant amount in view of the structure of the market. Many of the State's largest holding companies are represented in the Tampa market, and collectively there are 26 banking organizations operating 42 banks. In addition, the Tampa banking market is only moderately concentrated and has experienced a significant reduction in the concentration of deposits in recent years. The Board therefore concludes, for the reasons discussed and also based on the record, that consummation of the proposed transaction would have only slight adverse effects on competition in the relevant market.

Considerations relating to financial and managerial resources are regarded as consistent with approval of the application. Consummation of the proposed transaction should lead to the introduction of new and improved services for customers of American Bank because Applicant plans to introduce a trust department, credit cards, safe deposit boxes, and new consumer services at that Bank's facility. While these services are now available from Applicant in the Tampa market, their availability at American Bank's location would increase the banking services available in the market.

In light of the convenience and needs factors discussed above, the Board finds that considerations relating to the convenience and needs of the community to be served lend weight toward approval and are sufficient to outweigh any slight adverse competitive effects that might result from the merger.

Apple Capital Bank, Mount Jackson, Va., ***to merge with*** **The Stonewall Jackson Bank and Trust Company, Mount Jackson, Va.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (2-24-78)

The proposed merger is part of a plan through which The Stonewall Jackson Bank and Trust Company would become a subsidiary of F & M National Corporation, a bank holding company. The instant merger, however, would merely combine an existing bank with a nonoperating institution [Apple Capital Bank]; as such, and without regard to the acquisition of the surviving bank by F & M National Corporation, it would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (5-10-78)

The proposal is a transaction to facilitate the acquisition of The Stonewall Jackson Bank and Trust Company by F & M National Corporation, Winchester, Virginia, a bank holding company.

The proposed merger in itself, would have no adverse competitive effects. The financial and convenience and needs factors are consistent with approval of the application.

Southern Bank and Trust Company, Richmond, Va., ***to merge with*** **The Bank of Chesterfield, Chesterfield County, Va.**

SUMMARY REPORT BY THE ATTORNEY GENERAL

(No report received.)

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (5-31-78)

Southern Bank and Trust Company (Applicant) proposes to merge with The Bank of Chesterfield (Chesterfield Bank). Applicant is a subsidiary and the lead bank of Southern Bankshares. Inc., a holding company that owns 3 other banks and has total deposits of $253 million. Applicant has its main office and 5

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branches in Richmond, 3 branches in Henrico County, and 2 in Chesterfield County. All 4 offices of Chesterfield Bank are in Chesterfield County.

Offices of both banks are located in the Richmond standard metropolitan statistical area, which is the relevant market in this case. Applicant's parent holding company holds 9 per cent of the deposits in its market area and, upon consummation of the merger, would hold 9.6 per cent. Applicant has 2 branches in Chesterfield County, about 5 miles from offices of Chesterfield Bank. Some competition does exist between the banks involved in this proposal, but the competitive effect of the merger would be only slightly adverse.

The banking factors are satisfactory and consistent with approval of the merger. Upon consummation, Chesterfield Bank's offices, as branches of Applicant, will offer automated teller machines, individual retirement accounts, overdraft credit, and trust and investment services. The convenience and needs factor lends weight to approval and outweighs the slight adverse competitive effects.

Fidelity American Bank, Virginia Beach, Va., *to merge with* Fidelity American Bank, N.A., Tidewater, Portsmouth, Va.; Fidelity American Bank, Hampton Roads, Newport News, Va.; and Fidelity American Bank, Williamsburg, Va.

SUMMARY REPORT BY THE ATTORNEY GENERAL (4-27-78)

The merging banks are all wholly owned subsidiaries of the same bank holding company. As such, their proposed merger is essentially a corporate reorganization and would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (7-5-78)

All 4 banks involved in this proposal are subsidiaries of Fidelity American Bankshares, Inc., Lynchburg, Virginia, a bank holding company. Fidelity American Bank, Virginia Beach (Applicant), has also filed a membership application, and the resulting bank will be a new State member bank with deposits of about $213 million.

Applicant is the 7th largest holding company in Virginia and controls 5 per cent of banking deposits in the State.

The proposal would have no adverse competitive effects, and banking factors and the convenience and needs factor are consistent with approval of the application.

Flagship Bank of Tampa, Tampa, Fla., *to merge with* Flagship Bank of Town 'N Country, Tampa, Fla., Flagship Bank of Tampa—East, Tampa, Fla.; and Flagship Bank of Lutz, Lutz, Fla.

SUMMARY REPORT BY THE ATTORNEY GENERAL (7-14-78)

The merging banks are all wholly owned subsidiaries of the same bank holding company. As such, their proposed merger is essentially a corporate reorganization and would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (8-10-78)

Flagship Bank of Tampa (Applicant), a subsidiary of Flagship Banks, Inc., Miami Beach, a bank holding company, proposes to merge with 3 other subsidiaries of Flagship Banks, Inc. The proposed transaction is essentially a corporate reorganization and, as such, would have no effect on competition. The application does not involve the acquisition of an additional bank by the holding company, and, thus, the financial and managerial resources of the institutions involved are consistent with approval of the application.

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21. Mergers, Consolidations, Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors during 1978—Cont.

Chemical Bank, New York, N.Y., ***to merge with*** **Chemical Bank of Binghamton, Binghamton, N.Y.; Chemical Bank—Buffalo, Buffalo, N.Y.; Chemical Bank—Eastern, N.A., Greenwich, N.Y.; Chemical Bank of Rochester, Hilton, N.Y.; and Chemical Bank of Syracuse, Syracuse, N.Y.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (7-14-78)

The merging banks are all wholly owned subsidiaries of the same bank holding company. As such, their proposed merger is essentially a corporate reorganization and would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (8-11-78)

Chemical Bank (Applicant), a subsidiary of Chemical New York Corporation, a bank holding company, proposes to merge with 5 upstate New York banks that are also subsidiaries of Chemical New York Corporation. The proposed merger is essentially a corporate reorganization and, as such, raises no competitive issues. The application does not involve the acquisition of an additional bank by the holding company, and thus the financial and managerial resources of the institutions involved are consistent with approval of the application.

The Connecticut Bank and Trust Company, Hartford, Conn., ***to merge with*** **The Connecticut Bank and Trust Company, N.A., Norwalk, Conn.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (7-14-78)

The merging banks are both wholly owned subsidiaries of the same bank holding company. As such, their proposed merger is essentially a corporate reorganization and would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (8-15-78)

The Connecticut Bank and Trust Company (Applicant) and The Connecticut Bank and Trust Company, N.A. (CBT), are both subsidiaries of CBT Corporation, Hartford, a bank holding company. Since both banks involved in this transaction are subsidiaries of the same holding company, its consummation would not eliminate any existing or future competition, or increase the concentration of banking resources: it does not appear that approval of the application would have any adverse effect on other banks within the relevant banking market.

The financial and managerial resources and prospects of both banks and the resulting bank are consistent with approval. It is anticipated that the proposed merger will result in operational economies and a more efficient use of management skills and resources by CBT Corporation. In addition, public convenience in the service area of CBT may be enhanced as a result of access to services provided by Applicant, including trust and lending facilities. Accordingly, considerations relating to the convenience and needs of the communities to be served are consistent with approval.

The Conway Trust Company, Conway, N.H., ***to merge with*** **The Carroll County Trust Company, Conway, N.H.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (7-14-78)

The proposed merger is part of a plan through which The Carroll County Trust Company would become a subsidiary of Indian Head Banks, Inc., a bank holding company. The instant merger, however, would merely combine an existing bank with a nonoperating institution [The Conway Trust Company];

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as such, and without regard to the acquisition of the surviving bank by Indian Head Banks, Inc., it would have no effect on competition.

BASIS FOR APPROVAL BY BOARD OF GOVERNORS (8-25-78)

The proposal is a transaction to facilitate the acquisition of The Carroll County Trust Company by Indian Head Banks, Inc., a bank holding company.

The proposed merger would, in itself, have no adverse competitive effects. The financial and convenience and needs factors are consistent with approval of the application.

Bank of Utah, Ogden, Utah, *to merge with* Bank of Northern Utah, Clearfield, Utah

SUMMARY REPORT BY THE ATTORNEY GENERAL (7-20-78)

We have reviewed this proposed transaction and conclude that it would not have a significantly adverse effect upon competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (9-6-78)

Bank of Utah (Applicant) operates 13 offices in the State of Utah but has no branches in Clearfield, where the sole office of Bank of Northern Utah (BNU) is located. Applicant's nearest offices are a branch located in Roy City, 6 miles north of Clearfield, and another in East Layton, 7 miles southeast of Clearfield. There appears to be a slight overlap of the service areas of BNU and the Roy City office of Applicant. Therefore, consummation of the proposal may result in the elimination of a minimal amount of competition.

Competition, however, does not appear to be an issue. Utah operates under home office protection laws, which prohibit Applicant from branching *de novo* into the Clearfield banking market. Thus, Applicant's only means of entering this market appears to be through the proposed merger. Stockholders who own, directly or indirectly, 78.6 per cent of the outstanding shares of Applicant also own 68 per cent of the outstanding shares of BNU; Tennessee Homestead Company owns 48.3 per cent of the outstanding shares of Applicant as well as 24 per cent of those of BNU. Furthermore, 3 directors and 3 officers of Applicant hold the same positions in BNU. Although common ownership may have resulted in the elimination of some competition, considerations relating to competitive effects of this proposal are, at most, only slightly adverse. Moreover, it appears unlikely that denial of this application would disrupt the affiliation between these banks.

The range and quality of banking services provided to customers of BNU would be increased by the merger. To the extent that Applicant's trust department operations, credit card services, check protective service, increased lending limits, and interbranch banking capabilities would become available to BNU's customers, public benefit considerations weigh in favor of approval of the application.

First Virginia Bank—Eastern, Warrenton, Va., *to merge with* Bank of Warrenton, Warrenton, Va.

SUMMARY REPORT BY THE ATTORNEY GENERAL (8-8-78)

The proposed merger is part of a plan through which Bank of Warrenton would become a subsidiary of First Virginia Banks, Inc., a bank holding company. The instant merger, however, would merely combine an existing bank with a nonoperating institution [First Virginia Bank—Eastern]; as such, and without regard to the acquisition of the surviving bank by First Virginia Banks, Inc., it would have no effect on competition.

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21. Mergers, Consolidations, Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors during 1978—Cont.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (9-6-78)

The proposal is a transaction to facilitate the acquisition of Bank of Warrenton by First Virginia Banks, Inc., Falls Church, Virginia, a bank holding company.
The proposed merger would, in itself, have no adverse competitive effects. The financial and convenience and needs factors are consistent with approval of the application.

Bank of Utah, Ogden, Utah, ***to merge with*** **Bank of Brigham City, Brigham City, Utah**

SUMMARY REPORT BY THE ATTORNEY GENERAL (8-8-78)

We have reviewed this proposed transaction and conclude that it would not have a significantly adverse effect upon competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (9-20-78)

Bank of Utah (Applicant) is the 8th largest bank in the State and the 3rd largest in the Ogden metropolitan banking market. Bank of Brigham City (Brigham Bank) operates 1 branch office in Garland, 20 miles northwest of Brigham City. The 2 banks serve different banking markets, with the nearest offices 17 miles apart. They have substantial common ownership and management: 78.6 per cent of the outstanding shares of Applicant are held by owners of 69 per cent of the outstanding shares of Brigham Bank. The 2 banks also have 6 directors and 3 officers in common.
The Brigham City banking market, consisting of the counties of Box and Elder, is served by 4 banking institutions; Brigham Bank's market share of 5 per cent is the smallest. Under the State's home office protection laws, Applicant is prohibited from branching directly into Brigham City. The Board concluded that the merger would have no adverse effects on competition.
The area served by both banks has an exceptionally strong economic base, which should contribute to the continued growth and prosperity of the resulting bank. And the range and quality of banking services provided to Brigham Bank would be increased through the proposed merger.

The F.B.G. Bank of Mount Sterling, Mount Sterling, Ohio, ***to merge with*** **The Sterling State Bank, Mount Sterling, Ohio**

SUMMARY REPORT BY THE ATTORNEY GENERAL (7-31-78)

The proposed merger is part of a plan through which The Sterling State Bank would become a subsidiary of First Bank Group of Ohio, Inc., a bank holding company. The instant merger, however, would merely combine an existing bank with a nonoperating institution [The F.B.G. Bank of Mount Sterling]; as such, and without regard to the acquisition of the surviving bank by First Banc Group of Ohio, Inc., it would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (9-20-78)

The proposal is a transaction to facilitate the acquisition of The Sterling State Bank by First Banc Group of Ohio, Inc., Columbus, Ohio, a bank holding company.
The proposed merger would, in itself, have no adverse competitive effects. The financial and convenience and needs factors are consistent with approval of the application.

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Southern Bank and Trust Company, Richmond, Va., ***to merge with*** **Williamsburg National Bank, Williamsburg, Va.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (8-28-78)

The merging banks are both wholly owned subsidiaries of the same bank holding company. As such, their proposed merger is essentially a corporate reorganization and would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (9-29-78)

Both banks are subsidiaries of Southern Bankshares, Inc., Richmond, Virginia, a bank holding company, and thus consummation of the proposed merger would have no adverse competitive effects.

Banking factors are consistent with approval of the application, as is the convenience and needs factor. The merger is expected to result in more efficient operations and additional services.

First State Bank of Miami, Miami, Fla., ***to merge with*** **Hialeah—Miami Springs First State Bank, Hialeah, Fla.; North Hialeah First State Bank, Hialeah, Fla.; Airport First State Bank, Miami, Fla.; Miami Lakes First State Bank, Hialeah, Fla.; and North Miami First State Bank, North Miami, Fla.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (8-30-78)

The merging banks are all wholly owned subsidiaries of the same bank holding company. As such, their proposed merger is essentially a corporate reorganization and would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (10-3-78)

The proposed merger involves 5 subsidiaries of First State Banking Corporation, Miami, Florida, a bank holding company, and First State Bank of Miami, also a subsidiary of First State Banking Corporation. Since all the banks involved are subsidiaries of the same holding company, the transaction would have no effect on competition. The banks are generally in satisfactory condition and the banking factors are consistent with approval of the application. While the merger would have little effect on the convenience and needs of the communities to be served, this factor is also consistent with approval.

Bank of Virginia—Richmond, Richmond, Va., ***to merge with*** **Bank of Virginia, Richmond, Va.; Bank of Virginia—Eastern, Norfolk, Va.; Bank of Virginia—Eastern Shore, Hallwood, Va.; Bank of Virginia—Loudoun, Sterling, Va.; Bank of Virginia—Petersburg, Petersburg, Va.; Bank of Virginia—Potomac, Falls Church, Va.; Bank of Virginia—Shenandoah, Winchester, Va.; Bank of Virginia—Southwest, Roanoke, Va.; and Bank of Virginia—Warren, Front Royal, Va.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (7-31-78)

The proposed merger is part of a plan through which Bank of Virginia—Potomac, Bank of Virginia—Warren, Bank of Virginia—Eastern Shore, Bank of Virginia—Loudoun, Bank of Virginia—Eastern, Bank of Virginia—Petersburg, Bank of Virginia, Bank of Virginia—Southwest, and Bank of Virginia—Shenandoah would become subsidiaries of Bank of Virginia Company, a bank holding company. The instant merger, however, would merely combine the existing banks with a nonoperating institution [Bank of Virginia—Richmond]; as such, and without regard to the acquisition of the surviving banks by Bank of Virginia Company, it would have no effect on competition.

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21. Mergers, Consolidations, Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors during 1978—Cont.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (10-6-78)

Bank of Virginia—Richmond is a newly organized bank, which was formed as a vehicle to merge together the 9 banking subsidiaries of Bank of Virginia Company, Richmond, Virginia, a bank holding company. The resulting bank will operate under the charter of Bank of Virginia—Richmond and under the title of Bank of Virginia.

Relative to this proposal, Bank of Virginia Company has submitted an application for prior approval of the acquisition of Bank of Virginia—Richmond.

The proposed merger is merely a consolidation of the 9 existing banking subsidiaries of Bank of Virginia Company and, as such, would have no adverse competitive effects. All the banks involved are generally in satisfactory condition, and the banking factors are consistent with approval. Considerations relating to the convenience and needs of the communities to be served are also consistent with approval, to the extent that a pooling of resources within the merging banks and a reduction of duplicated services should result in more efficient operations.

The Connecticut Bank and Trust Company, Hartford, Conn., ***to merge with*** **Liberty National Bank, Stamford, Conn.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (10-13-78)

The closest offices of the 2 institutions are 4.5 miles apart. Although, according to the application, the primary service areas of the 2 institutions do not overlap, the parties derive deposits and loans from each service area. As of June 1, 1978, Bank [Liberty National] drew 5.8 per cent of its deposits; 12.1 per cent of its instalment loans; 14.7 per cent of its residential mortgage loans; and 10.7 per cent of its commercial loans from Applicant's [The Connecticut Bank and Trust Company] service area. As of the same date, Applicant drew 0.4 per cent of its deposits from Bank's primary service area. (Information on loans drawn from Bank's primary service area was not sufficient.) Thus, it appears that the proposed acquisition would eliminate some direct competition between the 2 institutions.

Applicant is the second largest bank in Connecticut, with 19.7 per cent of total deposits, while Bank ranks 35th with 0.2 per cent of total deposits. Although there are 21 commercial banks in Fairfield County, the market is highly concentrated, with the 4 largest commercial banks holding 71.4 per cent of total deposits. Applicant and Bank had market shares of 2.2 per cent and 0.6 per cent, respectively. The Stamford SMSA is also highly concentrated, with the 2 largest banks controlling 63.4 per cent of commercial bank deposits. Applicant and Bank have market shares of 2.5 per cent and 1.5 per cent, respectively. Thus, the proposed acquisition would result in slight increases in concentration in Connecticut, Fairfield County, and the Stamford SMSA.

Connecticut banking law precludes Applicant from branching into Stamford as a result of the home office protection provision of Connecticut's branching law (CGSA, Section 36–59). Applicant could enter the Stamford area through the establishment of a new bank owned by its parent holding company. Given Applicant's size and economic health, the continued growth of the Stamford area, and Applicant's presence in contiguous areas of Fairfield County, it appears to be a primary candidate for *de novo* entry into Stamford. Such would, of course, be more competitive since it would introduce a new competitor into the market, rather than eliminating an existing competitor via merger.

In sum, the proposed acquisition would have a slightly adverse effect on competition.

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BASIS FOR APPROVAL BY BOARD OF GOVERNORS (11-1-78)

The Connecticut Bank and Trust Company (Applicant) and a Norwalk-based bank, with deposits of $16 million, are the only 2 banking subsidiaries of CBT Corporation, a bank holding company. Permission to merge these subsidiaries was recently granted by the Federal Reserve Bank of Boston under delegated authority. Liberty National Bank (Liberty), which was established in 1972, operates 3 offices, all in Stamford. Applicant's nearest office to Liberty's is in Darien, 4.5 miles distant; there are 8 offices of other commercial banks in the intervening area. The home office protection feature of the Connecticut statutes prevents Applicant from entering Stamford through *de novo* branching. There is an insignificant amount of competition existing between the proponents.

Liberty's offices are in the Stamford-Norwalk section of the New York metropolitan banking market. Among the 16 commercial banking organizations represented in the Stamford-Norwalk area, CBT Corporation ranks 8th with 3.2 per cent of area deposits, while Liberty ranks 13th, with 1.1 per cent. In the New York metropolitan banking market, CBT Corporation would hold less than 1 per cent of market deposits following consummation of the instant proposal.

In Connecticut, Applicant now ranks 1st, based on deposit size, among the State's 61 commercial banking organizations and controls slightly more than 18 per cent of the deposits held by such organizations. Liberty holds only about 0.2 per cent of such deposits. Connecticut also has 65 mutual savings banks.

The over-all effect of the proposed merger on competition is considered slightly adverse.

Banking factors are consistent with approval, and the convenience and needs factor lends some weight to approval. For instance, although the area served by Liberty is also served by several other commercial banks, the proposed merger would result in an increase in the number of services available at the offices now operated by Liberty. In addition, the interest rate payable on savings accounts at Liberty's offices would be increased by 0.5 per cent.

Nova Bank and Trust Company, Newport News, Va., ***to merge with*** **First City Bank of Newport News, Newport News, Va.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (10-13-78)

The proposed merger is part of a plan through which First City Bank of Newport News would become a subsidiary of New Virginia Bancorporation, a bank holding company. The instant merger, however, would merely combine an existing bank with a nonoperating institution [Nova Bank and Trust Company]; as such, and without regard to the acquisition of the surviving bank by New Virginia Bancorporation, it would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (11-29-78)

The proposal is a transaction to facilitate the acquisition of First City Bank of Newport News by New Virginia Bancorporation, Springfield, Va., a bank holding company.

The proposed merger would, in itself, have no adverse competitive effects. The financial and convenience and needs factors are consistent with approval of the application.

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21. Mergers, Consolidations, Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors during 1978—Cont.

First Virginia Bank, Falls Church, Va., ***to merge with*** **First Virginia Bank/ Manassas National, Manassas, Va.**

SUMMARY REPORT BY THE ATTORNEY GENERAL (11-13-78)

The merging banks are both wholly owned subsidiaries of the same bank holding company. As such, their proposed merger is essentially a corporate reorganization and would have no effect on competition.

BASIS FOR APPROVAL BY FEDERAL RESERVE BANK (11-29-78)

Both banks are subsidiaries of First Virignia Banks, Inc., Falls Church, Virginia, a bank holding company that is the State's 6th largest banking organization, with 6.8 per cent of Statewide deposits. Because of common ownership, the merger would result in no change in the relative position of First Virginia Banks, Inc., in the State or in the relevant banking markets, and would have no adverse effects on existing or potential competition in the areas.

The financial and managerial resources and future prospects of the 2 banks proposing to merge and of the resulting institution are satisfactory and are considered to be consistent with approval of the application. Considerations relating to the convenience and needs of the community lend support to aoproval because the proposed merger would enable First Virginia Bank/ Manassas National to make larger loans without participations; in addition, there should be a pooling of resources within the merging banks and a reduction of duplicated services, resulting in more efficient operations and improved customer services.

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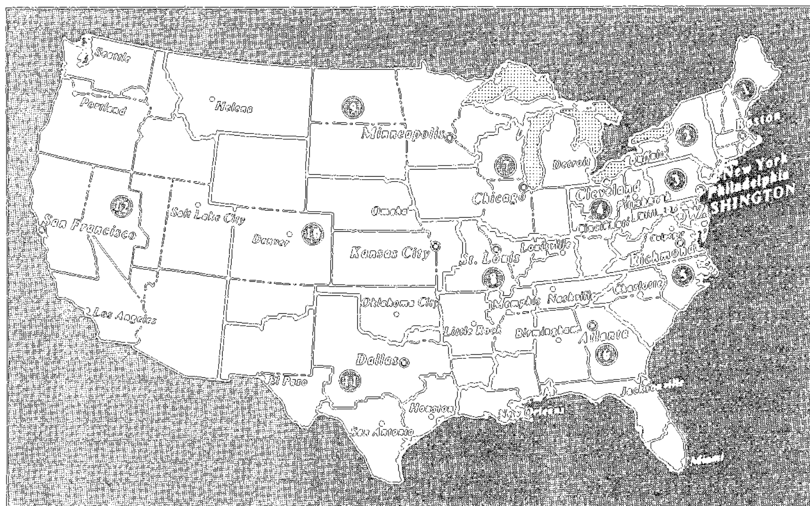
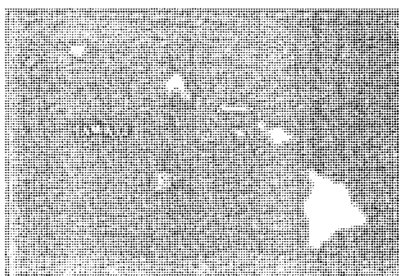
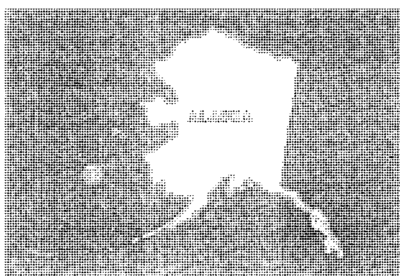
The Federal Reserve System

BOUNDARIES OF FEDERAL RESERVE DISTRICTS AND THEIR BRANCH TERRITORIES







Legend

- —— Boundaries of Federal Reserve Districts
- —— Boundaries of Federal Reserve Branch Territories
- ◎ Board of Governors of the Federal Reserve System
- ◉ Federal Reserve Bank Cities
- ◦ Federal Reserve Branch Cities
- · Federal Reserve Bank Facilities

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Board of Governors of the Federal Reserve System

December 31, 1978

	Term expires
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Vacant	January 31, 1982
NANCY H. TEETERS, of Indiana	January 31, 1984
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HENRY C. WALLICH, of Connecticut	January 31, 1988
Vacant	January 31, 1990

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[1] The designation as Chairman expires Mar. 7, 1982, unless the services of this member of the Board shall have terminated sooner.
[2] On loan from the Federal Reserve Bank of Atlanta.

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NATHANIEL E. BUTLER, *Assoc. Director*
JERAULD C. KLUCKMAN, *Assoc. Director*
ANNE GEARY, *Asst. Director*

DIVISION OF PERSONNEL

DAVID L. SHANNON, *Director*
JOHN R. WEIS, *Asst. Director*
CHARLES W. WOOD, *Asst. Director*

DIVISION OF ADMINISTRATIVE SERVICES

WALTER W. KREIMANN, *Director*
JOHN L. GRIZZARD, *Asst. Director*
JOHN D. SMITH, *Asst. Director*

OFFICE OF THE CONTROLLER

JOHN KAKALEC, *Controller*
EDWARD T. MULRENIN, *Asst. Controller*

DIVISION OF DATA PROCESSING

CHARLES L. HAMPTON, *Director*
BRUCE M. BEARDSLEY, *Assoc. Director*
UYLESS D. BLACK, *Asst. Director*
GLENN L. CUMMINS, *Asst. Director*
ROBERT J. ZEMEL, *Asst. Director*

[3] On loan from the Federal Reserve Bank of New York.

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Federal Reserve Bank of St. Louis

Federal Open Market Committee

December 31, 1978

MEMBERS

G. WILLIAM MILLER, *Chairman* (Board of Governors)

PAUL A. VOLCKER, *Vice Chairman* (elected by Federal Reserve Bank of New York)

ERNEST T. BAUGHMAN (elected by Federal Reserve Banks of Atlanta, St. Louis, and Dallas)

PHILIP E. COLDWELL (Board of Governors)

DAVID P. EASTBURN (elected by Federal Reserve Banks of Boston, Philadelphia, and Richmond)

J. CHARLES PARTEE (Board of Governors)

NANCY H. TEETERS (Board of Governors)

HENRY C. WALLICH (Board of Governors)

MARK H. WILLES (elected by Federal Reserve Banks of Minneapolis, Kansas City, and San Francisco)

WILLIS J. WINN (elected by Federal Reserve Banks of Cleveland and Chicago)

OFFICERS

MURRAY ALTMANN, *Secretary*

NORMAND R. V. BERNARD, *Assistant Secretary*

THOMAS J. O'CONNELL, *General Counsel*

EDWARD G. GUY, *Deputy General Counsel*

ROBERT E. MANNION, *Assistant General Counsel*

STEPHEN H. AXILROD, *Economist*

JOSEPH BURNS, *Associate Economist*

JOHN M. DAVIS, *Associate Economist*

RICHARD G. DAVIS, *Associate Economist*

EDWARD C. ETTIN, *Associate Economist*

IRA KAMINOW, *Associate Economist*

PETER M. KEIR, *Associate Economist*

JAMES L. KICHLINE, *Associate Economist*

JOHN D. PAULUS, *Associate Economist*

EDWIN M. TRUMAN, *Associate Economist*

JOSEPH S. ZEISEL, *Associate Economist*

ALAN R. HOLMES, *Manager, System Open Market Account*

PETER D. STERNLIGHT, *Deputy Manager for Domestic Operations*

SCOTT E. PARDEE, *Deputy Manager for Foreign Operations*

During 1978, meetings of the Federal Open Market Committee were generally held at monthly intervals. (See "Record of Policy Actions of the Federal Open Market Committee" in this REPORT.)

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Federal Reserve Bank of St. Louis

Federal Advisory Council

December 31, 1978

MEMBERS

District No. 1—HENRY S. WOODBRIDGE, President, Rhode Island Hospital Trust National Bank, Providence, R.I.

District No. 2—WALTER B. WRISTON, Chairman of the Board, Citibank, N.A., New York, N.Y.

District No. 3—WILLIAM B. EAGLESON, JR., Chairman and President, Girard Bank, Philadelphia, Pa.

District No. 4—M. BROCK WEIR, Chairman and Chief Executive Officer, Cleveland Trust Company, Cleveland, Ohio.

District No. 5—JOHN H. LUMPKIN, Chairman and Chief Executive Officer, The South Carolina National Bank, Columbia, S.C.

District No. 6—FRANK A. PLUMMER, Chairman of the Board, First Alabama Bank of Montgomery, N.A., Montgomery, Ala.

District No. 7—EDWARD BYRON SMITH, Chairman of the Board, Northern Trust Co., Chicago, Ill.

District No. 8—CLARENCE C. BARKSDALE, Chairman of the Board and Chief Executive Officer, First National Bank in St. Louis, St. Louis, Mo.

District No. 9—RICHARD H. VAUGHAN, President, Northwest Bancorporation, Minneapolis, Minn.

District No. 10—J. W. McLEAN, Chairman of the Board, The Liberty National Bank and Trust Company of Oklahoma City, Oklahoma City, Okla.

District No. 11—JAMES D. BERRY, Chairman of the Board and Chief Executive Officer, Republic of Texas Corporation, Dallas, Tex.

District No. 12—GILBERT F. BRADLEY, Chairman and Chief Executive Officer, Valley National Bank, Phoenix, Ariz.

OFFICERS

GILBERT F. BRADLEY, *President* J. W. McLEAN, *Vice President*
HERBERT V. PROCHNOW, *Secretary*
WILLIAM J. KORSVIK, *Associate Secretary*

EXECUTIVE COMMITTEE

GILBERT F. BRADLEY
J. W. McLEAN
FRANK A. PLUMMER
EDWARD BYRON SMITH
WALTER B. WRISTON

Meetings of the Federal Advisory Council were held on February 2–3, May 4–5, September 7–8, and November 2–3, 1978. The Board of Governors met with the Council on February 3, May 5, September 8, and November 3. The Council, which is composed of 12 representatives of the banking industry, one from each Federal Reserve district, is required by law to meet in Washington at least four times each year, and is authorized by the Federal Reserve Act to consult with and advise the Board on all matters within the jurisdiction of the Board.

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Consumer Advisory Council

December 31, 1978

LEONOR K. SULLIVAN, St. Louis, Missouri, *Chairman*
WILLIAM D. WARREN, Los Angeles, California, *Vice Chairman*

ROLAND E. BRANDEL, San Francisco, California
AGNES H. BRYANT, Detroit, Michigan
JOHN G. BULL, Fort Lauderdale, Florida
ROBERT V. BULLOCK, Frankfort, Kentucky
LINDA M. COHEN, Washington, D.C.
ANNE G. DRAPER, Washington, D.C.
CARL FELSENFELD, New York, New York
JEAN A. FOX, Pittsburgh, Pennsylvania
MARCIA A. HAKALA, Omaha, Nebraska
JOSEPH F. HOLT III, Los Angeles, California
RICHARD H. HOLTON, Berkeley, California
EDNA DECOURSEY JOHNSON, Baltimore, Maryland
RICHARD F. KERR, Cincinnati, Ohio
ROBERT J. KLEIN, New York, New York
PERCY W. LOY, Portland, Oregon
R. C. MORGAN, El Paso, Texas
REECE A. OVERCASH, JR., Dallas, Texas
RAYMOND J. SAULNIER, New York, New York
E. G. SCHUHART II, Amarillo, Texas
BLAIR C. SHICK, Cambridge, Massachusetts
JAMES E. SUTTON, Dallas, Texas
THOMAS R. SWAN, Portland, Maine
ANNE GARY TAYLOR, Alexandria, Virginia
RICHARD D. WAGNER, Simsbury, Connecticut
RICHARD L. WHEATLEY, JR., Stillwater, Oklahoma

Meetings between the Consumer Advisory Council and members of the Board of Governors were held on March 8–9, May 31–June 1, September 13–14, and December 6–7, 1978. The Council, which is composed of creditors, consumers, and others, is authorized by the Equal Credit Opportunity Act to meet periodically to advise the Board on consumer-related matters.

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Federal Reserve Banks and Branches

December 31, 1978

CHAIRMEN AND DEPUTY CHAIRMEN OF BOARDS OF DIRECTORS

Federal Reserve Bank	Chairman and Federal Reserve Agent	Deputy Chairman
Boston	Louis W. Cabot	Robert M. Solow
New York	Robert H. Knight	Boris Yavitz
Philadelphia	John W. Eckman	Werner C. Brown
Cleveland	Robert E. Kirby	Otis A. Singletary
Richmond	E. Angus Powell	Maceo A. Sloan
Atlanta	Clifford M. Kirtland, Jr.	William A. Fickling, Jr.
Chicago	Robert H. Strotz	John Sagan
St. Louis	Armand C. Stalnaker	William B. Walton
Minneapolis	James P. McFarland	Stephen F. Keating
Kansas City	Harold W. Andersen	Joseph H. Williams
Dallas	Irving A. Mathews	Charles T. Beaird
San Francisco	Joseph F. Alibrandi	Cornell C. Maier

CONFERENCE OF CHAIRMEN

The Chairmen of the Federal Reserve Banks are organized into a Conference of Chairmen that meets from time to time to consider matters of common interest and to consult with and advise the Board of Governors. Such meetings, attended also by Deputy Chairmen of the Reserve Banks, were held in Washington on June 13 and November 30–December 1, 1978.

E. Angus Powell, Chairman of the Federal Reserve Bank of Richmond, who was elected Chairman of the Conference and of its Executive Committee in December 1977, served in that capacity until the close of the 1978 meetings. Joseph F. Alibrandi, Chairman of the Federal Reserve Bank of San Francisco, and Harold W. Andersen, Chairman of the Federal Reserve Bank of Kansas City, served with Mr. Powell as members of the Executive Committee; Mr. Alibrandi also served as Vice Chairman of the Conference.

On December 1, 1978, Mr. Alibrandi was elected Chairman of the Conference and of its Executive Committee to serve for the succeeding year; Harold W. Andersen, Chairman of the Federal Reserve Bank of Kansas City, was elected Vice Chairman of the Conference and a member of the Executive Committee; and John W. Eckman, Chairman of the Federal Reserve Bank of Philadelphia, was elected as the other member of the Executive Committee.

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DIRECTORS

Class A and Class B directors are elected by the member banks of the district. Class C directors are appointed by the Board of Governors of the Federal Reserve System. One term in each class of directors expires each year. Directors are chosen without discrimination as to race, creed, color, sex, or national origin.

The Class A directors are chosen as representatives of member banks and, as a matter of practice, are active officers of member banks. Class B and Class C directors represent the public and are selected with due, but not exclusive, consideration to the interests of agriculture, commerce, industry, services, labor, and consumers. Class B and C directors may not be officers, directors, or employees of any bank, nor may Class C directors be stockholders of any bank. Annually, the Board of Governors designates one Class C director of each Reserve Bank to serve as Chairman of the Bank and one to serve as Deputy Chairman.

Federal Reserve Bank branches have either five or seven directors, of whom a majority are appointed by the board of directors of the parent Federal Reserve Bank. The others are appointed by the Board of Governors of the Federal Reserve System. The Chairmen of branch Bank boards are selected from among directors appointed by the Board of Governors.

District 1—BOSTON

		Term expires Dec. 31
Class A		
John Robinson	Farmington, Maine	1978
John Hunter, Jr.	President, Vermont National Bank, Brattleboro, Vt.	1979
Richard D. Hill	Chairman of the Board, First National Boston Corporation, Boston, Mass.	1980
Class B		
A. W. Van Sinderen	President, The Southern New England Telephone Company, New Haven, Conn.	1978
Carol R. Goldberg	President, Stop & Shop Manufacturing Company, Boston, Mass.	1979
Weston P. Figgins	Chairman of the Board, Wm. Filene's Sons Company, Boston, Mass.	1980
Class C		
Louis W. Cabot	Chairman of the Board, Cabot Corporation, Boston, Mass.	1978
Kenneth I. Guscott	President, Ken Guscott Associates, Boston, Mass.	1979
Robert M. Solow	Institute Professor, Massachusetts Institute of Technology, Cambridge, Mass.	1980

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District 2—NEW YORK

		Term expires Dec. 31
Class A		
James Whelden	President, Ballston Spa National Bank, Ballston Spa, N.Y.	1978
Ellmore C. Patterson	Chairman of the Executive Committee, Morgan Guaranty Trust Company of New York, New York, N.Y.	1979
Raymond W. Bauer	Chairman and President, United Counties Trust Company, Elizabeth, N.J.	1980
Class B		
John R. Mulhearn	President, New York Telephone Company, New York, N.Y.	1978
Maurice F. Granville	Chairman of the Board, Texaco Inc., White Plains, N.Y.	1979
William S. Sneath	Chairman of the Board, Union Carbide Corporation, New York, N.Y.	1980
Class C		
G. G. Michelson	Senior Vice President, Macy's New York, New York, N.Y.	1978
Boris Yavitz	Dean, Graduate School of Business, Columbia University, New York, N.Y.	1979
Robert H. Knight	Partner, Shearman & Sterling, New York, N.Y.	1980

BUFFALO BRANCH

Appointed by Federal Reserve Bank		
Robert J. Donough	President and Chief Executive Officer, Liberty National Bank and Trust Company, Buffalo, N.Y.	1978
M. Jane Dickman	Partner, Touche Ross & Co., Buffalo, N.Y.	1979
William W. Webber	Vice Chairman of the Board, Lincoln First Bank N.A., Rochester, N.Y.	1979
William S. Gavitt	President, The Lyons National Bank, Lyons, N.Y.	1980
Appointed by Board of Governors		
Donald R. Nesbitt	Owner, Silver Creek Farms, Albion, N.Y.	1978
Frederick D. Berkeley	Chairman of the Board and President, Graham Manufacturing Company, Inc., Batavia, N.Y.	1979
Paul A. Miller	President, Rochester Institute of Technology, Rochester, N.Y.	1980

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District 3—PHILADELPHIA

Term expires Dec. 31

Class A

Name	Position	Term expires Dec. 31
James Patchell	President and Chief Executive Officer, National Bank and Trust Company of Gloucester County, Woodbury, N.J.	1978
Donald J. Seebold	President, The First National Bank of Danville, Danville, Pa.	1979
Wilson M. Brown, Jr.	President and Chief Executive Officer, Southeast National Bank of Pennsylvania, Malvern, Pa.	1980

Class B

Name	Position	Term expires Dec. 31
Harold A. Shaub	President and Chief Executive Officer, Campbell Soup Co., Camden, N.J.	1978
William S. Masland	President and Chief Executive Officer, C. H. Masland & Sons, Carlisle, Pa.	1979
Jack K. Busby	Chairman and Chief Executive Officer, Pennsylvania Power & Light Company, Allentown, Pa.	1980

Class C

Name	Position	Term expires Dec. 31
John W. Eckman	Chairman and President, Rorer Group Inc., Fort Washington, Pa.	1978
Jean Crockett	Chairman, Department of Finance, University of Pennsylvania, Philadelphia, Pa.	1979
Werner C. Brown	Chairman, Hercules Incorporated, Wilmington, Del.	1980

District 4—CLEVELAND

Class A

Name	Position	Term expires Dec. 31
Richard P. Raish	President, First National Bank, Bellevue, Ohio	1978
John W. Alford	President, The Park National Bank, Newark, Ohio	1979
John A. Gelbach	Chairman of the Board, Central National Bank of Cleveland, Cleveland, Ohio	1980

Class B

Name	Position	Term expires Dec. 31
John J. Dwyer	President, Oglebay Norton Co., Cleveland, Ohio	1978
Charles Y. Lazarus	Chairman, The F. & R. Lazarus Co., Columbus, Ohio	1979
Hays T. Watkins	Chairman and President, Chessie System, Inc., Cleveland, Ohio	1980

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District 4—CLEVELAND—Cont.

		Term expires Dec. 31
Class C		
Otis A. Singletary	President, University of Kentucky, Lexington, Ky.	1978
Robert E. Kirby	Chairman and Chief Executive Officer, Westinghouse Electric Corp., Pittsburgh, Pa.	1979
Arnold R. Weber	Provost, Carnegie-Mellon University, Pittsburgh, Pa.	1980

CINCINNATI BRANCH

Appointed by Federal Reserve Bank		
Robert A. Kerr	Chairman and Chief Executive Officer, Winters National Bank and Trust Co., Dayton, Ohio	1978
Lawrence Hawkins	Senior Vice President, University of Cincinnati, Cincinnati, Ohio	1978
William N. Liggett	Chairman of the Board and Chief Executive Officer, The First National Bank of Cincinnati, Cincinnati, Ohio	1979
W. W. Hillenmeyer, Jr.	Chairman and Chief Executive Officer, First Security National Bank and Trust Company, Lexington, Ky.	1980
Appointed by Board of Governors		
Martin B. Friedman	President, Formica Corporation, Cincinnati, Ohio	1978
J. L. Jackson	President, Falcon Coal Company, Inc., Lexington, Ky.	1979
L. H. Rogers II	President and Chief Executive Officer, Omega Communications, Inc., Cincinnati, Ohio	1980

PITTSBURGH BRANCH

Appointed by Federal Reserve Bank		
R. Burt Gookin	Vice Chairman and Chief Executive Officer, H. J. Heinz Co., Pittsburgh, Pa.	1978
William E. Midkiff III	Chairman of the Board, The First National Bank in Steubenville, Steubenville, Ohio	1978
Peter Mortensen	President, F.N.B. Corporation, Sharon, Pa.	1979
William E. Bierer	President, Equibank N.A., Pittsburgh, Pa.	1980

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District 4—CLEVELAND—Cont.

Term expires Dec. 31

PITTSBURGH BRANCH—Cont.

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
William H. Knoell	President, Cyclops Corporation, Pittsburgh, Pa.	1978
G. Jackson Tankersley	President, Consolidated Natural Gas Company, Pittsburgh, Pa.	1979
Lloyd M. McBride	President, United Steelworkers of America, Pittsburgh, Pa.	1980

District 5—RICHMOND

Class A

Name	Position	Term expires Dec. 31
J. Owen Cole	Chairman of the Board, First National Bank of Maryland, Baltimore, Md.	1978
Frank B. Robards, Jr.	President, Rock Hill National Bank, Rock Hill, S.C.	1979
Frederic H. Phillips	President, New Bank of Roanoke, Roanoke, Va.	1980

Class B

Name	Position	Term expires Dec. 31
Paul E. Reichardt	Chairman of the Board and Chief Executive Officer, Washington Gas Light Company, Washington, D. C.	1978
Andrew L. Clark	President, Andy Clark Ford, Inc., Princeton, W. Va.	1979
Thomas A. Jordan	Secretary-Treasurer, Stuart Furniture Industries, Inc., Asheboro, N.C.	1980

Class C

Name	Position	Term expires Dec. 31
Maceo A. Sloan	Executive Vice President, North Carolina Mutual Life Insurance Co., Durham, N.C.	1978
E. Angus Powell	Partner, Midlothian Company, Midlothian, Va.	1979
Steven Muller	President, The Johns Hopkins University, Baltimore, Md.	1980

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District 5—RICHMOND—Cont.

Term expires Dec. 31

BALTIMORE BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
Pearl C. Brackett	Assistant/Deputy Manager, Baltimore Regional Chapter of American Red Cross, Baltimore, Md.	1978
Lacy I. Rice, Jr.	President, The Old National Bank of Martinsburg, Martinsburg, W. Va.	1979
A. R. Reppert	President, The Union National Bank of Clarksburg, Clarksburg, W. Va.	1979
Joseph M. Gough, Jr.	President, The First National Bank of St. Mary's, Leonardtown, Md.	1980

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
David W. Barton, Jr.	President, The Barton-Gillet Company, Baltimore, Md.	1978
I. E. Killian	President, Killian Enterprises, Inc., Gibson Island, Md.	1979
Catherine B. Doehler	Baltimore, Md.	1980

CHARLOTTE BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
William W. Bruner	Chairman and President, First National Bank of South Carolina, Columbia, S.C.	1978
Thomas L. Benson	President, The Conway National Bank, Conway, S.C.	1979
W. B. Apple, Jr.	President, First National Bank of Reidsville, Reidsville, N.C.	1979
John T. Fielder	President, J. B. Ivey and Company, Charlotte, N.C.	1980

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
Robert C. Edwards	President, Clemson University, Clemson, S.C.	1978
Naomi G. Albanese	Dean, School of Home Economics, University of North Carolina at Greensboro, Greensboro, N.C.	1979
Robert E. Elberson	President, Chief Executive Officer and Director, Hanes Corporation, Winston-Salem, N.C.	1980

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District 6—ATLANTA

		Term expires Dec. 31
Class A		
Sam I. Yarnell	Chairman, American National Bank and Trust Co., Chattanooga, Tenn.	1978
John T. Oliver, Jr.	President, First National Bank of Jasper, Jasper, Ala.	1979
Hugh M. Willson	President, Citizens National Bank, Athens, Tenn.	1980
Class B		
George W. Jenkins	Chairman, Publix Super Markets, Inc., Lakeland, Fla.	1978
Jean McArthur Davis	President, McArthur Dairy, Inc., Miami, Fla.	1979
Ulysses V. Goodwyn	Executive Vice President, Southern National Resources, Inc., Birmingham, Ala.	1980
Class C		
Fred Adams, Jr.	President, Cal-Maine Foods, Inc., Jackson, Miss.	1978
C. W. Kirtland, Jr.	President, Cox Broadcasting Corporation, Atlanta, Ga.	1979
Wm. A. Fickling, Jr.	President and Chairman, Charter Medical Corp., Macon, Ga.	1980

BIRMINGHAM BRANCH

Appointed by Federal Reserve Bank		
R. H. Woodrow, Jr.	Chairman of the Board and Chief Executive Officer, First National Bank of Birmingham, Birmingham, Ala.	1978
Drury Flowers	Chairman, First Alabama Bank of Dothan, Dothan, Ala.	1979
Martha H. Simms	Huntsville, Ala.	1979
George S. Shirley	President, The First National Bank of Tuscaloosa, Tuscaloosa, Ala.	1980
Appointed by Board of Governors		
Frank P. Samford, Jr.	Chairman of the Board, Liberty National Life Insurance Co., Birmingham, Ala.	1978
William H. Martin III	President and Chief Executive Officer, Martin Industries, Inc., Sheffield, Ala.	1979
Harold B. Blach, Jr.	President, Blach's Inc., Birmingham, Ala.	1980

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District 6—ATLANTA—Cont.

Term expires Dec. 31

JACKSONVILLE BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
John T. Cannon III	President, Barnett Bank of Cocoa, N.A., Cocoa, Fla.	1978
Richard E. Ehlis	Chairman of the Board and President, Florida National Bank of Lakeland, Lakeland, Fla.	1979
Wm. E. Arnold, Jr.	President, William E. Arnold Company, Jacksonville, Fla.	1979
DuBose Ausley	President and Chief Executive Officer, Capital City First National Bank, Tallahassee, Fla.	1980

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
James E. Lyons	President, Lyons Industrial Corporation, Winter Haven, Fla.	1978
Copeland D. Newbern	Chairman of the Board, Newbern Groves, Inc., Tampa, Fla.	1979
Joan W. Stein	Partner, Regency Square Shopping Center, Jacksonville, Fla.	1980

MIAMI BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
Sherrill E. Woods	President, First National Bank and Trust Company of Naples, Naples, Fla.	1978
Jane C. Cousins	President, Cousins Associates, Inc., Miami, Fla.	1978
Aristides R. Sastre	President, The Republic National Bank of Miami, Miami, Fla.	1979
Fred R. Millsaps	Chairman and President, Landmark Banking Corporation, Fort Lauderdale, Fla.	1980

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
Alvaro Luis Carta	President, Gulf + Western Americas Corporation, Vero Beach, Fla.	1978
Castle W. Jordan	President, Aegis Corporation, Coral Gables, Fla.	1979
David G. Robinson	President, Edison Community College, Fort Myers, Fla.	1980

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District 6—ATLANTA—Cont. *Term expires Dec. 31*

NASHVILLE BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
John W. Andersen	President, The First National Bank of Sullivan County, Kingsport, Tenn.	1978
Virgil H. Moore, Jr.	President, First Farmers and Merchants National Bank, Columbia, Tenn.	1979
Frank C. Thomas	President, Stearns Coal and Lumber Company, Knoxville, Tenn.	1979
James R. Austin	Chairman and Chief Executive Officer, Peoples National Bank, Shelbyville, Tenn.	1980

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
John C. Bolinger, Jr.	Management Consultant, Knoxville, Tenn	1978
Cecelia Adkins	Executive Director, Sunday School Publishing Board of the National Baptist Convention, U.S.A., Inc., Nashville, Tenn.	1979
Robert C. H. Mathews, Jr.	President, R. C. Mathews, Contractor, Inc., Nashville, Tenn.	1980

NEW ORLEANS BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
Wilmore W. Whitmore	President and Chief Executive Officer, First National Bank of Houma, Houma, La.	1978
Martin C. Miler	Chairman of the Board and President, The Hibernia National Bank, New Orleans, La.	1979
Geo. P. Hopkins, Jr.	President, George P. Hopkins, Inc., Contractor-Engineers, Gulfport, Miss.	1979
Wm. E. Howard, Jr.	Chairman of the Board, Commercial National Bank and Trust Company of Laurel, Laurel, Miss.	1980

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
Edwin J. Caplan	President, Caplan's Men's Shops, Inc., Alexandria, La.	1980
Levere C. Montgomery	President, Time Saver Stores, Inc., New Orleans, La.	1979
Geo. C. Cortright, Jr.	Partner, George C. Cortright Co., Rolling Fork, Miss.	1980

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District 7—CHICAGO

		Term expires Dec. 31
Class A		
A. Robert Abboud	Chairman of the Board, The First National Bank of Chicago, Chicago, Ill.	1978
Jay J. Delay	President, Huron Valley National Bank, Ann Arbor, Mich.	1979
John F. Spies	President, Iowa Trust and Savings Bank, Emmetsburg, Iowa	1980
Class B		
Oscar G. Mayer	Chairman of the Executive Committee, Oscar Mayer & Co., Inc., Madison, Wis.	1978
Paul V. Farver	Vice Chairman, Rolscreen Company, Pella, Iowa	1979
Arthur J. Decio	Chairman of the Board and Chief Executive Officer, Skyline Corporation, Elkhart, Ind.	1980
Class C		
Edward F. Brabec	Business Manager, Chicago Journeymen Plumbers, Local Union 130, U.A., Chicago, Ill.	1978
Robert H. Strotz	President, Northwestern University, Evanston, Ill.	1979
John Sagan	Vice President-Treasurer, Ford Motor Company, Dearborn, Mich.	1980

DETROIT BRANCH

Appointed by Federal Reserve Bank		
Joseph B. Foster	Chairman of the Board, Ann Arbor Bank, Ann Arbor, Mich.	1978
Chas. R. Montgomery	President, Michigan Consolidated Gas Company, Detroit, Mich.	1978
Rodkey Craighead	Chairman and Chief Executive Officer, Detroitbank Corporation, Detroit, Mich.	1979
Lawrence A. Johns	President, Isabella Bank and Trust, Mount Pleasant, Mich.	1980
Appointed by Board of Governors		
Herbert H. Dow	Director and Secretary, The Dow Chemical Company, Midland, Mich.	1978
Jordan B. Tatter	President and Chief Executive Officer, Southern Michigan Cold Storage Co., Benton Harbor, Mich.	1979
Howard F. Sims	President, Sims-Varner Associates, Inc., Detroit, Mich.	1980

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District 8—ST. LOUIS

		Term expires Dec. 31
Class A		
Wm. E. Weigel	Executive Vice President and Chief Executive Officer, First National Bank & Trust Co., Centralia, Ill.	1978
Raymond C. Burroughs	President and Chief Executive Officer, The City National Bank of Murphysboro, Murphysboro, Ill.	1979
Donald N. Brandin	Chairman and Chief Executive Officer, The Boatmen's National Bank, St. Louis, Mo.	1980
Class B		
Tom K. Smith, Jr.	Senior Vice President, Monsanto Company, St. Louis, Mo.	1978
Virginia M. Bailey	Owner, Eldo Properties, Little Rock, Ark.	1979
Ralph C. Bain	Vice President, Wabash Plastics, Inc., Evansville, Ind.	1980
Class C		
William B. Walton	Vice Chairman of the Board, Holiday Inns, Inc., Memphis, Tenn.	1978
Armand C. Stalnaker	Chairman and President, General American Life Insurance Co., St. Louis, Mo.	1979
William H. Stroube	Associate Dean of Faculty Programs, Western Kentucky University, Bowling Green, Ky.	1980

LITTLE ROCK BRANCH

Appointed by Federal Reserve Bank		
T. G. Vinson	President, The Citizens Bank, Batesville, Ark.	1978
Field Wasson	President, First National Bank, Siloam Springs, Ark.	1978
B. Finley Vinson	Vice Chairman of the Board, The First National Bank in Little Rock, Little Rock, Ark.	1979
Thos. E. Hayes, Jr.	President and Chief Executive Officer, The First National Bank of Hope, Hope, Ark.	1980
Appointed by Board of Governors		
G. Larry Kelley	President, Pickens-Bond Construction Co., Little Rock, Ark.	1978
E. Ray Kemp, Jr.	Vice Chairman of the Board and Chief Administrative Officer, Dillard Department Stores, Inc., Little Rock, Ark.	1979
Ronald W. Bailey	Executive Vice President and General Manager, Producers Rice Mill, Inc., Stuttgart, Ark.	1980

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District 8—ST. LOUIS—Cont.

		Term expires Dec. 31

LOUISVILLE BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
Tom G. Voss	President, The Seymour National Bank, Seymour, Ind.	1978
Fred B. Oney	President, The First National Bank of Carrollton, Carrollton, Ky.	1978
Howard J. Brenner	Vice Chairman of the Board, Tell City National Bank, Tell City, Ind.	1979
J. David Grissom	Chairman and Chief Executive Officer, Citizens Fidelity Bank and Trust Company, Louisville, Ky.	1980

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
James H. Davis	Chairman and Chief Executive Officer, Porter Paint Company, Louisville, Ky.	1978
James F. Thompson	Professor of Economics, Murray State University, Murray, Ky.	1979
Richard O. Donegan	Vice President and Group Executive, Major Appliance Business Group, Louisville, Ky.	1980

MEMPHIS BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
Wm. W. Mitchell	Chairman, First Tennessee Bank N.A., Memphis, Tenn,	1978
Stallings Lipford	President, First-Citizens National Bank of Dyersburg, Dyersburg, Tenn.	1978
Earl L. McCarroll	President, The Farmers Bank & Trust Co., Blytheville, Ark.	1978
Chas. S. Youngblood	President and Chief Executive Officer, First Columbus National Bank, Columbus, Miss.	1980

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
Jeanne L. Holley	Associate Professor of Business Education and Office Administration, University of Mississippi, University, Miss.	1978
Vacancy		1979
Frank A. Jones, Jr.	President, Cook Industries, Inc., Memphis, Tenn.	1980

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District 9—MINNEAPOLIS

		Term expires Dec. 31
Class A		
John S. Rouzie	Chairman, First National Bank of Bowman, Bowman, N. Dak.	1978
Nels E. Turnquist	President, National Bank of South Dakota, Sioux Falls, S. Dak.	1979
James H. Smaby	President, Commercial National Bank & Trust Co., Iron Mountain, Mich.	1980
Class B		
Russell G. Cleary	Chairman, President and Chief Executive Officer, G. Heileman Brewing Company, Inc., LaCrosse, Wis.	1978
James P. McFarland	Secretary-Treasurer, General Manager, Two Dot Land & Livestock Co., Harlowton, Mont.	1979
Donald P. Helgeson	Secretary and Vice President, Jack Frost, Inc., St. Cloud, Minn.	1980
Class C		
James P. McFarland	Retired Chairman, General Mills, Inc., Minneapolis, Minn.	1978
Sister Generose Gervais	Administrator, St. Mary's Hospital, Rochester, Minn.	1979
Stephen F. Keating	Vice Chairman of the Board, Honeywell, Inc., Minneapolis, Minn.	1980

HELENA BRANCH

Appointed by Federal Reserve Bank		
George H. Selover	President and General Manager, Selover Buick-Jeep, Inc., Billings, Mont.	1978
William B. Andrews	President, Northwestern Bank of Helena, Helena, Mont.	1978
Lynn D. Grobel	President, First National Bank of Glasgow, Glasgow, Mont.	1979
Appointed by Board of Governors		
Patricia P. Douglas	Vice President-Fiscal Affairs, University of Montana, Missoula, Mont.	1978
Norris E. Hanford	Fort Benton, Mont.	1979

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District 10—KANSAS CITY

Term expires Dec. 31

Class A

Name	Position	Term expires Dec. 31
James M. Kemper, Jr.	Chairman and President, Commerce BancShares, Inc., Kansas City, Mo.	1978
Philip Hamm	President, First National Bank & Trust Company, El Dorado, Kans.	1979
Craig Bachman	President, First National Bank of Centralia, Centralia, Kans.	1980

Class B

Name	Position	Term expires Dec. 31
Alan R. Sleeper	Rancher, Alden, Kans.	1978
John A. McKinney	President and Chief Executive Officer, Johns-Manville Corp., Denver, Colo.	1979
James G. Harlow, Jr.	President, Oklahoma Gas and Electric Co., Oklahoma City, Okla.	1980

Class C

Name	Position	Term expires Dec. 31
Harold W. Andersen	President, Omaha World-Herald Company, Omaha, Nebr.	1978
Paul H. Henson	Chairman and Chief Executive Officer, United Telecommunications, Inc., Westwood, Kans.	1979
Joseph H. Williams	Chairman, The Williams Companies, Tulsa, Okla.	1980

DENVER BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
William H. Vernon	Director, and Retired Chairman and Chief Executive Officer, Santa Fe National Bank, Santa Fe, N. Mex.	1978
Delano E. Scott	President and Chairman, The Routt County National Bank of Steamboat Springs, Steamboat Springs, Colo.	1978
Felix Buchenroth, Jr.	President, The Jackson State Bank, Jackson, Wyo.	1979

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
Vacancy		1978
A. L. Feldman	President and Chief Executive Officer, Frontier Airlines, Inc., Denver, Colo.	1979

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District 10—KANSAS CITY—Cont.

Term expires Dec. 31

OKLAHOMA CITY BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
V. M. Thompson, Jr.	Chairman and Chief Executive Officer, Utica National Bank and Trust Co., Tulsa, Okla.	1978
W. L. Stephenson, Jr.	Chairman of the Board, Central National Bank & Trust Co. of Enid, Enid, Okla.	1978
J. A. Maurer	Chairman, Security National Bank & Trust Co., Duncan, Okla.	1979

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
Harley Custer	General Manager, National Livestock Commission Association, Oklahoma City, Okla.	1978
Christine H. Anthony	Oklahoma City, Okla.	1979

OMAHA BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
F. Phillips Giltner	President, First National of Nebraska, Inc., Omaha, Nebr.	1978
Roy G. Dinsdale	Chairman of the Board, Farmers National Bank of Central City, Central City, Nebr.	1979
Joe J. Huckfeldt	President, Gering National Bank & Trust Co., Gering, Nebr.	1979

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
Edward F. Owen	President, Paxton & Vierling Steel Company, Omaha, Nebr.	1978
Durward B. Varner	Chairman and Chief Executive Officer, University of Nebraska Foundation, Lincoln, Nebr.	1979

District 11—DALLAS

Class A

Name	Position	Term expires Dec. 31
Robert H. Stewart III	Chairman of the Board, First International Bancshares, Inc., Dallas, Tex.	1978
Gene D. Adams	President, The First National Bank of Seymour, Seymour, Tex.	1979
Frank Junell	Chairman of the Board, The Central National Bank of San Angelo, San Angelo, Tex.	1980

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District 11—DALLAS—Cont.		*Term expires Dec. 13*
Class B		
Thomas W. Herrick	Cattle and Investments, Amarillo, Tex.	1978
Stewart Orton	President, Foley's Division of Federated Dept. Stores, Inc., Houston, Tex.	1979
Gerald D. Hines	Owner, Gerald D. Hines Interests, Houston, Tex.	1980
Class C		
Charles T. Beaird	Publisher, Shreveport Journal, Shreveport, La.	1978
Margaret S. Wilson	Chairman of the Board and Chief Executive Officer, Scarbroughs, Austin, Tex.	1979
Irving A. Mathews	Chairman of the Board and Chief Executive Officer, Frost Bros., Inc., San Antonio, Tex.	1980

EL PASO BRANCH

Appointed by Federal Reserve Bank		
Reed H. Chittim	President, First National Bank of Lea County, Hobbs, N. Mex.	1978
Arnold B. Peinado, Jr.	Partner, AVC Development, El Paso, Tex.	1978
Arthur L. Gonzales	President, First City National Bank of El Paso, El Paso, Tex.	1979
C. E. Leyendecker	President, Mimbres Valley Bank, Deming, N. Mex.	1980
Appointed by Board of Governors		
J. A. Salas-Porras	Executive Director, BI Language Services, El Paso, Tex.	1978
A. J. Losee	President, Losee & Carson, P.A., Artesia, N. Mex.	1979
Chester J. Kesey	Partner, Kesey Bros. Enterprises, Pecos, Tex.	1980

HOUSTON BRANCH

Appointed by Federal Reserve Bank		
Bookman Peters	President, The City National Bank of Bryan, Bryan, Tex.	1978
Nat S. Rogers	Chairman of the Board, First City National Bank of Houston, Houston, Tex.	1978
Page K. Stubblefield	Chairman of the Board, Victoria Bank & Trust Company, Victoria, Tex.	1979
Vacancy		1980

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District 11—DALLAS—Cont.

Term expires Dec. 31

HOUSTON BRANCH—Cont.

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
Alvin I. Thomas	President, Prairie View A&M University, Prairie View, Tex.	1978
Jerome L. Howard	Chairman of the Board and Chief Executive Officer, Mortgage & Trust, Inc., Houston, Tex.	1979
Gene M. Woodfin	Chairman of the Board and Chief Executive Officer, Marathon Manufacturing Company, Houston, Tex.	1980

SAN ANTONIO BRANCH

Appointed by Federal Reserve Bank

Name	Position	Term expires Dec. 31
Richard W. Calvert	Chairman of the Board, National Bank of Commerce of San Antonio, San Antonio, Tex.	1978
John H. Holcomb	Owner-Manager, Progreso Haciendas Company, Progreso, Tex.	1978
Ben R. Low	Vice President, Commerce North Bank, N.A., San Antonio, Tex.	1979
John H. Garner	President and Chief Executive Officer, Corpus Christi National Bank, Corpus Christi, Tex.	1980

Appointed by Board of Governors

Name	Position	Term expires Dec. 31
Pete J. Morales, Jr.	President and General Manager, Morales Feed Lots, Inc., Devine, Tex.	1978
Pat Legan	Owner, Legan Properties, San Antonio, Tex.	1979
John J. McKetta	E. P. Schock Professor of Chemical Engineering, The University of Texas, Austin, Tex.	1980

District 12—SAN FRANCISCO

Class A

Name	Position	Term expires Dec. 31
Ronald S. Hanson	President and Chief Executive Officer, The First National Bank of Logan, Logan, Utah	1978
Fred. G. Larkin, Jr.	Chairman of the Board and Chief Executive Officer, Security Pacific National Bank, Los Angeles, Calif.	1979

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District 12—SAN FRANCISCO—Cont.		*Term expires Dec. 31*
Ole R. Mettler	President and Chairman of the Board, Farmers & Merchants Bank of Central California, Lodi, Calif.	1980
Class B		
Malcolm T. Stamper	President, The Boeing Company, Seattle, Wash.	1978
Clair L. Peck, Jr.	Chairman of the Board, C. L. Peck Contractor, Los Angeles, Calif.	1979
J. R. Vaughan	Chairman, President and Chief Executive Officer, Knudsen Corporation, Los Angeles, Calif.	1980
Class C		
Joseph F. Alibrandi	President and Chief Executive Officer, Whittaker Corp., Los Angeles, Calif.	1978
Dorothy W. Nelson	Dean and Professor of Law, University of Southern Calif., Los Angeles, Calif.	1979
Cornell C. Maier	President and Chief Executive Officer, Kaiser Aluminum & Chemical Corp., Oakland, Calif.	1980

LOS ANGELES BRANCH

Appointed by Federal Reserve Bank		
W. Gordon Ferguson	President, National Bank of Whittier, Whittier, Calif.	1978
Joseph J. Pinola	Chairman and Chief Executive Officer, Western Bancorporation, Los Angeles, Calif.	1979
Fern Jellison	General Manager, Social Services Department, City of Los Angeles, Los Angeles, Calif.	1979
James D. McMahon	President, Santa Clarita National Bank, Newhall, Calif.	1980
Appointed by Board of Governors		
Harvey A. Proctor	Chairman of the Board, Southern California Gas Company, Los Angeles, Calif.	1978
Vacancy		1979
Caroline L. Amanson	Chairman of the Board, Caroline Leonetti, Ltd., Beverly Hills, Calif	1980

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District 12—SAN FRANCISCO—Cont.

PORTLAND BRANCH

		Term expires Dec. 31
Appointed by Federal Reserve Bank		
Robert F. Wallace	Chairman of the Board, First National Bank of Oregon, Portland, Ore.	1978
Robert A. Young	President, Northwest National Bank, Vancouver, Wash.	1978
Merle G. Bryan	President, Forest Grove National Bank, Forest Grove, Ore.	1979
Kenneth L. Smith	General Manager, The Confederated Tribes of Warm Springs, Warm Springs, Ore.	1980
Appointed by Board of Governors		
Jean Mater	Partner and General Manager, Mater Engineering, Corvallis, Ore.	1978
Phillip W. Schneider	Northwest Regional Executive, National Wildlife Federation, Portland, Ore.	1979
Loran L. Stewart	Director, Bohemia, Inc., Eugene, Ore.	1980

SALT LAKE CITY BRANCH

		Term expires Dec. 31
Appointed by Federal Reserve Bank		
David P. Gardner	President, University of Utah, Salt Lake City, Utah	1978
Robert E. Bryans	Chairman of the Board and Chief Executive Officer, Walker Bank and Trust Company, Salt Lake City, Utah	1978
Fred H. Stringham	President, Valley Bank and Trust Company, South Salt Lake, Utah	1979
Mary S. Knox	Chairman, Idaho State Bank, Glenns Ferry, Idaho	1980
Appointed by Board of Governors		
Sam Bennion	President and Chief Executive Officer, V-1 Oil Company, Idaho Falls, Idaho	1978
Robert A. Erkins	Geothermal Agri/Aquaculturist, Bliss, Idaho	1979
Joe L. Terteling	Chief Executive Officer, J. A. Terteling & Sons, Inc., Boise, Idaho	1980

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District 12—SAN FRANCISCO—Cont.

SEATTLE BRANCH

		Term expires Dec. 31
Appointed by Federal Reserve Bank		
Douglas S. Gamble	President and Chief Executive Officer, Pacific Gamble Robinson Co., Seattle, Wash.	1978
Harry S. Goodfellow	Chairman of the Board and Chief Executive Officer, Old National Bank of Washington, Spokane, Wash.	1978
Donald L. Mellish	Chairman of the Board, National Bank of Alaska, Anchorage, Alaska	1979
Rufus C. Smith	Chairman, The First National Bank of Enumclaw, Enumclaw, Wash.	1980
Appointed by Board of Governors		
Lloyd E. Cooney	President and General Manager, KIRO-Radio & Television, Seattle, Wash.	1978
Merle D. Adlum	President, Inlandboatmen's Union of the Pacific, Seattle, Wash.	1979
Virginia L. Parks	Vice President for Finance and Business, Seattle University, Seattle, Wash.	1980

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PRESIDENTS AND VICE PRESIDENTS

December 31, 1978

Federal Reserve Bank or branch	President First Vice President	Vice Presidents	
Boston	Frank E. Morris James A. McIntosh	Daniel Aquilino [1]	R. W. Eisenmenger [1]
		T. F. Hunt, Jr.[1]	Niels O. Larsen [1]
		Richard A. Walker [1]	Bruce W. Bean
		T. E. Cimeno, Jr.	F. K. Cummings
		Norman S. Fieleke	Luther M. Hoyle, Jr.
		Jay W. Kim	Kenneth W. Kulesza
		D. A. Pelletier	Richard E. Randall
		Laurence H. Stone	Walter T. Sullivan
		Richard F. Syron	J. M. Thayer, Jr.
		Herbert F. Wass	
New York	Paul A. Volcker T. M. Timlen, Jr.	Alan R. Holmes [2]	Edward G. Guy [1]
		P. B. Henderson, Jr.[1]	F. W. Piderit, Jr.[1]
		Thomas C. Sloane [1]	Peter D. Sternlight [1]
		James O. Aston	Peter Bakstansky
		W. H. Braun, Jr.	E. Gerald Corrigan
		Chester B. Feldberg	Peter Fousek
		Ronald B. Gray	Margaret Greene
		Whitney R. Irwin	Scott E. Pardee
		Edwin R. Powers	A. M. Puckett
		Geri M. Riegger	F. C. Schadrack, Jr.
		F. L. Smedley	Robert C. Thoman
		H. W. Whiteman, Jr.	H. David Willey
Buffalo		John T. Keane	
Philadelphia	David P. Eastburn Richard L. Smoot	K. G. Adack [1]	Edward G. Boehne [1]
		Hugh Chairnoff	Thomas K. Desch
		Peter M. DiPlacido	Richard W. Epps
		James F. Gaylord	Hiliary H. Holloway
		W. Lee Hoskins	Ira Kaminow
		A. A. Kudelich	Donald J. McAneny
		C. William Metz	L. C. Murdoch, Jr.
		Bipin C. Shah	
Cleveland	Willis J. Winn W. H. MacDonald	John M. Davis, Jr.[1]	W. H. Hendricks [1]
		Donald C. Benjamin	John E. Birky
		George E. Booth, Jr.	Paul Breidenbach
		R. Joseph Ginnane	Harry W. Huning
		R. Thomas King	T. E. Orminston, Jr.
		Lester M. Selby	Harold J. Swart
		Donald C. Vincel	
Cincinnati		R. E. Showalter [1]	Charles A. Cerino
Pittsburgh		Robert D. Duggan [1]	William R. Taggart
Richmond	Robert P. Black George C. Rankin	Welford S. Farmer [1]	James Parthemos [1]
		John F. Rand [1]	R. E. Sanders, Jr.[1]
		Elizabeth W. Angle	L. W. Bostian, Jr.
		J. A. Broaddus, Jr.	George B. Evans
		Roy L. Fauber	William C. Glover
		W. D. Martin III	R. D. McTeer, Jr.

For notes see last page of listing.

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PRESIDENTS AND VICE PRESIDENTS—Continued

Federal Reserve Bank or branch	President First Vice President	Vice Presidents	
Richmond—Cont.		A. V. Myers, Jr.	C. D. Porter, Jr.
		Aubrey N. Snellings	Andrew L. Tilton
		James F. Tucker	Joseph F. Viverette
Baltimore...	....	J. R. Monhollon [1]	W. E. Pascoe III
		Gerald L. Wilson	
Charlotte....	....	S. P. Fishburne [1]	Boyd Z. Eubanks
		Thomas E. Snider	
Culpeper [3]...	....	A. D. Tinkelenberg	John G. Stoides
Atlanta......	Monroe Kimbrel	R. P. Forrestal [1]	Billy H. Hargett [1]
	Kyle K. Fossum	Arthur H. Kantner [1]	Brown R. Rawlings [1]
		Harry Brandt	W. R. Caldwell
		William N. Cox III	W. M. Davis
		Delmar Harrison	Robert E. Heck
		William G. Pfaff	H. Terry Smith
		Pierre M. Viguerie	
Birmingham.	....	Hiram J. Honea	
Jacksonville .	....	Charles D. East	
Miami......	....	F. J. Craven, Jr.	
Nashville....	....	Jeffrey J. Wells	
New Orleans.	....	George C. Guynn	
Chicago.....	Robert P. Mayo	Ward J. Larson [1]	James R. Morrison [1]
	Daniel M. Doyle	Karl A. Scheld [1]	Harry S. Schultz [1]
		Bruce L. Smyth [1]	R. D. Abrahamson
		Paul J. Bettini	George W. Cloos
		Robert P. Cornelisen	Franklin D. Dryer
		Rudolph W. Dybeck	William H. Cram
		Joseph G. Kvasnicka	Richard A. Moffatt
		William T. Newport	Dorothy M. Nichols
		Louis J. Purol	William Rooney
		R. M. Scheider	Roby L. Sloan
		Adolph J. Stojetz	Thomas C. Tucker
		Carl E. Vander Wilt	Eugene J. Wagner
		Allen G. Wolkey	
Detroit......	....	William C. Conrad [1]	F. S. Dominick
		R. M. Fitzgerald	Ronald Zile
St. Louis....	Lawrence K. Roos	Anotol B. Balbach [1]	Ruth A. Bryant
	D. W. Moriarty, Jr.	Melvin A. Carr	J. P. Garbarini [1]
		Denis S. Karnosky	James R. Kennedy
		John F. Otting, Jr.	F. G. Russell, Jr.[1]
		Warren G. Snover	Robert W. Thomas
		Harold E. Uthoff [1]	Delmer Weisz
Little Rock..	....	John F. Breen	
Louisville...	....	Donald L. Henry [1]	
Memphis....	....	L. Terry Britt	

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PRESIDENTS AND VICE PRESIDENTS—Continued

Federal Reserve Bank or branch	President First Vice President	Vice Presidents	
Minneapolis	Mark H. Willes Thomas E. Gainor	Melvin L. Burstein Lester G. Gable Gary P. Hanson D. R. Hellweg J. A. MacDonald [1] Clarence W. Nelson R. W. Worcester	L. W. Fernelius [1] Roland D. Graham [1] Bruce J. Hedblom Howard L. Knous David R. McDonald John D. Paulus [1]
Helena	....	John D. Johnson	
Kansas City	Roger Guffey Henry R. Czerwinski	W. T. Billington [1] Thomas E. Davis [1] James R. Bell Cecil B. Foley Jay K. Mast M. L. Mothersead Robert E. Scott John F. Zoellner	James R. Bowen [1] J. D. Hamilton [1] James A. Cacy Robert F. Knight G. H. Miller, Jr. Barry K. Robinson Donald A. Slover
Denver	....	Wayne W. Martin [1]	
Oklahoma City	....	William G. Evans	
Omaha	....	Robert D. Hamilton	
Dallas	Ernest T. Baughman Robert H. Boykin	Joseph E. Burns [1] C. J. Pickering Harry E. Robinson [1] Tony J. Salvaggio [1]	C. C. Cochran III [1] W. M. Pritchett George F. Rudy E. W. Vorlop, Jr.
El Paso	....	Joel L. Koonce, Jr.	Frederic W. Reed
Houston	....	J. Z. Rowe	
San Antonio	....	Carl H. Moore	
San Francisco	John J. Balles John B. Williams	John J. Carson [1] Donald V. Masten [1] Donald K. Carson H. Peter Franzel Warren H. Hutchins Thomas E. Judge Rix Maurer, Jr. W. Von Turk	Richard T. Griffith [1] Kent O. Sims [1] Robert C. Dietz Kenneth A. Grant Henry B. Jamison Michael W. Keran Louis E. Reilly C. Woessner, Jr.
Los Angeles	....	Richard C. Dunn [1]	James M. Davis
Portland	....	Angelo S. Carella	
Salt Lake City	....	A. Grant Holman	
Seattle	....	Gerald R. Kelly [1]	

[1] Senior Vice President.
[2] Executive Vice President.
[3] Culpeper Center is not considered a branch.

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CONFERENCE OF PRESIDENTS

The Presidents of the Federal Reserve Banks are organized into a Conference of Presidents that meets occasionally to consider matters of common interest and to consult with and advise the Board of Governors. At a meeting on December 20, 1977, John J. Balles and Robert P. Black, Presidents of the Federal Reserve Banks of San Francisco and Richmond, respectively, were elected Chairman and Vice Chairman, respectively, for the forthcoming Conference year, ending with the December 1978 meeting.

At the December 1977 meeting, Adelle Foley and Bradley H. Gunter, of the Federal Reserve Banks of San Francisco and Richmond, were appointed Secretary and Assistant Secretary, respectively.

CONFERENCE OF FIRST VICE PRESIDENTS

The Conference of First Vice Presidents of the Federal Reserve Banks was organized in 1969 to meet from time to time to consider primarily operational matters. On December 23, 1977, John B. Williams, First Vice President of the Federal Reserve Bank of San Francisco, was elected Chairman, and George Rankin, First Vice President of the Federal Reserve Bank of Richmond, was elected Vice Chairman of the Conference for the calendar year 1978. Adelle Foley and Bradley H. Gunter were appointed Secretary and Assistant Secretary, respectively.

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