REPORT OF OPEN
MARKET OPERATIONS

Mr. Sternlight made the following statement:

Desk operations in the period since the last meeting of the Committee aimed first for steady money market conditions centered on a 6 1/2 percent funds rate, then for a slight firming, and still later for a return to the 6 1/2 percent rate. Daily operations were complicated by changing estimates of monetary growth, sizable errors in the projection of reserves, variability in member bank borrowing, and shifts in market sentiment from seeming complacency to great skittishness--all against the background of a major Treasury financing operation. None of these factors by itself was particularly unusual, but in combination they produced some problems.

Early in the period, projections of the monetary aggregates were stronger than those reviewed at the last meeting, but not sufficiently strong to call for a change in the System's stance, so the Desk continued to pursue conditions associated with a 6 1/2 percent Federal funds rate. By the last few days of October, however, the aggregates looked significantly stronger--with M_1 above its range and M_2 not far from the top. The Account Management concluded that some response was called for, and began to seek a funds rate around 6 1/2 - 6 5/8 percent. Moreover, with the Treasury's financing operations about to begin, it was considered desirable to make the System's intention known promptly.

Our efforts failed at first to impart that slightly firmer tone, but then we got more of a reaction than we had sought or expected--particularly in light of a later softening in the aggregates that led to a return to the 6 1/2 percent funds objective.

Statistically, Desk operations during the period were dominated by short-term reserve adjustments, responding to the usual swings in Treasury balances, but also to partly unexpected swings in float, and to sizable variations in member bank borrowings. In addition to daily execution of matched sale-purchase transactions with foreign accounts, the Desk arranged such transactions in the market on ten days, while making repurchase agreements on four days. Outright holdings of bills were reduced by about $1.3 billion, including sales to foreign accounts and redemptions, as well as the aforementioned bill sale in the market.

Market yields underwent some fluctuations during the period, especially around the time that the Desk temporarily sought a firmer money market midway through the period, and again near the end in the wake of comments that allayed earlier concern about differences on monetary policy between the Federal Reserve and the Adminisration, and published declines in the money supply. On balance over the whole period, changes were modest. Three- and six-month bills were auctioned yesterday at about 6.09 and 6.37 percent, down from 6.28 and 6.50 percent just before the last meeting. At mid-period, just before the Desk's outright bill sale, the three-month bill was down to about 6 percent. Yields on most Treasury coupon issues out to about 3 years' maturity declined some 10 - 20 basis points over the interval. Yields on most intermediate issues (say 3 to 10 years) were down a few basis points while longer issues were up a few basis points as price gains in the final days approximately offset earlier declines. All three Treasury coupon issues closed at premiums above where they were auctioned.

The Treasury must continue to borrow sizable amounts over the next month. About $1 1/4 billion will be raised in the next sale of 2-year notes, while a 4-year note sale is also likely, as well as some sizable recourse to the bill market.