FEDERAL RESERVE

press release

For immediate release January 2, 1968.

The Board of Governors of the Federal Reserve System and the Federal Open Market Committee today released the attached record of policy actions taken by the Federal Open Market Committee at its meeting on October 3, 1967. Such records are made available approximately 90 days after the date of each meeting of the Committee and are also published in the monthly Federal Reserve Bulletin and in the Board's Annual Report.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on October 3, 1967

Authority to effect transactions in System Account.

Reports at this meeting indicated that underlying economic conditions had strengthened and that prospects were for more rapid growth later in the year, apart from the effects of the strike at a major automobile producer that was now in its fourth week. More complete data confirmed earlier indications that industrial production had increased further in August, and while output had probably declined in September, it appeared likely that growth would resume when the automobile industry returned to full production. Retail sales had continued to rise rapidly in August, according to the advance estimate, and housing starts had edged up. Price increases for industrial commodities continued to be widespread.

The latest information tended to support earlier expectations of a substantial increase in real GNP in the third quarter. Also, an acceleration in growth still appeared in prospect for the fourth quarter, when it was expected that final sales would rise considerably further and that business inventories would increase modestly. As before, the expectations for the fourth quarter were based on the assumptions that work stoppages in the automobile industry would be of relatively short duration and limited extent, and that a surcharge on Federal income taxes--which was still pending before Congress--would not go into effect before the end of the year.

Average prices of industrial commodities again increased appreciably from mid-August to mid-September, according to preliminary

estimates, and the number of announced increases that were to become effective after the latter date suggested that the average would advance further in the following month. The consumer price index, which since March had been rising more rapidly than earlier, increased at a sizable rate in August. Unit labor costs in manufacturing were expected to remain under upward pressure in coming months, when it appeared likely that wage increases would more than offset gains in productivity.

The large deficit in the U.S. balance of payments on the "official reserve transactions" basis in the second quarter was followed by a large surplus in the third quarter as a result of heavy inflows of liquid funds, particularly in July and August, through foreign branches of U.S. banks. The deficit on the "liquidity" basis was estimated to have increased somewhat in the third quarter, although a decline would have been recorded had it not been for certain types of official transactions that had held down the second-quarter deficit. The merchandise trade surplus increased in August as a result of a reduction in imports. Prospects for renewed strength in exports had been enhanced by recent signs of industrial recovery in Germany and Britain, but imports also were expected to rise with expansion in U.S. business activity.

In Britain the improvement in exports and in the basic payments balance that had been hoped for in 1967 had not materialized thus far, in part because of the slowdown in economic activity on the continent and the balance of payments costs of the Middle East crisis, and sterling remained under pressure in foreign exchange markets. The

Bank of Canada had raised its discount rate from 4-1/2 to 5 per cent on September 27. This action was generally interpreted as a technical adjustment to the sharp increases in market interest rates that had occurred in Canada over the preceding 6 months.

On September 22 the U.S. Treasury announced that it would auction $4.5 billion of April and June tax-anticipation bills on October 3, the date of this meeting, for payment on October 9. The Treasury also indicated that it would add $100 million to each of its weekly bill offerings for 13 weeks beginning with the auction of October 9. Since early July the Treasury had raised about $10 billion of new cash through sales of bills--including today's offering of tax-anticipation bills--and nearly $3 billion through sales of coupon-bearing securities, and it appeared that the Treasury would need to raise substantial further amounts of cash in the remaining months of 1967. An announcement was expected in late October of the terms for refunding U.S. Government securities maturing in mid-November, of which $2.6 billion were held by the public.

System open market operations since the preceding meeting of the Committee had been directed at maintaining steady conditions in the money market. In the 3 weeks ending September 27 free reserves of member banks had averaged about $270 million and member bank borrowings about $85 million, both within the ranges prevailing recently, and the Federal funds rate had averaged about 4 per cent, slightly higher than in July and August. After the preceding meeting of the Committee the market rate on 3-month Treasury bills had risen sharply--reaching 4.60 per cent on September 22--chiefly as a result

of market anticipations of additional Treasury bill financing. The bill rate had subsequently declined, however, and on the day before this meeting it was 4.40 per cent, only 6 basis points above its level 3 weeks earlier. Rates on other short-term market instruments increased further or remained at advanced levels.

In capital markets the volume of new securities offered to the public had moderated recently. Although flotations by State and local governments in September and those in prospect for October were considerably above their reduced August level, the presently estimated volume of new corporate offerings in September and October was only about half the extraordinarily large volume of July and August. Nevertheless, bond yields were subject to renewed upward pressures, with yields on long-term Treasury bonds rising to levels above their 1966 highs. In part, the pressures in capital markets reflected apprehension over the large cash needs of the Treasury in prospect for the near term. They also reflected concern about developing inflationary pressures, growing doubts about the prospects for congressional enactment of the proposed income tax surcharge, and accompanying uncertainties concerning the course of monetary policy.

In August interest rates on conventional mortgages on new homes edged up, and secondary-market yields on Federally underwritten mortgages increased. Inflows of funds to nonbank depositary-type institutions remained large--although not quite so large in August, after seasonal adjustment, as in the spring and early summer.

Demands for business loans at commercial banks were relatively light in early September but they appeared to have picked up around the midmonth tax-payment period. Growth in total time and savings deposits moderated considerably, mainly because of a sizable reduction in the volume of negotiable CD's outstanding. Private demand deposits and the money supply changed little, but U.S. Government demand deposits increased further from their June low. According to preliminary estimates, daily-average member bank deposits--the bank credit proxy--rose at an annual rate of 9-1/2 per cent from August to September, well below the rate of more than 15 per cent earlier in the summer.

Staff projections suggested that if money market conditions remained unchanged the bank credit proxy would rise at an annual rate in the 10 to 13 per cent range from September to October. About half of the expansion was expected to be in U.S. Government deposits, as a result of heavy borrowing by the Treasury during October. Growth in time and savings deposits appeared likely to be at a somewhat more rapid rate than in the preceding month, but less rapid than the average rate earlier in the year. Private demand deposits--and the money supply--were expected to rise only slightly.

Many members of the Committee thought that current and prospective inflationary pressures and the rapid rate of bank credit growth in recent months offered strong grounds for seeking somewhat greater monetary restraint at this time. Some members also pointed to the unsatisfactory balance of payments situation as arguing for a firming of monetary policy. The majority believed, however, that

these considerations were outweighed by others militating against a change in policy at present. The latter included the desirability of awaiting firmer indications of the probable actions by Congress with respect to Federal taxes and expenditures; the uncertainties regarding the extent and duration of the automobile industry strike; and the risk that under present financial market conditions any firming action at this time would lead to sharply higher interest rates, with possible undesired effects on financial intermediaries domestically and on the position of sterling in foreign exchange markets. The Treasury's current bill financing and, more importantly, the November refunding soon to follow also were cited as considerations arguing against a change in monetary policy at this juncture.

The Committee concluded that open market operations should be directed at maintaining about the prevailing conditions in the money market, but that operations should be modified, to the extent permitted by Treasury financing, to moderate any apparent tendency for bank credit to expand more than currently expected. The following current economic policy directive was issued to the Federal Reserve Bank of New York:

> The economic and financial developments reviewed at this meeting indicate that, apart from the effects of the strike in the automobile industry, underlying economic conditions have strengthened and prospects favor more rapid growth later in the year. Upward pressures on costs persist, average prices of industrial commodities have risen further, and the rate of increase in consumer prices remains high. While there recently have been large inflows of liquid funds from abroad through foreign branches of U.S. banks, the balance of payments continues to reflect a substantial underlying deficit. Bank credit expansion has continued large,

although there was some moderation in September from the rapid July-August rate. The volume of corporate bond flotations has slackened, but Federal and State and local government financing demands remain large and most interest rates have on balance moved up somewhat further. The President's new fiscal program is still pending before Congress. In this situation, it is the policy of the Federal Open Market Committee to foster financial conditions, including bank credit growth, conducive to sustainable economic expansion, recognizing the need for reasonable price stability for both domestic and balance of payments purposes.

To implement this policy, System open market operations until the next meeting of the Committee shall be conducted with a view to maintaining about the prevailing conditions in the money market; but operations shall be modified, to the extent permitted by Treasury financing, to moderate any apparent tendency for bank credit to expand significantly more than currently expected.

Votes for this action: Messrs. Hayes, Brimmer, Daane, Maisel, Mitchell, Robertson, Sherrill, Swan, and Wayne. Votes against this action: Messrs. Francis and Scanlon.

Messrs. Francis and Scanlon dissented from this action because they assessed the balance of considerations at issue differently from the majority and favored seeking greater monetary restraint. In their judgment, in view of the prospects for further price inflation the risks in not acting at this time to moderate the rapid growth of bank credit outweighed the various considerations seen as militating against a firmer monetary policy.