



FEDERAL RESERVE

press release

For immediate release

January 5, 1970

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 7, 1969. Such records are made available approximately 90 days after the date of each meeting of the Committee and will be found in the Federal Reserve Bulletin and the Board's Annual Report.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on October 7, 1969

1. Authority to effect transactions in System Account.

According to staff estimates, expansion in real GNP continued in the third quarter at about the 2 per cent annual rate of the second quarter, as an increase in inventory investment approximately offset further slackening in growth of private final sales. Average prices, as measured by the GNP deflator, were estimated to have advanced substantially. Staff projections suggested that real GNP would grow more slowly in the fourth quarter and that it might change little in the first half of 1970. With pressures on resources expected to ease over that period, some moderation in the rate of price advance was projected.

A number of monthly measures of economic activity had weakened recently. Nonfarm employment was about unchanged in September and the unemployment rate rose sharply to 4.0 from 3.5 per cent in August. Industrial production edged down in August, and tentative estimates suggested that it changed little or declined slightly in September. It appeared from weekly data for most of September that retail sales in that month were about the same as in August and that, after adjustment for price increases, such sales remained below the level

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of a year earlier. New orders at manufacturers of durable goods declined appreciably in August, and housing starts fell for the seventh consecutive month.

Prices of a large number of industrial commodities increased from mid-August to mid-September and the average advanced substantially further. The over-all wholesale price index rose only slightly, however, as a result of another decline in prices of farm products and foods. In August the consumer price index again increased considerably.

The staff projections of GNP for the current and the next two quarters were based on the assumptions that the income tax surcharge would be continued at 5 per cent through the first half of 1970, that the investment tax credit would be repealed, and that social security benefits would be increased by 10 per cent on April 1. The projections suggested that expansion in aggregate final demands would continue to moderate through the second quarter of 1970 and that the rate of inventory accumulation would be declining after the turn of the year.

U.S. merchandise exports rose more than imports in August, so the trade surplus increased a little. With respect to the over-all balance of payments, available data indicated that in August and September the deficit on the liquidity basis had been very large, although not so large as in preceding months, and that the balance on the official settlements basis had shifted into deficit. The official settlements balance had been in surplus for more than a year prior to

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August mainly as a result of increases in outstanding Euro-dollar borrowings of U.S. banks through their foreign branches, but there apparently had been little net change in those borrowings after July. Speculative flows of funds into Germany during September contributed to the shift in the official settlements balance.

Recent developments in foreign exchange markets had been dominated by events connected with the German mark. Demands for marks increased in early September in anticipation of a possible revaluation of that currency after the German elections scheduled for September 28, and by Wednesday, September 24, the German Federal Bank had acquired a substantial volume of dollars in active but orderly trading. The German authorities closed their exchange markets the next two days and, after a brief resumption of trading, again on Monday, September 29. The government then announced that the mark would be allowed to float temporarily, and the exchange rate immediately broke through its previous upper limit. Subsequently the mark strengthened further, reaching a premium above par of about 6-1/2 per cent at the time of this meeting. During the period, the German Federal Bank frequently sold dollars to moderate fluctuations in the rate. The rise in the exchange rate and the expectation that the mark would be revalued once a new German Government was formed led to some reduction in the earlier tensions in foreign exchange markets, although the French franc and the Italian lira remained under selling pressure.

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Earlier in September discount rates had been increased by the central banks of Germany, Belgium, Switzerland, Austria, and Norway. Despite the tightening of conditions in domestic European money markets, interest rates in the Euro-dollar market--which had risen steadily during August--declined moderately after early September, partly because of the easing in demands by U.S. banks for Euro-dollars.

On September 17 the Treasury announced that in exchange for securities maturing on October 1 and December 15, 1969, it would offer three new notes having, respectively, maturities of about 20 months, 3 years and 8 months, and 6 years and 10 months, and yields of 8, 7.75, and 7.59 per cent. The new issues were initially well received and rose to a premium in the market. Of the \$7.6 billion of maturing securities held by the public, about \$5.8 billion were exchanged for the new issues, including somewhat more than \$1 billion for each of the two longer-term notes. Following this financing, the Treasury announced that on October 8 it would auction \$2 billion of tax-anticipation bills due in April 1970. The Treasury was expected to raise additional funds during the fourth quarter to meet further cash needs.

Treasury cash balances at both commercial banks and Federal Reserve Banks had been reduced to very low levels prior to the mid-September tax date, and in the period September 5-16 the Treasury

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had temporarily financed some of its cash needs through sales of special short-term certificates of indebtedness to the Federal Reserve. The volume of such certificates reached a 16-year high of \$1.1 billion on September 10,^{1/} but the Treasury was able to redeem all outstanding certificates by September 17 and subsequently to rebuild its cash balances to a substantial level.

System open market operations since the previous meeting of the Committee had been directed at maintaining firm conditions in the money and short-term credit markets. Sizable operations were required to offset the impact on bank reserves and money market conditions of substantial changes in Treasury cash balances and large shifts of funds among banks stemming from the Treasury refunding and from foreign central bank transactions. Federal funds traded mainly in a range of 8-1/2 to 9-1/2 per cent; the average effective rate of about 9-1/8 per cent was slightly higher than in the preceding interval. Member bank borrowings averaged \$1,075 million in the 4 weeks ending October 1, down from an average of \$1,250 million in the previous 4 weeks. Excess reserves were little changed on the average, and so net borrowed reserves also declined.

^{1/} The volume of special certificates held by the Federal Reserve totaled \$322 million on September 5 through 7, \$653 million on September 8, \$830 million on September 9, \$1,102 million on September 10, \$862 million on September 11, \$759 million on September 12 through 14, \$513 million on September 15, and \$972 million on September 16.

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Against the background of continuing credit restraint and limited availability of funds, most market interest rates had risen to new highs in the period since the previous meeting of the Committee. Yield increases were relatively pronounced in the capital markets which absorbed large amounts of new corporate, Federal agency, and intermediate-term Treasury issues. Most recently, however, yields on Treasury and new corporate bonds had stabilized following the good reception accorded a sizable new Federal agency offering, some purchases of Treasury notes and bonds by official accounts, and the publication of the 4 per cent unemployment figure for September. Yields on State and local government bonds had moved counter to the general trend in September; they had declined somewhat as a result of a continuing light volume of new issues and of developments in the Congress relating to proposed legislation affecting the tax-exempt status of such obligations.

Most short-term interest rates also had risen since the previous meeting. Rates on Treasury bills were an exception; they were relatively stable for most of the period--mainly because of reinvestment demands generated by the Treasury refunding and by foreign central bank purchases--and had declined in recent days. The market rate on 3-month Treasury bills, at 6.94 per cent on the day before this meeting, was 15 basis points below its level 4 weeks earlier.

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Conditions in markets for residential mortgages continued to tighten in September. It appeared that savings flows at nonbank thrift institutions had remained weak during that month, and limited data available for the first few days of October suggested that net outflows following quarterly interest crediting would be larger than usual.

At commercial banks, business loans outstanding increased moderately in September but holdings of U.S. Government securities declined sharply as banks sold Treasury bills acquired in the late-August bill-strip financing. The bank credit proxy--daily-average member bank deposits--increased at an annual rate of 2.5 per cent from August to September. On balance, there was a small reduction in the average outstanding volume of funds obtained by banks from "nondeposit" sources--including Euro-dollar borrowings, funds obtained by sales of loans to nonbank customers under repurchase agreements, and funds obtained through sales of commercial paper by bank affiliates. After adjustment for this development, the proxy series was estimated to have risen at an annual rate of about 2 per cent on the average in September. In the third quarter as a whole the proxy series so adjusted was estimated to have declined at an annual rate of 4.2 per cent.

The increase in the average level of member bank deposits in September was attributable almost entirely to a sharp rise in

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U.S. Government deposits after the midmonth tax date. Private demand deposits and the money stock^{1/} changed little. Total time and savings deposits declined at a much slower rate than earlier in the year, partly because of a marked reduction in net outflows of consumer-type deposits. In addition, there was a substantial increase in late September in foreign official time deposits. Further run-offs of large-denomination CD's occurred during the month, particularly at banks outside of New York.

Staff projections suggested that the average level of member bank deposits would decline from September to October at an annual rate of 5 to 8 per cent if prevailing conditions were maintained in money and short-term credit markets. It appeared likely that the combined total outstanding of funds obtained from nondeposit sources would increase a little on the average--perhaps by an amount equivalent to 1 percentage point or less in the credit proxy. Among deposit categories, reductions were anticipated in the average level of both Government and private demand deposits, and the money stock was projected to decline at an annual rate of 2 to 5 per cent.

^{1/} The regular annual benchmark corrections and revisions of seasonal adjustment factors for the money stock series had been made since the previous meeting of the Committee. The effect of the adjustment on the statistics for 1969 was to raise the estimated annual rate of growth during the first quarter from 2.9 to 4.1 per cent, and to lower the estimated second-quarter growth rate from 4.7 to 4.5 per cent. During the third quarter the annual rate of increase in the money stock series (on the new basis) was estimated at a fraction of 1 per cent.

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Continued reductions were expected in both large-denomination CD's and other time and savings deposits. The run-off of CD's appeared likely to moderate appreciably, however, partly because the volume of foreign official deposits was expected to increase further.

The Committee decided that a relaxation of monetary restraint would not be appropriate at this time in light of the persistence of inflationary pressures and expectations. It was also noted in this connection that fiscal policy was likely to become less restrictive in early 1970 even if, as recommended by the administration, the income tax surcharge was continued at 5 per cent through the first half of the year. At the same time, the Committee agreed that an intensification of monetary restraint would not be desirable at present in view of the considerable degree of restraint already in effect and of the indications that the rate of economic expansion was moderating.

The Committee concluded that open market operations should be directed at maintaining the prevailing firm conditions in money and short-term credit markets, subject to the proviso that operations should be modified if bank credit appeared to be deviating significantly from current projections.

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

The information reviewed at this meeting suggests that the pace of expansion in real economic activity was sustained in the third quarter by an acceleration of inventory investment, which about offset a further slackening in growth of private final sales. Some monthly economic measures have weakened recently, and slower over-all growth is projected for the fourth quarter. Substantial upward pressures on prices and costs are persisting. Most market interest rates recently have risen to new highs as demands for funds have pressed against limited supplies. In September, on average, the money supply changed little as U.S. Government deposits rose considerably further, and bank credit increased slightly after 2 months of substantial decline. The outstanding volume of large-denomination CD's decreased further in September, and flows of consumer-type time and savings funds at banks and nonbank thrift institutions appear to have remained relatively weak. The U.S. foreign trade surplus increased a little in August. In August and September the deficit in the over-all balance of payments on the liquidity basis was very large, although not as large as in preceding months; and the official settlements balance, which had been in surplus for more than a year, shifted into deficit, reflecting slackened Euro-dollar borrowing by U.S. banks and new speculative flows into Germany. Exchange market tensions were reduced somewhat when the German Government decided to cease temporarily official sales of marks, after which the exchange rate for that currency rose above the official parity. In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to the reduction of inflationary pressures, with a view to encouraging sustainable economic growth and attaining reasonable equilibrium in the country's balance of payments.

To implement this policy, System open market operations until the next meeting of the Committee shall be conducted with a view to maintaining the prevailing firm conditions in money and short-term credit markets; provided, however, that operations shall be modified if bank credit appears to be deviating significantly from current projections.

Votes for this action: Messrs. Martin, Hayes, Bopp, Brimmer, Clay, Coldwell, Daane, Mitchell, Robertson, Scanlon, and Sherrill. Vote against this action: Mr. Maisel.

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In dissenting from this action Mr. Maisel noted that interest rates on all types of market securities had risen substantially on balance in the period since late April, and that during this period the Committee's directives--like that favored by the majority today--had called for maintenance of prevailing firm conditions in money and short-term credit markets. He also noted that the behavior of key monetary aggregates, including member bank reserves, the money stock, and bank credit, had been considerably weaker in the third quarter--either declining more rapidly or rising more slowly--than in the first half of the year; and that sharp declines in the aggregates were projected for October if prevailing money market conditions were maintained. As at the two previous meetings, Mr. Maisel expressed the view that such evidence indicated a steady increase in monetary restrictiveness. He favored permitting more flexibility in money market conditions in order to maintain but not intensify the present degree of monetary restraint measured in terms of key aggregates and interest rates.

2. Amendments to continuing authority directive.

On recommendation of the Manager of the System Open Market Account, the Committee made two amendments to the continuing authority directive issued to the Federal Reserve Bank of New York regarding domestic open market operations. In addition, the dollar limit specified in paragraph 2 of the directive on Federal Reserve Bank

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holdings of special short-term certificates of indebtedness purchased directly from the Treasury, which had been temporarily increased from \$1 billion to \$2 billion at the previous meeting, reverted to \$1 billion under the terms of the action the Committee had taken then.

One of the amendments made today also affected paragraph 2; it involved the addition of language authorizing Reserve Banks other than the New York Bank to purchase special short-term certificates from the Treasury for their own account at times when the New York Reserve Bank was closed. With this amendment, paragraph 2 read as follows:

2. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York to purchase directly from the Treasury for the account of the Federal Reserve Bank of New York, or, if the New York Reserve Bank is closed, any other Reserve Bank 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 $\frac{1}{4}$ 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 \$1 billion.

The second amendment to the directive consisted of the addition of a new paragraph 3, authorizing the Reserve Banks to engage under certain conditions in lending of U.S. Government

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securities held in the System Open Market Account. The new paragraph read as follows:

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

Votes for these actions: Messrs.
Martin, Hayes, Bopp, Brimmer, Clay,
Coldwell, Daane, Maisel, Mitchell,
Robertson, Scanlon, and Sherrill.
Votes against these actions: None.

The amendment to paragraph 2 was made in view of the possibility that the Treasury might need temporary accommodation at times, such as the forthcoming Columbus Day holiday, when the New York Reserve Bank was closed and some other Reserve Banks remained open.

The action to add the new paragraph 3 was taken after the Manager had advised that the problem of delivery failures in the Government securities market had worsened significantly over the past year, partly because private facilities for lending such securities had become inadequate; that delivery failures were markedly impairing the performance of the market; and that the functioning of the market would be improved if securities held in the System Open Market Account could be lent, for the express purpose of avoiding delivery failures, to Government securities dealers doing business with the Federal Reserve Bank of New York and to banks participating in securities clearing

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arrangements conducted through a Reserve Bank. The Committee concurred in the Manager's judgment that under existing circumstances such lending of securities from the System Open Market Account was reasonably necessary to the effective conduct of open market operations and to the effectuation of open market policies. It was agreed that the authorization would be reviewed periodically to determine whether the contemplated lending activity remained necessary.

The initial instructions specified by the Committee in conjunction with this authorization included a \$75 million limit on the par value of securities involved in outstanding loans to any individual dealer at any time and a limit of three business days on the duration of loans to dealers, with those loans eligible for renewal under certain circumstances. The instructions also specified that both the dealers and the banks that borrowed securities were to deposit and pledge collateral consisting of U.S. Government securities of greater current market value than the securities borrowed. In addition, the lending fee to be charged on such securities loans was set at a rate higher than the prevailing fee charged by private lenders, in order to encourage continued maximum use of available private facilities for lending of Government securities.

3. Amendment to authorization for System foreign currency operations.

The Committee approved increases from \$100 million to \$200 million equivalent in the System swap arrangements with the Austrian National Bank, the National Bank of Denmark, and the Bank of Norway,

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and the corresponding amendments to paragraph 2 of the authorization for System foreign currency operations, effective immediately. As a result of this action, paragraph 2 read as follows:

2. The Federal Open Market Committee directs the Federal Reserve Bank of New York to maintain reciprocal currency arrangements ("swap" arrangements) for 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:

<u>Foreign bank</u>	<u>Amount of arrangement (millions of dollars equivalent)</u>
Austrian National Bank	200
National Bank of Belgium	500
Bank of Canada	1,000
National Bank of Denmark	200
Bank of England	2,000
Bank of France	1,000
German Federal Bank	1,000
Bank of Italy	1,000
Bank of Japan	1,000
Bank of Mexico	130
Netherlands Bank	300
Bank of Norway	200
Bank of Sweden	250
Swiss National Bank	600
Bank for International Settlements:	
Dollars against Swiss francs	600
Dollars against authorized European currencies other than Swiss francs	1,000

Votes for this action: Messrs.
Martin, Hayes, Bopp, Brimmer, Clay,
Coldwell, Daane, Maisel, Mitchell,
Robertson, Scanlon, and Sherrill.
Votes against this action: None.

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While Austria, Denmark, and Norway each had a strong current account in its international payments balance, all three countries had experienced reserve losses recently, for the most part as a result of the pull of high Euro-dollar interest rates and of speculation on a revaluation of the German mark. The indicated action was taken on recommendation of the Special Manager, who advised that it should prove helpful in providing against the contingency of destabilizing short-run speculative pressures on the currencies of the countries involved.