FEDERAL RESERVE
press release

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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 January 11, 1972.

Such records are made available approximately 90 days after the date of each meeting of the Committee and are published in the Federal Reserve Bulletin and the Board's Annual Report. The summary descriptions of economic and financial conditions they contain are based on the information that was available to the Committee at the time of the meeting, rather than on data as they may have been revised since then.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on January 11, 1972

1. Current Economic Policy Directive.

The information reviewed at this meeting suggested that the rate of growth in real output of goods and services (real gross national product) had stepped up in the fourth quarter of 1971 and that prices, which had been subject to Government controls since mid-August, had risen relatively little from the third to the fourth quarter. Staff projections suggested that the faster pace of growth in real GNP would continue in the first half of 1972.

In December nonfarm payroll employment and industrial production rose further, although to a large extent the gains were attributable to post-strike recovery in coal mining. The unemployment rate edged up to 6.1 from 6.0 per cent in November. Retail sales fell in December, according to the advance report, in part because sales of new cars dropped from the high rates prevailing during the first phase of the new economic program.

The rates of increase in prices and wages, which had slowed sharply during the freeze in effect from mid-August to mid-November, picked up afterward. Under the post-freeze program, some increases in wages--both previously scheduled and newly negotiated--were allowed to go into effect, some of the many pending applications for price increases were approved, and a general increase in residential rents was authorized.

The latest staff projections for the first half of 1972 were similar to those of 4 weeks earlier, although the expansion now expected in consumer spending was not so rapid. Also, the projected rise in Federal outlays in the first quarter had been increased as a consequence of a recently enacted Government pay raise effective in early January. It was still anticipated that business capital outlays, residential construction, and State and local government expenditures would grow at substantial rates and that business inventory investment would increase further.

The Finance Ministers and central bank Governors of the Group of Ten, meeting at the Smithsonian Institution in Washington, reached agreement on December 18 regarding revaluations of foreign currencies against the dollar and a widening of permissible margins for exchange rate fluctuations. Following announcement of the agreement, market exchange rates for major foreign currencies against the dollar generally moved up to levels a little above their new lower limits. Outflows of short-term capital from the United States--which had been very large during much of 1971--came to a halt, and some funds flowed back before the year-end. However, the U.S. basic balance of payments remained in deficit and foreign official reserves declined only a little.

Demands for business loans at commercial banks remained weak in December, and most large banks reduced their prime rates around the end of that month. Real estate and consumer loans continued to expand at a rapid pace in December and banks sharply increased their holdings of securities.

The narrowly defined money stock (private demand deposits plus currency in circulation, or M_1), which had not grown on balance from August to November, rose somewhat from November to December. Over the fourth quarter M_1 increased at an annual rate of about 1 per cent, after rising at rates of about 3.5 per cent over the third quarter and 10 per cent over the first half of 1971.[1/] Inflows of savings to commercial banks increased in December and the money stock more broadly defined (M_1 plus commercial bank time deposits other than large-denomination CD's, or M_2) rose at a substantial rate. Growth in the bank credit proxy--daily-average member bank deposits, adjusted to include funds from nondeposit sources--also was substantial as the average volume of both large-denomination CD's outstanding and U.S. Government deposits expanded. At the same time, banks reduced their outstanding borrowings of Euro-dollars by large amounts. Over the fourth quarter M_2 and the proxy series increased at annual rates of about 8 and 9.5 per cent, respectively.

1/ Growth rates cited are calculated on the basis of the daily-average level in the last month of the period relative to that of the preceding period.

System open market operations in the period since the last meeting of the Committee had been complicated by year-end churning in the money market and by uncertainties regarding the likely volume of reflows of short-term capital following the Smithsonian agreement. It was expected that if the reflows were large they would be accompanied by heavy foreign central bank sales of Treasury securities. In order to leave scope for future outright purchases of securities to moderate the market impact of such sales, the System made extensive use of repurchase agreements in the latter part of December to supply reserves on a temporary basis. In fact, however, reflows during the period were of quite modest dimensions.

Over the period as a whole System operations had been directed at fostering a substantial easing in money market conditions, against the background of the behavior of the monetary aggregates--particularly the continuing sluggishness of M_1. The Federal funds rate was about 3-5/8 per cent at the time of this meeting, down from the level of about 4-3/8 per cent prevailing at the time of the preceding meeting. In the 4 weeks ending January 5, member bank borrowings averaged $110 million compared with $395 million in the preceding 4 weeks.

At the time of this meeting interest rates on most types of market securities were lower than they had been in mid-December. Short-term rates had fallen, in part because of the easing of money market conditions associated with the System's reserve-supplying operations and because of anticipations on the part of market participants of still greater ease. Even with the auction on December 22 of $2.5 billion of tax-anticipation bills, Treasury bill rates had come under strong downward pressure as the reflow of short-term capital from abroad--and the consequent sales of bills by foreign central banks--proved to be far less than the market had expected. On the day before this meeting of the Committee, the market rate on 3-month bills was about 3.00 per cent compared with 3.95 per cent 4 weeks earlier.

Declines in rates for long-term securities were much more moderate. Early in the period capital markets were still under the influence of the Treasury's November financing, and later they were affected by discussion of the possibility that the February financing--the terms of which were expected to be announced near the end of January--would include an advance refunding. Public offerings of new corporate bonds were light, as is usual in December, but offerings of new State and local government bonds were contraseasonally large. It was expected that the volume of corporate issues would rebound in January but that issues of State and local governments would taper off.

Yields in the secondary market for federally insured mortgages declined slightly further in December. Inflows of savings to nonbank thrift institutions, which had slowed in

November, increased in December as the relative attractiveness of savings shares and deposits was enhanced by the further declines in market interest rates.

In the Committee's discussion considerable concern was expressed about the persistent sluggishness of key monetary aggregates, and a number of members advocated action to provide sufficient reserves to support the faster monetary growth that they believed was required by the economic situation and outlook. It was noted in this connection that the level of member bank reserves, as well as that of M_1, had changed little during the fourth quarter despite a progressive easing of money market conditions. In the interest of assuring the provision of reserves needed for adequate growth in monetary aggregates, the Committee decided that in the period until its next meeting open market operations, while continuing to take appropriate account of conditions in the money market, should be guided more by the course of total reserves than had been customary in the past.

The members also agreed that in the course of operations account should be taken of international developments and, beginning late in the month, of the forthcoming Treasury financing.

In placing greater emphasis on total reserves, the Committee took note of a staff analysis suggesting that moderate rates of growth in M_1 and M_2 in January and February were likely to be associated with a large increase in total reserves from December to January and then a decline in February--mainly as a consequence of recent and anticipated changes in U.S. Government deposits, and allowing for the 2-week lag between member bank deposits and required reserves. Against the background of this analysis, a majority agreed that an annual rate of growth in total reserves of roughly 20 to 25 per cent from December to January would be satisfactory, provided that it could be attained without undue easing of money market conditions.

The following current economic 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 increased more rapidly in the fourth quarter than it had in the third quarter, but the unemployment rate remained high. In recent weeks wage and price developments have reflected some increases that had been deferred under the 90-day freeze. The narrowly defined money stock, which had not grown on balance from August to November, rose somewhat in December, while both the broadly defined money stock and the bank credit proxy increased substantially. Market interest rates, particularly short-term rates, have declined in recent weeks. After international agreement was reached in December on new central exchange rates and on wider margins of permissible variation, market exchange rates for major foreign currencies against the dollar initially moved to levels a little above their new lower limits. The volume of capital reflows to the United States has been modest, however, and the underlying U.S. balance of payments remains in deficit. In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions consistent with the aims of the new governmental program, including sustainable real economic growth and increased employment, abatement of inflationary pressures, and attainment of reasonable equilibrium in the country's balance of payments.

To implement this policy, while taking account of international developments and the forthcoming Treasury financing, the Committee seeks to promote the degree of ease in bank reserve and money market conditions essential to greater growth in monetary aggregates over the months ahead.

Votes for this action: Messrs. Burns, Clay, Daane, Maisel, Mayo, Mitchell, Morris, Robertson, and Sheehan. Votes against this action: Messrs. Hayes, Brimmer, and Kimbrel.

Messrs. Hayes, Brimmer, and Kimbrel differed somewhat in their reasons for dissenting from this action. Mr. Hayes considered the emphasis placed on total reserves as an operating target to be an undesirable step; in his judgment, reserves were much less meaningful than other measures, such as the monetary and credit aggregates and interest rates, as an instrument for working toward the Committee's basic economic objectives. Also, he was reluctant to issue a directive that might involve a substantial further easing of money market conditions, since the Committee had already moved rapidly in that direction and since it appeared to him that the economic outlook had improved somewhat in recent months. He was concerned about the risk that a further sharp decline in short-term interest rates might subject financial markets to unnecessary whipsawing and might tend to rekindle inflationary expectations.

Mr. Brimmer shared the majority's views concerning broad objectives of policy at this time, and he indicated that he would have voted favorably on the directive were it not for the decision to give special emphasis to total reserves as an operating target during coming weeks. In his judgment the Committee should have had more discussion of the implications of that decision, and in any case it should have postponed the decision until after it had held a contemplated meeting to be devoted primarily to discussion of its general procedures with respect to operating targets.

Mr. Kimbrel favored supplying reserves at a rate that would accommodate orderly economic expansion. He voted against the directive because he thought it involved risks of depressing short-term interest rates to unsustainably low levels and of producing excessive rates of growth in the monetary aggregates in the future.

2. Ratification of earlier actions.

Earlier in the course of this meeting the Committee, by unanimous vote, ratified the action taken by the members on December 20, 1971, adding the clause "while taking account of international developments" at the end of the final sentence of the current economic policy directive then in effect.

Also, with Mr. Robertson dissenting, the Committee ratified the action taken by vote of a majority on December 23, 1971, to suspend, until close of business on the day of the next meeting, the lower limit (specified in paragraph 1(c) of the continuing authority directive with respect to domestic open market operations) on interest rates on repurchase agreements arranged by the Federal Reserve Bank of New York with nonbank dealers. The suspended provision specified that such repurchase agreements were to be made "at rates not less than (1) the discount rate of the Federal Reserve Bank of New York at the time such agreement is entered into, or (2) the average issuing rate on the most recent issue of 3-month Treasury bills, whichever is the lower."

The two actions in question had been taken for reasons set forth in the policy record for the meeting held on December 14, 1971. Mr. Robertson dissented from ratification of the second action for the same reasons that had led him to dissent from the action itself, as described in that policy record.