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 April 15-16, 1974.

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 April 15-16, 1974[1/]

Domestic policy directive

The information reviewed at this meeting suggested that real output of goods and services had declined appreciably in the first quarter of 1974--in large part because of the impact of the oil shortage--and that the GNP implicit deflator had risen at an exceptionally fast pace. Staff projections continued to suggest that real output would change little in the second quarter and that the rise in prices would remain rapid.

In March industrial production declined moderately, after having receded more in January and February than had been indicated by earlier estimates for those months. Employment in manufacturing establishments also declined further in March, while employment in other nonagricultural sectors changed little. The unemployment rate, at 5.1 per cent, was about the same as in the preceding 2 months; both the labor force and total employment remained near the levels of January. According to the advance report, retail sales expanded moderately in March.

1/ This meeting began on the afternoon of April 15 and continued on the following morning.

Wholesale prices of farm and food products declined in March, reflecting for the most part decreases in prices of livestock, meats, grains, cotton, and wool. Wholesale prices of industrial commodities rose sharply; while price increases were widespread, they were extraordinarily large for iron and steel, nonferrous metals, fuels and power, chemicals, and some types of machinery. In February the consumer price index had risen substantially further, with a significant share of the rise again accounted for by large increases in foods, fuels, and power. The index of average hourly earnings of production workers on nonfarm payrolls advanced moderately in the first quarter of the year, after having risen substantially in the second half of 1973, but there were signs that the slowdown resulted at least in part from temporary influences.

The latest staff projections, like those of 4 weeks earlier, suggested that easing of the oil shortage following termination of the Arab embargo on oil shipments to the United States would have no more than a marginally expansive impact on over-all real output until the summer. For the second quarter, expectations were that business fixed investment would continue to expand; that government purchases of goods and services would grow at a substantial rate; and that personal consumption expenditures would strengthen. It was also anticipated, however, that residential construction outlays would fall further and that net exports would continue to decline.

According to the staff projections, real GNP would grow moderately in the second half of the year. It was anticipated that residential construction outlays would turn up; that business fixed investment would rise further; that government purchases of goods and services would continue to grow at a fairly rapid pace; and that disposable personal income and consumption expenditures would expand appreciably more than in the first half.

In foreign exchange markets the dollar depreciated against leading foreign currencies in March and the first few days of April and then recovered somewhat. Market activity in late March and early April was dominated by shifting expectations concerning the value of the German mark. The U.S. balance of payments on the official settlements basis, which had shifted from a substantial surplus in January to a deficit in February, was in deficit again in March. The surplus on U.S. merchandise trade had fallen sharply in February, chiefly because of a large rise in the cost of imported fuel.

Growth in total loans and investments at U.S. commercial banks remained rapid in March, reflecting an exceptionally large increase in business loans. In contrast with February, effective rates on bank loans were favorable relative to rates in the commercial paper market, encouraging businesses to concentrate their strong credit demands at banks. In late March and early April the prime rate applicable to large corporations was raised in five steps from 8-3/4 per cent to 10 per cent at most banks.

In March the narrowly defined money stock (M_1)[2/] again expanded at a rapid pace. Over the first quarter as a whole, however, M_1 grew at an annual rate of about 6.5 per cent, down from a rate of about 7.5 per cent in the preceding quarter.[3/] Banks' net inflows of time and savings deposits other than large-denomination CD's slowed substantially in March, and the broader measure of the money stock (M_2)[4/] rose more moderately than M_1. In order to help finance growth in loans, banks stepped up the issuance of large-denomination CD's and increased borrowings in

2/ Private demand deposits plus currency in circulation.

3/ Growth rates cited are calculated on the basis of the daily-average level in the last month of the quarter relative to that in the last month of the preceding quarter. The measure of the money stock subsequently was revised upward to reflect new benchmark data for deposits at nonmember banks; on the revised basis M_1 grew at an annual rate of about 7 per cent over the first quarter, down from a rate of about 9 per cent in the preceding quarter.

4/ M_1 plus commercial bank time and savings deposits other than large-denomination CD's.

the Euro-dollar market in March and early April. As a result, the bank credit proxy[5/] expanded sharply.

Net deposit inflows at nonbank thrift institutions in March remained at about the improved rate of the immediately preceding months. Growth in the measure of the money stock that includes such deposits (M_3)[6/]--like growth in M_2--was more moderate than that in M_1. Contract interest rates on conventional mortgages and yields in the secondary market for Federally insured mortgages rose somewhat in March, after having declined over the preceding 5 months.

On March 20 the Treasury announced that it would raise $4 billion in new money by auctioning an additional $2.5 billion of June tax-anticipation bills on March 26 and $1.5 billion of 2-year notes on March 28. The bills and notes were sold at average prices to yield 8.306 and 8.08 per cent, respectively. The Treasury was expected to announce on May 1 the terms of its mid-May refunding; of the maturing issues, $4.05 billion were held by the public.

System open market operations since the March 18-19 meeting had been guided by the Committee's decision to seek

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5/ Daily-average member banks deposits, adjusted to include funds from nondeposit sources.

6/ M_2 plus time and savings deposits at mutual savings banks and at savings and loan associations.

bank reserve and money market conditions that would moderate growth in monetary aggregates over the months ahead, while taking account of financial market developments, including the prospective Treasury financing. Soon after the meeting, operations were directed toward additional tightening in bank reserve and money market conditions. The Federal funds rate rose somewhat and member bank borrowings increased appreciably.

Toward the end of the inter-meeting period, available data suggested that in the March-April period M_1 would grow at a rate somewhat above the specified range of tolerance and that--for the most part because of banks' issuance of large-denomination CD's and borrowings in the Euro-dollar and commercial paper markets--reserves available to support private nonbank deposits (RPD's) would grow at a rate well above the specified range. Operations were directed toward further tightening in bank reserve and money market conditions, and the Federal funds rate--which had been around 9-3/8 per cent just before the March meeting--rose further to about 10-1/4 per cent. In the 3 weeks ending April 10, member bank borrowings averaged about $1,470 million, about $315 million above the average in the preceding 4 weeks.

Short- and long-term market interest rates rose considerably further in the period between the Committee's meeting on

March 18-19 and this meeting--in response to strong business credit demands, to the tightening in money market conditions, and to growing market expectations that economic activity in the months ahead would not be as weak as had been thought earlier. However, toward the end of the period Treasury bill rates moved downward against the trend of other short-term rates, in part because of demands for bills by foreign monetary authorities and also by small investors who were attracted by the high yield relative to interest rates available on time deposits. At the time of this meeting the market rate on 3-month Treasury bills was 7.95 per cent, down from an inter-meeting period high of 8.65 per cent on April 4-5 but unchanged from the rate at the time of the March meeting.

In markets for long-term securities, the rise in rates led to somewhat unsettled conditions for a time. Some offerings of new corporate and State and local government bonds that had been scheduled for March and early April were postponed or canceled. Nevertheless, the volume of new public offerings of corporate bonds was moderately larger in March than in February, while the volume of State and local government offerings was little changed. A small increase in the over-all volume of public offerings was in prospect for April.

A staff analysis suggested that growth in the demand for money over the second and third quarters of 1974 was likely to be somewhat greater than had been expected earlier. Consequently, it appeared likely that if M_1 were to be held to a growth rate consistent with the Committee's earlier longer-run objectives for the monetary aggregates, money market conditions would continue to tighten in the period immediately ahead and market interest rates would rise somewhat further. As a result, net inflows of consumer-type time and savings deposits to banks and nonbank thrift institutions would decline, bringing about reductions in the rates of growth in both M_2 and M_3. The analysis also indicated that if the rate of growth in M_1 were to be moderately higher than that consistent with the Committee's earlier longer-run objectives, little change in money market conditions and in market interest rates would be likely; under these conditions, net inflows of consumer-type time and savings deposits to banks and nonbank thrift institutions would decline less.

The staff analysis suggested that, because of the sizable increase that had taken place in early April, expansion in M_1 over the April-May period as a whole would be at a somewhat higher rate than desired for the longer term, even if money market conditions were to tighten further in the period immediately ahead. Growth in M_2 in the 2-month period also was expected to be somewhat higher than desired for the longer run, even though net inflows of consumer-type time and savings deposits to banks and nonbank thrift institutions were expected to recede.

The Committee concluded that the economic situation and outlook continued to call for moderate growth in monetary aggregates over the longer run and that, in view of the rapid monetary expansion recently, it would seek to achieve less rapid growth in monetary aggregates over the months ahead. The longer-run growth rate for M_1 accepted by the Committee was revised upward slightly, however, since attainment of the growth rate contemplated previously appeared likely to be associated with sizable declines in net inflows of consumer-type time and savings deposits to banks and nonbank thrift institutions.

Taking account of the staff analysis, the Committee decided that progress toward its objective of moderating monetary growth could be achieved even if rates of expansion in the aggregates over the April-May period were temporarily above those desired for the longer term. At the same time, however, the members agreed that more rapid progress toward moderate monetary growth should be accepted in the event that growth rates in the period ahead proved to be lower than expected at present. Consequently, they decided that the ranges of tolerance for the 2-month period should be wide enough to allow for such lower rates of growth. Specifically, for the April-May period the Committee adopted ranges of tolerance of 3 to 7 per cent and 5-1/2 to 8-1/2 per cent for the annual rates of growth in M_1 and M_2, respectively. The members agreed that rates of growth within those ranges would be likely to involve RPD growth during the same period at an annual rate within a 6 to 11 per cent range of tolerance, and they decided that in the period until the next meeting the weekly average Federal funds rate might be permitted to vary in an orderly fashion from as low as 9-3/4 per cent to as high as 10-3/4 per cent, if necessary, in the course of operations.

The members also agreed that, in the conduct of operations, account should be taken of the forthcoming Treasury financing and of international and domestic financial market developments. 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 and constraints.

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 declined appreciably in the first quarter and that price increases were exceptionally large. The decline in economic activity reflected mainly the impact of the oil shortage, which is being eased by the ending of the oil embargo. In March industrial production and manufacturing employment receded further, but retail sales strengthened. The unemployment rate changed little, remaining slightly above 5 per cent. Prices of farm and food products declined in March, but increases among industrial commodities were widespread and extraordinarily large. Advances in wage rates were moderate in the first quarter.

In March the dollar depreciated further against leading foreign currencies, and the balance of payments was in deficit on the official settlements basis. The U.S. trade surplus diminished again in February as the cost of imported oil rose sharply.

The narrowly defined money stock increased sharply again in March. Broader measures of the money stock rose more moderately, however, as net inflows of consumer-type time deposits at banks slowed substantially. Business short-term credit demands remained strong, with demands at banks exceptionally large. To help finance loan growth, banks in late March and early April stepped up the issuance of large-denomination CD's and also increased borrowings from abroad. Both short- and long-term market interest rates have risen considerably further in recent weeks.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to resisting inflationary pressures, supporting a resumption of real economic growth, and maintaining equilibrium in the country's balance of payments.

To implement this policy, while taking account of the forthcoming Treasury financing and of international and domestic financial market developments, the Committee seeks to achieve bank reserve and money market conditions that would moderate growth in monetary aggregates over the months ahead.

Votes for this action: Messrs. Burns, Hayes, Black, Brimmer, Bucher, Clay, Holland, Kimbrel, Mitchell, Sheehan, Wallich, and Winn. Votes against this action: None.

Subsequent to the meeting it appeared that in the April-May period the annual rates of growth in the monetary aggregates would be above the upper limits of the ranges that had been specified by the Committee. Largely because of unexpectedly strong money market pressures, the Federal funds rate was around 11 per cent on April 22 and 23, and in the statement week ending April 24 it seemed likely to average slightly above the upper limit of 10-3/4 per cent set by the Committee. The System Account Manager reported that in order to bring the funds rate back within the range of tolerance he would have to expand reserve-supplying operations, thus stimulating further growth of the monetary aggregates. On April 24, in view of those circumstances and against the background of the increase in Federal Reserve discount rates announced that day, Chairman Burns recommended that the upper limit of the funds rate constraint be raised by one-quarter of a percentage point to 11 per cent. The members of the Committee--with the exception of Mr. Bucher--concurred in the Chairman's recommendation.

In mid-May available data suggested that in the April-May period the annual rates of growth in M_1 and M_2 would be within the short-run ranges of tolerance specified by the Committee while the rate of growth in RPD's would be well above its specified range. The Federal funds rate remained above the 11 per cent upper limit of the Committee's range of tolerance despite System efforts to achieve a lower rate; in the statement week ending May 15, it averaged 11.46 per cent. Major member banks apparently preferred to avoid borrowing at the discount window, bidding in the Federal funds market instead. In addition, a technical market shortage of collateral for repurchase agreements hampered efforts to provide reserves. In any event, it would have been difficult to bring the funds rate back down to 11 per cent without providing nonborrowed reserves through open market operations on a scale that would have risked market misinterpretation of the System's policy intent. On May 17 Chairman Burns recommended that the Committee take note of the difficulties faced by the System Account Manager in recent days and, in view of the likelihood that those conditions would persist over the next few days, that it change the ceiling guideline for the funds rate from 11 to 11-1/4 per cent. The members--with the exception of Mr. Holland--concurred in the Chairman's recommendation.