FEDERAL RESERVE
press release

For immediate release February 5, 1975

The Board of Governors of the Federal Reserve System and the Federal Open Market Committee today released the attached records of policy actions taken by the Federal Open Market Committee at its meetings on November 19 and December 16-17, 1974. As in the past, the record for the December meeting of the Committee has been released along with the record for the November meeting rather than in accordance with the usual schedule of approximately 90 days after the meeting in order to complete the published record for the year in advance of the Chairman's testimony at the Congressional hearings on the Economic Report of the President and the Annual Report of the Council of Economic Advisers.

These records will be published in the Board's Annual Report for 1974 and in the Federal Reserve Bulletin. 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 meetings, rather than on data as they may have been revised since then.

Attachments

REVISED DRAFT

CONFIDENTIAL (FR) January 9, 1975

RECORD OF POLICY ACTIONS OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on November 19, 1974

Domestic policy directive

The information reviewed at this meeting suggested that real output of goods and services--which had declined at an annual rate of about 3 per cent in the third quarter of the year and of about 4.5 per cent in the first half--was falling significantly further in the current quarter while prices and wages were continuing to rise at a rapid pace. Staff projections, like those of 5 weeks earlier, suggested that contraction in real economic activity would persist during the first half of 1975 and that the rate of increase in prices would remain rapid, although not so rapid as throughout 1974.

After having changed little since May, industrial production declined in October as a result of widespread decreases among consumer goods as well as industrial and construction materials; although auto output increased somewhat in October, it was being curtailed in November because of declining sales and a record level of inventories. Total retail sales edged down in October, reflecting the weakness in auto sales. Nonfarm payroll employment changed little. However, the unemployment rate rose further, from 5.8 to 6.0 per cent, and in late October and early November claims for unemployment insurance continued to increase. Although a new labor contract had just been negotiated in the coal industry, the length of the strike that had begun on November 12 was uncertain because of the need for ratification by the union membership; a prolonged strike could induce substantial curtailments in output and employment in other industries.

Wholesale prices of industrial commodities rose substantially further in October--reflecting increases in motor vehicles, machinery, and chemicals--but as in September, the rise was well below the extraordinarily rapid rate earlier in the year. Wholesale prices of farm and food products increased sharply after having declined moderately in September. The index of average hourly earnings for private nonfarm production workers continued to advance at a relatively rapid pace. In September the consumer price index had increased substantially further.

Staff projections for the first half of 1975 were similar to those made 5 weeks earlier: it was still anticipated that the rise in both disposable personal income and personal consumption expenditures would be little, if any, greater than the increase in consumer prices; that the expansion in business fixed investment would taper off; and that the pace of business inventory investment would moderate. However, residential construction activity now was expected to decline somewhat less in the first quarter and then to turn up in the second quarter.

The exchange rate for the dollar against leading foreign currencies--which had turned down in early September--continued downward between mid-October and mid-November, in part because of a decline in interest rates in the United States relative to rates in most other countries. The U.S. merchandise trade deficit, already sizable in the second quarter of the year, increased substantially in the third quarter, reflecting a large decline in exports of agricultural commodities and a further rise in imports. However, U.S. banks and U.S. agencies and branches of foreign banks sharply reduced their lending abroad.

Total loans and investments at U.S. commercial banks, after having declined in September, were unchanged in October. The growth in outstanding business loans was moderate--as prime business borrowers continued to be attracted to the commercial paper market by declines in rates in that market--and bank holdings of Treasury securities declined further. Banks reduced their Euro-dollar borrowings and their outstanding volume of large-denomination CD's. Between mid-October and mid-November, most banks reduced the prime rate applicable to large corporations in four steps from 11-3/4 per cent to 10-3/4 per cent, but the reduction was substantially less than the decline in commercial paper rates.

On November 13 the Board of Governors announced a restructuring of member bank reserve requirements that would release reserves to the banking system in the week beginning December 12 and thus would help to meet the seasonal need for reserves over the following weeks.[1/] The action also was designed to improve the liquidity of the banking system by encouraging banks to alter the structure of their time deposits in favor of the longer-term maturities; toward that end, reserve requirements on longer-term time deposits were reduced and those on shorter-term time deposits were raised.

The narrowly defined money stock (M_1)[2/] rose at an annual rate of about 5 per cent in October, compared with rates of about 1.5 per cent in the third quarter and 6 per cent in the first half of the year.[3/] Net inflows of consumer-type time and savings

1/ On November 18 the Board announced a modification of the restructuring of reserve requirements.

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 period relative to that in the last month preceding the period. Measures of the money stock subsequently were revised to reflect new benchmark data for deposits at nonmember banks; on the revised basis M_1 grew at an annual rate of about 4 per cent in October.

deposits to banks and to nonbank thrift institutions also picked up in October, and the more broadly defined measures of the money stock (M_2[4/] and M_3[5/]) expanded appreciably.

The Treasury raised new money on October 23 by auctioning $1 billion of 4-1/2-year notes at an average price to yield 7.89 per cent. In its regular quarterly financing the Treasury auctioned $4.85 billion of notes and bonds to refund $4.3 billion of publicly held securities having mid-November maturities and to raise $550 million of new money: on November 6, 7, and 8, respectively, it sold $2.5 billion of 3-year notes at an average price to yield 7.85 per cent; $1.75 billion of 7-year notes at an average price to yield 7.82 per cent; and $600 million of a reopened 24-1/2-year bond at an average price to yield 8.21 per cent to maturity. On November 14 the Treasury announced that later in the month it would raise more new money by auctioning $3.5 billion of April and June tax-anticipation bills and $1 billion of a strip of bills made up of additions to the weekly bills maturing in late December and early January.

System open market operations since the October meeting had been guided by the Committee's decision to seek bank reserve

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

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

and money market conditions consistent with a resumption of moderate growth in monetary aggregates over the months ahead, while taking account of the forthcoming Treasury financing and of developments in domestic and international financial markets. Data that had become available a few days after that meeting suggested that in the October-November period M_1 would grow at a rate in the lower part of the 4-3/4 to 7-1/4 per cent range of tolerance that had been specified by the Committee. In accordance with the understanding that the weekly average rate for Federal funds would be permitted to decline to about the midpoint of its specified range of 9 to 10-1/2 per cent so long as the monetary aggregates did not appear to be growing at rates at or above the upper limits of their specified ranges, System operations had been directed toward some further easing in bank reserve and money market conditions. In the final days of October the funds rate was about 9-3/4 per cent, compared with an average of about 10-1/8 per cent in the statement week ending October 16.

On October 31 the available data suggested that in the October-November period the annual rate of growth in M_1 would be at the midpoint of the specified range, reflecting an expectation that growth in M_1 would accelerate in November from an October rate that was estimated to be near the lower limit of the range. The rate of growth in M_2 in the 2-month period appeared to be at the upper limit of its range. In view of the behavior of the aggregates, the System ordinarily would have become more restrictive in its reserve-supplying operations--to the extent consistent with even-keel considerations--expecting that the weekly-average Federal funds rate would rise slightly above 9-3/4 per cent. However, a majority of the members concurred in the Chairman's recommendation of October 31 that the target for the funds rate be reduced to 9-1/2 per cent for the time being, in view of the evidence of additional weakness in economic activity, restraint in the lending policies of banks and other institutions, and the severe financial problems of the construction industry. In the days before this meeting the funds rate was about 9-1/2 per cent.

Most short-term market interest rates declined considerably further in the inter-meeting period--despite the large additions to the supplies of Treasury bills--in response to the continuing decline in the Federal funds rate. However, Treasury bill rates moved up again following the November 14 announcement that the Treasury would auction a substantial volume of tax-anticipation bills to raise new money. On the day before this meeting the rate on 3-month Treasury bills was 7.52 per cent, compared with 7.17 per cent on November 14 and with 7.63 per cent on the last market day before the October meeting.

Markets for long-term securities also improved, as many investors concluded that long-term rates had passed their peaks. Yields on Treasury and corporate bonds declined, although the volume of public offerings of corporate bonds in October and in prospect for November was unusually large. Contract interest rates on new commitments for conventional home mortgages in the primary market turned down in October, while yields on commitments in the secondary market for Federally underwritten home mortgages continued to decline.

The Committee concluded that the economic situation and outlook called for moderate growth in the monetary aggregates over the longer run. A staff analysis suggested that growth in M_1--although still relatively sluggish in October--would be fairly rapid in the November-December period, reflecting the cumulative impact of the decline in interest rates that had occurred in recent months and the temporary effects of a substantial decline in U.S. Government deposits. Nevertheless, it appeared likely that if M_1 were to grow at a rate consistent with the Committee's longer-run objectives for the monetary aggregates, money market conditions would have to ease slightly further in the period immediately ahead. Such easing probably would be accompanied by little, if any, further decline in other market interest rates.

The staff analysis suggested that net inflows to banks of time and savings deposits other than large-denomination CD's, which had picked up sharply in October, would remain substantial in the period immediately ahead and that net inflows to nonbank thrift institutions would imporve further. Expansion in bank credit was likely to be moderate, in part because banks had adopted more cautious loan and investment policies.

Taking account of the staff analysis and in light of the recent relatively slow growth of the monetary aggregates, the Committee concluded that its objective of moderate monetary growth could be ~~achieved~~ FURTHERED with RELATIVELY RAPID rates of expansion in the NOVEMBER-DECEMBER PERIOD ~~near-term that-were-temporarily-above-those-desired-for-the-longer-term~~. Specifically, the Committee adopted ranges of tolerance for the November-December period of 6-1/2 to 9-1/2 per cent and 8 to 10-1/2 per cent for the annual rates of growth in M_1 and M_2, respectively. The members agreed that such growth rates would be likely to involve growth in reserves available to support private nonbank deposits (RPD's) within a range of tolerance of 2-1/2 to 5-1/2 per cent. They decided that in the period until the next meeting the weekly average Federal funds rate be permitted to vary in an orderly fashion from as low as 8-1/2 per cent to as high as 10 per cent, if necessary, in the course of operations.

The members also agreed that, in the conduct of operations, account should be taken of developments in domestic and international financial markets. 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 is falling significantly further in the current quarter while price and wage increases are continuing large. In October industrial production declined--after having changed little since May--and the unemployment rate increased further, from 5.8 to 6.0 per cent. In recent weeks sizable cutbacks in automobile production have been announced, and claims for unemployment insurance have continued to increase. There are major uncertainties concerning the duration of the coal strike; a lengthy shutdown would have substantial effects on other industries. The October rise in wholesale prices of industrial commodities, although substantial, remained well below the extraordinarily rapid rate in the first 8 months of the year; prices of farm products and foods increased sharply.
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> In recent weeks the dollar has declined further against leading foreign currencies. In the third quarter the U.S. foreign trade deficit was substantially larger than in the second quarter, but U.S. banks sharply reduced their foreign lending.

Growth of the narrowly defined money stock picked up from the slow pace of the third quarter to an annual rate of about 5 per cent in October. Net inflows of consumer-type time and savings deposits at banks and at nonbank thrift institutions also improved in October, and the money supply measures more broadly defined expanded appreciably. Bank credit outstanding changed little, and banks reduced their borrowing through Euro-dollars and large-denomination CD's. Since mid-October markets for short- and long-term securities have improved, despite heavy Treasury financing and a large volume of corporate security issues. Interest rates on market securities in general have declined further, and mortgage yields also have fallen somewhat. On November 13 the Board of Governors announced a restructuring of member bank reserve requirements, which will have the effect of releasing reserves to the banking system in the week beginning December 12.

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 achieving equilibrium in the country's balance of payments.

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

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