FEDERAL RESERVE

press release

For immediate release November 3, 1975

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 September 16, 1975.

Such records are made available approximately 45 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 September 16, 1975

1. Domestic policy directive

The information reviewed at this meeting suggested that output of goods and services--which had turned up in the second quarter--was increasing appreciably in the current quarter and that prices, on the average, were rising at a somewhat faster pace than in the first half of the year. Staff projections suggested that expansion in output would remain strong in the fourth quarter and that the rate of growth would then moderate somewhat in the first half of 1976.

In August the pace of economic recovery appeared to have gained momentum; both industrial production and employment in nonfarm establishments advanced more than in July. The average workweek of production workers in manufacturing industries continued to lengthen, and for the first time since October 1974 it approached 40 hours. The unemployment rate--which had declined from 9.2 per cent in May to 8.4 per cent in July--was unchanged, as the civilian labor force increased about as much as total employment. Retail sales apparently declined slightly in August, following 4 months of large gains in real as well as in dollar-value terms.

The increase in the index of average hourly earnings for private nonfarm production workers was large in August, after having been relatively small in July; over recent months, on the average, the advance has been somewhat less rapid than in 1974 and in the first quarter of 1975. The wholesale price index for industrial commodities rose somewhat more in August than in July, in part because the rise in August reflected earlier increases in gasoline prices; the index for farm and food products declined slightly. In July the rise in the consumer price index had accelerated further, owing chiefly to sizable increases in retail prices of foods, gasoline, fuel oil, and used cars.

Staff projections continued to suggest that nominal GNP would expand rapidly in the second half of 1975 as a result of a vigorous recovery in output and a somewhat faster rise in average prices than in the first half, mainly reflecting increases in prices of foods and energy products. As a month earlier, it was expected that business inventory liquidation would slow sharply from the extraordinary rate in the second quarter; that real consumption expenditures would grow at a substantial pace; that residential construction would pick up; and that business fixed investment outlays would begin to strengthen late in the year. However, it also was anticipated that--in view of the projected strength of the domestic recovery--imports would expand more than exports.

The exchange value of the dollar against leading foreign currencies--which had appreciated considerably from late June to mid-August--rose somewhat further to mid-September, in part because interest rate developments here and abroad continued to favor the dollar. In July U.S. merchandise imports rose sharply, to a considerable extent because of a large increase in imports of fuels from the depressed level in June, and the U.S. foreign trade surplus declined from the very high rates in June and in the second quarter as a whole. Private capital transactions reported by banks shifted to a net inflow in July from net outflows in earlier months. U.S. liabilities to foreign official agencies declined, after having increased earlier, as some countries sold dollars to support their currencies in the foreign exchange markets.

Total loans and investments at U.S. commercial banks continued to expand at a moderate pace in August. Outstanding loans to businesses declined slightly, but banks again added a substantial amount to their holdings of U.S. Government securities. The outstanding volume of commercial paper issued by nonfinancial businesses--which had turned up in July--rose again in August, reflecting a modest strengthening in business demands for short-term credit and a lower cost of funds in the commercial paper market than at banks. In mid-September a number of banks raised the prime rate further, from 7-3/4 to 8 per cent.

Expansion in M_1 picked up somewhat in August from the low rate in July, when it had been limited to a significant degree by adjustment of money balances after the May-June bulge associated with special disbursements by the Treasury. Growth in M_2 and M_3 slowed further in August, however, as inflows of consumer-type time and savings deposits to banks and to nonbank thrift institutions continued to moderate, in part because of the increased attractiveness of alternative investments. Banks reduced the outstanding volume of large-denomination CD's for the seventh consecutive month, in response to continued growth in other deposits and to weakness in loan demand.

On September 10 the Treasury announced an estimate of its borrowing needs for the rest of 1975, which involved raising $22 billion to $25 billion of new money. For the period through the third week in October, the Treasury's financing plans included auctions of $2 billion of 29-month notes, $6 billion of 2-year notes, and $1.9 billion of 1-year bills. Of the total of $9.9 billion, $7 billion represented new money.

Short-term market interest rates--which had increased appreciably from mid-June to mid-August--subsequently changed relatively little, despite increased Treasury and private demands for funds in the short-term market. On the day before this meeting, the market rate on 3-month Treasury bills was 6.50 per cent, compared with 6.42 per cent on the day before the August meeting.

Yields on longer-term Treasury and corporate securities edged lower over most of the inter-meeting period, in response mainly to the stability in short-term markets and to a substantial decline in offerings of new securities. However, yields adjusted upward after September 10 when the Treasury announced its sizable borrowing requirements over the rest of this year. Yields on State and local government securities rose to new highs in early September, because of widespread concern about possible repercussions of New York City's financial crisis; on September 9 a State program to assist the City was enacted. In home mortgage markets, yields advanced throughout the inter-meeting period, as demands for funds expanded while the outlook for their cost and availability became more uncertain.

System open market operations since the August 19 meeting had been guided by the Committee's decision to seek bank reserve and money market conditions consistent with moderate growth in monetary aggregates over the months ahead. It had been expected that the weekly average for the Federal funds rate might vary in an orderly fashion within a range of 5-3/4 to 7 per cent, with the understanding that operations would not be directed toward moving the rate above or below the 6-1/8 to 6-1/4 per cent area prevailing at that time unless it appeared that in the August-September period growth in the monetary aggregates would be substantially stronger or weaker than expected. Data that became available in early September suggested that in the 2-month period M_1 would grow at a rate in the lower part of the range of tolerance that had been specified by the Committee and that M_2 would grow at a rate slightly below the lower limit of its range. All available members of the Committee concurred in Chairman Burns' recommendation of September 5 that--in view of the likelihood of substantial strengthening in demands for money and credit over coming months and the prospect that a decline in the Federal funds rate might have to be reversed shortly--the Manager be instructed to continue until the next meeting to maintain reserve conditions consistent with a Federal funds rate in the 6-1/8 to 6-1/4 per cent area, while leaning toward the lower figure. On the average, the Federal funds rate remained in that area over the rest of the period until this meeting.

At its July meeting the Committee had agreed that growth in the monetary and credit aggregates on the average over the period from the second quarter of 1975 to the second quarter of 1976 at rates within the following ranges appeared to be consistent with its broad economic aims: M_1, 5 to 7-1/2 per cent; M_2, 8-1/2 to 10-1/2 per cent; M_3, 10 to 12 per cent; and the bank credit proxy, 6-1/2 to 9-1/2 per cent. In its discussion of current policy at this meeting the Committee took note of the indications that economic activity was now on the increase and of the likelihood that expansion in nominal GNP over coming quarters would be associated with considerable strengthening in the demand for money and credit. The continuing unsettlement in financial markets and the successive large-scale Treasury financing operations scheduled for coming weeks were also taken into account.

In view of the economic outlook, none of the members favored operations to ease bank reserve and money market conditions in the period immediately ahead. Some advocated operations to achieve some modest firming, whenever feasible without disrupting markets, in order to help restrain monetary growth later. And others noted that they would be willing to act promptly to seek firmer conditions if and when the rate of growth in the monetary aggregates accelerated substantially, but that they preferred not to base such action on projections that monetary growth would exceed the desired rates over the longer run.

At the conclusion of the discussion the Committee decided to seek bank reserve and money market conditions consistent with moderate growth in the monetary aggregates over the months ahead, while taking account of developments in domestic and international financial markets. Specifically, the members agreed that growth in M_1 and M_2 over the September-October period at annual rates within ranges of tolerance of 5 to 8 per cent and 7 to 9-1/2 per cent, respectively, would be acceptable. It was thought that such growth rates would be likely to involve annual rates of change in reserves available to support private nonbank deposits (RPD's) within a range of 1 to 4 per cent.

The members agreed that in the period until the next meeting the weekly average for the Federal funds rate might be expected to vary in an orderly fashion within a range of 6 to 7 per cent. It was understood, however, that if developments with respect to the aggregates suggested the need to move the Federal funds rate above 6-3/4 per cent, open market operations toward that end would not be undertaken until after the Chairman had consulted with the Committee.

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

The information reviewed at this meeting suggests that output of goods and services--which had turned up in the second quarter--is increasing appreciably further in the current quarter. In August industrial production and nonfarm payroll employment expanded at a faster pace than in July, and the average workweek in manufacturing continued to lengthen. The unemployment rate remained at 8.4 per cent, as the civilian labor force increased about as much as total employment. Retail sales apparently declined slightly, following 4 months of large gains. The index of wholesale prices of industrial commodities rose somewhat more in August than in July, chiefly because of increases in prices of energy products; prices of farm and food products declined slightly. The advance in average wage rates over recent months has been somewhat less rapid than in 1974 and early 1975.

In recent weeks the exchange value of the dollar against leading foreign currencies has risen somewhat further. In July the U.S. foreign trade surplus declined from the very high second-quarter level, as imports rose sharply. Bank-reported capital movements showed a net inflow, in contrast to the net outflows of earlier months, while U.S. liabilities to foreign official agencies, which earlier had been rising, declined.

Expansion in M_1 picked up somewhat in August from the low July rate. Growth in M_2 and M_3 slowed further, however, as inflows of consumer-type time and savings deposits to banks and to nonbank thrift institutions continued to moderate, reflecting in part the increased attractiveness of alternative investments. Interest rates on short-term securities and on longer-term Treasury and corporate securities have shown little net change in recent weeks, except that longer-term yields adjusted upward following the Treasury's September 10 announcement of its sizable borrowing requirements over the rest of this year. Yields on State and local government securities rose to new highs in early September, as a result of widespread concern about possible repercussions of New York City's financial crisis; on September 9 a State program to assist the City was enacted.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to stimulating economic recovery, while resisting inflationary pressures and contributing to a sustainable pattern of international transactions.

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, Volcker, Baughman, Bucher, Coldwell, Eastburn, Holland, Jackson, MacLaury, Mayo, Mitchell, and Wallich. Votes against this action: None.

Subsequent to the meeting, on October 2, the available data suggested that in the September-October period both M_1 and M_2 would grow at rates well below the lower limits of the ranges of tolerance that had been specified by the Committee. The Federal funds rate had averaged 6.36 per cent during the statement week ending October 1 and most recently had been about 6-1/4 per cent. In view of the weakness of the aggregates and of the unsettled market for municipal securities, Chairman Burns recommended that the Manager be instructed to aim at a Federal funds rate of 6-1/8 per cent immediately and to aim to reduce the rate to 6 per cent over the next few days. The

Chairman also recommended that the lower limit of the funds rate constraint be reduced to 5-3/4 per cent, in order to provide leeway for further operations in the event that current weakness of the aggregates was confirmed by incoming data in the following week. All available members of the Committee--with the exception of Mr. Bucher--concurred in the Chairman's recommendations. Mr. Bucher, while concurring in the first recommendation, preferred not to reduce the lower limit of the constraint before data on the aggregates became available in the following week.

2. Authorization for domestic open market operations

On October 3, 1975, Committee members voted to increase from $3 billion to $4 billion the limit on changes between Committee meetings in System Account holdings of U.S. Government and Federal agency securities specified in paragraph 1(a) of the authorization for domestic open market operations, effective immediately, for the period ending with the close of business on October 21, 1975.

Votes for this action: Messrs. Burns, Volcker, Baughman, Bucher, Coldwell, Eastburn, Jackson, MacLaury, Mayo, Mitchell, and Wallich. Votes against this action: None.

Absent and not voting: Mr. Holland.

This action was taken on recommendation of the System Account Manager, who had advised that large-scale purchases of Treasury and Federal agency securities since the September meeting of the Committee--required mainly to counter the effect of a rise in Treasury balances at the Reserve Banks--had reduced the leeway available for further purchases to about $300 million. While projections for coming weeks suggested that the System would be in a position to absorb rather than to provide reserves, the Manager believed that in view of the fragile state of confidence in financial markets, especially the municipal market, it would be desirable for the Desk to have additional flexibility to deal with unfolding developments.