FEDERAL RESERVE

press release

For immediate release January 5, 1976

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 November 18, 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 November 18, 1975

Domestic policy directive

The information reviewed at this meeting suggested that output of goods and services--which had increased at an annual rate of 11 per cent in the third quarter--was expanding more moderately in the current quarter and that prices were continuing to rise at a relatively fast pace. Staff projections continued to suggest that growth would moderate further in the first half of 1976 and that the rate of increase in prices would slow somewhat over the period to mid-1976.

In October retail sales had risen somewhat, according to the advance report, after 2 months of little net change from the higher levels reached in July. Industrial production continued to recover, although at a considerably less rapid pace than in the preceding 4 months. Recovery in nonfarm payroll employment also was less rapid than in earlier months, and the average workweek in manufacturing was unchanged. The unemployment rate rose from 8.3 to 8.6 per cent, reflecting a sizable increase in the civilian labor force.

The index of average hourly earnings for private nonfarm production workers rose substantially in October. The rise in average wholesale prices of industrial commodities--which had accelerated in August and September--was even more rapid in October, reflecting in part previously announced increases in prices of 1976-model automobiles and of steel. The index for farm and food products rose sharply further, but after mid-October--the date used for the index--prices of many agricultural products declined. In September the consumer price index had risen moderately; increases in prices of new automobiles and of transit fares in New York City accounted for much of the rise.

Staff projections for the fourth quarter and for the first half of 1976 were similar to those of 4 weeks earlier. They suggested that growth in personal consumption expenditures would be considerable--although less than in the third quarter--and that business inventories would shift from substantial liquidation in the third quarter to small accumulation in the fourth quarter and then to moderate accumulation. It was also anticipated that residential construction would continue to expand and that business fixed investment would begin to recover. However, growth in State and local government purchases of goods and services--which had slowed in the third quarter--was expected to remain at a reduced rate over the current and next two quarters. In addition, exports were projected to rise less than imports.

The exchange value of the dollar had moved in a narrow range in recent weeks. In September both U.S. merchandise exports and imports increased, and the foreign trade surplus remained substantial; the surplus for the third quarter as a whole was nearly as great as the average surplus for the first two quarters. Private capital transactions reported by banks, which had shown net inflows in July and August, apparently shifted back to a net outflow in September. The volume of offerings of new foreign bonds in the U.S. market has been at record levels this year.

Total loans and investments at U.S. commercial banks expanded moderately in October, on a seasonally adjusted basis. Outstanding loans to business--which had declined in most months earlier this year--rose appreciably; however, the increase in total short-term business borrowing was small as the outstanding volume of commercial paper issued by nonfinancial corporations declined further. Banks reduced their holdings of Treasury securities, but they increased their holdings of Federal agency and other securities by an almost equivalent amount. In late October and early November most banks reduced the prime rate applicable to large business borrowers from 8 to 7-1/2 per cent, and one major bank reduced it to 7-1/4 per cent.

M_1 grew at an annual rate of 6.9 per cent from the average level during the second quarter to the average level during the third quarter, but it rose relatively little in the months of the third quarter and declined in October. Inflows of consumer-type time and savings deposits to banks and to nonbank thrift institutions remained moderate in October, and growth in M_2 and M_3 slowed further. From the second-quarter average to the third-quarter average, M_2 and M_3 grew at annual rates of 10.4 per cent and 13.1 per cent, respectively.

System open market operations since the October 21 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 understood that operations would be directed toward moving the Federal funds rate down from the prevailing level of around 5-3/4 per cent to 5-1/2 per cent by the end of the statement week following the meeting, unless new data suggested that growth in the monetary aggregates in the October-November period would exceed the rates expected at the time of the meeting.

The new data that became available shortly after the meeting did suggest that monetary growth would be somewhat stronger than had been expected, and operations to ease bank reserve and money market conditions were delayed. Subsequently, however, new data suggested less strength in monetary growth, so System operations were directed toward some easing in the Federal funds rate. In the days immediately preceding this meeting, the rate was around 5-1/4 per cent.

Short-term market interest rates declined further over the inter-meeting period, in response to the decline in the Federal funds rate and to increased demands for high-grade liquid assets. On the day before this meeting, the market rate on 3-month Treasury bills was 5.45 per cent, down from 5.90 per cent on the day before the October meeting and from 6.50 per cent just before the September meeting.

Yields on longer-term Treasury and corporate securities also declined during most of the inter-meeting period, in response to the easing in short-term markets. However, yields on State and local goverment securities were subject to the influence of shifting expectations concerning resolution of New York's financial problems; they rose in late October and early November and then eased somewhat. Despite the adverse impact of the New York situation, the volume of offerings of municipal bonds was relatively large in October.

At its previous meeting, the Committee had agreed that growth in the monetary aggregates on the average over the period from the third quarter of 1975 to the third 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, 7-1/2 to 10-1/2 per cent; and M_3, 9 to 12 per cent. The associated range for growth in the bank credit proxy was 6 to 9 per cent. It was understood that the longer-term ranges, as well as the particular list of aggregates for which such ranges were specified, would be subject to review and modification at subsequent meetings. It also was understood that, as a result of short-run factors, growth rates from month to month might well fall outside the ranges contemplated for annual periods.

In the discussion of current policy at this meeting, the Committee took note of a staff analysis suggesting that, in view of the projected expansion in GNP, M_1 was likely to grow substantially faster over the months ahead than it had over the immediately preceding months. In addition, inflows of time and savings deposits to banks and nonbank thrift institutions were expected to pick up somewhat over the weeks ahead from the pace in late summer and early fall, in response to the decline in market interest rates that had occurred since that time.

During the discussion reference was made to the uncertain strength of the economic recovery over the quarters ahead and to the persistence of inflationary pressures. In addition, the unresolved financial problems of New York were recognized as a potential source of disturbance in financial markets that might have significant effects on the course of the recovery.

Some Committee members took the position that the objective of open market operations in the period immediately ahead should be to maintain prevailing money market conditions. Among the reasons advanced for this course were the sensitive state of financial markets and the judgment that changing relationships tended to make monetary growth rates unreliable guides to monetary policy at present. Other members, who preferred to continue to base operating decisions in the period immediately ahead primarily on the behavior of the monetary aggregates, expressed concern about their sluggish growth over recent months. In general, these members were willing to see some further easing in money market conditions, should that prove to be necessary in the pursuit of moderate monetary growth over the months immediately ahead. They also were willing to accept some tightening in money market conditions, in the event that the monetary aggregates began to grow at excessive rates.

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 more than usual account of developments in domestic and international financial markets. Specifically, the members agreed that, in light of the low rates of increase in recent months, growth in M_1 and M_2 over the November-December period at annual rates within ranges of tolerance of 6 to 10 per cent and 7-1/2 to 10-1/2 per cent, respectively, would be acceptable. It was thought that such growth rates would be likely to involve an annual rate of growth in reserves available to support private nonbank deposits (RPD's) within a range of 4-1/2 to 8-1/2 per cent.

The members agreed that 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 4-1/2 to 5-1/2 per cent. It was contemplated that System operations would be directed toward moving the Federal funds rate down to the middle of that range if the data becoming available in the weeks ahead suggested that the several monetary aggregates were growing at rates close to the midpoints of their ranges of tolerance.

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 increased sharply in the third quarter--is expanding more moderately in the current quarter. Retail sales are reported to have risen in October, after 2 months of little net change. Industrial production and nonfarm payroll employment continued to recover, although at a less rapid rate than in the summer months. The unemployment rate rose to 8.6 per cent from 8.3 per cent in September, reflecting a sizable increase in the civilian labor force. Average wholesale prices of industrial commodities increased more in October than in the immediately preceding months, and prices of farm and food products rose sharply further. However, since mid-October prices of many agricultural products have declined. The advance in average wage rates in October was substantial.

Since mid-October the exchange value of the dollar against leading foreign currencies has moved in a narrow range. The U.S. foreign trade surplus in September remained substantial, as both exports and imports rose moderately. Bank-reported private capital flows appear to have shifted to net outflows since September, and the volume of offerings of new foreign bonds in the U.S. market has been at record levels.

M_1 rose at a 6.9 per cent annual rate from the average level during the second quarter to the average level during the third quarter. However, M_1 grew relatively little in the months of the third quarter and it declined in October. Inflows of consumer-type time and savings deposits to banks and to nonbank thrift institutions remained moderate in October, and growth in M_2 and M_3 slowed further. Most short- and long-term interest rates have declined further in recent weeks. Conditions in markets for State and local government securities have continued to be adversely affected by New York's financial problems.

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

To implement this policy, while taking more than usual 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, Baughman, Bucher, Coldwell, Holland, MacLaury, Mayo, Mitchell, and Wallich. Votes against this action: Messrs. Volcker, Eastburn, and Jackson.

Messrs. Volcker and Jackson dissented from this action because they thought prevailing money market conditions should be maintained for the time being, in part because of current uncertainties about the short-run relationship between monetary growth and interest rates. In addition, Mr. Volcker indicated that he would prefer to avoid any significant tightening in money market conditions because of uncertainties about the economic outlook and the sensitivity of financial markets to New York and other problems, and to avoid any significant easing simply in response to the recent declines in the money supply, which were expected to be reversed before long. In the opinion of Mr. Jackson, performance of the broader monetary aggregates--such as M_3--and general conditions in credit markets were about right in the context of the current economic situation.

Mr. Eastburn dissented because he believed that the System should be more aggressive in supplying reserves in order to compensate for recent shortfalls in the rate of monetary expansion from the Committee's longer-run growth ranges. He indicated that he would place less weight on the Federal funds rate constraint because, in his judgment, too much emphasis on money market conditions had misled the Committee in the past. Accordingly, he preferred a range of tolerance for the Federal funds rate that was lower than the range adopted by the Committee and a directive with less emphasis on money market conditions.