FEDERAL RESERVE press release

For Use at 4:10 p.m. December 22, 1980

The Federal Reserve Board 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, 1980. This record also includes policy actions taken during the period between the meeting on November 18, and the next regularly scheduled meeting held on December 19.

Such records for each meeting of the Committee are made available a few days after the next regularly scheduled meeting 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 solely on the information that was available to the Committee at the time of the meeting.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on November 18, 1980

Domestic policy directive

The information reviewed at this meeting suggested that real GNP, which had increased at an annual rate of 1 percent in the third quarter following a sharp second-quarter contraction, was expanding further in the current quarter. Average prices, as measured by the fixed-weight price index for gross domestic business product, appeared to be continuing to rise at a rapid pace, close to the annual rate of 10-1/2 percent experienced in the second and third quarters.

The index of industrial production rose an estimated 1.6 percent in October, following substantial gains in each of the two preceding months. Over the three-month period, industrial production increased 4 percent, but the index in October was still about 4 percent below its level in the first quarter of 1980. Capacity utilization in manufacturing increased about 1 percentage point further in October to 77.6 percent, but remained about 6 percentage points below the first-quarter rate.

Nonfarm payroll employment expanded substantially in October for the third consecutive month, and the unemployment rate remained at about 7-1/2 percent. Employment gains were widespread, but were especially strong in durable goods manufacturing and construction -- industries in which earlier job losses had been sizable -- and the average workweek in manufacturing lengthened slightly.

The dollar value of retail sales changed little in October, according to the advance report, following a large increase over the four preceding months. Sales of new automobiles were at an annual rate of 9.0 million units in October, up from 8.8 million in September.

Private housing starts rose further in September to an annual rate of more than 1.5 million units, reflecting in part a bulge in starts of federally subsidized units at the end of the fiscal year. Sales of new houses declined in September for the second successive month, although sales of existing houses rose further. Fragmentary data for October suggested that housing activity was weakening.

Producer prices of finished goods rose substantially in October after a small decline in September. Consumer prices rose at an accelerated pace in September, reflecting not only continued sharp advances in food prices but increases in most other categories as well. The index of average hourly earnings of private nonfarm production workers rose at an annual rate of 9 percent over the first ten months of the year, compared with an increase of about 8-1/4 percent during 1979.

In foreign exchange markets the trade-weighted value of the dollar against major foreign currencies had risen about 3 percent over the interval since the Committee's meeting in mid-October. In September the U.S. foreign trade deficit was essentially unchanged from the August level; in the third quarter the deficit was sharply below the average of the first two quarters and was the smallest since the second quarter of 1976. The volume and value of oil imports fell sharply in the third quarter, while the value of exports -- especially agricultural products -- increased.

At its meeting on October 21, the Committee had decided that open market operations in the period until this meeting should be directed toward expansion of reserve aggregates consistent with growth of M-1A, M-1B, and M-2 over the period from September to December at annual rates of about 2-1/2 percent, 5 percent, and 7-1/4 percent respectively, or somewhat less, provided that in the period until the next regular meeting the weekly average federal funds rate remained within a range of 9 to 15 percent. Early in the intermeeting period, incoming data indicated that the monetary aggregates, particularly M-1A and M-1B, were growing much faster than both the rates projected at the time of the meeting and the rates consistent with the Committee's objectives for the September-to-December period. Required reserves and member bank demands for reserves expanded substantially in relation to the constrained supply of reserves being made available through open market operations. Consequently, member bank borrowings increased sharply, to an average of $1.7 billion in the three statement weeks ending on November 12 from an average of $1.3 billion in the five weeks between the September and October meetings. These developments were associated with additional upward pressures on the federal funds rate and other short-term interest rates; in mid-November the funds rate averaged 14-1/2 percent, compared with about 12-1/2 percent in the days just before the Committee's meeting on October 21.

After the markets closed on November 14, the Board of Governors announced an increase in Federal Reserve discount rates from 11 to 12 percent and a surcharge of 2 percentage points on frequent borrowing of large institutions. The actions, which were effective on Monday, November 17, were taken in view of the prevailing level of short-term market interest rates and the recent rapid growth in the monetary aggregates and bank credit. On November 17, the day before this meeting, federal funds traded at an average rate of about 16-1/4 percent.

Growth in M-1A and M-1B moderated further in October, but the annual rates of about 9 and 11 percent respectively were substantially above those consistent with the Committee's objectives for the period from September to December. Expansion in M-2 accelerated slightly in October, to an annual rate of about 9 percent, reflecting a pickup in growth of nontransaction accounts included in that aggregate; growth in M-3 also accelerated somewhat. From the fourth quarter of 1979 through October, growth of M-1A was in the upper part of the range set by the Committee for the year ending in the fourth quarter of 1980; M-1B and M-2 grew at rates somewhat above the upper ends of their respective ranges, while M-3 grew at a rate near the upper end of its range.

Expansion in total credit outstanding at U.S. commercial banks was relatively rapid in October, although somewhat below the pace in August and September. Bank holdings of securities grew at about the same pace in October as in the previous month, while growth in total loans moderated somewhat despite continuing strength in business loans. Outstanding commercial paper of nonfinancial corporations fell by a record amount in October, extending the decline that began in August.

Short-term market interest rates rose 1-3/4 to 3 percentage points further over the intermeeting period, while long-term rates increased about 3/4 percentage point. Over the interval, the prime rate charged by commercial banks on short-term business loans was raised from 14 to 16-1/4 percent. In home mortgage markets, average rates on new commitments rose about 40 basis points further over the intermeeting period, and available information suggested a slowing in new commitment activity at nonbank thrift institutions most recently.

The staff projections presented at this meeting suggested that growth in real GNP would be a little greater in the fourth quarter as a whole than in the third. However, the recovery in activity appeared to be in the process of weakening, and the projections suggested little growth in real GNP and some increase in the unemployment rate over the next few quarters. The rise in the fixed-weight price index for gross domestic business product was projected to be only a little less rapid over the year ahead than during the past year.

In the Committee discussion of the economic situation and its implications for policy, the members considered the possibility that the greater-than-anticipated strength of the recovery in recent months would be followed in early 1981 by a decline in real GNP. It was recognized that in the near term the recent rise in interest rates would be an important force restraining activity in some sectors. At the same time, the higher interest rates resulted in part from the continuing rapid pace of inflation, which remained a major source of concern and of current and prospective instability. The observation was made that, assuming monetary expansion in line with the Committee's longer-run objectives, the progress of recovery in the months ahead was likely to be limited unless inflation abated. It was also noted, however, that the rise in prices had not slowed and that once again the economy might be subjected to shocks from substantial increases in prices of both energy and foods, and perhaps from a reduction in supplies of energy as well. The outlook was clouded, moreover, by unusual uncertainty regarding prospective federal outlays, especially for national defense, by the increases in federal taxes effective at the beginning of the new year, and by the prospects for legislation next year to reduce federal taxes.

At its meeting in July, the Committee had reaffirmed the ranges for monetary growth in 1980 that it had established in February. Thus, the Committee had agreed that from the fourth quarter of 1979 to the fourth quarter of 1980, average rates of growth in the monetary aggregates within the following ranges appeared to be consistent with broad economic aims: M-1A, 3-1/2 to 6 percent; M-1B, 4 to 6-1/2 percent; M-2, 6 to 9 percent; and M-3, 6-1/2 to 9-1/2 percent. The associated range for the rate of growth in commercial bank credit was 6 to 9 percent. For the period from the fourth quarter of 1980 to the fourth quarter of 1981, the Committee looked toward a reduction in the ranges for growth of M-1A, M-1B, and M-2 on the order of 1/2 percentage point from the ranges adopted for 1980, abstracting from institutional influences affecting the behavior of the aggregates. It was understood that the longer-run ranges would be reconsidered as conditions warranted.

In contemplating policy for the period immediately ahead, the Committee noted that growth of the narrower monetary aggregates in October had substantially exceeded the rates consistent with the objectives for growth over the period from September to December adopted at the meeting on October 21. If those objectives were to be realized, M-1A would have to decline slightly over the final two months of the year and growth of M-1B would have to be very slow.

According to a staff analysis, the demand for money had been quite strong in recent months because recovery in economic activity and in nominal GNP had been much larger than anticipated. Growth of transaction balances was projected to slow significantly over the remainder of the year, in part because of the lagged effect on the demand for money of the sharp rise in interest rates over recent months and in part because of the apparent weakening of the recovery in activity.

In the Committee's discussion of policy for the period immediately ahead, the members generally favored pursuit of a sharp reduction in monetary expansion from the rapid pace of recent months. Such a slowing might already be developing for the reasons given in the staff analysis, but it was emphasized that uncertainties were great concerning the projection of a weakening in the pace of the business recovery and also about the impact of nominal GNP and current levels of interest rates on monetary growth.

In the circumstances, most members favored reaffirming essentially the objectives for monetary growth over the period from September to December that had been adopted at the meeting in mid-October, with the same proviso that somewhat less growth would be acceptable if it emerged. A number of members preferred adoption of somewhat higher growth rates over the near term, with a view to scaling down monetary growth over a slightly longer period than the six weeks remaining before the end of the year, but they also were willing to accept slower growth if it emerged. In addition, some sentiment was expressed for specification of somewhat lower rates of monetary growth.

While favoring sharply reduced growth of the monetary aggregates in the period immediately ahead, a number of members expressed concern about inadvertently contributing to the volatility of interest rates, because of the implications of such volatility for economic activity, for inflationary psychology, and for the functioning of financial markets. Specifically, a substantial reduction in the provision of nonborrowed reserves or other measures in a highly aggressive pursuit of the short-run monetary growth rates being contemplated might lead promptly to further increases in interest rates, which were probably already constraining the business recovery and slowing monetary growth. Subsequent declines in rates might be unduly large, and if monetary growth accelerated again in lagged response, inflationary expectations could well be heightened. At the same time, an aggressive response to any temporary slackening in the demand for money that developed in the period just ahead appeared inappropriate, particularly in the light of the excessive monetary growth of recent months. In either case, the result might be undesirable instability in both interest rates and monetary growth over time, which could generate uncertainty about the basic thrust of Federal Reserve policy. Reflecting these concerns, some members suggested setting the upper limit of the intermeeting range for the federal funds rate relatively close to the average rate in the latest statement week, while others suggested setting a lower limit not much below the latest week's average.

At the conclusion of the discussion, the Committee decided to specify essentially the same monetary growth rates for the period from September to December that had been adopted at the meeting in October, with a range for the federal funds rate that was somewhat narrower and was centered on about the average rate in the most recent statement week. Thus, the Committee agreed that open market operations in the period until the next meeting should be directed toward expansion of reserve aggregates consistent with growth of M-1A, M-1B, and M-2 over the September-to-December period at annual rates of about 2-1/2 percent, 5 percent, and 7-3/4 percent respectively, or somewhat less, provided that in the period before the next regular meeting the weekly average federal funds rate remained within a range of 13 to 17 percent. While some shortfall from the specified rates of monetary growth would be accepted, it was also understood that operations would not be directed toward placing substantial additional pressures on bank reserve positions unless growth of the monetary aggregates and the associated demands for reserves proved to be significantly greater than anticipated. If it appeared during the period before the next regular meeting that the constraint on the federal funds rate was inconsistent with the objective for the expansion of reserves, the Manager for Domestic Operations was promptly to notify the Chairman, who would then decide whether the situation called for supplementary instructions from 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 real GNP is recovering further in the fourth quarter from the sharp contraction in the second quarter, while prices on the average continue to rise rapidly. In October industrial production and nonfarm payroll employment expanded substantially for the third consecutive month, and the unemployment rate remained around 7½ percent. The value of retail sales changed little, following four months of recovery. The rise in the index of average hourly earnings over the first ten months of 1980 was somewhat more rapid than in 1979.
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> The weighted average value of the dollar in exchange markets on balance has risen further over the past month. The U.S. trade deficit was essentially unchanged in September, and the rate in the third quarter was sharply lower than that in the first half.
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> Growth in M-1A and M-1B moderated further in October but was still relatively rapid; growth in M-2 accelerated slightly, reflecting a pickup in expansion of its nontransactions component. From the fourth quarter of 1979 to October, growth of M-1A was in the upper part of the range set by the Committee for growth over the year ending in the fourth quarter of 1980, while growth of M-1B and M-2 was somewhat above the upper limits of their ranges. Expansion in commercial bank credit was rapid in October, although not so rapid as in August and September. Market interest rates have risen sharply in recent weeks; average rates on new home mortgage commitments have continued upward. On November 14 the Board of Governors announced an increase in Federal Reserve discount rates from 11 to 12 percent and a surcharge of 2 percentage points on frequent borrowing of large member banks from Federal Reserve banks.

The Federal Open Market Committee seeks to foster monetary and financial conditions that will help to reduce inflation, encourage economic recovery, and contribute to a sustainable pattern of international transactions. At its meeting in July, the Committee agreed that these objectives would be furthered by growth of M-1A, M-1B, M-2, and M-3 from the fourth quarter of 1979 to the fourth quarter of 1980 within ranges of 3½ to 6 percent, 4 to 6½ percent, 6 to 9 percent, and 6½ to 9½ percent respectively. The associated range for bank credit was 6 to 9 percent. For the period from the fourth quarter of 1980 to the fourth quarter of 1981, the Committee looked toward a reduction in the ranges for growth of M-1A, M-1B, and M-2 on the order of ½ percentage point from the ranges adopted for 1980, abstracting from institutional influences affecting the behavior of the aggregates. These ranges will be reconsidered as conditions warrant.

In the short run, the Committee seeks behavior of reserve aggregates consistent with growth of M-1A, M-1B, and M-2 over the period from September to December at annual rates of about 2½ percent, 5 percent, and 7-3/4 percent respectively, or somewhat less, provided that in the period before the next regular meeting the weekly average federal funds rate remains within a range of 13 to 17 percent.

If it appears during the period before the next meeting that the constraint on the federal funds rate is inconsistent with the objective for the expansion of reserves, the Manager for Domestic Operations is promptly to notify the Chairman, who will then decide whether the situation calls for supplementary instructions from the Committee.

Votes for this action: Messrs. Volcker, Gramley, Guffey, Morris, Partee, Rice, Roos, Schultz, Solomon, and Wallich. Votes against this action: Mrs. Teeters and Mr. Winn.

Mrs. Teeters dissented from this action because she believed that it would result in additional increases in interest rates, which would intensify downward pressures on demands for housing, automobiles, and business fixed capital and thus risk a major contraction in economic activity with a substantial rise in unemployment. In her view, open market operations over the weeks immediately ahead should be directed toward maintaining the federal funds rate within a range of 11 to 15 percent.

Mr. Winn dissented from this action because he favored specification of lower rates of expansion in the monetary aggregates for the period from September to December than those adopted at this meeting. In his view, more vigorous action was appropriate in order to enhance the prospects for restraining the expansion of the monetary aggregates and establishing growth paths consistent with the monetary growth objectives for 1981 contemplated by the Committee in July 1980.

Shortly after the meeting, incoming data indicated that M-1A and M-1B were growing much faster than the rates consistent with the Committee's objectives for the period from September to December. Required reserves and member bank demands for reserves had expanded substantially in relation to the supply of reserves being made available through open market operations, and member bank borrowings had increased further. These developments were associated with additional upward pressure on the federal funds rate, which in the first statement week after the meeting had been at about or somewhat above the upper limit of the range of 13 to 17 percent specified by the Committee. In a telephone conference on November 26, the Committee raised the upper limit of the intermeeting range for the funds rate to 18 percent.

> On November 26, the Committee modified the domestic policy directive adopted at its meeting on November 18, 1980, to raise the upper limit of the range for the federal funds rate to 18 percent.
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> > Votes for this action: Messrs. Volcker, Gramley, Guffey, Morris, Partee, Rice, Schultz, Solomon, Wallich, and Baughman. Vote against this action: Mrs. Teeters. Absent: Messrs. Roos and Winn. (Mr. Baughman voted as alternate for Mr. Roos.)

Mrs. Teeters dissented from this action for essentially the same reasons that she dissented from the action to adopt the domestic policy directive at the Committee's meeting on November 18, 1980.

On December 4, after closing of the markets, the Board of Governors announced an increase in Federal Reserve discount rates. In light of the current level of market interest rates and consistent with existing policy to restrain excessive growth in money and credit, the Board approved an increase from 12 to 13 percent in the basic rate and an increase from 2 to 3 percentage points in the surcharge on frequent borrowings of large institutions, effective December 5.

The increase in discount rates exerted additional upward pressure on the federal funds rate. In trading during the morning of December 5, the rate generally was well above 18 percent, the level to which the upper limit of the intermeeting range for the weekly average funds rate had been raised about a week earlier, and other short-term interest rates rose substantially as well. At the same time, incoming data suggested that M-1A and M-1B currently might be growing a little less rapidly than projected a week earlier, which would imply a somewhat lower level of required reserves and also some reduction in member bank demands for reserves in relation to the supply being made available through open market operations.

Thus, it was possible that the additional upward pressure on the federal funds rate would prove to be transitory. Alternatively, pursuit of the Committee's short-run objective for the growth of reserve might be associated with a federal funds rate above the upper limit of the existing range, even if some weakness in demands for reserves developed, but the extent of any upward pressure on the rate was difficult to gauge while markets were in the process of adjusting to the discount rate action. In light of these uncertainties, the Committee decided in a telephone conference in the afternoon of December 5 to take account of the repercussions of the increases in discount rates by providing the Manager for Domestic Operations with leeway to pursue the Committee's short-run objectives for the behavior of reserve aggregates without operations being precisely constrained in the current statement week by the 18 percent upper limit of the intermeeting range for the federal funds rate, pending another consultation in about a week if one appeared to be desirable.

> On December 5, the Committee modified the domestic policy directive adopted at its meeting on November 18, 1980, and subsequently modified on November 26, to take account of the action of the Board of Governors on December 4 to raise discount rates by providing leeway for pursuit of the Committee's short-run objectives for the behavior of reserve aggregates without operations being precisely constrained in the current statement week by the 18 percent upper limit of the intermeeting range for the federal funds rate.

Votes for this action: Messrs. Volcker, Gramley, Guffey, Morris, Partee, Rice, Roos, Solomon, and Winn. Votes against this action: Mrs. Teeters and Mr. Wallich. Absent: Mr. Schultz.

Mrs. Teeters dissented from this action for essentially the same reasons that she dissented from the action to adopt the domestic policy directive at the Committee's meeting on November 18, 1980.

Mr. Wallich dissented from this action because he preferred to raise the upper limit of the federal funds rate range for the remainder of the intermeeting period, which in his view would be consistent with the action on the preceding day to raise Federal Reserve discount rates.

The Committee held another telephone conference in the afternoon of Friday, December 12. In the statement week ending December 10, the federal funds rate had averaged about 18-3/4 percent, and since then the rate had been in a range of 19 to 20 percent. At the same time, the most recent data tended to support the indications of the week before that M-1A and M-1B currently might be growing a little less rapidly than projected earlier and that the demand for reserves could be easing. Market conditions were unsettled, however, and there was considerable uncertainty about the relationship between money market conditions and objectives for the behavior of reserves. In these circumstances, the Committee decided to extend through the period before the next regular meeting, scheduled for December 19, the leeway for open market operations that it had voted to approve on December 5.

On December 12, the Committee modified the domestic policy directive issued on November 18, 1980, and subsequently modified on November 26 and December 5, to extend through the period before the next regular meeting leeway for pursuit of the Committee's short-run objectives for the behavior of reserve aggregates without operations being precisely constrained by the 18 percent upper limit of the intermeeting range for the federal funds rate.

Votes for this action: Messrs. Volcker, Gramley, Guffey, Morris, Partee, Rice, Roos, Schultz, Solomon, and Winn. Vote against this action: Mrs. Teeters. Absent: Mr. Wallich.

Mrs. Teeters dissented from this action for essentially the same reasons that she dissented from the action to adopt the domestic policy directive at the Committee's meeting on November 18, 1980.