FEDERAL RESERVE

press release

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June 29, 1967.

The Board of Governors of the Federal Reserve System and the Federal Open Market Committee have adopted revisions of their respective Rules relating to the availability of information to the public. The revised Rules have been transmitted for publication in the Federal Register, to become effective July 4, 1967. They are designed to carry out the purposes of the Public Information section of the former Administrative Procedure Act, as revised last year and now codified in section 552 of Title 5 of the United States Code, which will become effective as of that date.

Under the new Rules, unpublished records of the Board and the Committee will be made available upon request unless the particular records fall within stated exemptions contained in the new law, whereas under the former Rules unpublished records generally were not made available for public inspection except with the express approval of the Board and the Committee. After July 4, records will be made available unless they are of the type that cannot properly be disclosed and fall within one of the following exemptions of the new law because they are

(1) exempted from disclosure by statute or executive order;

(2) contained in or related to examination, operating, or condition reports;

(3) privileged or related to the business, personal, or financial affairs of any person and furnished in confidence;

(4) contained in investigatory files compiled for law enforcement purposes (except to the extent available by law to a private party);

(5) related solely to internal personnel rules and practices or other internal practices of the Board, or are contained in personnel, medical, and similar files; or

(6) contained in inter-agency or intra-agency memoranda or letters that would not be routinely available by law to a private party in litigation with the Board.

In accordance with the revised Rules of the Federal Open Market Committee, the current economic policy directive relating to domestic open market operations, in the form adopted at each meeting of the Committee, will be published in the Federal Register approximately 90 days after its adoption. Committee meetings are usually held at three or four week intervals. A statement summarizing the reasons underlying the Committee's policy decisions, along with the votes of the members, will be made available to the public at the same time. Such statements, consisting of entries for the record of policy actions of the Committee, have been included in prior years as part of the Board's

Annual Report to Congress pursuant to the requirements of section 10 of the Federal Reserve Act, and they will continue to be carried in that Report.

The current economic policy directive adopted by the Federal Open Market Committee at its meeting on April 4, 1967, together with the Committee's continuing authority directive for domestic open market operations, its authorization for System foreign currency operations, and its foreign currency directive, as the latter documents are now in effect, have been submitted for publication in the Federal Register. The Board and the Committee are also making available at this time entries with respect to policy actions taken at the four meetings of the Committee held this year through April 4.

The Board and the Federal Open Market Committee are taking this occasion to transmit to the National Archives detailed records of discussions and actions at the Committee's meetings during the calendar year 1961, although the new law does not require public disclosure of records of deliberations of any Federal agency. Similar records of such meetings for the years prior to 1961 were made public in the same manner in 1964, as announced in the Federal Reserve Bulletin for August 1964. Copies of the 1961 records will be made available, within the next few weeks, at each Federal Reserve Bank and Branch for the convenient reference of interested parties. The same procedure was followed with respect to earlier records.

There are attached copies of the Rules regarding availability of information of the Board of Governors of the Federal Reserve System and the Federal Open Market Committee and copies of the Committee's directives and authorization as sent to the Federal Register. There are also attached copies of the policy record entries of the Federal Open Market Committee for its meetings held this year through April 4.

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RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Section 10 of the Federal Reserve Act provides that the Board of Governors shall keep a complete record of the actions taken by the Board and by the Federal Open Market Committee on all questions of policy relating to open market operations, that it shall record therein the votes taken in connection with the determination of open market policies and the reasons underlying each such action, and that it shall include in its Annual Report to the Congress a full account of such actions.

The Board and the Committee have decided to make available at this time the entries with respect to the policy actions taken at the 4 meetings of the Federal Open Market Committee held from the beginning of the calendar year 1967 through April 4, 1967, in the form in which they will appear in the Board's 54th Annual Report. It is planned to publish entries for policy actions taken subsequent to April 4, 1967, on a regular basis, with each entry to be published approximately 90 days following the date of the meeting at which the corresponding policy action or actions were taken.

The entries include the votes on the policy decisions made at the meetings as well as a resume of the basis for the decisions. The summary descriptions of economic and financial conditions included in the entries are based on the information that was available to the Committee at the time of the meetings, rather than on data for the periods in question as they may have been subsequently revised.

It will be noted from the record of policy actions that in some cases the decisions were by unanimous vote and that in other cases dissents were recorded. The fact that a decision in favor of a general policy was by a large majority, or even that it was by unanimous vote, does not necessarily mean that all members of the Committee were equally agreed as to the reasons for the particular decision or as to the precise operations in the open market that were called for to implement the general policy.

The policy directives of the Federal Open Market Committee are issued to the Federal Reserve Bank of New York as the Bank selected by the Committee to execute transactions for the System Open Market Account. Both the Manager of the System Open Market Account and the Special Manager of the Account for foreign currency operations attend the meetings of the Committee. In the area of domestic open market activities the Bank operates under 2 separate directives from the Open Market Committee--a continuing authority directive and a current economic policy directive. At the beginning of the calendar year the continuing authority directive in effect was as follows:

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, to the extent necessary to carry out the most recent current economic policy directive adopted at a meeting of the Committee:

(a) To buy or sell U.S. Government securities in the open market, from or to Government securities dealers and foreign and international accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the System Open Market Account at market prices and, for such Account, to exchange maturing U.S. Government securities with the Treasury or allow them to mature without replacement; provided that the aggregate amount of such securities held in such Account at the close of business on the day of a meeting of the Committee at which action is taken with respect to a current economic policy directive shall not be increased or decreased by more than $2.0 billion during the period commencing with the opening of business on the day following such meeting and ending with the close of business on the day of the next such meeting;

(b) To buy or sell prime bankers' acceptances of the kinds designated in the Regulation of the Federal Open Market Committee in the open market, from or to acceptance dealers and foreign accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the account of the Federal Reserve Bank of New York at market discount rates; provided that the aggregate amount of bankers' acceptances held at any one time shall not exceed $125 million or 10 per cent of the total of bankers' acceptances outstanding as shown in the most recent acceptance survey conducted by the Federal Reserve Bank of New York;

(c) To buy U.S. Government securities, obligations that are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States, and prime bankers' acceptances with maturities of 6 months or less at the time of purchase, from nonbank dealers for the account of the Federal Reserve Bank of New York under agreements for repurchase of such securities, obligations, or acceptances in 15 calendar days or less, at rates not less than (1) the discount rate of the Federal Reserve Bank of New York at the time such agreement is entered into, or (2) the average issuing rate on the most recent issue of 3-month Treasury bills, whichever is the lower; provided that in the event Government securities or agency issues covered by any such agreement are not repurchased by the dealer pursuant to the agreement or a renewal thereof, they shall be sold in the market or transferred to the System Open Market Account; and provided further that in the event bankers' acceptances covered by any such agreement are not repurchased by the seller, they shall continue to be held by the Federal Reserve Bank or shall be sold in the open market.

2. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York to purchase directly from the Treasury for the account of the Federal Reserve Bank of New York (with discretion, in cases where it seems desirable, to issue participations to one or more Federal Reserve Banks) such amounts of special short-term certificates of indebtedness as may be necessary from time to time for the temporary accommodation of the Treasury; provided that the rate charged on such certificates shall be a rate 1/4 of 1 per cent below the discount rate of the Federal Reserve Bank of New York at the time of such purchases, and provided further than the total amount of such certificates held at any one time by the Federal Reserve Banks shall not exceed $1 billion.

The current economic policy directive in effect at the beginning of 1967 was that issued at the meeting held on December 13, 1966. It read as follows:

The economic and financial developments reviewed at this meeting indicate that over-all domestic economic activity is continuing to expand, with rising defense expenditures but with additional evidences of moderating tendencies in the private economy. While there has been some slowing in the pace of advance of most broad price measures, upward price pressures persist for many finished goods and services. Bank credit and money have shown no net expansion in recent months. Although demands on bond markets have increased, upward pressures on long-term interest rates have moderated. The balance of payments remains a serious problem. In this situation, it is the Federal Open Market Committee's policy to foster money and credit conditions conducive to noninflationary economic expansion and progress toward reasonable equilibrium in the country's balance of payments.

To implement this policy, System open market operations until the next meeting of the Committee shall be conducted with a view to attaining somewhat easier conditions in the money market, unless bank credit appears to be resuming a rapid rate of expansion.

In the foreign currency area, the Federal Reserve Bank of New York operates under an authorization for System foreign currency operations and a foreign currency directive. The authorization in effect at the beginning of the year read as follows:

AUTHORIZATION FOR SYSTEM FOREIGN CURRENCY OPERATIONS

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, for System Open Market Account, to the extent necessary to carry out the Committee's foreign currency directive:

A. To purchase and sell the following foreign currencies in the form of cable transfers through spot or forward transactions on the open market at home and abroad, including transactions with the U.S. Stabilization Fund established by Section 10 of the Gold Reserve Act of 1934, with foreign monetary authorities, and with the Bank for International Settlements:

Austrian schillings
Belgian francs
Canadian dollars
Pounds sterling
French francs
German marks
Italian lire
Japanese yen
Netherlands guilders
Swedish kronor
Swiss francs

B. To hold foreign currencies listed in paragraph A above, up to the following limits:

(1) Currencies held spot or purchased forward, up to the amounts necessary to fulfill outstanding forward commitments;
(2) Additional currencies held spot or purchased forward, up to the amount necessary for System operations to exert a market influence but not exceeding $150 million equivalent; and
(3) Sterling purchased on a covered or guaranteed basis in terms of the dollar, under agreement with the Bank of England, up to $200 million equivalent.

C. To have outstanding forward commitments undertaken under paragraph A above to deliver foreign currencies, up to the following limits:

(1) Commitments to deliver to the Stabilization Fund foreign currencies in which the United States Treasury has outstanding indebtedness, up to $200 million equivalent;
(2) Commitments to deliver Italian lire, under special arrangements with the Bank of Italy, up to $500 million equivalent; and

(3) Other forward commitments to deliver foreign currencies, up to $275 million equivalent.

D. To draw foreign currencies and to permit foreign banks to draw dollars under the reciprocal currency arrangements listed in paragraph 2 below, provided that drawings by either party to any such arrangement shall be fully liquidated within 12 months after any amount outstanding at that time was first drawn, unless the Committee, because of exceptional circumstances, specifically authorizes a delay.

2. The Federal Open Market Committee directs the Federal Reserve Bank of New York to maintain reciprocal currency arrangements ("swap" arrangements) for System Open Market Account with the following foreign banks, which are among those designated by the Board of Governors of the Federal Reserve System under Section 214.5 of Regulation N, Relations with Foreign Banks and Bankers, and with the approval of the Committee to renew such arrangements on maturity:

Foreign bank	Amount of arrangement (millions of dollars equivalent)	Maximum period of arrangement (months)
Austrian National Bank	100	12
National Bank of Belgium	150	12
Bank of Canada	500	12
Bank of England	1,350	12
Bank of France	100	3
German Federal Bank	400	6
Bank of Italy	600	12
Bank of Japan	450	12
Netherland Bank	150	3
Bank of Sweden	100	12
Swiss National Bank	200	6
Bank for International Settlements		
System drawings in Swiss francs	200	6
System drawings in authorized European currencies other than Swiss francs	200	6

3. All transactions in foreign currencies undertaken under paragraph 1(A) above shall be at prevailing market rates and no attempt shall be made to establish rates that appear to be out of line with underlying market forces. Insofar as is practicable, foreign currencies shall be purchased through spot transactions when rates for those currencies are at or below par and sold through spot transactions when such rates are at or above par, except when transactions at other rates (i) are specifically authorized by the

Committee, (ii) are necessary to acquire currencies to meet System commitments, or (iii) are necessary to acquire currencies for the Stabilization Fund, provided that these currencies are resold forward to the Stabilization Fund at the same rate.

4. It shall be the practice to arrange with foreign central banks for the coordination of foreign currency transactions. In making operating arrangements with foreign central banks on System holdings of foreign currencies, the Federal Reserve Bank of New York shall not commit itself to maintain any specific balance, unless authorized by the Federal Open Market Committee. Any agreements or understandings concerning the administration of the accounts maintained by the Federal Reserve Bank of New York with the foreign banks designated by the Board of Governors under Section 214.5 of Regulation N shall be referred for review and approval to the Committee.

5. Foreign currency holdings shall be invested insofar as practicable, considering needs for minimum working balances. Such investments shall be in accordance with Section 14(e) of the Federal Reserve Act.

6. A Subcommittee consisting of the Chairman and the Vice Chairman of the Committee and the Vice Chairman of the Board of Governors (or in the absence of the Chairman or of the Vice Chairman of the Board of Governors the members of the Board designated by the Chairman as alternates, and in the absence of the Vice Chairman of the Committee his alternate) is authorized to act on behalf of the Committee when it is necessary to enable the Federal Reserve Bank of New York to engage in foreign currency operations before the Committee can be consulted. All actions taken by the Subcommittee under this paragraph shall be reported promptly to the Committee.

7. The Chairman (and in his absence the Vice Chairman of the Committee, and in the absence of both, the Vice Chairman of the Board of Governors) is authorized:

A. With the approval of the Committee, to enter into any needed agreement or understanding with the Secretary of the Treasury about the division of responsibility for foreign currency operations between the System and the Secretary;

B. To keep the Secretary of the Treasury fully advised concerning System foreign currency operations, and to consult with the Secretary on such policy matters as may relate to the Secretary's responsibilities; and

C. From time to time, to transmit appropriate reports and information to the National Advisory Council on International Monetary and Financial Policies.

8. Staff officers of the Committee are authorized to transmit pertinent information on System foreign currency operations to appropriate officials of the Treasury Department.

9. All Federal Reserve Banks shall participate in the foreign currency operations for System Account in accordance with paragraph 3 G (1) of the Board of Governors' Statement of Procedure with Respect to Foreign Relationships of Federal Reserve Banks dated January 1, 1944.

10. The Special Manager of the System Open Market Account for foreign currency operations shall keep the Committee informed on conditions in foreign exchange markets and on transactions he has made and shall render such reports as the Committee may specify.

The foreign currency directive in effect at the beginning of the year read as follows:

FOREIGN CURRENCY DIRECTIVE

1. The basic purposes of System operations in foreign currencies are:

A. To help safeguard the value of the dollar in international exchange markets;

B. To aid in making the system of international payments more efficient;

C. To further monetary cooperation with central banks of other countries having convertible currencies, with the International Monetary Fund, and with other international payments institutions;

D. To help insure that market movements in exchange rates, within the limits stated in the International Monetary Fund Agreement or established by central bank practices, reflect the interaction of underlying economic forces and thus serve as efficient guides to current financial decisions, private and public; and

E. To facilitate growth in international liquidity in accordance with the needs of an expanding world economy.

2. Unless otherwise expressly authorized by the Federal Open Market Committee, System operations in foreign currencies shall be undertaken only when necessary:

A. To cushion or moderate fluctuations in the flows of international payments, if such fluctuations (1) are deemed to reflect transitional market unsettlement or other temporary forces and therefore are expected to be reversed in the foreseeable future; and (2) are deemed to be disequilibrating or otherwise to have potentially destabilizing effects on U.S. or foreign official reserves or on exchange markets, for example, by occasioning market anxieties, undesirable speculative activity, or excessive leads and lags in international payments;

B. To temper and smooth out abrupt changes in spot exchange rates, and to moderate forward premiums and discounts judged to be disequilibrating. Whenever supply or demand persists in influencing exchange rates in one direction, System transactions should be modified or curtailed unless upon review and reassessment of the situation the Committee directs othewise;

C. To aid in avoiding disorderly conditions in exchange markets. Special factors that might make for exchange market instabilities include (1) responses to short-run increases in international political tension, (2) differences in phasing of international economic activity that give rise to unusually large interest rate differentials between major markets, and (3) market rumors of a character likely to stimulate speculative transactions. Whenever exchange market instability threatens to produce disorderly conditions, System transactions may be undertaken if the Special Manager reaches a judgment that they may help to reestablish supply and demand balance at a level more consistent with the prevailing flow of underlying payments. In such cases, the Special Manager shall consult as soon as practicable with the Committee or, in an emergency, with the members of the Subcommittee designated for that purpose in paragraph 6 of the Authorization for System foreign currency operations; and

D. To adjust System balances within the limits established in the Authorization for System foreign currency operations in light of probable future needs for currencies.

3. System drawings under the swap arrangements are appropriate when necessary to obtain foreign currencies for the purposes stated in paragraph 2 above.

4. Unless otherwise expressly authorized by the Committee, transactions in forward exchange, either outright or in conjunction

with spot transactions, may be undertaken only (i) to prevent forward premiums or discounts from giving rise to disequilibrating movements of short-term funds; (ii) to minimize speculative disturbances; (iii) to supplement existing market supplies of forward cover, directly or indirectly, as a means of encouraging the retention or accumulation of dollar holdings by private foreign holders; (iv) to allow greater flexibility in covering System or Treasury commitments, including commitments under swap arrangements; (v) to facilitate the use of one currency for the settlement of System or Treasury commitments denominated in other currencies; and (vi) to provide cover for System holdings of foreign currencies.

January 10, 1967

Authority to effect transactions in System Account.

Expansionary forces in the economy were moderating as 1966 ended, and business inventory/sales ratios had risen substantially. With inventory accumulation expected to slow, a reduced rate of over-all economic growth appeared likely in the first quarter of the new year.

Gross national product was estimated to have increased substantially in the fourth quarter of 1966, but much of the advance appeared to reflect the sharp rise in inventory accumulation. Growth slackened in consumer spending for goods, in business capital outlays, and, apparently, in Federal defense expenditures. The downtrend in residential construction activity that had begun in the spring of 1966 continued in the fourth quarter, although in November housing starts recovered most of their sharp October decline. Industrial production was little changed during the quarter at about the level reached in August, as output curtailments in such industries as steel, construction materials, automobiles, and some household appliances offset continued gains in certain other industries. There had been some rise recently in claims for unemployment compensation, but labor market conditions generally remained strong in the closing months of 1966.

With respect to the outlook for the first quarter of 1967, prospective business efforts to hold down the pace of inventory accumulation appeared likely to lead to a marked slowing of the growth rate in GNP, to some decline in industrial production, and to a moderate increase in the unemployment rate from the level of around 3.8 per cent that had prevailed recently. Defense outlays were expected to remain an expansive influence, although the evidence available at the time of this meeting suggested some further slackening in the growth of such spending as well as in business capital outlays. On the other hand, the extended decline in residential construction was expected to level out in the first quarter as a result of improvement in mortgage markets. Yields on home mortgages touched a record high in November, the latest month for which data were available, but net inflows of funds to savings and loan associations and other major mortgage lenders had recovered recently, and there were indications of some actual or prospective easing in the supply of mortgage funds.

The pace of advance of broad price measures had slowed recently; indeed, the wholesale price index declined in November for the second successive month, to a level 2.3 per cent above a year earlier, as a further reduction in prices of foodstuffs more than offset a small increase in prices of industrial commodities. The earlier succession of substantial increases in consumer prices was broken in November, when retail food prices declined somewhat and the total index rose by only one-tenth of 1 per cent. However, unit labor costs in manufacturing had risen further in recent months, as a result both of more rapid increases in average hourly earnings and of smaller gains in productivity.

Tentative estimates indicated some deterioration in the U.S. balance of payments in the fourth quarter of 1966, as an apparent improvement in the merchandise trade surplus was more than offset by an indicated worsening on capital account. While full information was not yet available on fourth-quarter developments, it appeared that the deficit on the "liquidity" basis of calculation had increased despite substantial special receipts from Germany at the year-end, and that the balance on the "official reserve transactions" basis had reverted to deficit even though there had been large net inflows of liquid funds through foreign branches of U.S. banks during the quarter.[1/] Abroad, the German Federal Bank announced a reduction in its discount rate, from 5 per cent to 4-1/2 per cent, effective January 6, 1967.

1/ The balance on the "liquidity" basis is measured by changes in U.S. reserves and in liquid U.S. liabilities to all foreigners. The balance on the "official reserve transactions" basis is measured by changes in U.S. reserves and in liquid and certain nonliquid liabilities to foreign official agencies, mainly monetary authorities. The latter balance differs from the former by (1) treating changes in liquid U.S. liabilities to foreigners other than official agencies as ordinary capital flows, and (2) treating changes in certain nonliquid liabilities to foreign monetary authorities as financing items rather than as ordinary capital flows.

System open market operations since the preceding meeting had been directed at achieving somewhat easier conditions in the money market against a background of year-end seasonal churning. Net borrowed reserves of member banks fluctuated widely over the four statement weeks ending January 4, but on the average they were somewhat smaller than in the preceding 4 weeks--about $170 million, as compared with $215 million. The market yield on 3-month Treasury bills declined more than 20 basis points to 4.80 per cent in the third week of December and subsequently remained near that level. Other money market rates declined less, partly for seasonal reasons and partly because large financing needs of Government security dealers added to demands for short-term funds.

A buoyant atmosphere pervaded bond markets in recent weeks, as signs of moderating tendencies in the economy continued to appear and as it became increasingly evident to market participants that monetary policy had shifted toward less restraint--a view reinforced by the System's action on December 27, 1966, rescinding the letter of September 1 to member banks regarding lending to business and discount window administration.[1/] Despite large recent and prospective offerings of corporate and municipal securities and a recent public sale of $600 million of participation certificates by the

1/ For the text of the September 1 letter, see the Federal Reserve Bulletin for September 1966, pp. 1338-39; for the text of the December 27 announcement, see the Bulletin for January 1967, p. 83.

Federal National Mortgage Association, yields on Treasury, corporate, and municipal bonds all declined, with yields on long-term Treasury bonds returning to about their levels at the end of 1965, following the increase in the discount rate. Near the end of January the Treasury was expected to announce the terms on which it would refund securities maturing in mid-February, of which about $3.8 billion were held by the public.

The recent declines in security yields were accompanied by resumed expansion in commercial bank credit and private deposits. Bank credit, which had declined on balance since August, increased substantially between the last Wednesdays of November and December. The increase was attributable primarily to expansion in holdings of Government securities and in short-term loans to security dealers and brokers, as banks acted to rebuild their sharply reduced liquidity positions. Business loans did not rise, apparently because of both a continuation of restrictive lending policies and some further weakening in demands for such loans.

Time and savings deposits expanded relatively fast in December following slow growth since August, when banks began to experience sizable runoffs of negotiable certificates of deposit (CD's). Although a record volume of CD's matured in December, banks were able to increase the net volume outstanding somewhat as declines in market yields on competitive instruments, particularly Treasury bills, enhanced the relative attractiveness of CD's to investors.

Expansion in the money supply (private demand deposits plus currency outside of banks), which had resumed in mid-November after a period of irregular decline beginning in July, continued in December, reflecting in large part a reduction in Government deposits at commercial banks. In 1966 as a whole the money supply increased by a little less than 2 per cent, compared with a 4.7 per cent rise in 1965.

Staff projections at the time of the Committee's preceding meeting had suggested that there would be relatively little increase from November to December in daily-average deposits of member banks--the "bank credit proxy"[1]--if the then-existing money market conditions were maintained. But with easier conditions prevailing in the latter part of the month, these deposits increased at an annual rate of 3.4 per cent in December as a whole.

Current staff projections suggested that member bank deposit expansion would increase temporarily to an annual rate in the 7 to 9 per cent range on the average during January (largely as a result of

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1/ Since mid-1966 the Committee had been making increased use of daily-average statistics on total member bank deposits as a "bank credit proxy"--that is, as the best available measure, although indirect, of developing movements in bank credit. Because they can be compiled on a daily basis with a very short lag, the deposit figures are more nearly current than available bank loan and investment data. Moreover, average deposit figures for a calendar month are much less subject to the influence of single-date fluctuations than are the available month-end data on total bank credit, which represent estimates of loans and investments at all commercial banks on one day--the last Wednesday--of each month. For statistics on daily-average member bank deposits, see the Federal Reserve Bulletin for October 1966, p. 1478, and subsequent months. Some brief comments on the relation between the member bank deposit series and the bank credit statistics are given in the note on p. 1460 of the October 1966 Bulletin.

expansion that had occurred around the turn of the year), and to a somewhat more rapid rate in that month if there were some further easing of money market conditions. All of the projected increase in January was in time and savings deposits and Government deposits; private demand deposits were expected to decline somewhat, resulting in little or no growth in the money supply.

In the Committee's discussion it was noted that appropriate monetary policy over coming months would depend importantly on the nature of Federal fiscal policies. For the immediate future, however, in light of the continued slackening of various expansionary forces in the economy and the prospect for slower over-all growth in early 1967, the Committee decided that it would be desirable to relax monetary restraint somewhat further. The members agreed that the renewed expansion in bank credit and the money supply in December was appropriate; and a majority, taking note of the staff projections for the money supply and for member bank deposits, thought that somewhat easier money market conditions should be sought unless bank credit appeared to be expanding significantly faster than expected.

The Committee agreed that the forthcoming Treasury financing should be taken into account in the conduct of open market operations, although it was expected that the financing would be a routine one and that requirements for maintaining an "even keel" in the money market would not come into play until late in the month. Some sentiment was expressed for extending System reserve-supplying security purchases in intermediate- and longer-term Treasury securities, both to stimulate flows of funds into longer-term markets, including mortgage markets, and--for balance of payments reasons--to avoid depressing short-term interest rates unduly.

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

> The economic and financial developments reviewed at this meeting indicate further moderation in various expansionary forces and sharply increased inventory accumulation. The pace of advance of broad price measures has slowed, although upward price and cost pressures persist for many finished goods and services. Partly reflecting the recent modification of monetary policy, financial market conditions have become less taut than earlier and bank credit expansion has resumed. With respect to the balance of payments, trends in international transactions indicate a continuing serious problem. In this situation, it is the Federal Open Market Committee's policy to foster money and credit conditions conducive to noninflationary economic expansion and progress toward reasonable equilibrium in the country's balance of payments.
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> To implement this policy, and taking account of forthcoming Treasury financing, System open market operations until the next meeting of the Committee shall be conducted with a view to attaining somewhat easier conditions in the money market, unless bank credit appears to be expanding significantly faster than currently anticipated.

Votes for this action: Messrs. Martin, Brimmer, Clay, Daane, Hickman, Maisel, Mitchell, Robertson, and Wayne. Votes against this action: Messrs. Irons, Shepardson, and Treiber.

The members dissenting from this action thought that it would be preferable not to relax monetary restraint further at this time. Among the considerations they advanced were the continuing balance of payments problem and the desirability of awaiting further information on prospective Federal taxes and expenditures before changing monetary policy further. Individual dissenting members also expressed the judgments that, despite present indications of slower economic growth early in 1967, the longer-run prospects for the economy were not weak; and that the rate at which member bank deposits were expected to grow in January, given no change in money market conditions, was appropriate.

February 7, 1967

Authority to effect transactions in System Account.

The pace of economic expansion continued to moderate in early 1967, according to reports at this meeting. Tentative estimates indicated that industrial production had declined somewhat in January and that, with sales of new automobiles falling further, total retail sales had failed to increase. Layoffs and short workweeks continued to be reported in the automobile industry and in some consumer appliance industries, but the labor market as a whole apparently remained strong.

Staff projections suggested that expansion in GNP would be at a sharply slower pace in the first half of 1967 than in 1966. Inventory accumulation was expected to decline markedly from its recent advanced rate, slower growth was anticipated in defense spending and business capital outlays, and only a small increase was expected in real takings of goods by consumers. On the other hand, it appeared likely that the substantial decline in residential construction would end and that State and local government outlays would continue to expand.

Projections by the Council of Economic Advisers, contained in its recent annual report, also indicated slowing of the economic advance in the first half of 1967. The Council expected expansion to accelerate in the second half of the year, when it anticipated a strong rise in residential construction, an end to the decline in the rate of inventory investment, and a rise in transfer payments (primarily as a result of a proposed increase at midyear in social security benefits). The Council foresaw a sizable stimulus from fiscal policy in the first half of the year, but the administration's budget recommendations provided for a shift in the direction of fiscal restraint at midyear in the form of a 6 per cent surcharge on income tax liabilities of individuals and corporations.

In December the wholesale price index was stable and the consumer price index again rose by only one-tenth of 1 per cent. Effective February 1, the minimum wage was increased and its coverage extended under the terms of legislation enacted in 1966. Unit labor costs in manufacturing were estimated to have been 2.7 per cent above their year-earlier level in the fourth quarter of 1966, and it appeared likely that such costs would continue to rise.

The deficit in the U.S. balance of payments on the "liquidity" basis of calculation was estimated to have been at an annual rate of about $2 billion in the fourth quarter of 1966, despite larger dollar receipts from various official transactions. For the full year the deficit on this basis was estimated at $1.4 billion. On the "official reserve transactions" basis there was a small deficit in the fourth quarter but a surplus of $175 million for the year. Partial data for January indicated a continued sizable deficit on both bases of calculation. Liabilities of U.S. banks to their foreign branches declined in late December and early January, but remained well above their level in the spring of 1966.

Abroad, interest rates had declined substantially from their recent peaks in the Euro-dollar market and in various national markets. The Bank of England reduced its discount rate from 7 to 6-1/2 per cent on January 26, and subsequently the central banks of Canada, Belgium, and Sweden reduced their discount rates by varying amounts.

Open market operations since the last meeting of the Committee had been directed at attaining somewhat easier conditions in the money market. Net borrowed reserves averaged about $60 million in January and member bank borrowings about $475 million, compared with $190 million and $530 million, respectively, in December. Rates on Federal funds moved generally lower, and they fell sharply in the last week of January when float rose temporarily in the wake of a severe snowstorm in the midwest. The yield on 3-month Treasury bills declined further, from 4.80 per cent 4 weeks earlier to less than 4.50 per cent, although by the time of this meeting it had backed up slightly. Rates on other short-term instruments also moved significantly lower. A major New York City bank reduced its prime lending rate from 6 to 5-1/2 per cent on January 26, and subsequently many other banks lowered their prime rates, but generally to 5-3/4 per cent.

Long-term security yields also had declined sharply further in recent weeks. Yields on new corporate bonds reached their lowest levels since April 1966, and those on Treasury and municipal bonds fell to levels prevailing prior to the increase in the discount rate in December 1965. Although the market atmosphere became cautious at times, mainly because of reports of a growing calendar of corporate and municipal offerings, sentiment was buoyed by various developments. These included the evidences of further easing of monetary policy; the President's statement--in his State of the Union message of January 10--that he was proposing a surcharge on income taxes and would strive to lower interest rates; and the reductions in discount rates by foreign central banks and in prime rates by domestic commercial banks. Activity in the stock market was extremely heavy, and prices of common stocks advanced virtually without interruption after the first of the year.

On January 25 the Treasury announced that it would refund securities maturing in mid-February with a cash offering of two new securities, a 15-month note and a 5-year note, both bearirg 4-3/4 per cent coupons and priced to yield 4.85 and 4.84 per cent, respectively. With market yields declining, the new issues were heavily oversubscribed. The Treasury was expected to announce in late February or early March an offering of tax-anticipation bills due in June, and a large volume of Federal agency securities and participation certificates was expected to be marketed before midyear.

Net inflows of savings funds to depositary-type institutions increased considerably in late 1966 and early 1967, and conditions in markets for home mortgages appeared to have eased further recently. The rate of new mortgage commitments still appeared to be lagging, however, as many institutions used a large part of the inflows to improve their liquidity positions. Housing starts declined less than seasonally in December, but the annual rate remained relatively low.

The rate of increase in total bank credit between late December and late January was the highest since mid-1966. Banks substantially increased their holdings of municipal and Federal agency securities and their loans to businesses and security dealers. The sharp rise in business loans, following 5 months of slow net growth, was in part a reflection of a temporary concentration of corporate needs for funds to make accelerated tax payments.

Growth in time and savings deposits, which had resumed in December, accelerated in January. The increase was centered in large-denomination negotiable CD's, which became increasingly attractive to investors as yields on competitive market instruments declined. The net increase in such CD's outstanding at weekly reporting banks was at a record high in January, and in the 6 weeks after mid-December such banks recovered more than two-thirds of the runoff they had experienced in the preceding 4 months. The average maturity of new issues of CD's was lengthened significantly in January for the first time since mid-1966, and recently many banks had reduced their offering rates on CD's.

As a result of the marked increase in time deposits--together with a substantial rise in Government deposits, which was offset in part by a decline in private demand deposits--the bank credit proxy (daily-average member bank deposits) rose more from December to

January than had been expected, even in the light of the easing of money market conditions that had occurred. New staff projections suggested that, if money market conditions remained unchanged, bank credit as measured by the proxy series would rise at an annual rate of about 9 to 11 per cent from January to February. The projections allowed for continued rapid growth in time deposits, resumed growth in private demand deposits, and some decline in Government deposits.

The Committee decided that it would be appropriate at this time to maintain the easier money market conditions achieved under the policies adopted at the three preceding meetings, unless bank credit appeared to be deviating significantly from its expected course. Various reasons were advanced by individual members against a further deliberate relaxation of monetary policy at present. These included the recent and projected growth rates of bank credit, which some members considered to be at about the upper end of a desirable range in the current circumstances; the likelihood that much of the impact on the economy of the policy actions already taken was still to come; the risk that unduly rapid easing might necessitate a sharp reversal of policy later in the year; the possibility that speculative excesses would be encouraged by continued increases in prices of fixed income securities; and concern about the implications of rising labor costs for the foreign trade balance and of declining domestic interest rates for international capital flows. The current Treasury financing also was mentioned, although "even keel" considerations were considered less important than usual in view of the market reception of the new securities.

At the same time, in light of the short-run economic outlook there was considerable sentiment for "leaning toward ease" in open market operations. In particular, the Committee agreed that efforts should be made to resist any sharp rises in interest rates but that rates should be permitted to decline if market forces worked in that direction. It was noted in this connection that the recent declines in interest rates had reflected expectational factors to an important extent, and that long-term rates were particularly vulnerable at present to a change in expectations.

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

> The economic and financial developments reviewed at this meeting indicate further moderation in various expansionary forces, with continued large inventory accumulation. The pace of advance of broad price measures has slowed, although upward price and cost pressures persist for many goods and services. Interest rates have declined markedly, financial conditions generally are considerably easier, and bank credit expansion recently has been vigorous. While interest rates abroad have also declined, trends in international transactions indicate a continuing serious balance of payments problem. In this situation, it is the Federal Open Market Committee's policy to foster money and credit conditions, including bank credit growth, conducive to noninflationary economic expansion and progress toward reasonable equilibrium in the country's balance of payments.
>
> To implement this policy, and taking account of the current Treasury financing, System open market operations until the next meeting of the Committee shall be conducted

> with a view to maintaining the prevailing conditions of ease in the money market, but operations shall be modified as necessary to moderate any apparently significant deviations of bank credit from current expectations.

> Votes for this action: Messrs. Martin, Hayes, Brimmer, Clay, Daane, Hickman, Irons, Maisel, Robertson, Shepardson, and Wayne. Vote against this action: Mr. Mitchell.

Mr. Mitchell dissented from this action because he favored moving somewhat further toward ease. He was inclined to give more credence to the present expectations for a weaker economic performance in the first half of the year than to those for a stronger performance in the second half, and he thought that the major economic risk for the immediate future was that a downturn in over-all economic activity might be precipitated by the expected inventory adjustment.

March 7, 1967

1. Authority to effect transactions in System Account.

Evidences of marked slowing in the pace of economic expansion were reported at this meeting. In February, according to tentative estimates, industrial production fell for the second consecutive month, sales of new automobiles decreased sharply further, and total retail sales declined from their reduced December-January level. Although the unemployment rate remained at 3.7 per cent in January, signs of easing demands for labor were beginning to appear in such sensitive indicators as the length of the workweek in manufacturing, claims for unemployment insurance, and indexes of "help wanted" advertisements. On the other hand, residential construction activity turned up in January, after 10 months of decline, as conditions in mortgage markets continued to ease.

Staff projections of GNP for the first half of 1967, which earlier had suggested a sharply reduced rate of growth, had been lowered somewhat further and now implied only moderate increases in dollar GNP and little rise in real output of goods and services. A large reduction in the rate of business inventory accumulation was still expected, although there was little evidence as yet to suggest that the adjustment had begun; in January, with retail sales sluggish, inventories of manufacturers rose sharply further despite cutbacks in production, and manufacturers' stock/sales ratios advanced to the highest levels since 1961. Defense spending was expected to continue increasing, although at a slower rate; and residential construction outlays were expected to be about the same in the first quarter as a whole as in the fourth quarter of 1966, and to rise in the second quarter. However, continuing lack of strength in consumer demands for durable goods was suggested by a Census Bureau survey taken in mid-January, which found that smaller proportions of consumers were planning to buy new cars and household durable goods than was the case a year earlier. It was indicated that a Department of Commerce-Securities and Exchange Commission survey, taken in February, would show that businesses planned to make outlays on new plant and equipment in the first half of 1967 at a rate no higher than that actually recorded in the fourth quarter of 1966.

The consumer price index was unchanged in January, but average wholesale prices of both industrial commodities and foodstuffs rose. Advance estimates for February suggested that average prices of industrial commodities had remained stable in that month and that prices of foodstuffs had declined somewhat. Unit labor costs in manufacturing rose sharply further in January.

With respect to balance of payments developments, capital outflows from the United States had increased relatively little recently despite the easing of domestic monetary conditions. On the other hand, revised data indicated that the surplus on U.S.

merchandise trade had not improved in the fourth quarter of 1966, as had been reported earlier. Growth in imports, which previously appeared to have leveled off in late 1966, was now shown to have continued at a reduced rate through January 1967, and estimates of growth in exports in the fourth quarter had been revised downward. Prospects still favored improvement in the trade surplus over coming months, when slowing inventory accumulation was expected to reduce the demand for imports.

Abroad, economic activity had been slackening for several months in a number of industrial countries, including the United Kingdom and Germany, and monetary and fiscal policies were being relaxed somewhat. The German Federal Bank, which along with the Bank of England and a number of other central banks had reduced its discount rate earlier in the year, announced a further reduction, from 4-1/2 to 4 per cent, on February 17. Reserve requirements of German commercial banks were lowered effective March 1.

Conditions in domestic financial markets had passed through two distinct phases since the preceding meeting of the Committee, with a period of firmer money markets, congested bond markets, and rising long- and short-term interest rates followed by a period of easier financial conditions and declining rates. Shifts in expectations of market participants contributed importantly to these developments.

Early in the period concern developed about the viability of the levels to which interest rates had fallen, in view of a steady stream of additions to an already large calendar of corporate and municipal security issues, large inventories of securities held by underwriters, and rumors of renewed sales of FNMA participation certificates. Moreover, market participants began to reappraise the prospects for monetary policy, partly because of congressional testimony by various officials suggesting a strengthening of economic forces in the second half of the year. A belief that the trend of monetary policy toward greater ease had been halted, and perhaps reversed, was strengthened by the development of firmer conditions in the money market, as reflected by increases in rates on Treasury bills and Federal funds and advances in lending rates to Government securities dealers posted by major New York City banks. The System injected a large volume of reserves through open market operations in an effort to cope with these firming tendencies, but operations were complicated by persistent shortfalls of reserve availability from initial projections.

Subsequently, money market conditions again turned easier, earlier expectations regarding monetary policy were gradually restored, and long-term interest rates--particularly on Treasury securities--declined somewhat. These developments were initially stimulated by large-scale official purchases of Treasury securities on February 24 in conjunction with arrangements undertaken to avoid a rise in the Federal debt above the legal ceiling, and by concurrent purchases of bills for System Account to supply reserves. The view that monetary policy was still trending toward ease was reinforced on February 28 when the Board of Governors announced a reduction in member bank reserve requirements for the purpose of meeting developing credit needs throughout the country. Reserve requirements against savings deposits and the first $5 million of other time deposits at each member bank were reduced in two successive steps: from 4 to 3-1/2 per cent, and then to 3 per cent, effective with the reserve computation periods beginning March 2, 1967, and March 16, 1967, respectively.

By the day before this meeting the yield on 3-month Treasury bills had fallen to about 4.35 per cent, roughly 20 basis points below its level at the time of the preceding meeting, and other money market conditions in general were about as easy as they had been 4 weeks earlier. In February as a whole, member bank borrowings averaged about $365 million, compared with $475 million in January; and excess reserves exceeded borrowings by about $35 million, in contrast with a net borrowed reserve position of about $65 million in the preceding month.

Following congressional approval of legislation raising the temporary debt ceiling on March 1, the Treasury announced that $2.7 billion of tax-anticipation bills due in June would be auctioned on March 7, the day of this meeting. Treasury cash balances were expected to reach relatively low levels before the March 13 payment date for these bills, and it was possible that the Treasury would need to borrow directly from the Federal Reserve for short periods.

Bank credit expanded further between the last Wednesdays of January and February, although apparently at a rate below that of the two preceding months. Banks used the additions to their reserves mainly to improve their liquidity positions; acquisitions of securities continued heavy, but business loans increased relatively little and total loans declined. Time and savings deposits grew sharply further on the average from January to February, although the rate of expansion moderated considerably over the course of the latter month as large money market banks became less aggressive sellers of negotiable CD's. Private demand deposits and the total money supply rose, after declining in January, and Government deposits at commercial banks were about unchanged.

Daily-average member bank deposits--the bank credit proxy--increased at an annual rate of about 15 per cent from January to February, more than had been expected. Most of the rise occurred early in February, when time deposits were growing rapidly. New staff projections for March suggested that growth in the proxy would be at an annual rate of about 6 to 8 per cent if money market conditions were unchanged, and somewhat larger if money market conditions were eased somewhat further. It appeared unlikely that banks would resume aggressive selling of negotiable CD's in the near future, in view of their large CD sales in recent months and the uncertain outlook for loan demands following the March and April dividend and tax dates. Accordingly, time deposits were projected to expand considerably less on the average in March than in February. The projections also allowed for a substantially higher average level of private demand deposits, reflecting sharp increases late in February, and some decline in the average level of Government deposits.

The Committee agreed that somewhat easier money market conditions were desirable at present to combat the effects of weakening tendencies in the economy, and that still easier conditions should be sought if bank credit appeared to be expanding significantly less than expected. Individual members mentioned various intermediate objectives, including those of encouraging sustained growth in the money supply and further declines in long-term interest rates, of stimulating banks to relax their lending policies more rapidly than they had to date, and of confirming market interpretations that the current reduction in reserve requirements was intended to be an easing action rather than simply an alternative to open market operations as a means of meeting seasonal reserve needs. Some members stressed the desirability of avoiding sharp shifts in expectations regarding the near-term course of monetary policy, such as had occurred in February. Others, while sharing this position, placed equal weight on the need to avoid generating expectations that monetary policy was moving more rapidly toward ease than in fact was the case. In the course of the discussion several members expressed the view that a reduction in the discount rate might well be considered soon, although none indicated that he would favor such action immediately.

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

> The economic and financial developments reviewed at this meeting indicate some decline in industrial production and a marked slowing of expansion in overall economic activity. Lack of growth in retail sales may be retarding adjustment of inventory accumulation from its recent excessive rate. Average commodity prices have changed little recently, but unit labor costs in manufacturing have risen further. Bank credit expansion has been vigorous and, after a period of rising interest rates and congested bond markets, financial conditions have again turned easier. Recent data suggest little improvement in the foreign trade surplus but also little increase in the outflow of U.S. capital. In several important countries abroad, economic activity has been softening for several months and monetary and

fiscal policies have eased somewhat. In this situation, it is the Federal Open Market Committee's policy to foster money and credit conditions, including bank credit growth, conducive to combatting the effects of weakening tendencies in the economy, while recognizing the need for progress toward reasonable equilibrium in the country's balance of payments.

To implement this policy against the background of the current reductions in reserve requirements, System open market operations until the next meeting of the Committee shall be conducted with a view to attaining somewhat easier conditions in the money market, and to attaining still easier conditions if bank credit appears to be expanding significantly less than currently anticipated.

Votes for this action: Messrs. Martin, Hayes, Brimmer, Daane, Francis, Maisel, Mitchell, Robertson, Scanlon, Shepardson, Swan, and Wayne. Votes against this action: None.

2. Amendment of continuing authority directive.

On recommendation of the System Account Manager, Section 1(b) of the continuing authority directive to the Federal Reserve Bank of New York regarding domestic open market operations was amended to clarify the language describing the two limits specified on aggregate holdings of bankers' acceptances by the Federal Reserve Bank of New York, in accordance with the manner in which that language had always been interpreted. Specifically, the phrase "whichever is the lower" was added at the end of the paragraph, following the description of the two limits. With this change, Section 1(b) read as follows:

To buy or sell prime bankers' acceptances of the kinds designated in the Regulation of the Federal Open Market Committee in the open market, from or to acceptance dealers and foreign accounts maintained at the Federal

> Reserve Bank of New York, on a cash, regular or deferred delivery basis, for the account of the Federal Reserve Bank of New York at market discount rates; provided that the aggregate amount of bankers' acceptances held at any one time shall not exceed (1) $125 million or (2) 10 per cent of the total of bankers' acceptances outstanding as shown in the most recent acceptance survey conducted by the Federal Reserve Bank of New York, whichever is the lower.

After reviewing various amendments to the continuing authority directive that had been made during the past year, the Committee renewed the directive in its existing form (as set forth in the preface to this record of Federal Open Market Committee policy actions), except for the change resulting from this amendment.

> Votes for this action: Messrs. Martin, Hayes, Brimmer, Daane, Francis, Maisel, Mitchell, Robertson, Scanlon, Shepardson, Swan, and Wayne. Votes against this action: None.

3. Review of continuing authorizations.

This being the first meeting of the Federal Open Market Committee following the election of new members from the Federal Reserve Banks to serve for the year beginning March 1, 1967, and their assumption of duties, the Committee followed its customary practice of reviewing all of its continuing authorizations and directives. The action taken with respect to the continuing authority directive for domestic open market operations has been described in the preceding portion of the entry for this date.

The Committee reaffirmed its authorization for System foreign currency operations and its foreign currency directive, in the forms in which both were outstanding at the beginning of the year 1967, as set forth in the preface to this record of policy actions.

Votes for these actions: Messrs. Martin, Hayes, Brimmer, Daane, Francis, Maisel, Mitchell, Robertson, Scanlon, Shepardson, Swan, and Wayne. Votes against these actions: None.

April 4, 1967

Authority to effect transactions in System Account.

Recent information supported earlier indications of a marked slowing in the pace of economic expansion and suggested that the anticipated curtailment in the rate of business inventory accumulation was under way. The latest staff projections for the first half of 1967, like those of 4 weeks earlier, implied only moderate increases in dollar GNP and little rise in real output.

Both retail sales and industrial production declined in February, as tentative estimates had suggested. In March sales of new automobiles remained close to their reduced February level, and it appeared from weekly data for most of the month that total sales continued sluggish. The production decline in February brought the capacity utilization rate in manufacturing down to 87 per cent from the 91 per cent level that had prevailed during most of 1966, and was associated with sharp reductions at factories in employment, in length of the average workweek, and in payrolls. Total nonfarm employment continued to rise, however, and the unemployment rate remained at the January level of 3.7 per cent.

With respect to inventories, accumulation by manufacturers slowed markedly in February from its earlier rapid pace. Stocks of wholesalers and retailers had not grown in January; as a result, there was a substantial reduction in that month in the over-all rate of inventory growth.

The staff projections of GNP allowed for large reductions in the rate of inventory accumulation in both the first and second quarters of 1967. Although Federal spending for defense and non-defense purposes apparently was rising somewhat more rapidly than had been expected, near-term prospects for most other broad categories of final demand did not appear strong. Growth in incomes was expected to slow in the second quarter--implying continued weakness in consumer spending for goods. Longer-term prospects for residential construction remained favorable, but declines in building permits and housing starts in February suggested that a strong expansion in that sector was not in immediate prospect. The results of the recent Commerce-SEC survey of business plans for plant and equipment expenditures indicated a decrease in such spending (from the fourth-quarter rate) in the first half of 1967, followed by a moderate rise in the second half. For the year as a whole, if reported plans were realized, fixed capital outlays would be 3.9 per cent above those of 1966, in contrast to increases of more than 15 per cent in each of the past 3 years. While the survey was made before the President proposed legislation to restore the tax incentives for investment that had been suspended in October 1966, it appeared unlikely that enactment of such legislation would have a significant effect on outlays until after midyear.

The consumer price index rose slightly in February; since October 1966 it had advanced at an annual rate of 1 per cent, compared with a 4 per cent rate earlier in 1966. Average wholesale prices declined in February, and according to advance estimates, they were unchanged in March at a level slightly below their peak of the preceding September. Unit labor costs continued to rise in February, and for the first quarter it appeared likely that they would average more than 4 per cent above a year earlier.

Tentative estimates of the U.S. balance of payments in the first quarter suggested that, despite some improvement in the merchandise trade surplus, the deficit was larger than in the preceding quarter on both the "liquidity" and "official reserve transactions" bases of calculation. However, it appeared that all of the increase in the liquidity deficit and part of that in the official settlements deficit was accounted for by differential effects in the two quarters of various types of special transactions. Much of the rise in the official settlements deficit reflected repayments by U.S. banks during the early weeks of the year of funds borrowed abroad through their foreign branches.

The widespread slowdown in economic activity in Western Europe, which had begun around mid-1966, apparently continued in the first few months of 1967 although in the United Kingdom there were indications that the decline in activity might be leveling out. Since the beginning of the year monetary and fiscal policy actions had been taken in a number of countries to stimulate activity, including numerous reductions in central bank discount rates. On March 16 the Bank of England reduced its discount rate for the second time in 1967, from 6-1/2 to 6 per cent. Discount rate reductions also were made in March by the central banks of Sweden and the Netherlands.

System open market operations since the preceding meeting of the Committee had been directed at fostering somewhat easier conditions in the money market. Growth in total and nonborrowed reserves of member banks was rapid in March, as it had been in the first 2 months of the year. Free reserves rose to an average of $165 million from about $35 million in February, member bank borrowings declined to about $200 million from $365 million, and rates on Federal funds and on bank loans to Government securities dealers moved into lower ranges. Interest rates on short-term market securities fell considerably further as a result of System operations and of other factors, including further reports of weakness in economic indicators, reductions in foreign discount rates, and widespread expectations of an early cut in the Federal Reserve discount rate. The market yield on 3-month Treasury bills declined by about 35 basis points, to slightly less than 4 per cent. On March 22 a large New York City bank lowered its prime lending rate from 5-3/4 per cent to 5-1/2 per cent, and subsequently many other banks took similar action.

Long-term interest rates had also moved down somewhat in recent weeks, but they remained above the 1967 lows, which had been reached in late January and early February. The declines were limited by extremely large flotations of bonds in March, including a record volume of corporate offerings, continued heavy sales of new municipal securities, and a sizable issue of FNMA participation certificates. The volume of offerings appeared likely to remain large in April, although not so large as in March.

The Treasury was expected to announce near the end of April the terms on which it would refund securities maturing in mid-May, of which $2.9 billion were held by the public. On Friday, March 10, the Treasury temporarily replenished its cash balances by selling a special certificate of indebtedness in the amount of $149 million to the Federal Reserve. The certificate was redeemed 3 days later.

Inflows of funds to savings and loan associations and mutual savings banks were exceptionally large in February, and growth appeared to continue in March. With supplies of mortgage funds exceeding demands, conditions in mortgage markets eased further. Depositary-type institutions used a large part of their increased inflows to repay indebtedness and to acquire marketable securities.

Commercial banks also continued to experience substantial inflows of time and savings deposits in March. Expansion in such deposits over the last 4 months--December through March--had been at an annual rate of 16 per cent, nearly twice the rate for the full year 1966. Growth in large-denomination CD's had moderated considerably since early in 1967, but passbook savings deposits began to rise sharply in mid-February after almost a year of continuous decline. Demand deposits and the money supply also expanded sharply in March. The annual rate of growth in the money supply over the December-March period was 6 per cent, compared with a rise of slightly less than 2 per cent in 1966.

Commercial banks made further sizable additions to their holdings of securities in March, and in contrast with February also expanded their loan volume substantially. A large increase in business loans was associated, in part, with the needs of businesses to finance their payments of income taxes and withheld individual and social security taxes. From February to March the bank credit proxy--daily-average member bank deposits--rose at an annual rate of 15 per cent, the same as from January to February and more than had been expected.

Staff projections for April suggested that the bank credit proxy would expand at an annual rate in the 10 to 13 per cent range if monetary policy remained unchanged, and somewhat more rapidly if easier money market conditions were sought. The demand for business loans was expected to be enlarged temporarily because of an unusually sharp rise in April in the volume of accelerated tax payments. The projections allowed for some slackening in growth of time and savings deposits from the exceptionally rapid pace of recent months, for a large increase in Government deposits, and for a small decline in private demand deposits. With currency holdings expected to continue rising, the money supply was projected to remain about unchanged.

There was broad agreement at this meeting that it would be desirable shortly to reduce the Federal Reserve discount rate, which had been maintained at 4-1/2 per cent since December 1965, in order to bring it into better alignment with market interest rates. It was noted that lack of such action might result in a reversal of the recent downward trends in interest rates, which reflected in part anticipations of a reduction in the discount rate. Individual members of the Committee suggested that a lower discount rate would also help to encourage further declines in yields on long-term securities and mortgage loans; in rates paid by depositary-type institutions, which had been relatively sticky in the recent period of declining yields; and in discount rates of foreign central banks.

As to what degree of reduction in the discount rate would be most desirable, one possibility discussed was a cut of 1/4 of a percentage point, with a second 1/4 point reduction to be made later if it appeared warranted by unfolding developments. However, most of the members favored a reduction of the discount rate by 1/2 of a percentage point, for various reasons. A smaller reduction, they thought, was likely to be interpreted by financial market participants as a cautionary signal regarding System policy intentions, and thus might lead to a back-up in market interest rates that would be difficult to offset without very large injections of reserves. Also, a reduction of 1/4 point would create uncertainties regarding the possibility of further discount rate action--an effect deemed undesirable in a period preceding a Treasury refunding operation. Moreover, a 1/2 point cut was viewed as likely to have significantly stronger effects than the more modest action in encouraging reductions in other interest rates domestically and abroad.

With respect to open market operations, a number of members expressed the view that recent growth rates in member bank reserves, bank credit, and the money supply--while appropriate temporarily in light of the slowing of the business expansion--were too high to be sustained for an extended period. In particular, they questioned the desirability of any policy course that might tend to accelerate growth in these financial aggregates, given the lagged effects of monetary policy and the possibility that business activity would be expanding more vigorously later in the year. These members suggested that operations might be directed toward maintaining the prevailing state of net reserve availability, or of money market conditions in general, with such modifications as might be necessary to moderate apparently significant deviations of bank credit growth in either direction from current expectations.

Other members favored open market operations consistent with the somewhat easier money market conditions that they expected would follow the anticipated reduction in the discount rate, or operations directed at attaining somewhat greater reserve availability. In general, these members thought that continued expansion in financial aggregates at rates in the neighborhood of those recently prevailing would be appropriate in the present economic and financial environment.

At the conclusion of the discussion the Committee agreed that open market operations should be directed at attaining somewhat easier conditions in the money market by supporting the easing expected to result from the anticipated discount rate action, but not at achieving further easing independently of that action unless bank credit appeared to be expanding significantly less than currently anticipated. With this understanding, the Committee voted to issue the following current economic policy directive to the Federal Reserve Bank of New York:

> The economic and financial developments reviewed at this meeting support earlier indications of a marked slowing of expansion in over-all economic activity. Retail sales have continued sluggish and curtailment in the rate of business inventory accumulation is in process. Average commodity prices have changed little recently, but unit labor costs in manufacturing have risen further. Bank credit expansion has remained vigorous, short-term interest rates have declined markedly further, and long-term rates have moved down somewhat despite very heavy securities market flotations. The balance of payments deficit increased in the first quarter despite some improvement in the foreign trade surplus. In several important countries abroad, monetary and fiscal policies have eased further in response to slackened economic activity. In this situation, it is the Federal Open Market Committee's policy to foster money and credit conditions, including bank credit growth, conducive to combatting the effects of weakening tendencies in the economy, while recognizing the need for progress toward reasonable equilibrium in the country's balance of payments.
>
> To implement this policy, System open market operations until the next meeting of the Committee shall be conducted with a view to attaining somewhat easier conditions in the money market, and to attaining still easier conditions if bank credit appears to be expanding significantly less than currently anticipated.

Votes for this action: Messrs. Martin, Hayes, Brimmer, Daane, Francis, Maisel, Mitchell, Robertson, Scanlon, Shepardson, Swan, and Wayne. Votes against this action: None.