FEDERAL RESERVE

press release

For immediate release February 7, 1972

The Board of Governors of the Federal Reserve System and the Federal Open Market Committee today released the attached records of policy actions taken by the Federal Open Market Committee at its meetings on November 16 and December 14, 1971. These records will be published in the Board's Annual Report for 1971 and in the Federal Reserve Bulletin. The summary descriptions of economic and financial conditions they contain are based on the information that was available to the Committee at the time of the meetings, rather than on data as they may have been revised since then.

Attachments

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on November 16, 1971

Authority to effect transactions in System Account.

Preliminary estimates of the Commerce Department indicated that expansion in real output of goods and services had slowed to an annual rate of about 3 per cent in the third quarter, in part because producers and users of steel were working down inventories accumulated earlier against the threat of a steel strike. Growth in real output appeared to be accelerating in the fourth quarter, and staff projections suggested that a faster pace of expansion would be sustained in the first half of 1972.

In October industrial production increased slightly as widespread gains among industries were offset in large part by a strike-induced curtailment in coal. Because of the coal and dock strikes, employment fell in the mining and transportation sectors, and total nonfarm payroll employment changed little following a sizable gain in September. The unemployment rate declined to 5.8 from 6.0 per cent, in part because expansion in the civilian labor force slowed considerably. According to early estimates, retail sales increased slightly further in October to a level appreciably higher than the monthly average for the third quarter. The volume of private housing starts, which had fallen in September from a record high level, rose somewhat in October.

Price developments from mid-September to mid-October--the middle period of the 90-day freeze--continued to be characterized by a sharply reduced number of increases, and the wholesale index for industrial commodities was stable following a slight decline in September. The rise in average wage rates slowed sharply in September and October. In early November the Price Commission and the Pay Board announced the basic policies and initial regulations for the post-freeze phase of the stabilization program.

The latest staff projections for the fourth quarter of 1971 and the first half of 1972 were similar to those of 4 weeks earlier, although the rate of expansion in real GNP now anticipated was not quite so large as before. In the current quarter growth appeared to be accelerating mainly because of faster expansion in the real volume of consumer spending and an increase in inventory investment from the reduced rate of the third quarter. Federal outlays were expected to rise in part because of the military pay increase that became effective in mid-November.

For the first half of 1972, the projections continued to suggest substantial further growth in consumer spending--in response to gains in disposable income arising from tax reductions and increases in social security benefits as well as from expansion in output and employment--and further increases in inventory investment. It was anticipated also that business capital outlays would pick up, that State and local government expenditures would continue to expand rapidly, and that residential construction would advance moderately further.

The flow of merchandise through East Coast and Gulf ports was accelerated in September in anticipation of the dock strike that began in October, but the acceleration in exports far exceeded that in imports and the trade balance shifted into surplus. For the third quarter as a whole imports exceeded exports, although by less than the large margin in the second quarter.

In late October and early November trading generally was thin in foreign exchange markets, and on occasion rates moved sharply as traders attempted to assess the progress in negotiations on new exchange rate relationships. The outflow of short-term capital declined further, and the rise in reserves of foreign central banks slowed markedly. On a weighted average basis, rates for major foreign currencies changed little against the dollar.

On October 27 the Treasury announced that in its mid-November financing it would offer two new securities--a 7-year, 6 per cent note priced to yield 6.04 per cent and a 15-year, 6-1/8 per cent bond priced to yield 6.15 per cent--in exchange for notes and bonds maturing in November 1971 and in May and August 1972. This combination of a refunding and a pre-refunding was well received. Of the nearly $12 billion of eligible issues held by the public, $5.8 billion were exchanged for the new issues, and only $1.3 billion--34 per cent--of the issues maturing in November were redeemed for cash even though the offering did not include a short-term issue. To cover the redemptions and to raise additional cash, on November 9 the Treasury auctioned $2-3/4 billion of a 4-7/8 per cent, 15-month note at an average yield of 4.91 per cent.

Interest rates on market securities generally had continued to decline following the October 19 meeting of the Committee. The course of rates was influenced by a gradual easing in money market conditions during the period and by market expectations of further easing. Downward pressure on short-term rates was intensified by the relatively small market supply of Treasury bills, which resulted in part from purchases of short-term Treasury securities by foreign central banks. On the day before this meeting the market rate on 3-month Treasury bills was about 4.15 per cent, 30 basis points below its level 4 weeks earlier. Federal Reserve discount rates were reduced 1/4 of a percentage point, to 4-3/4 per cent, at seven Reserve Banks on November 11 and at four additional Banks in the period through the date of this meeting.

In capital markets, the estimated volume of new corporate and State and local government bonds issued in October was smaller than in September. However, declining yields apparently stimulated offerings, and the volume of new issues expected during the rest of the year remained relatively large.

Contract interest rates on conventional new-home mortgages edged lower in October, marking the first decrease since last spring. Yields in the more sensitive secondary market for federally insured mortgages, which had turned down in August, continued to decline. Inflows of savings funds to nonbank thrift institutions slowed somewhat in October but were close to the average rate of the third quarter.

At commercial banks, business loans outstanding rose relatively little during October. Major banks reduced their prime lending rates from 6 to 5-3/4 per cent late in the month and then to 5-1/2 per cent in early November, and some banks announced that they were adopting a "floating" prime rate. Real estate and consumer loans continued to expand rapidly in October, and banks again reduced their holdings of U.S. Government securities and increased their holdings of other securities.

According to preliminary estimates, the narrowly defined money stock (private demand deposits plus currency in circulation, or M_1) declined further in October. The broader measure of money (M_1 plus commercial bank time deposits other than large-denomination CD's, or M_2) increased as a result of a marked expansion of inflows of consumer-type time and savings deposits, but the rise in M_2 was somewhat smaller than had been expected. Growth in the bank credit proxy--daily-average member bank deposits, adjusted to include funds from nondeposit sources--slowed substantially, as U.S. Government deposits declined and the volume of large-denomination CD's outstanding increased less than in September. Offering rates on such CD's had been reduced late in September and they were cut further during October.

System open market operations in the period since the October 19 meeting of the Committee had been directed at achieving a gradual easing of money market conditions in light of the continuing tendency of the monetary aggregates to fall below expected paths. The Federal funds rate declined from about 5-1/4 per cent shortly before the preceding meeting to about 4-3/4 per cent. In the 4 weeks ending November 10 member bank borrowings averaged about $270 million, compared with about $330 million in the preceding 4 weeks.

Staff analysis suggested that the effects of two factors that had been tending in recent months to hold down demands for money--moderation of inflationary expectations as a result of the new economic program, and lagged reactions to the high short-term interest rates of late spring and early summer--probably had about run their course. According to the analysis, if money market conditions were similar to those prevailing or slightly easier, M_1 would begin to grow again in December and would expand faster over the first quarter--at a pace more nearly in line than recently with growing transactions demands. For M_2, prospects favored a fourth-quarter rate of growth somewhat above the 4.5 per cent annual rate recorded in the third quarter.[1/] Only a small further step-up in growth of M_2 was anticipated in early 1972, however, because inflows of consumer-type time and savings deposits were expected to slow as consumer spending expanded. As to the bank credit proxy, it appeared likely that the rise over the fourth quarter would be held to modest proportions by a decline in U.S. Government deposits from their high September level.

1/ Calculated on the basis of the daily-average level in the last month of the quarter relative to that of the preceding quarter.

In the Committee's discussion it was noted that business and consumer confidence was being adversely affected by widespread uncertainties connected with the transition from the 90-day freeze to the post-freeze stabilization program and with the unsettled international monetary situation. The view was expressed that it would be particularly unfortunate in this climate for the recent weak performance of the monetary aggregates to persist for long, since the lack of significant growth in the aggregates could become an important independent source of uncertainty. At the same time, some members cautioned against unduly aggressive action to stimulate monetary expansion.

The Committee decided that open market operations in the coming period should be directed at promoting somewhat greater growth in monetary and credit aggregates over the months ahead, recognizing that pursuit of that objective might require appreciably easier money market conditions. The following current economic policy directive was issued to the Federal Reserve Bank of New York:

> The information reviewed at this meeting indicates that real output of goods and services expanded modestly in the third quarter, but greater growth appears in prospect for the current quarter. Although the unemployment rate has declined recently, it remains high. Available data indicate that the 90-day freeze effectively limited increases in prices and wages, and basic policies for the post-freeze stabilization program have been announced. The narrowly defined money stock declined further in October, but inflows of consumer-type time and savings deposits to banks expanded considerably and the broadly defined money stock increased moderately. Expansion in the bank credit proxy slowed substantially as the volume of large-denomination CD's outstanding rose less than in September and as U.S. Government deposits were reduced.

Interest rates on both short- and long-term market securities have continued to decline in recent weeks and Federal Reserve discount rates were reduced by one-quarter of a percentage point to 4-3/4 per cent. The U.S. foreign trade balance was raised in September by a sharp acceleration of export shipments in advance of an East Coast port strike. In recent weeks net outflows of short-term capital apparently have diminished further, market exchange rates for foreign currencies against the dollar on average have not changed much, and foreign official reserve holdings have increased less than they did in September. In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions consistent with the aims of the new governmental program, including sustainable real economic growth and increased employment, abatement of inflationary pressures, and attainment of reasonable equilibrium in the country's balance of payments.

To implement this policy, the Committee seeks to promote somewhat greater growth in monetary and credit aggregates over the months ahead. System open market operations until the next meeting of the Committee shall be conducted with a view to achieving bank reserve and money market conditions consistent with that objective.

Votes for this action: Messrs. Burns, Hayes, Brimmer, Clay, Daane, Kimbrel, Maisel, Mayo, Mitchell, Morris, and Robertson. Votes against this action: None.