FEDERAL RESERVE press release

For Use at 4:30 p.m. March 30, 1984

The Federal Reserve Board and the Federal Open Market Committee today released the attached record of policy actions taken by the Federal Open Market Committee at its meeting on January 30-31, 1984.

Such records for each meeting of the Committee are made available a few days after the next regularly scheduled meeting and are published in the Federal Reserve Bulletin and the Board's Annual Report. The summary descriptions of economic and financial conditions they contain are based solely on the information that was available to the Committee at the time of the meeting.

Attachment

RECORD OF POLICY ACTIONS OF THE
FEDERAL OPEN MARKET COMMITTEE

Meeting Held on January 30-31, 1984

Domestic policy directive

The information reviewed at this meeting indicated that growth in real gross national product had moderated to an annual rate of about 4-1/2 percent in the fourth quarter of 1983, following expansion at annual rates of about 9-3/4 percent and 7-1/2 percent in the second and third quarters respectively. Strength in personal consumption expenditures and further substantial expansion in business fixed investment in the fourth quarter were major factors in the continued growth of economic activity. Price and wage increases generally remained moderate, though advances in some indexes were somewhat larger than in the spring and summer.

The index of industrial production increased 1/2 percent in December, following gains of about 3/4 percent in October and November. Production of consumer durable goods strengthened in December, as auto assemblies increased substantially, and output of business equipment continued to rise at a relatively rapid pace; production changed little in most other major market groupings.

Nonfarm payroll employment advanced about 230,000 further in December, compared with an average monthly increase of about 325,000 since the first quarter. Employment gains continued to be widespread across industry groupings and were particularly marked in manufacturing and service industries. The civilian unemployment rate declined 0.2 percentage point further to 8.2 percent.

The nominal value of retail sales was reported to have changed little in December, after large gains in preceding months. Sales at furniture and appliance stores and at automotive outlets remained strong, but were about offset by declines at food and apparel stores and gasoline stations. Although the reported data for retail sales in the pre-holiday weeks proved weaker than had been suggested by qualitative reports, real personal consumption expenditures for the fourth quarter as a whole rose at an annual rate of about 6-1/2 percent. One factor in that rise was a strengthening in automobile demand; sales of new domestic autos rose to an annual rate of about 7-3/4 million units in December, after averaging about 7 million units in other recent months. In the last 20 days of December, auto sales were at an annual rate of nearly 8 million units, a selling pace that was maintained through the first 20 days of January.

Private housing starts declined about 5 percent in December, but for the fourth quarter were at a rate close to the 1.7 million units recorded for the year as a whole. Sales of new and existing homes, which had changed little in November, rose about 28 percent and 8-1/2 percent respectively in December. The exceptional rise in sales of new homes reflected a record volume of activity in the South; sales in other regions held steady or declined.

Recent data indicate very considerable strength in business capital spending. Shipments of nondefense capital goods increased markedly in November and December. Real expenditures on equipment rose at an exceptionally rapid pace in the fourth quarter, when they registered one of the largest quarterly increases in the postwar period. Strong sales of heavy industrial machinery and communications equipment and a continued brisk pace of truck sales contributed to the fourth-quarter gain.

The producer price index for finished goods was unchanged on balance in November and December. For the year 1983 the index increased about 1/2 percent. The consumer price index rose marginally less in November and December than the 3-3/4 percent rate recorded for the year as a whole. The rise in the index of average hourly earnings was somewhat larger in the fourth quarter than in the preceding two quarters, but over 1983 the index rose a little less than 4 percent, compared with 6 percent over 1982.

In foreign exchange markets the trade-weighted value of the dollar against major foreign currencies had appreciated on balance by about 1 percent further since the latter part of December, with most of the rise occurring in early January. After mid-January the dollar receded from its peak and then moved somewhat erratically, partly reflecting uncertainties among market participants regarding the outlook for economic activity and interest rates in the United States. The U.S. foreign trade deficit was higher in the fourth quarter than in the third; a sharp rise in non-oil imports accounted for the increase, as oil imports declined and exports changed little.

At its meeting on December 19-20, 1983, the Federal Open Market Committee had decided that in the short run, open market operations should be directed toward maintaining at least the existing degree of reserve restraint. The members anticipated that such a policy would be associated with growth of both M2 and M3 at annual rates of around 8 percent from November to March, and that growth of M1 at an annual rate of around 6 percent over the four-month period was likely to be consistent with the objectives for the broader aggregates. Expansion in total domestic nonfinancial debt was expected to be within the tentative range of 8 to 11 percent established for the year 1984. It was agreed that, depending on evidence about the continuing strength of economic recovery and other factors bearing on the business and inflation outlook, somewhat greater restraint would be acceptable should the aggregates expand more rapidly.

M2 and M3 expanded at annual rates of about 8 percent and 8-1/2 percent respectively in December and apparently continued to grow at moderate rates in January.[1/] Expansion in M1 accelerated in January, after several months of reduced growth. By the fourth quarter of 1983, M2 was at a level close to the midpoint of the Committee's range for the year, M3 was around

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1/ The growth rates cited are based on revised data for the monetary aggregates, reflecting new benchmarks and revised seasonal factors and a minor change in the definition of M3 to include term Eurodollars that U.S. residents hold in Canada and the United Kingdom and at foreign branches of U.S. banks elsewhere.

The monetary aggregates are defined as follows: M1 comprises demand deposits at commercial banks and thrift institutions, currency in circulation, travelers checks of nonbank issuers, negotiable order of withdrawal (NOW) and automatic transfer service (ATS) accounts at banks and thrift institutions, and credit union share draft accounts. M2 contains M1 and savings and small-denomination time deposits (including money market deposit accounts (MMDAs)) at all depository institutions, overnight repurchase agreements (RPs) at commercial banks, overnight Eurodollars held at foreign branches of U.S. banks by U.S. residents other than banks, and money market mutual fund shares other than those restricted to institutions. M3 is M2 plus large-denomination time deposits at all depository institutions, large-denomination term RPs at commercial banks and savings and loan associations, institution-only money market mutual funds, and term Eurodollars held by U.S. residents in Canada and the United Kingdom and at foreign branches of U.S. banks elsewhere.

the upper limit of its range, and M1 was near the middle of the Committee's monitoring range for the second half of the year.

The debt of domestic nonfinancial sectors expanded at an annual rate of about 10 percent in both November and December. For the year ending December 1983, debt grew 10-1/2 percent, well within the Committee's monitoring range of 8-1/2 percent to 11-1/2 percent. Growth in total credit at U.S. commercial banks remained strong in December, at an annual rate of about 13 percent, as additional lending activity offset a reduced pace of securities acquisition. The increased loan demand reflected a further pickup in all major categories of loans--business, consumer, and real estate. Businesses continued to rely heavily on external financing as expenditures for inventories and fixed investment evidently began to outpace growth in internally generated funds. In addition to the expansion in borrowing from banks, commercial paper issued by nonfinancial corporations rose sharply in December.

Nonborrowed reserves expanded at a modest rate on average in December and January while total reserves grew only slightly, as the average level of adjustment plus seasonal borrowing declined somewhat. Borrowing temporarily bulged to $1.3 billion in the reserve statement week that encompassed the year-end statement date, but averaged about $650 million during the other weeks of the intermeeting interval.

The federal funds rate averaged close to 9-1/2 percent over the intermeeting period, little changed from the level prevailing just before the December meeting. Most other market rates moved somewhat lower, reflecting a perception of a slowing in the economic expansion and an abatement of seasonal pressures after the mid-December tax date. Yields on private short-term debt and on corporate and municipal bonds declined about 1/2 to 5/8 percentage point while yields on most Treasury securities fell about 1/4 percentage point. Average rates on new commitments for fixed-rate conventional home mortgage loans also fell slightly over the intermeeting period.

The staff projections presented at this meeting continued to indicate that real GNP would grow at a moderate pace in 1984. Consumption expenditures, new residential construction, and business inventory investment were projected to expand at reduced rates in 1984. Business fixed investment was expected to remain a source of strength, and export demand was believed likely to improve in conjunction with rising world economic activity and an expected drop in the foreign exchange value of the dollar. A decline in the unemployment rate was anticipated over the projection period. Prices were expected to increase marginally more than in 1983.

In the Committee's discussion of the economic situation and outlook, the members agreed that growth in real GNP was likely to moderate in 1984 and that the rate of unemployment would probably fall somewhat further by year-end. The members referred to the performance of real GNP in the fourth quarter and to other recent data that suggested slower economic expansion. On the other hand, it was observed that domestic final demands were well maintained in the fourth quarter and that economic activity would continue to be sustained by a stimulative fiscal policy.

Most of the members expected prices to rise somewhat faster on average in 1984 than in 1983, reflecting growing cost pressures likely to be associated with the cyclical rise in capacity utilization rates and declining unemployment and special circumstances such as the impact of adverse weather conditions on food prices. Concern was also expressed that a possible decline in the foreign exchange value of the dollar could also tend to have some inflationary impact on the domestic economy; that impact, one member commented, would be greater if it occurred at a time when the economy had a reduced margin of idle capacity.

For this meeting, the individual members of the Committee had prepared specific projections of economic activity, the rate of unemployment, and average prices. For the period from the fourth quarter of 1983 to the fourth quarter of 1984, the central tendency of the members' projections for growth in real GNP was in a range of 4 to 4-3/4 percent, while the range for all members was 3-1/2 to 5 percent. The central tendency for the GNP deflator was a range of 4-1/2 to 5 percent, and for growth in nominal GNP it was a range of 9 to 10 percent. Projections for the rate of unemployment in the fourth quarter of 1984 varied from 7-1/4 to 8 percent, with a central tendency of 7-1/4 to 7-3/4 percent. These projections were based on the Committee's objectives for monetary and credit growth established at this meeting, and on the assumption that any legislation to reduce substantially the deficit in the federal budget would affect mainly the years beyond 1984.

The members expressed a great deal of concern at this meeting about the risks that unprecedented deficits in the federal budget posed for the sustainability of the economic expansion and the stability of financial markets, domestic and international. Unless decisive action were taken to reduce the deficits, federal financing needs would continue to absorb a large part of available net savings in the economy and curtail the availability of credit to private borrowers at a time in the cyclical expansion when business credit demands were likely to be growing. The result would be to increase pressures in financial markets with potentially adverse consequences for interest-sensitive sectors of the economy such as housing and long-term business investment. Moreover, unprecedented net capital inflows from abroad, which helped to finance domestic credit needs, might well prove to be unsustainable and their eventual diminution or reversal could have highly unsettling effects on domestic credit markets. Concern was also expressed about the risks to the domestic economy and financial markets from other international conditions, such as the severe debt-servicing problems of several developing countries.

At this meeting the Committee completed the review, begun at the December meeting, of the 1984 growth ranges for the monetary and credit aggregates that it had tentatively set in July within the framework of the Full Employment and Balanced Growth Act of 1978 (the Humphrey-Hawkins Act). Those tentative ranges included growth of 6-1/2 to 9-1/2 percent for M2 and 6 to 9 percent for M3 during the period from the fourth quarter of 1983 to the fourth quarter of 1984. The Committee had indicated that growth of M1 in a range of 4 to 8 percent over the same period was likely to be consistent with the ranges for the broader aggregates. The associated range for total domestic nonfinancial debt was provisionally set at 8 to 11 percent for 1984.

In the Committee's discussion, nearly all the members indicated that the ranges tentatively established for 1984 remained acceptable, although some expressed a preference for slightly lower ranges for one or more of the aggregates. The members viewed the various ranges under consideration as broadly consistent with the objectives of promoting sustainable growth in economic activity and encouraging progress toward price stability. While all of the tentative ranges for 1984 represented reductions from the 1983 ranges, slight further reductions would, in the view of some members, help to underscore the Committee's commitment to an anti-inflationary policy. With regard to the range for M2, a small additional reduction was also favored on technical grounds to make the resulting range for 1984 more consistent with the reduced ranges contemplated for the other monetary aggregates. The 1983 range for M2 had been set slightly on the high side to allow for some residual shifting of funds into that aggregate associated with the introduction of money market deposit accounts; those shifts had in fact occurred to about the extent expected, but they now appeared to have been virtually completed.

The ranges under consideration for 1984 assumed that the relationships between the monetary aggregates and nominal GNP -- the velocity of money -- would be broadly consistent with past trends and cyclical patterns following atypical behavior in 1982 and early 1983. A tendency for velocity to rise as 1983 progressed suggested a return toward earlier velocity patterns, but several Committee members believed that more experience was needed before that trend was confirmed. Accordingly, they emphasized the desirability of interpreting actual monetary growth in the context of the emerging performance of the economy, the outlook for inflation, and conditions in domestic and international financial markets. The members also recognized that recent regulatory and institutional developments might be reflected in some permanent changes in the underlying trends of velocity, particularly that of M1. Those changes were not yet knowable, given the limited experience under the deregulated institutional structure.

In this situation most members agreed that for the time being substantial weight should continue to be placed on M2 and M3 in policy implementation, while growth in M1 should be evaluated in light of the performance of the broader aggregates. The view was expressed that emphasis on the broader aggregates appropriately recognized the remaining uncertainties with respect to the relationship between M1 and economic activity, and it was also observed that the use of a relatively wide range for M1 tended to work in the same direction. However, one member urged placing primary emphasis on M1 and also supported a narrower range for that aggregate, noting that the introduction of contemporaneous reserve accounting provided an opportunity to exert closer control over its short-run behavior. A number of other members supported giving M1 greater weight, if not primary emphasis, in light of what they viewed as the emergence of a more predictable pattern in its velocity, at least in relation to that of M2 and of M3. Still other members were not prepared to increase the policy role of M1, at least at this time. In the view of these members, the prospective behavior of M1 velocity remained subject to unusual uncertainties, in part because of the institutional changes reflected in the increased role in M1 of NOW and Super NOW components which bear interest and serve both a transactions and a longer-term savings function. These and related changes made it difficult to anticipate the public's demand for cash balances under varying circumstances or the response of depository institutions in altering terms on the newer components of M1.

Nearly all the members agreed that the Committee should not increase the weight given to the behavior of total domestic nonfinancial debt but should continue to monitor the expansion in such debt. However, one member favored giving primary emphasis to this variable. Most of the members endorsed a reduction in its range for 1984 in light of its historical relationship with nominal GNP. The upper part of the tentative range allowed for the possibility that its growth might outpace that of nominal GNP in 1984 as had often occurred in the second year of past cyclical recoveries.

After further discussion most of the members indicated that they favored or found acceptable the reduced ranges for monetary and credit growth that the Committee had tentatively approved in July for 1984, subject to a further reduction of 1/2 percentage point in the range for M2. A few members would have preferred an additional reduction of 1/2 percentage point in the range for M1. It was anticipated that actual growth of the broader aggregates and total debt of domestic nonfinancial sectors might fluctuate in the upper part of their ranges. For M1, growth around the midpoint of its range appeared likely on the assumption of relatively normal growth in its velocity, but if velocity growth remained weak compared with historical experience, M1 expansion might appropriately be higher in the range. The actual growth of M2 and M3 would be affected by the aggressiveness with which depository institutions sought to influence their share of total credit growth in an environment where interest rate ceilings had largely been deregulated. Growth in the broader aggregates was also thought likely to be affected by inflows of capital from abroad. In particular, a portion of bank credit expansion during 1984 might be funded through nonresident placements in the Euro-dollar market rather than directly in domestic deposits. Such expansion would not be reflected in M2 or M3, and growth in those aggregates would therefore tend to be somewhat restrained relative to growth in bank credit and nominal GNP.

At the conclusion of its discussion the Committee adopted the ranges for monetary and credit growth in 1984 that had been tentatively approved in July, but with a reduction of 1/2 percentage point in the range for M2 from the tentative target. The behavior of all of the aggregates would be interpreted against the background of economic and financial developments, including conditions in domestic credit and international markets. The Committee did not anticipate any further regulatory or statutory changes that would significantly affect monetary growth rates in 1984. However, if some outstanding proposals for change were enacted and took effect in 1984, such as the payment of interest on demand deposits and/or on reserve balances, the Committee would have to reconsider its monetary growth ranges, especially for M1.

The following paragraphs relating to the longer-run ranges were approved:

> The Committee established growth ranges for the broader aggregates of 6 to 9 percent for both M2 and M3 for the period from the fourth quarter of 1983 to the fourth quarter of 1984. The Committee also considered that a range of 4 to 8 percent for M1 would be appropriate for the same period, taking account of the possibility that, in the light of the changed composition of M1, its relationship to GNP over time may be shifting. Pending further experience, growth in that aggregate will need to be interpreted in the light of the growth in the other monetary aggregates, which for the time being would continue to receive substantial weight. The associated range for total domestic nonfinancial debt was set at 8 to 11 percent for the year 1984.
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> The Committee understood that policy implementation would require continuing appraisal of the relationships not only among the various measures of money and credit but also between those aggregates and nominal GNP, including evaluation of conditions in domestic credit and foreign exchange markets.

Votes for this action: Messrs. Volcker, Solomon, Gramley, Guffey, Keehn, Martin, Partee, Rice, Roberts, Mrs. Teeters, and Mr. Wallich. Vote against this action: Mr. Morris.

Mr. Morris dissented from this action because he believed that regulatory changes and financial innovations had made M1, M2, and M3 unsuitable targets for monetary policy since, in his view, they were no longer predictably related to nominal GNP. Accordingly, he preferrred to focus on total domestic nonfinancial debt and total liquid assets as intermediate targets for monetary policy.

In the Committee's discussion of policy for the short run, all of the members indicated that they could support a policy directed toward maintaining essentially the existing degree of restraint on reserve positions. Such a policy was thought likely to be associated with short-run growth in the monetary aggregates consistent with the Committee's objectives for the year. With regard to deviations in pressure on reserve positions toward lesser or greater restraint in response to incoming information, many members endorsed a symmetrical approach that would relate any deviation in either direction to the behavior of the monetary aggregates and to emerging indications of the strength of the business expansion and inflationary pressures in the economy. Other members preferred somewhat more asymmetrical approaches. A few members would give more weight to the potential need for easing of reserve conditions should monetary growth prove weaker than anticipated, while being a bit more tolerant, up to a point, of some tendency for the aggregates to strengthen. Other members believed the Committee should be prepared to move promptly toward restraint if monetary growth should accelerate, particularly in the context of a more ebullient economy. No member anticipated developments that would call for a substantial change in the degree of reserve pressure over the weeks ahead.

In their discussion the members took note of uncertainties associated with the introduction of contemporaneous reserve accounting on February 2. The members agreed that no substantial changes would be made in open market operating procedures at this time, but they anticipated the passage of some time before depository institutions fully adjusted their reserve management to the new accounting system. In that interval, for instance, depository institutions might want to hold more excess reserves than usual. The members agreed that such developments would need to be accommodated by adjustments to reserve paths.

At the conclusion of the Committee's discussion, the members indicated their acceptance of a short-run policy directed at maintaining the existing degree of restraint on reserve positions. The members expected such a policy to be associated with growth of both M2 and M3 at an annual rate of around 8 percent for the period from December to March and growth of M1 at an annual rate of about 7 percent over the 3-month period. The rate of expansion in total domestic nonfinancial debt was thought likely to be within the Committee's monitoring range for 1984. The members agreed that lesser restraint on reserve conditions would be acceptable in the event of a significant shortfall in the growth of the aggregates over the period ahead, while somewhat greater restraint might be acceptable in the context of more rapid growth in the aggregates. In either case, the need for lesser or greater restraint on reserves would also be evaluated against the background of developments relating to the strength of the business expansion and of inflationary pressures. It was agreed that the intermeeting range for the federal funds rate, which provides a mechanism for initiating consultation of the Committee, would remain at 6 to 10 percent.

The following directive, embodying the Committee's longer-run ranges and its short-run operating instructions, was issued to the Federal Reserve Bank of New York:

> The information reviewed at this meeting indicates that the advance in real GNP moderated in the fourth quarter, following rapid expansion in the spring and summer. In December, industrial production and nonfarm payroll employment increased somewhat further and the civilian unemployment rate declined 0.2 percentage point to 8.2 percent. Retail sales were reported to have changed little in December following sizable gains in preceding months. Housing starts declined in December but for the fourth quarter as a whole were close to their average for the year. Recent data indicate substantial strength in business capital spending. Producer prices were about unchanged on average in November and December, and consumer prices increased at about the moderate pace recorded for the year as a whole. The index of average hourly earnings rose somewhat faster in the fourth quarter than in the previous quarter, but for the year 1983 the index increased more slowly than in 1982.
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> The foreign exchange value of the dollar against a trade-weighted average of major foreign currencies has appreciated somewhat further since the latter part of December, with most of the rise occurring in early January. In the fourth quarter the U.S. foreign trade deficit was markedly higher than in the third quarter, reflecting a sharp rise in non-oil imports.
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> M2 and M3 have expanded at moderate rates over the past two months. Expansion in M1 apparently accelerated in January, following several months of reduced growth. By the fourth quarter M2 was at a level close to the midpoint of the Committee's range for 1983, M3 was around the upper limit of its range, and M1 was around the middle of the Committee's monitoring range for the second half of the year. Most interest rates have declined somewhat since the latter part of December.

The Federal Open Market Committee seeks to foster monetary and financial conditions that will help to reduce inflation further, promote growth in output on a sustainable basis, and contribute to an improved pattern of international transactions. The Committee established growth ranges for the broader aggregates of 6 to 9 percent for both M2 and M3 for the period from the fourth quarter of 1983 to the fourth quarter of 1984. The Committee also considered that a range of 4 to 8 percent for M1 would be appropriate for the same period, taking account of the possibility that, in the light of the changed composition of M1, its relationship to GNP over time may be shifting. Pending further experience, growth in that aggregate will need to be interpreted in the light of the growth in the other monetary aggregates, which for the time being would continue to receive substantial weight. The associated range for total domestic nonfinancial debt was set at 8 to 11 percent for the year 1984.

The Committee understood that policy implementation would require continuing appraisal of the relationships not only among the various measures of money and credit but also between those aggregates and nominal GNP, including evaluation of conditions in domestic credit and foreign exchange markets.

In the short run, the Committee seeks to maintain the existing degree of pressure on bank reserve positions, anticipating that approach will be consistent with growth of M2 and M3 each at annual rates of about 8 percent and M1 at an annual rate of about 7 percent during the period from December to March. Growth in nonfinancial debt is expected to be within the range established for the year. Lesser restraint would be acceptable in the context of a shortfall in monetary and credit growth from current expectations, while somewhat greater restraint might be acceptable with more rapid expansion of the aggregates, both viewed in the context of the strength of the business expansion and inflationary pressures.

In implementing policy in the weeks ahead, the Manager was instructed to take account of the uncertainties associated with the introduction of the system of more contemporaneous reserve requirements, particularly including the possibility that depository institutions, during a transition period, may desire to hold more excess reserves.

> The Chairman may call for Committee consultation if it appears to the Manager for Domestic Operations that pursuit of the monetary objectives and related reserve paths during the period before the next meeting is likely to be associated with a federal funds rate persistently outside a range of 6 to 10 percent.

> Votes for the short-run operational paragraphs: Messrs. Volcker, Solomon, Gramley, Guffey, Keehn, Martin, Morris, Partee, Rice, Roberts, Mrs. Teeters, and Mr. Wallich. Votes against this action: None.

On March 20, the Committee held a telephone conference to review monetary and economic developments following the January 30-31 meeting, including some increase in interest rates over the period. It was noted that economic activity in most sectors was rising with considerable momentum, helping to generate strong demands for credit. While measures of monetary growth have remained broadly in line with objectives for the year, it was also felt that, in the light of current and prospective developments, the Committee would need to remain alert to the possibility of excessive growth in credit and money. Against that background, it was the consensus of the Committee that, in the short interval until the next scheduled meeting, pursuit of the degree of reserve restraint and associated reserve paths, consistent with the money and credit objectives set at the January 30-31 meeting, should not be constrained by a federal funds rate at or above the monitoring range set at that meeting.