FEDERAL RESERVE

press release

For immediate release January 22, 1968

The Board of Governors of the Federal Reserve System and the Federal Open Market Committee today released the attached record of policy actions taken by the Federal Open Market Committee at its meeting on October 24, 1967. Such records are made available approximately 90 days after the date of each meeting of the Committee and will be found in the Federal Reserve Bulletin and the Board's Annual Report.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on October 24, 1967

Authority to effect transactions in System Account.

Underlying economic conditions continued strong despite recent weakness in some key measures of activity resulting from strikes in the automobile and other industries. In the third quarter, according to preliminary Commerce Department figures, real GNP rose substantially and average prices--as measured by the GNP "deflator"--increased more rapidly than they had earlier in the year. It appeared likely that the rate of growth in real output would step up in the fourth quarter if major work stoppages were limited in duration and extent and that inflationary pressures would continue. Expectations had diminished that a surcharge on Federal income taxes, as recommended by the President, would be enacted before the year-end.

Both nonfarm employment and industrial production declined in September, largely as a result of strikes. The unemployment rate rose to 4.1 per cent from 3.8 per cent in August, mainly because of an unusually large increase in the number of women in the labor force. However, continued tightness in over-all labor market conditions was indicated by other evidence, including a decline in the unemployment rate for adult men to an extremely low level and a rise in the index of help-wanted advertising. Against the background of tight labor markets and recent rapid increases in consumer prices, it appeared likely that settlements in current wage negotiations would be of a nature to maintain upward pressures on costs.

In the fourth quarter business inventories were expected to increase modestly--as they had in the third quarter--and further advances were anticipated in most major categories of final demand. Growth in consumer expenditures had been smaller than expected in the third quarter; estimates of retail sales for July and August, particularly at nondurable goods stores, had been revised downward sharply, and the advance estimate for September showed little improvement. However, it appeared likely that consumer spending would increase considerably in the fourth quarter, when the rate of growth in disposable income was expected to rise further unless retarded by extended major strikes or restrained by enactment of a tax increase. Further advances also seemed to be in prospect for residential construction, which had risen substantially in the third quarter, and for business fixed investment, which had turned up after declining moderately in the first half of the year. Growth in defense spending had slowed markedly after midyear, but a sharp rise in total Federal outlays was anticipated in the final quarter largely because of expected increases in civilian and military pay.

With respect to the U.S. balance of payments, substantial deficits had been recorded in each of the first three quarters of 1967 on the "liquidity" basis of calculation, and another such deficit appeared likely in the fourth quarter. The balance on the "official reserve transactions" basis had swung widely in recent quarters as a result of wide fluctuations in liabilities of U.S. banks to their foreign branches, but for the first three quarters of 1967 as a whole there had been a sizable deficit on this basis also. Sterling continued under pressure in foreign exchange markets, and on October 19 the Bank of England raised its discount rate from 5-1/2 to 6 per cent.

On October 3 the Treasury auctioned $1.5 billion of tax-anticipation bills maturing in April and $3.0 billion maturing in June at average issuing rates of 4.93 and 5.11 per cent, respectively. Commercial banks initially absorbed almost all of the new issues, which carried 75 per cent tax-and-loan-account privileges. Bids for the June tax bills exceeded the amount offered by an unusually small margin. An announcement was anticipated on the day following this meeting of the terms on which the Treasury would refund securities maturing in mid-November, of which $2.6 billion were held by the public. The Treasury was expected to raise some new cash in connection with that refunding.

System open market operations since the preceding meeting of the Committee had continued to be directed at maintaining steady conditions in the money market. Free reserves of member banks fluctuated widely in the 3 weeks ending October 18, but their average of about $265 million was little changed from that of the preceding 3 weeks. Both excess reserves and borrowings of member banks increased; borrowings averaged about $170 million, compared with $85 million in the preceding period. Rates on Federal funds and on bank loans to Government securities dealers rose somewhat in the first half of October, but after that they moved down again.

Interest rates on most short-term market instruments had advanced further since the preceding meeting of the Committee. The market rate on 3-month Treasury bills, at 4.58 per cent on the day before this meeting, was 18 basis points higher than 3 weeks earlier. In part this increase reflected the shift in the maturity dates of 3-month bills to January from the December dates that are attractive to many investors. It also reflected the increased bill supplies resulting from the Treasury's tax-anticipation bill offering in early October and the continued $100 million additions to the weekly bill offerings.

Bond yields had risen significantly further in recent weeks; yields on municipal bonds had advanced to their highest levels since the early 1930's, and those on corporate and long-term Treasury bonds to levels not reached since the early 1920's. These developments reflected diminishing confidence in financial markets that a tax increase would be enacted and a related heightening of expectations that monetary policy would become firmer. In this atmosphere investors were becoming more reluctant to acquire long-term securities and borrowers were increasingly tending to anticipate later needs. The volume of new corporate securities offered publicly in October was now expected to be considerably larger than the reduced offerings of September, and the November calendar was growing rapidly. Flotations of municipal securities were expected to decline in October--partly because a number of issues had been postponed or reduced in size--but it appeared likely that the volume of such issues would increase again in November.

Interest rates on conventional mortgages on new homes remained at their advanced August level in September, and secondary-market yields on Federally underwritten mortgages rose for the fifth consecutive month. Although inflows of funds to nonbank depositary institutions continued large, in the third quarter as a whole they were below the record volume of the second quarter, after allowance for seasonal influences.

At commercial banks, loans on securities and loans to nonbank financial institutions increased markedly in September and apparently also in early October. Growth in business loans appeared to have stepped up somewhat in recent weeks from its earlier slow pace, but to a large extent the increased demands for such loans probably reflected needs to finance payments to the Treasury of corporate income taxes in September and of withheld taxes in early October. As to total bank credit, estimates of recent and current growth rates had been revised upward somewhat since the preceding meeting of the Committee. The bank credit proxy--daily-average member bank deposits--now was estimated to have risen at about a 10-1/2 per cent annual rate from August to September and was projected to rise at a rate in the range of 12 to 15 per cent from September to October. The money supply, which earlier had been expected to grow relatively little in October, was now projected to rise in that month at an annual rate in the 7 to 9 per cent range.

Growth in both the bank credit proxy and the money supply was expected to moderate somewhat in November--to annual rates in the ranges of 7 to 10 per cent and 4 to 6 per cent, respectively--if money market conditions were unchanged. Although the outlook for business loan demands was particularly uncertain at present, on balance such demands appeared likely to remain moderate in both November and December.

The Committee decided that the forthcoming Treasury financing precluded any change in monetary policy at this time. Some members favored no policy change on other grounds also, including the continuing uncertainties regarding the probable outcome of the current congressional debate on fiscal policy measures. Also cited in this connection was the judgment that a considerable degree of restraint was already being imposed on potential borrowing and spending by the high levels to which long-term interest rates had risen. In addition, it was noted that further increases in market interest rates at this time might well have undesired effects on flows of funds to financial intermediaries and on the position of sterling in foreign exchange markets.

Other members indicated that in the absence of Treasury financing activity they would have been inclined to advocate some firming of monetary policy in an effort to slow the rapid growth of bank credit and the money supply. In their judgment, current and prospective inflationary pressures and the continued large deficits in the balance of payments argued strongly for such a course.

At the conclusion of the discussion 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 that, apart from the effects of strikes in the automobile and other industries, underlying economic conditions continue strong and prospects favor more rapid growth in the months ahead. Upward pressures on costs persist, average prices of industrial commodities have risen further, and the rate of increase in consumer prices remains high. While there recently have been large inflows of liquid funds from abroad through foreign branches of U.S. banks, the balance of payments continues to reflect a substantial underlying deficit. Bank credit expansion has continued large. The volume of new security issues is expanding again and interest rates have risen further, reflecting in part increased uncertainties in financial markets concerning enactment of the President's fiscal program. In this situation, it is the policy of the Federal Open Market Committee to foster financial conditions, including bank credit growth, conducive to sustainable economic expansion, recognizing the need for reasonable price stability for both domestic and balance of payments purposes.

To implement this policy, while taking account of forthcoming Treasury financing activity, System open market operations until the next meeting of the Committee shall be conducted with a view to maintaining about the prevailing conditions in the money market; but operations shall be modified, to the extent permitted by Treasury financing, to moderate any apparent tendency for bank credit to expand significantly more than currently expected.

Votes for this action: Messrs. Martin, Brimmer, Maisel, Mitchell, Robertson, Scanlon, Sherrill, Swan, Wayne, and Treiber. Vote against this action: Mr. Francis.

Mr. Francis dissented from this action because he favored seeking whatever degree of firming in money market conditions would be required to moderate substantially the growth in bank credit and the money supply by the end of the year. He agreed that Treasury financing operations would have to be taken into account to some extent in implementing such a policy. Nevertheless, he thought that the national interest called for greater monetary restraint now to curb inflationary pressures and to protect the foreign trade component of the U.S. balance of payments.