FEDERAL RESERVE

press release

For immediate release April 15, 1970

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 January 15, 1970. 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 January 15, 1970

Authority to effect transactions in System Account.

Growth in real gross national product came to a halt in the fourth quarter of 1969, according to preliminary Commerce Department estimates, but prices and costs were continuing to rise rapidly. Staff projections suggested that there would be little change in real economic activity in early 1970. It appeared likely that upward pressures on prices would persist, although perhaps moderating somewhat as the year progressed.

Signs of weakness in the economy at the year-end were reflected in various monthly economic series. Industrial production had declined in December for the fifth successive month. Although the unemployment rate remained at the low November level of 3.4 per cent, nonfarm employment had edged down, and employment in manufacturing was reduced for the fourth month in a row. Retail sales were about unchanged in December, and after adjustment for price increases, they remained below the level of a year earlier. Housing starts and manufacturers' new orders for durable goods had continued downward in November, the latest month for which data were available.

Average wholesale prices rose considerably further from mid-November to mid-December for both industrial commodities and farm and food products. Among industrial commodities, advances were particularly marked for nonferrous metals and for machinery and equipment. The consumer price index again rose substantially in November.

The Commerce Department figures for the fourth quarter indicated that real GNP had leveled out primarily because of a reduction in the rate of inventory accumulation by business; growth in final sales slowed only moderately further. The staff projections for the first half of 1970 suggested that the rate of inventory accumulation would decline further and that growth in final sales would remain sluggish. It appeared likely that Federal expenditures and residential construction outlays would decline in both the first and second quarters and that growth in spending by State and local governments would remain slow.

There were some elements of strength in the outlook, including reported plans by businesses to increase outlays on new plant and equipment substantially further in 1970. In addition, under recent legislation the income tax surcharge had been reduced from 10 to 5 per cent as of January 1 (and would be eliminated as of July 1), and social security benefits had been raised by 15 per cent as of January 1--with the higher payments, including a retroactive payment, to begin in April. However, the stimulating effect of this legislation on consumer spending was expected to be offset in part by other factors tending to slow growth in personal income and by some rise in the saving rate.

The small surplus in U.S. foreign trade that had been recorded in the third quarter was maintained in the first 2 months of the fourth quarter, as both exports and imports increased moderately. With respect to the over-all payments balance, extremely heavy capital inflows in the final weeks of the year resulted in large surpluses in December and in the fourth quarter as a whole on both the "liquidity" and "official reserve transactions" bases of calculation.[1/] It appeared that the year-end inflow reflected further repatriations out of German mark holdings together with the return of funds from various sources by U.S. corporations partly in order to comply with U.S. Government controls on direct investments abroad. Some of the inflow was reversed early in January.

The Treasury was expected to announce in late January the terms on which it would refund bonds maturing in mid-February. It seemed likely that the Treasury would decide to refund bonds maturing

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 (sometimes referred to as the "official settlements" 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 ordinary capital flows.

in mid-March at the same time. About $6.7 billion of such securities would mature on those two dates, of which $5.6 billion were held by the public.

System open market operations since the mid-December meeting of the Committee had been directed at maintaining the prevailing firm conditions in the money market. When seasonal forces around the turn of the year tended to produce considerable tautness in the money market--as reflected in effective Federal funds rates of 9.5 and 9.75 per cent on a number of days--the pressure on marginal reserve positions of member banks was eased somewhat. The average rate on Federal funds in the 4 weeks ending January 7 was slightly below 9 per cent, little changed from the preceding 3 weeks. Average member bank borrowings declined by about $200 million, to approximately $1.0 billion; average net borrowed reserves declined somewhat more as a result of a seasonal increase in excess reserves at year-end.

In the opening weeks of 1970 interest rates moved down for Treasury securities of all maturities and for new corporate and municipal bonds. These reductions reflected in part the demands of small investors who were employing funds that they had withdrawn from depositary institutions. For corporate and municipal bonds the reductions extended declines that had been under way since early and mid-December, respectively. Yields on Treasury securities, however, had remained under upward pressure until the end of 1969, for various reasons--including dealer efforts to hold down inventories in the face of high financing costs; bank sales of coupon-bearing issues in reaction to certain provisions of the newly enacted Tax Reform Act; and sales of Treasury bills by foreign official institutions. Three-month Treasury bill rates had reached record highs on December 29--8.08 per cent for the market rate and 8.10 per cent for the average auction rate. But by the day before this meeting the market rate on 3-month bills had fallen to 7.87 per cent, about the same as it had been a month earlier. However, yields on Treasury notes and bonds were still above their mid-December levels.

Both commercial banks and nonbank thrift institutions--savings and loan associations and mutual savings banks--apparently had experienced very heavy outflows of consumer-type time and savings funds after year-end interest and dividend crediting. Earlier, in response to reduced net inflows of savings funds and pessimistic appraisals of the outlook, the thrift institutions had cut back their new mortgage commitments substantially. With mortgage interest rates continuing under upward pressure, the ceiling rate on federally underwritten home mortgages was raised from 7-1/2 to 8-1/2 per cent, effective January 5.

In December total time and savings deposits of commercial banks had increased for the first time in a year. Flows of consumer-type deposits had remained weak in that month, and holdings by domestic depositors of large-denomination negotiable certificates of deposit (CD's) had continued to contract. However, there was a sizable further rise in foreign official time deposits. Over the fourth quarter as a whole total time and savings deposits had been about unchanged.

Private demand deposits and the money stock declined during most of December. However, they increased sharply in the final week of the year--as a result in part of various technical factors and in part of exceptionally large year-end money flows, apparently including the repatriation of funds from abroad by corporations in compliance with Government controls on foreign direct investments. The year-end surge, which was believed likely to prove temporary, was sufficient to cause the money stock to grow at an annual rate of about 2 per cent from November to December and about 1 per cent over the fourth quarter as a whole. In the third quarter the money stock had not grown.

Bank credit, as measured by the proxy series--daily-average member bank deposits[1/]--declined from November to December at an

1/ In recent years the Committee has been making use of daily-average statistics on total member bank deposits as a "bank credit proxy"--that is, the best available measure, although indirect, of developing movements in bank credit. Because the deposit figures are compiled on a daily basis with a very short lag, they 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 table in the statistical section of the Federal Reserve Bulletin (p. A-17 of the January 1970 issue).

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 Bulletin for October 1966. As indicated in that note, movements in total member bank deposits and in commercial bank credit can diverge for various reasons, including changes in "nondeposit" liabilities of banks. Changes in U.S. bank liabilities to foreign branches and, more recently, in funds raised by other means--particularly the sale of commercial paper by bank affiliates--have become important sources of such divergence. Accordingly, an "adjusted" proxy series, taking approximate account of such changes, is also calculated for Committee use.

annual rate of 0.5 per cent. After adjustment for changes in the outstanding volume of funds obtained by banks from "nondeposit" sources--including a reduction in the average level of their Euro-dollar borrowings through foreign branches and a rise in the volume of funds obtained through sales of commercial paper by bank affil-iates--the proxy series increased at an annual rate of 1.5 per cent from November to December. The adjusted bank credit proxy rose at a 2 per cent annual rate during the fourth quarter, following a decline at a 4.3 per cent rate in the third quarter.

Staff projections suggested that the adjusted bank credit proxy would decline over the first quarter and the money stock would change little on balance, assuming maintenance of prevailing money market conditions and no changes in maximum interest rates payable on time and savings deposits under the Board's Regulation Q. The adjusted proxy series was projected to contract at annual rates of 1 to 4 per cent from December to January and 4 to 7 per cent from January to February, in large part because of anticipated net reduc-tions in time and savings deposits.

While taking note of the leveling off in real economic activ-ity, the Committee agreed that any marked relaxation of monetary restraint would be premature at present in light of the persistence of inflationary pressures and expectations. At the same time, con-siderable concern was expressed about the prospect that in the first quarter both bank credit and the money stock would continue to show no significant growth if prevailing money market conditions and Regulation Q ceiling rates were maintained. In this connection it was reported that the Board of Governors planned shortly to consider increases in the Regulation Q ceilings.

In the discussion of open market policy, some members expressed the view that the specific money market conditions sought--within the range of conditions sufficiently firm to be consistent with a posture of monetary restraint--should be those most likely to be conducive to modest growth in bank credit and the money stock over the first quarter. Other members thought that a slight lessening of pressures on the money market might be accommodated, but they nevertheless favored relying mainly on early action with respect to Regulation Q in the effort to encourage some growth in bank credit. Still others indicated that on balance they were inclined toward maintaining the prevailing conditions in the money market.

The Committee concluded that in the conduct of open market operations increased stress should be placed on the objective of achieving modest growth in the monetary aggregates, with about equal weight being given to bank credit and the money stock. It was agreed that operations should be directed at maintaining firm conditions in the money market, but that they should be modified if it appeared that the objective with respect to the aggregates was not being achieved. It was also agreed that account should be taken of the forthcoming Treasury refunding, and of the effects of any action by the Board with respect to Regulation Q.

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

> The information reviewed at this meeting suggests that real economic activity leveled off in the fourth quarter of 1969 and that little change is in prospect for the early part of 1970. Prices and costs, however, are continuing to rise at a rapid pace. Most market interest rates have receded from highs reached during December. Bank credit and the money supply increased slightly on average in December and also over the fourth quarter as a whole. Outstanding large-denomination CD's held by domestic depositors have continued to contract in recent months while foreign official time deposits have expanded considerably. Flows of consumer-type time and savings funds at banks and non-bank thrift institutions have remained weak, and there apparently were sizable net outflows after year-end interest crediting. U.S. imports and exports have both grown further in recent months but through November the trade balance showed little or no further improvement from the third-quarter level. At the year-end the over-all balance of payments statistics were buoyed by large temporary inflows of U.S. corporate funds. In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to the orderly reduction of inflationary pressures, with a view to encouraging sustainable economic growth and attaining reasonable equilibrium in the country's balance of payments.
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> To implement this policy, while taking account of the forthcoming Treasury refunding, possible bank regulatory changes and the Committee's desire to see a modest growth in money and bank credit, System open market operations until the next meeting of the Committee shall be conducted with a view to maintaining firm conditions in the money market; provided, however, that operations shall be modified if money and bank credit appear to be deviating significantly from current projections.

Votes for this action: Messrs. Martin, Hayes, Bopp, Brimmer, Clay, Coldwell, Daane, Maisel, Mitchell, Robertson, Scanlon, and Sherrill. Votes against this action: None.