FEDERAL RESERVE

press release

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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 21-22, 1974.

Such records are made available approximately 90 days after the date of each meeting of the Committee 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 on the information that was available to the Committee at the time of the meeting, rather than on data as they may have been revised since then.

Attachment

RECORD OF POLICY ACTIONS
OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting held on January 21-22, 1974[1/]

1. Domestic policy directive

Preliminary estimates of the Commerce Department indicated that growth in real output of goods and services (real gross national product) had slowed to an annual rate of 1.3 per cent in the fourth quarter of 1973--from 3.5 per cent in the third quarter--and that the rise in the GNP implicit deflator had accelerated to an annual rate of about 8 per cent, in part as a result of the impact of the oil shortage. Staff projections suggested that economic activity would weaken further in the first half of 1974 and that prices would rise somewhat more sharply than had been expected 5 weeks earlier.

In December industrial production declined, as output of automobiles fell sharply and residential and commercial use of electricity and gas was substantially reduced; the gain in industrial production from the third to the fourth quarter of 1973 was small. Nonfarm payroll employment--which had grown rapidly in the first 11 months of the year--expanded little in December, when some workers were laid off as a result of the energy situation, and the unemployment rate rose further to 4.9 per cent. Retail sales declined in December

1/ This meeting was held over a 2-day period, beginning on the evening of January 21, 1974, in order to enable the Committee to hear reports from members who had attended international gatherings without infringing on the time available for its deliberations on current monetary policy.

and changed little in the fourth quarter as a whole, chiefly because of a drop in demand for the larger automobiles and for some other durable goods.

Wholesale prices of industrial commodities rose sharply further in December; as in the preceding 2 months, increases were large for fuels and were substantial and widespread among other industrial commodities. Wholesale prices of farm and food products, which had declined for 3 months, turned up, reflecting sizable increases in prices of grains, animal feeds, oilseeds, fats and oils, and raw cotton. In the closing months of 1973 the consumer price index continued upward at a rapid rate as a result of the rise in prices of various types of energy and increases in prices of foods and services. The index of average hourly earnings of production workers on private nonfarm payrolls also continued to move up at a fast pace, but real spendable weekly earnings of production workers declined in the fourth quarter of the year, as they had over the first three quarters.

Staff projections for the first half of 1974 still suggested that the shortfall in supplies of petroleum products would lead to additional curtailment in expenditures for automobiles and related goods and services. Consequently, real consumption expenditures, which had declined in the fourth quarter of 1973, would remain weak. As before, it was anticipated that the decline in residential construction would be extended but that the expansion in business fixed investment would remain relatively strong and that growth in State and local government purchases of goods and services would continue at a substantial rate. The over-all increase in nominal GNP projected for the first half of the year was now somewhat greater than had been expected 5 weeks earlier, owing to larger increases in prices, mainly in those of petroleum products.

In late December the large price increase for crude oil imposed by producing countries generated new uncertainties and fears about foreign trade prospects for oil-importing countries, about the size and direction of international flows of funds, and about the course of economic activity in major industrial countries. Participants in foreign exchange markets apparently believed that the United States would be the principal recipient of the capital flows arising from the investment of oil producers' receipts; as a result, major foreign currencies depreciated significantly further against the dollar in late December and early January--even while some foreign monetary authorities intervened in the markets, selling large amounts of dollars to limit depreciation of their currencies.

U.S. merchandise imports had risen substantially in November, in part because of earlier sharp increases in prices of petroleum products. Exports also had advanced, but U.S. merchandise trade had been in approximate balance, following 2 months of large surpluses.

Total loans and investments at U.S. commercial banks increased relatively little in December, and growth in bank credit over the fourth quarter was moderate. Expansion in outstanding business loans--which had picked up in November--slowed again in December, as some borrowers apparently used proceeds of new bond issues to pay down bank loans. Real estate and consumer loans grew at about the same rates as in November, remaining well below rates earlier in the year. And while banks added to their holdings of State and local government securities, they further reduced their holdings of Treasury issues.

The narrowly defined money stock (M_1)[2/] continued to grow at a rapid pace in December, but growth was somewhat faster over the November-December period than it otherwise would have been because of temporary increases in deposits held by foreign commercial banks; weekly data suggested that on balance M_1 changed little between mid-December and mid-January. In December

2/ Private demand deposits plus currency in circulation.

inflows of time and savings deposits other than large-denomination certificates of deposits (CD's) were still sizable, although somewhat less than in November, and growth in the more broadly defined money stock (M_2)[3/] remained substantial. The outstanding volume of large-denomination CD's expanded, contributing to a moderate pick-up in growth in the bank credit proxy[4/] from very slow rates in October and November. In late December and early January the outstanding volume of such CD's expanded further, and the credit proxy grew at a faster rate.

Net deposit inflows at nonbank thrift institutions--which had improved significantly in October and November--expanded slightly further in December, reflecting primarily a larger-than-seasonal amount of interest credited to accounts at the month's end; growth in the measure of the money stock that includes such deposits (M_3)[5/]--like growth in M_2--remained substantial. Contract interest rates on conventional mortgages were unchanged in December, after having declined over the two preceding months, but yields in the secondary market for Federally insured mortgages declined for the third consecutive month.

3/ M_1 plus commercial bank time and savings deposits other than large-denomination CD's.

4/ Daily-average member bank deposits, adjusted to include funds from nondeposit sources.

5/ M_2 plus time and savings deposits at mutual savings banks and at savings and loan associations.

Following the Committee meeting in mid-December, System open market operations had been directed initially toward achieving some easing in bank reserve and money market conditions --in accordance with the Committee's decision to seek such easing, provided that the monetary aggregates did not appear to be growing excessively. As a result the Federal funds rate declined to a level of around 9-3/4 per cent in the early days of January--from around 10-1/8 per cent in the two statement weeks before the December meeting--and member bank borrowings declined to an average of about $1,010 million in the 3 weeks ending January 9 from an average of about $1,390 million in the preceding 4 weeks.

On January 11, after incoming data had suggested that in the December-January period the annual rate of growth in reserves available to support private nonbank deposits (RPD's) might be close to the upper limit of the specified range and that rates of growth in M_1 and M_2 might exceed acceptable ranges, a majority of the available members concurred in a recommendation by the Chairman that, in view of the sensitive state of financial markets and the general economic situation, the System aim to maintain prevailing money market conditions for the time being. The funds rate remained around 9-3/4 per cent until the last few days before this meeting when it averaged about 9-5/8 per cent; in the statement week ending January 16, member bank borrowings were about $990 million.

Changes in market interest rates since mid-December had been mixed. Long-term rates in general had risen in response to a relatively heavy volume of capital market financing. The over-all volume of new public offerings of corporate and State and local government bonds--which had expanded in the October-November period--declined less than seasonally in December, and a substantial increase was in prospect for January.

In short-term markets some private rates had declined since mid-December, reflecting the slackening in business demands for short-term credit and the inflow of funds from abroad. However, Treasury bill rates had risen, apparently because money market conditions had eased less than market participants had expected and because foreign monetary authorities had sold a substantial volume of bills in association with their intervention in foreign exchange markets.

The Treasury was expected to announce on January 30 the terms of its mid-February refunding. Of the maturing issues, $4.5 billion were held by the public.

A staff analysis suggested that, because of the larger rise in prices and higher projected rate of expansion in nominal GNP, growth in the demand for money over the first half of 1974 was likely to be somewhat greater than had been expected earlier. It appeared likely that if M_1 were to grow at a rate consistent with the Committee's earlier longer-run objectives for the monetary aggregates, money market conditions would tighten somewhat in the period immediately ahead and market interest rates in general would rise. As a result, net inflows of consumer-type time and savings deposits to banks and nonbank thrift institutions might decline appreciably, reducing the rates of growth in both M_2 and M_3. This analysis implied that a moderately higher rate of growth in M_1 would be associated with little change or possibly some easing in money market conditions; under these conditions, net inflows of consumer-type time and savings deposits likely would be maintained or would expand somewhat from recent rates.

According to the staff analysis, expansion in M_1 was likely to be relatively slow on the average in the January-February period--following the rapid pace over the preceding 2 months that was attributable in part to the transitory increases in deposits held by foreign commercial banks. However, growth was expected to be faster in the second quarter, reflecting the temporary effects of large refunds of Federal income taxes and initial payments of increased social security benefits. It was also anticipated that growth in bank credit would pick up this winter from the low rate of the fourth quarter of 1973 and that the outstanding volume of large-denomination CD's, which had turned up in mid-December, would expand at a moderate pace.

The Committee agreed that the economic situation and outlook called for moderate growth in monetary aggregates over the longer run, including a slightly higher rate of growth in M_1 than contemplated earlier. Taking account of the staff analysis, the Committee concluded that growth in M_1 and M_2 over the January-February period at annual rates within ranges of tolerance of 3 to 6 per cent and 6 to 9 per cent, respectively, would be consistent with its longer-run objectives for the monetary aggregates. The members agreed that such growth rates would be likely to involve RPD growth during the January-February period at an annual rate within a 4-3/4 to 7-3/4 per cent range of tolerance, and they decided that in the period until the next meeting the weekly average Federal funds rate might be permitted to vary in an orderly fashion from as low as 8-3/4 per cent to as high as 10 per cent, if necessary, in the course of operations. It was understood that a slight easing in reserve and money market conditions would be sought promptly, provided that the data becoming available later in the week of the meeting did not suggest that the monetary aggregates were growing rapidly.

The members also agreed that, in the conduct of operations, account should be taken of the forthcoming Treasury financing and of international and domestic financial market developments. It was understood that the Chairman might call upon the Committee to consider the need for supplementary instructions before the next scheduled meeting if significant inconsistencies appeared to be developing among the Committee's various objectives and constraints.

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

> The information reviewed at this meeting indicates that growth in real output of goods and services was slow in the fourth quarter of 1973, in part because of the fuel situation. Prices continued to rise sharply in December, reflecting additional increases for petroleum products and widespread advances among other goods and services. A further weakening in activity and sharp rise in prices appear to be in prospect for early 1974. In December nonfarm payroll employment changed little, and the unemployment rate increased further. Wage rates have continued to rise substantially in recent months, although not so sharply as prices.
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> Major foreign currencies have depreciated further against the dollar since mid-December, and some foreign monetary authorities have continued to sell dollars in exchange markets. Steep price increases imposed by oil-producing countries have heightened fears of economic disruption in many countries and of large and erratic international flows of funds.
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> The narrowly defined money stock increased substantially in the last 2 months of 1973, partly reflecting increased foreign deposits, but it has changed little on balance over recent weeks. Net inflows of consumer-type time deposits remained sizable at both banks and nonbank thrift institutions. Bank credit expansion, which was moderate over the closing months of 1973, has accelerated in recent weeks as banks have stepped up issuance of large-denomination CD's. Since mid-December, interest rate movements have been mixed; yields on most long-term securities and on Treasury bills have risen on balance, while some private short-term rates have declined.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to resisting inflationary pressures, cushioning the effects on production and employment growing out of the oil shortage, and maintaining equilibrium in the country's balance of payments.

To implement this policy, while taking account of the forthcoming Treasury financing and of international and domestic financial market developments, the Committee seeks to achieve bank reserve and money market conditions consistent with moderate growth in monetary aggregates over the months ahead.

Votes for this action: Messrs. Burns, Balles, Brimmer, Bucher, Daane, Holland, Mayo, Mitchell, Morris, and Sheehan. Votes against this action: Messrs. Hayes and Francis.

In dissenting, both Mr. Hayes and Mr. Francis indicated that they favored no change in the Committee's longer-run objectives for growth in the monetary aggregates, and Mr. Hayes also was opposed to a range of tolerance for the Federal funds rate that was skewed to the low side of the range that had prevailed in recent days. In Mr. Hayes' view, the probabilities favored a relatively mild business slowdown in 1974 as a whole, and in light of the rapid monetary growth in recent months, the Committee should lean against the strong inflationary pressures that remained the major economic problem. Mr. Francis believed that the actual and prospective slowdown in economic activity resulted wholly from capacity, supply, and price-distorting constraints, rather than from a weakening in demand, and that any easing in monetary policy would increase inflationary pressures without expanding real output or reducing unemployment.

2. Ratification of earlier action

By unanimous vote, the Committee ratified the action for which a majority of the members had voted on January 4, 1974, increasing from $2 billion to $3 billion the limit on changes between Committee meetings in System Account holdings of U.S. Government and Federal agency securities specified in paragraph 1(a) of the authorization for domestic open market operations, effective for the period from January 4 through the close of business on January 22, 1974.

The action in question had been taken on recommendation of the System Account Manager. The Manager had advised that a substantial volume of open market purchases of securities had been required in the period since the Committee's meeting on December 18, 1973, in order to offset reserve absorption resulting from market factors and that a near-term need to supply reserves was in prospect; he had further advised that strength of the dollar in foreign exchange markets suggested that foreign official sales of U.S. Treasury bills might be heavy and that the System should be in a position to acquire some of those bills while offsetting any undesired effects on bank reserves by other means.

3. Authorization for foreign currency operations

The Committee approved an increase from $2 billion to $3 billion in the System's swap arrangement with the Bank of Italy, and the corresponding amendment to paragraph 2 of the authorization for foreign currency operations, subject to the understanding that the action would become effective upon approval by the Subcommittee (consisting of the Chairman and Vice Chairman of the Committee and the Vice Chairman of the Board of Governors) designated in the Committee's rules of procedure, after consultation with the U.S. Treasury.

> Votes for this action: Messrs. Burns, Hayes, Balles, Brimmer, Bucher, Daane, Francis, Holland, Mayo, Mitchell, Morris, and Sheehan. Votes against this action: None.

On January 29, 1974, the Subcommittee approved the indicated increase, effective February 1, 1974. Accordingly, as of the latter date, paragraph 2 of the authorization read as follows:

> The Federal Open Market Committee directs the Federal Reserve Bank of New York to maintain reciprocal currency arrangements ("swap" arrangements) for the System Open Market Account for periods up to a maximum of 12 months 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)
Austrian National Bank	250
National Bank of Belgium	1,000
Bank of Canada	2,000
National Bank of Denmark	250
Bank of England	2,000
Bank of France	2,000
German Federal Bank	2,000
Bank of Italy	3,000
Bank of Japan	2,000
Bank of Mexico	180
Netherlands Bank	500
Bank of Norway	250
Bank of Sweden	300
Swiss National Bank	1,400
Bank for International Settlements:	
Dollars against Swiss francs	600
Dollars against other European currencies	1,250

This action was taken on the grounds that it would prove helpful in coping with possible exchange market pressures on the lira arising from the oil crisis, and thus would contribute to international monetary stability.