FEDERAL RESERVE

press release

For immediate release July 7, 1975

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 May 20, 1975.

Such records are made available approximately 45 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 May 20, 1975

1. Domestic policy directive

The information reviewed at this meeting suggested that real output of goods and services--which had fallen sharply in the fourth quarter of 1974 and the first quarter of 1975--was declining much less rapidly in the current quarter and that the rise in prices was moderating further. Staff projections, like those of 5 weeks earlier, suggested that real economic activity would turn up later in the year and that the rise in prices would continue to slow.

The pace of decline in industrial production, which had been less rapid in March than in the preceding 4 months, moderated further in April. Nonfarm payroll employment changed little and total employment rose, but the unemployment rate increased further, from 8.7 to 8.9 per cent, as the labor force continued to grow at a considerable pace. According to the advance report, retail sales had risen in April, despite a further decline in the number of new cars sold.

The index of average hourly earnings for private nonfarm production workers was unchanged in April, after having risen sharply in March; over the first 4 months of the year the rate of advance in the index was considerably less rapid than that in the second half of 1974. Average wholesale prices of industrial commodities changed little in April, as in March, while wholesale prices of farm and food products increased sharply, following 5 months of large decreases. In March the rise in the consumer price index had slowed further from the pace in the first 2 months of the year.

Staff projections still suggested that in the current quarter the decline in real GNP would be small and that nominal GNP would turn up, although expectations now were for only a slight rather than a substantial increase in residential construction. It was still anticipated that inventory liquidation would moderate from the exceptional pace in the first quarter and that personal consumption expenditures would expand but that business fixed investment would decline further. The projected upturn in real GNP in the second half reflected expectations that growth in consumption expenditures would accelerate in response to expansive fiscal policy measures, that the upturn in residential construction would gain momentum, and that the pace of inventory liquidation would moderate further.

Since mid-April the average exchange value of the dollar against leading foreign currencies had receded somewhat, but it was still slightly above the low in early March. The U.S. foreign trade balance--which had been in large deficit in the last three quarters of 1974--shifted into substantial surplus in the first quarter of this year, in considerable part because the volume of imports was reduced by the decline in business activity in this country. Net outflows of funds through banks expanded substantially in the first quarter, as outstanding loans to foreigners continued to increase while liabilities to foreigners declined.

Total loans and investments at U.S. commercial banks continued to expand at a slow pace from the end of March to the end of April. Outstanding loans to business declined further, as business demands for credit remained weak both at banks and in the commercial paper market; outstanding loans to nonbank financial institutions, securities dealers, and consumers also declined, while real estate loans increased by only a modest amount. As in February and March, banks increased their holdings of U.S. Government securities considerably.

Growth in both the narrowly defined and the more broadly defined money stock ($M_1$ and $M_2$)--which had been substantial in

March--was moderate in April, as disbursements of income tax refunds slowed to about the pace of a year earlier. The measure of the money stock that includes deposits at nonbank thrift institutions ($M_3$) grew more rapidly; although net inflows to thrift institutions subsided from the extremely high rates in March, they remained substantial. In April, as in the preceding 2 months, banks reduced the outstanding volume of large-denomination CD's in response to the growth in other deposits and to the continued weakness in loan demand, and the bank credit proxy grew at a relatively slow pace.

On May 1 the Treasury announced that it would auction up to $5 billion of notes and bonds, of which $3.8 billion represented refunding of publicly held notes that were to mature on May 15. In auctions on May 6, 7, and 8, respectively, the Treasury sold $2.75 billion of 3-1/4-year notes at an average price to yield 7.7 per cent, $1.5 billion of 7-year notes at an average price to yield 8.0 per cent, and $750 million of 30-year bonds at an average price to yield 8.3 per cent. The Treasury also announced on May 1 that its over-all borrowing needs for the current fiscal year would be $5 billion less than had been previously stated, owing to larger-than-expected receipts of taxes.

System open market operations since the April 14-15 meeting had been guided by the Committee's decision to seek bank reserve and money market conditions consistent with somewhat more rapid growth in monetary aggregates over the months ahead than had occurred on average in recent months, while taking account of the forthcoming Treasury financing and of developments in domestic and international financial markets. The monetary aggregates had been expected to grow at relatively rapid rates in the April-May period--because of the large volume of tax rebates scheduled to begin in May, of the rise in nominal GNP anticipated for the second quarter, and of the lagged effects on the demand for money of earlier declines in short-term interest rates--and operations initially had been directed toward maintaining about the prevailing bank reserve and money market conditions. However, data that became available subsequently suggested that in the April-May period the growth rate of $M_1$ would be near the lower limit of the range of tolerance that had been specified by the Committee and growth in $M_2$ would be below its tolerance range. Accordingly, operations were directed toward achieving some easing in bank reserve and money market conditions, although the System proceeded cautiously in order to avoid exaggerated market effects during a period of heavy Treasury financing. In the days preceding this meeting the Federal funds rate was about 5-1/8 per cent, compared with a rate of about 5-1/2 per cent shortly before the April meeting.

Short-term market interest rates--which had risen a little between mid-March and mid-April--declined somewhat in early May, reflecting the Treasury's announcement of reduced borrowing needs, the easing in money market conditions, and the continued weakness in business demands for short-term credit. On the day before this meeting the market rate on 3-month Treasury bills was 5.11 per cent, compared with 5.53 per cent at the time of the April meeting. Effective May 16, Federal Reserve discount rates were reduced from 6-1/4 to 6 per cent at 10 Reserve Banks; shortly thereafter, rates were reduced at the remaining two Banks.

Yields on longer-term securities rose in late April but turned down after the beginning of May; over the inter-meeting period they changed little. The volume of public offerings of corporate bonds in April, although smaller than in March, was still large, and an increase was in prospect for May. Offerings of State and local government issues in April and the calendar for May also were heavy. Yields on home mortgages rose somewhat during April, after having declined persistently since September of last year.

At its previous meeting, the Committee had agreed that growth in the monetary and credit aggregates on average over the period from March 1975 to March 1976 at rates within the following ranges presently appeared to be consistent with its broad economic objectives: $M_1$, 5 to 7-1/2 per cent; $M_2$, 8-1/2 to 10-1/2 per cent; $M_3$, 10 to 12 per cent; and the bank credit proxy, 6-1/2 to 9-1/2 per cent. It was understood that these ranges, as well as the particular list of aggregates for which such ranges were specified, were subject to review and modification at subsequent meetings. It also was understood that from month to month the rates of growth of the various aggregates might well fall outside ranges contemplated for annual periods as a result of short-run factors.

At this meeting the Committee took note of a staff analysis indicating that the rate of growth of the monetary aggregates would probably be increased temporarily during May and June by the tax rebates, totaling about $8 billion, which the Treasury would pay out in those months. It seemed likely that a sizable portion of the rebates would be held for a time in demand balances before being used to acquire assets, repay debt, or increase spending, and that some part would be placed directly in savings accounts.

To allow for the expected temporary bulge in money holdings, the Committee agreed that relatively rapid growth in $M_1$ and $M_2$ over the May-June period--at annual rates within ranges of tolerance of 7 to 9-1/2 per cent and 9 to 11-1/2 per cent, respectively--would be acceptable. Such growth rates were thought likely to involve growth in reserves available to support private nonbank deposits (RPD's) at a rate within a range of 1-1/2 to 4 per cent, and they were expected to be consistent with a weekly average Federal funds rate in a range of 4-1/2 to 5-1/2 per cent.

In the course of the Committee's discussion a number of members expressed the view that upward pressures on interest rates would be particularly undesirable at present, in light of the sensitive state of financial markets and of uncertainties with respect to the timing and strength of the economic recovery that now appeared to be in process of developing. There was no sentiment for aggressive easing operations for the purpose of reducing market interest rates further. Some members urged, however, that the

System should be prepared to respond promptly should the monetary aggregates be unexpectedly weak.

The Committee decided that open market operating decisions in the period until the next meeting should be based to a greater extent than usual on the state of financial markets, with the objective of maintaining money market conditions about like those now prevailing so long as the monetary aggregates appeared to be growing at rates within acceptable ranges of tolerance. The following domestic policy directive was issued to the Federal Reserve Bank of New York:

> The information reviewed at this meeting suggests that real output of goods and services--after having fallen sharply for two quarters--is declining much less rapidly in the current quarter. In April the pace of the decline in industrial production moderated considerably further, and total employment rose. However, the unemployment rate increased again, from 8.7 to 8.9 per cent, as the civilian labor force increased considerably. Average wholesale prices of industrial commodities changed little in April, as in March; prices of farm and food products rose sharply, following several months of large decreases. The advance in average wage rates so far this year has been considerably less rapid than the increase during the second half of 1974.
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> The foreign exchange value of the dollar has declined somewhat since mid-April, but it is still above the low of early March. U.S. imports fell sharply in the first quarter, and the foreign trade balance was in substantial surplus, in contrast to the deficits of preceding quarters. Net outflows of funds through banks were large in the first quarter, as loans to foreigners continued to increase while liabilities to foreigners declined.

Both $M_1$ and $M_2$ grew moderately in April, but $M_3$ grew more rapidly as inflows of deposits to nonbank thrift institutions remained substantial. Business demands for short-term credit remained weak, both at banks and in the commercial paper market, while demands in the long-term market continued strong. Since mid-April short-term market interest rates have declined somewhat. Most longer-term yields have changed little on balance, and mortgage rates have risen. Federal Reserve discount rates were reduced from 6-1/4 to 6 per cent in mid-May.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions conducive to stimulating economic recovery, while resisting inflationary pressures and working toward equilibrium in the country's balance of payments.

To implement this policy, while taking account of developments in domestic and international financial markets, the Committee seeks to maintain about the prevailing money market conditions over the period immediately ahead, provided that monetary aggregates generally appear to be growing within currently acceptable short-run ranges of tolerance.

Votes for this action: Messrs. Burns, Hayes, Baughman, Bucher, Coldwell, Eastburn, Holland, MacLaury, Mayo, Mitchell, and Wallich. Votes against this action: None.

Absent and not voting: Mr. Sheehan.

2. Amendment to authorization for domestic open market operations

On April 30, 1975, Committee members voted to increase from $3 billion to $4 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 immediately, for the period ending with the close of business on May 20, 1975.

> Votes for this action: Messrs. Burns, Hayes, Coldwell, Eastburn, Holland, MacLaury, Mayo, Mitchell, Wallich, and Francis. Votes against this action: None. Abstention: Mr. Sheehan.
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> Absent and not voting: Messrs. Bucher and Baughman. (Mr. Francis voted as alternate for Mr. Baughman.)

This action was taken on recommendation of the System Account Manager. The Manager advised that large-scale securities purchases had been necessary to carry out the Committee's objectives in the period since the previous meeting because an extremely large volume of reserves had been absorbed by a rise in the Treasury's balances at Reserve Banks to record levels, and that a temporary increase in the leeway for System purchases appeared desirable in light of the prospective near-term needs to supply reserves.

At this meeting, the Committee decided to maintain the $4 billion limit for the period through the close of business on June 17, 1975. This action was taken on the recommendation of the Deputy Manager for Domestic Operations, who advised that an expected sharp decrease in Treasury balances at the Reserve Banks in the period ahead might necessitate an unusually large volume of securities sales by the System to absorb reserves.

> Votes for this action: Messrs. Burns, Hayes, Baughman, Bucher, Coldwell, Eastburn, Holland, MacLaury, Mayo, Mitchell, and Wallich. Votes against this action: None.
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> Absent and not voting: Mr. Sheehan.