FEDERAL RESERVE press release

For Use at 4:10 p.m.

April 2, 1982

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 February 1-2, 1982.

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 February 1-2, 1982

1. Domestic policy directive

Preliminary estimates of the Commerce Department indicated that real gross national product had declined at an annual rate of about 5-1/4 percent in the fourth quarter of 1981. Average prices, as measured by the fixed-weight price index for gross domestic business product, increased at an annual rate of about 7 percent, much less rapidly than over the first three quarters of the year. During 1981, real GNP and nominal GNP grew about 3/4 percent and 9-1/4 percent respectively, and the price index referred to above rose about 9 percent.

The index of industrial production fell 2.1 percent further in December, for a cumulative decline of about 7 percent over the last five months of 1981. The decline in December again was broadly based, reflecting output reductions for nearly all major product groupings, and it was particularly sharp for durable consumer goods and both durable and nondurable goods materials. Available data, notably for the automotive and steel industries, suggested further production cutbacks in January.

Total nonfarm payroll employment declined sharply in December for the third consecutive month. Job losses in manufacturing continued sizable, totaling more than 700,000 in the fourth quarter. The unemployment rate rose an additional 0.5 percentage point in December to 8.9 percent.

The nominal value of retail sales increased somewhat further in December, but the level remained below the average for the third quarter. Sales of new domestic automobiles fell to an annual rate of 4.9 million units in December, the lowest monthly pace in 22 years. Auto sales picked up in the first few weeks of January but continued at an exceptionally low rate.

Private housing starts rose 13 percent in December from the depressed rate in November, but remained below an annual rate of 1 million units. Nearly all of the increase was in multifamily units. Sales of existing homes picked up somewhat in December, as had sales of new homes in November; nevertheless, total home sales in November were about one-third below their year-earlier level.

The producer price index for finished goods rose 0.3 percent in December, compared with 0.5 percent in November. During 1981 the index rose 7 percent, compared with the increase of nearly 12 percent over 1980. Producer prices of consumer foods rose only a little during 1981, and the rise in energy prices moderated, as a surge early in the year after decontrol of oil prices was followed by some decline in the second half. Producer prices of other consumer goods and capital equipment also rose less rapidly in 1981 than in 1980. The consumer price index rose 0.4 percent in December; over the year the index increased about 9 percent, compared with a rise of about 12-1/2 percent over 1980. Increases were smaller in 1981 than in 1980 for all major components of the index.

The rise in the index of average hourly earnings slowed considerably in the final three months of 1981 from the pace earlier in the year. Over the year, the index rose about 8-1/4 percent, compared with an increase of about 9-1/2 percent over 1980.

In foreign exchange markets the trade-weighted value of the dollar against major foreign currencies rose about 4 percent during January, reflecting primarily responses to the widening differential between U.S. and foreign interest rates. Foreign monetary authorities intervened considerably to resist the depreciation of their currencies. The U.S. trade deficit increased in the fourth quarter from the rate in the previous two quarters, as nonagricultural exports declined and non-oil imports rose.

At its meeting on December 21-22, 1981, the Committee had decided that open market operations in the period until this meeting should be directed toward behavior of reserve aggregates consistent with growth of M1 and M2 from November 1981 to March 1982 at annual rates of around 4 to 5 percent and around 9 to 10 percent respectively. In setting the objective for M1, the Committee took account of the relatively rapid growth that had already taken place through the first part of December. The intermeeting range for the federal funds rate, which provides a mechanism for initiating consultation of the Committee between regularly scheduled meetings, was set at 10 to 14 percent.

M1 grew at an annual rate of 11-1/2 percent in December and accelerated in January to a rate estimated to be above 20 percent. Expansion in checkable deposits other than demand accounts (other checkable deposits, or OCDs), which accounted for a substantial part of the acceleration of M1 growth in November and December, apparently was even more rapid in January. Growth of M2 moderated in December to an annual rate of about 7-3/4 percent but picked up in January to a rate estimated at about 11 percent; the substantial growth over the two months reflected strength in the more liquid of the nontransaction components as well as in M1.[1/] Some evidence suggested that the disproportionate growth in NOW and similar accounts in recent months had resulted at least in part from a desire of individuals to hold liquid balances because of uncertainties about economic prospects and interest rates.

The pace of monetary growth in December and January raised required reserves and generated demands for reserves considerably in excess of the volume supplied during the intermeeting period through System open market operations. Consequently, borrowings from Federal Reserve Banks

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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 some minor changes in the definition of M2, that were published on February 5. As redefined, M2 no longer includes institution-only money market mutual funds (which remain in M3) and includes retail repurchase agreements (RPs) in denominations of less than $100,000 (which were already in M3).

M1 comprises demand deposits at commercial banks and thrift institutions, currency in circulation, travelers checks, negotiable orders 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 at all depository institutions, overnight RPs at commercial banks and retail RPs at all depository institutions, overnight Eurodollars held at Caribbean branches of member 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 saving and loan associations, and institution-only money market mutual funds.

for purposes of adjusting reserve positions expanded sharply; borrowings averaged nearly $1.3 billion in the four statement weeks ending January 27, compared with an average of about $425 million in the four weeks ending December 23. The federal funds rate rose from around 12-1/4 percent in the days preceding the December meeting to about 14 percent in the days just before this meeting.

Against a background of continued rapid growth in monetary aggregates and large prospective federal deficits, market interest rates had risen on balance since the Committee's meeting in December: short-term rates increased about 1-1/2 to 2-1/2 percentage points and bond yields rose about 1/2 to 1 percentage point. The prime rate charged by most commercial banks on short-term business loans remained at 15-3/4 percent during the intermeeting interval. Average rates on new commitments for fixed-rate conventional home mortgage loans increased nearly 3/4 of a percentage point.

Total credit at U.S. commercial banks, adjusted for shifts of assets from U. S. offices of banks to recently established international banking facilities (IBFs), expanded at an annual rate of about 11 percent in December.[1/] Growth in business loans accelerated substantially, and security, real estate, and consumer loans also registered sizable gains. From the fourth quarter of 1980 to the fourth quarter of 1981, bank credit expanded 8-3/4 percent. Issuance of commercial paper by nonfinancial institutions was relatively strong in December, but slowed in early January.

1/ International banking facilities began operations on December 3, 1981. The adjustment made in calculating growth in bank credit involved adding back assets estimated to have been transferred from U. S. banking offices to IBFs.

Staff projections presented at this meeting suggested that real GNP would decline further in the current quarter and then begin to recover in the second quarter. The unemployment rate was expected to increase to a peak in the second quarter, while inflation, as measured by the fixed-weight price index for gross domestic business product, was projected to slow further over the year.

Views of Committee members concerning economic activity and prices during 1982 generally differed little from the staff projections. The members thought that recovery in activity most likely would begin before long, although they differed somewhat with regard to its probable strength. Their projections of growth in real GNP over the year ending in the fourth quarter of 1982 ranged from 1/2 percent to 3 percent. However, a number of members expressed concern about the risk that the recession might be prolonged by greater weakness in business capital investment than currently anticipated or by other developments. Members were unanimous in the view that the reduction in the rise in prices was likely to continue: their projections for the increase in the GNP implicit deflator over the year ranged from 6-1/2 and 7-3/4 percent, compared with a rise of about 8-1/2 percent over the year ending in the fourth quarter of 1981.

At this meeting, the Committee completed the review, begun at the meeting in December 1981, of the ranges for growth of monetary aggregates over the period from the fourth quarter of 1981 to the fourth quarter of 1982 within the framework of the Full Employment and Balanced Growth Act of 1978. At its meeting in July 1981, the Committee had reaffirmed the ranges for growth over the year ending in the fourth quarter of 1981 that it had set in early February. These ranges were 3 to 5-1/2 percent for M1-A and 3-1/2 to 6 percent for M1-B, abstracting from the impact of the introduction of NOW accounts on a nationwide basis; 6 to 9 percent for M2; and 6-1/2 to 9-1/2 percent for M3. The associated range for growth of commercial bank credit was 6 to 9 percent. For the year ending in the fourth quarter of 1982, the Committee had tentatively agreed that growth of M1, M2, and M3 within ranges of 2-1/2 to 5-1/2 percent, 6 to 9 percent, and 6-1/2 to 9-1/2 percent respectively would be appropriate.[1/]

When the Committee reaffirmed the ranges for 1981 at its meeting in July, it recognized that the divergence in growth of the various monetary aggregates was proving to be considerably greater than had been anticipated at the beginning of the year, even after allowance for the effects of shifts into NOW accounts. Thus it was thought likely and desirable that growth of M1-B over the year would be near the lower bound of its range and that growth of M2 and M3 might well be around the upper ends of their ranges.

The divergence in behavior between the narrow monetary aggregate and the broader ones proved to be even greater than had been expected at midyear. From the fourth quarter of 1980 to the fourth quarter of 1981, growth of M1-B adjusted for shifts into NOW accounts was about 2-1/4 percent, approximately 1-1/4 percentage points below the lower end of its

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1/ In looking ahead to 1982, it had been decided to abandon the compilation of M1-A and the shift-adjusted M1-B (that is, M1-B adjusted to exclude that portion of flows into NOW accounts in 1981 estimated to have come from other interest-bearing assets rather than from demand deposits). The remaining aggregate for M1 is the one formerly labeled M1-B, which includes the total amount of NOW accounts.

range. Growth in this aggregate over the year was slow in relation to growth of nominal GNP, as financial innovations and high interest rates induced changes in cash-management techniques. Growth of M2 and M3 over the year was about 9-1/2 percent and 11-1/4 percent respectively, about 1/2 percentage point and 1-3/4 percentage points above the upper ends of their ranges. The relatively strong growth of M2 reflected in part shifts of funds from market instruments to money market mutual funds and the expansion of small savers certificates at depository institutions in response to liberalization of interest rate ceilings; M3 grew more than M2 because of a substantial expansion in large-denomination CDs, as depository institutions increased their managed liabilities to support expansion in loans and investments.

In contemplating ranges for 1982, the Committee continued to face unusual uncertainties concerning the forces affecting monetary growth. It seemed likely that the recent expansion in NOW accounts would prove to be mostly a temporary aberration in individuals' liquidity preferences and that the relationship between growth of money and of nominal GNP would be closer to historical patterns. The ongoing changes in financial technology, which had reduced demand for M1 for most of 1981, were generally presumed to have effects in 1982 consistent with earlier experience, unless such arrangements as "sweeps" of individual checking accounts into money market funds or other instruments became widespread. With respect to M2, growth could be augmented if the scheduled reduction in federal income taxes or other influences raised the personal saving rate or if depository institutions attracted an exceptionally large flow of funds into individual retirement accounts (IRAs) from sources not included in M2.

In the Committee's discussion of ranges for monetary growth in 1982, the members were in agreement on the need to maintain the commitment to the long-standing goal of restraining growth of money and credit, thereby contributing to a further reduction in the rate of inflation and providing the basis for restoration of economic stability and sustainable growth in output. Nevertheless, members differed somewhat in their views concerning the particular ranges most appropriate for the year.

For M1, most members favored reaffirming the range of 2-1/2 to 5-1/2 percent that had been tentatively adopted at the meeting in July 1981. One member advocated a somewhat higher range, with a view to promoting more growth of real GNP and a lower rate of unemployment. In addition, some sentiment was expressed for retaining the range of 2-1/2 to 5-1/2 percent but taking the base level of M1 in the fourth quarter of 1981 to be the lower end of the Committee's range for last year. Such an adjustment of the base would in effect recognize that the recent burst in growth of M1 had brought its level more in line with the lower end of the 1981 range and, unless the burst proved to be temporary, could provide a more appropriate starting point.

Members differed somewhat more in their views concerning the broader monetary aggregates. Most desired to reaffirm the tentative range of 6 to 9 percent adopted last July. However, a substantial number initially favored specification of slightly higher ranges, largely because of their assessments of the likely impact of various developments that would tend to raise growth of M2 relative to that of M1. One member suggested that in pursuit of its objectives during the course of the year the Committee give more weight to M2 than to M1, because of the volatility of the behavior of the narrower aggregate in the short run reflecting, among other things, the response of NOW accounts to changing liquidity preferences and interest rates. More generally, it was felt that considerable weight should be given to M2 in interpreting developments during the year.

At the conclusion of the discussion, the Committee decided to reaffirm the ranges for 1982 that had been tentatively established in mid-1981. Thus the Committee adopted the following ranges for growth of the monetary aggregates from the fourth quarter of 1981 to the fourth quarter of 1982: for M1, 2-1/2 to 5-1/2 percent; for M2, 6 to 9 percent; and for M3, 6-1/2 to 9-1/2 percent. The associated range for commercial bank credit was 6 to 9 percent.

In setting the range for M1, the Committee recognized that the recent rapid increase in that aggregate placed it in January well above the average in the fourth quarter of 1981 but that it was too early to judge conclusively the extent to which the upsurge reflected temporary influences rather than a basic change in the amount of money needed to finance growth of nominal GNP. On the assumption that the relationship between growth of M1 and the expansion of nominal GNP was likely to be closer to normal than it had been in 1981, the Committee contemplated that growth of M1 in 1982 might acceptably be in the upper part of its range. The lower part of the range was considered appropriate to allow for the possibility that institutional or regulatory changes would speed the process of economizing on the cash balances included in M1. The Committee also contemplated that growth of M2 was likely to be high within its range, although growth still would be somewhat below that in 1981. However, growth of M2 might appropriately reach or even slightly exceed the upper end of its range if personal savings grew much more rapidly in relation to income than anticipated or if depository institutions attracted an exceptionally large flow of funds into IRAs from sources outside measured M2. In light of the unusual growth of NOW accounts in recent weeks, it was emphasized that the Committee might wish to reconsider the range for M1 should evidence suggest a more lasting change in individuals' liquidity preferences; in any event, it would reconsider the ranges in July within the framework of the Full Employment and Balanced Growth Act of 1978.

> The Committee adopted the following ranges for growth in the monetary aggregates for the period from the fourth quarter of 1981 to the fourth quarter of 1982: M1, 2-1/2 to 5-1/2 percent; M2, 6 to 9 percent; and M3, 6-1/2 to 9-1/2 percent. The associated range for bank credit is 6 to 9 percent.
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> > Votes for this action: Messrs. Volcker, Solomon, Boehne, Boykin, Corrigan, Gramley, Keehn, Partee, Rice, Schultz, and Wallich. Vote against this action: Mrs. Teeters.

Mrs. Teeters dissented from this action because she believed that somewhat higher monetary growth over the year ahead was needed to promote adequate expansion in economic activity and a reduction in the rate of unemployment. Specifically, she favored a range for M1 that was at least 1/2 percentage point higher than that adopted by the Committee and a range for M2 that provided for somewhat greater growth in the broader aggregate relative to that in M1.

In contemplating its objectives for monetary growth over the remainder of the first quarter of the new year, the Committee took account of the very rapid rise in M1 in recent months, especially in January. Given the apparent persistence of slow growth in nominal GNP in the first quarter, it seemed quite likely that the demand for money would abate substantially over the months ahead. Even if M1 grew no further from January to March, its income velocity on the average for the first quarter could well decline at a postwar record rate. While some decline in M1 seemed desirable, the Committee did not feel that much stronger measures than those already in place would be necessary or appropriate in the period immediately ahead to force such a decline.

Against this background, the Committee decided to seek behavior of reserve aggregates associated with no further growth of M1 from January to March and with growth of M2 at an annual rate of around 8 percent, with a view to bringing growth of both aggregates over time into their longer-run target ranges for the year. It was also agreed that some decline in M1, which would be associated with a faster return to its longer-run range, would be acceptable in the context of reduced pressure in the money market. The intermeeting range for the federal funds rate, which provides a mechanism for initiating consultation of the Committee, was set at 12 to 16 percent.

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

The information reviewed at this meeting indicates that real GNP declined appreciably in the fourth quarter of 1981 and that prices on the average rose much less rapidly than over the first three quarters of the year. In December industrial production and nonfarm payroll employment declined sharply for the third consecutive month, and the unemployment rate rose an additional 0.5 percentage point to 8.9 percent. The nominal value of retail sales increased somewhat further, but the level was still below the average for the third quarter. Although housing starts expanded, they remained at a depressed level. The rise in the index of average hourly earnings was considerably less rapid over the fourth quarter of 1981 than on the average earlier in the year.

The weighted average value of the dollar against major foreign currencies rose substantially during January; foreign monetary authorities intervened considerably to resist the depreciation of their currencies. In the fourth quarter the U.S. foreign trade deficit increased from the rate in the previous two quarters.

M1 grew rapidly in December and January, reflecting in part rapid expansion in checkable deposits other than demand accounts. Growth of M2 also was substantial, owing to strength in the more liquid of the nontransaction components as well as in M1. Short-term market interest rates and bond yields on balance have risen further in recent weeks, and mortgage interest rates have also increased.

The Federal Open Market Committee seeks to foster monetary and financial conditions that will help to reduce inflation, promote a resumption of growth in output on a sustainable basis, and contribute to a sustainable pattern of international transactions. The Committee agreed that its objectives would be furthered by growth of M1, M2, and M3 from the fourth quarter of 1981 to the fourth quarter of 1982 within ranges of 2-1/2 to 5-1/2 percent, 6 to 9 percent, and 6-1/2 to 9-1/2 percent respectively. The associated range for bank credit was 6 to 9 percent.

The Committee seeks behavior of reserve aggregates over the balance of the quarter consistent with bringing M1 and M2 over time into their longer-run target ranges for the year. Taking account of the recent surge in growth of M1, the Committee seeks no further growth in M1 for the January-to-March period and growth in M2 at an annual rate of around 8 percent. Some decline in M1 would be associated with more rapid attainment of the longer-run range and would be acceptable in the context of reduced pressure in the money market. 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 12 to 16 percent.

Votes for this action: Messrs. Volcker, Solomon, Boehne, Boykin, Corrigan, Gramley, Keehn, Partee, Rice, Schultz, Mrs. Teeters, and Mr. Wallich. Votes against this action: None.