

REPORT OF OPEN
MARKET OPERATIONS

Reporting on open market operations, Mr. Sternlight made the following statement:

Trading desk operations since the last meeting of the Committee produced a gradual easing of reserve availability, in seeking to accommodate moderate growth of the monetary aggregates. Prior to the November meeting, Federal funds had been trading around 5 percent. Pursuant to the Committee's instructions, to be followed if aggregates appeared to be turning out about in line with expectations, the Desk sought and achieved a funds rate around 4 7/8 percent within a few days after the November 16 meeting, and a rate of about 4 3/4 percent in the final week of November. The decline was assisted by the 1/4 percent cut in discount rates announced on November 19.

By the first few days of December it appeared that M_1 growth was running to the low side of the desired range, but M_2 was holding up well and pending a clarification of the outlook the Desk continued to seek a funds rate around 4 3/4 percent. Given the momentum of the preceding rate decline, however, which had affected market anticipations even though the Desk's moves had been gradual, funds actually averaged around 4.67 in the first full week of December--a shade easier than was desired at that point. By the end of the first week in December growth in the aggregates, especially M_1 , appeared somewhat weaker than earlier and the Desk undertook a little easier posture, seeking--

and achieving--a funds rate in the $4 \frac{5}{8}$ - $4 \frac{3}{4}$ percent area. In the several days preceding today's meeting available information on the aggregates suggested still weaker growth in M_1 and the Desk has sought a funds rate around $4 \frac{5}{8}$ percent. Actual trading in the last few days has been largely in a range of $4 \frac{1}{2}$ - $4 \frac{3}{4}$ percent.

Outright operations during the period included the purchase of \$758 million of Treasury coupon issues and \$115 million of agency issues, in three market go-arounds. The impact of these operations, undertaken near the beginning and end of the interval, was approximately offset by net sales of some \$865 million of bills. Bill sales were concentrated in the middle part of the period when the usual run-down of Treasury balances at the Reserve Banks provided reserves. Reserves were also drained by some \$77 million in redemptions of agency issues. Bills were sold mainly to foreign accounts, but bills were sold in the market on December 3 when there was a need to absorb reserves in the midst of an exuberant atmosphere in the securities markets stimulated by the widespread view that further significant easing lay immediately ahead. As usual, there was also substantial day-to-day use of repurchase agreements and matched sale-purchase transactions to even out the impact of short-term reserve flows and help achieve funds rate objectives.

Interest rates declined across a broad front during the inter-meeting period, especially in the first two weeks as the market saw the Federal funds rate gradually declining,

reinforced by the discount rate cut and a flow of news that emphasized the sluggishness of the economy. Rates have moved irregularly since early December as market participants have reacted alternately to signs of renewed strength or continued pause in the economy, and to indications that they interpreted as suggesting that monetary policy was or was not tending still easier. Some renewed impetus to rate declines was provided near the end of the period by the Board's announcement of a small reduction in reserve requirements, although the market gave up most of its early gains just after that move as market participants saw no accompanying decline in the funds rate.

For the period as a whole, rate declines ranged around 60 basis points for Treasury bills, or somewhat more than the decline in Federal funds rates. Three- and six-month bills were auctioned last Friday at 4.27 and 4.50 percent, respectively, down from about 4.89 and 5.02 percent the day before the last auction. Similarly, a two-year Treasury note was auctioned yesterday to yield 5.37 percent, down from 5.86 percent on a like maturity a month earlier. Yield declines of some 50 to 70 basis points extended to Treasury maturities out to about 10 years, and long term issues were down by some 45 basis points.

In the corporate area, yield declines ranged around 30 basis points, while tax-exempt yields were down some 30 to 60 basis points. One factor supporting the municipal market was the New York court decision declaring unconstitutional the moratorium on repayment of New York City notes. While this decision has posed fresh problems for New York it has bolstered

investor confidence in the meaning of full faith and credit general obligations.

As a footnote to yesterday's discussion of non-borrowed reserves, this would have been another period when the Desk would have aimed for a higher funds rate in pursuing a nonborrowed reserve path. This would have occurred despite weakness in M_1 , in part because CDs and interbank deposits exceeded expectations.

Finally, I would like to report that the Desk began trading with three more dealers during the past month-- Bache-Halsey Stuart, Weeden and Co., and Carroll, McEntee & McGinley. These firms met our standards for volume and diversity of activity. This brings to 31 the number of dealers trading with the Desk--11 banks and 20 nonbanks. A year ago we traded with 27 dealers and 5 years ago with 21.