



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

STRICTLY CONFIDENTIAL (FR)
CLASS I - FOMC

TO: Federal Open Market Committee

DATE: January 6, 1984

FROM: Chairman Volcker

Attached for consideration is a draft statement--reflecting the consensus of opinion expressed in our discussion at the December FOMC meeting--that can be released to the public in the next week or two giving the Committee's view about the implications of the shift to contemporaneous reserve requirements for open market operating procedures. This statement will be considered at a telephone conference scheduled for 2:15 p.m. EST on Wednesday, January 11.

Also attached is the press release that the Board will issue on publication changes involved in the shift to CRR.

Attachments

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Beginning Thursday, February 2, the new contemporaneous reserve requirement (CRR) system will become effective. In that connection, questions have been raised about the implications of this change for the Federal Reserve's open market operating procedures. This issue has been considered by the Federal Open Market Committee. Taking account of technical transitional uncertainties as well as policy judgments about the role of M1 and other monetary aggregates under current circumstances, the Committee agreed to make no substantial change in current operating procedures for the time being.

Background

The new CRR system differs from the present lagged reserve requirement structure in two principal ways. First, required reserves against transactions deposits will have to be held on an essentially contemporaneous basis, instead of being lagged by two weeks. Second, the reserve holding period has been lengthened from one week to two weeks (with the relevant period for deposits also lengthened to roughly the same two weeks--the 2-week deposit period running from Tuesday to the second Monday, and the reserve period running from Thursday to the second Wednesday).

This structural change in the reserve accounting system has tightened the linkage between reserves and the current behavior of transactions deposits--demand deposits and interest-bearing savings accounts with full checking privileges (NOW accounts). These deposits, along with currency held by the public, comprise M1, the measure of money most nearly related to the transactions needs of the economy. But because M1 includes NOW accounts, which have grown substantially in volume over the past few

years, it is also affected by saving propensities and patterns. The Committee has been placing less weight than formerly on M1 because of the institutional changes that have altered its composition, affected its behavior, and increased uncertainties about its relationship to the economy.

Other, broader aggregates--M2 and M3--encompass M1 plus other highly liquid assets and forms of saving, such as money market funds accounts and time and savings deposits held at banks and thrift institutions. Some of these other assets also, in one degree or another, serve transactions purposes, though they are not, by law, subject to transactions reserve requirements. In general, the bulk of the assets in the broad aggregates are not subject to reserve requirements, although nonpersonal time deposits bear a relatively small lagged requirement.

Open market operations and CRR

Adaptations in open market operating procedures to CRR must take account of certain technical and transitional issues as well as the policy issue about the weight to be given M1 and other monetary aggregates in operations. The more technical and transitional issues involve how the depository system as a whole adjusts to the new reserve requirement system--which may influence demands for excess reserves, attitudes toward the discount window, and the speed of asset and liability adjustments generally. It can be expected that some time will elapse before banks and other depository institutions have fully adjusted their reserve management, as well as portfolio and liability management, to the new system. Money managers have to become accustomed to operating without certain knowledge of their required reserves for a full reserve averaging period during most of that period. In addition, usual start-up problems with new data systems will

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probably add to uncertainties at least for a while. Such data problems would also affect the timing and reliability of figures available to the Federal Reserve.

These technical issues aside, the new reserve requirement structure would potentially permit somewhat closer short-term control of M1 in particular. With CRR, if open market operations were geared primarily to M1, an "automatic" tightening or easing of reserve positions that worked to bring M1 under control would tend to occur somewhat more promptly than with lagged reserve accounting.

Whether operating procedures should be adapted for this purpose does not depend on the technical characteristics of the reserve requirement system in place but rather on broader policy judgments about the relative weight to be given to M1 as a target and the desirability of achieving close short-run control of that aggregate. With less weight placed on M1, and relatively more on broader aggregates less closely related to reserves, "automatic" changes in reserve pressures in response to short-run movements in M1 alone may not be appropriate.

In light of these various considerations--transitional uncertainties and the weight currently placed on M1 in policy implementation--the Committee agreed that no substantial change would be made in open market operating procedures for the time being. These operating procedures will be reviewed after a transitional period in the context of the role played by the monetary aggregates, particularly M1, in policy implementation and the potential implicit in CRR for achieving closer short-run control of M1.

CRR Statistical press release
1/6/84

For immediate release

The Federal Reserve Board today announced a series of changes in the content and timing of its statistical releases on money stock and reserves data that will occur with the forthcoming conversion to contemporaneous reserve requirements (CRR).

Under contemporaneous reserves, the reserve computation and maintenance periods will change from one to two weeks. Reserves will be maintained beginning two days after the opening of the computation period for transaction accounts. At present, there is a two-week lag from the beginning of the one-week computation period to the beginning of the one-week reserve maintenance period.

The initial computation period for required reserves on transactions accounts will begin Tuesday, January 31, and end Monday, February 13. The initial reserve maintenance period will begin Thursday, February 2, and end Wednesday, February 15.

Money stock and reserves data will continue to be issued on a weekly basis with the following changes:

Money Stock and Liquid Assets -- H.6

The H.6 will be published each Thursday at 4:15 p.m., one day earlier than now. It will be essentially unchanged in content. M1 and certain other deposit data will continue to be published weekly, but the figures will pertain to a week ending on a Monday, consistent with the CRR reporting cycle. The last publication of the current H.6 will be on February 10, and the initial publication of the new H.6 is scheduled for February 16. It is anticipated that the February 16 release also will contain revisions associated with the annual benchmark and

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seasonal factor review. Historical data reflecting all these changes will be available upon request as soon thereafter as possible; data for weeks ending on Monday, both seasonally adjusted and not seasonally adjusted, will be extended back to 1975.

Factors Affecting Reserves of Depository Institutions
and Condition Statement of F.R. Banks -- H.4.1

The H.4.1 will be published each Thursday at 4:15 p.m.--a day earlier than now--and will continue to show weekly average and Wednesday data for reserve balances at the Federal Reserve and factors affecting reserves during the week ended the preceeding Wednesday, including borrowing at the discount window. It also will continue to show the Wednesday condition statement for the Federal Reserve Banks, both consolidated and for each District separately. However, all reserves items that depend on a calculation of required reserves--such as excess reserves and total reserves--will no longer appear on the H.4.1; they will be shown on the H.3 on a two-week average basis. The last publication of the current H.4.1 will be on February 3, and the first publication on the new basis is scheduled for February 9.

Aggregate Reserves of Depository Institutions and Monetary Base -- H.3

The H.3 will be published each Thursday at 4:15 p.m., rather than the current Monday afternoon. All reserves items that depend on the calculation of required reserves--including total, nonborrowed and excess reserves and the monetary base--will be shown on the basis of averages of two weeks ended every second Wednesday, corresponding to the reserve maintenance period under CRR. Preliminary estimates of these two-week averages will be published for the first time on alternate Thursdays, with a lag of one day from the Wednesday end of the two-week reserve maintenance period. Data revisions will be published on

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intervening Thursdays. The last publication of the old H.3 will be on February 6 and the first publication of the new H.3 is scheduled for February 16. Final historical data for the reserves series on the old basis, including any revisions to most recent data, will be made available upon request.

As experience is gained about the magnitude of revisions to the published preliminary estimates of these two-week reserves series, consideration will be given to whether that publication schedule should be retained or perhaps delayed a week. Depending on this experience, consideration may also be given, on the other hand, to the feasibility of publishing estimates of weekly reserve series.

Weekly Summary of Reserves and Interest Rates -- H.9

The H.9--now published each Friday at 4:15 p.m.--will be discontinued, because each reserves item will be published on Thursdays on either the H.4.1 or the H.3, and interest rate data will continue to be published the following Monday on the release Selected Interest Rates -- H.15. The last H.9 will be published on February 3.

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In light of the substantial changes to data reporting and reserve computation and maintenance systems occasioned by CRR, transitional delays in meeting publication schedules for money stock and reserves data may occur initially and data revisions for a time could be larger than normal.

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