MEMORANDUM OF DISCUSSION

A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington, D. C., on Tuesday, January 16, 1973, at 9:30 a.m.

PRESENT: Mr. Burns, Chairman
Mr. Brimmer
Mr. Bucher
Mr. Coldwell
Mr. Daane
Mr. Eastburn
Mr. MacLaury
Mr. Mitchell
Mr. Robertson
Mr. Sheehan
Mr. Winn
Mr. Treiber, Alternate for Mr. Hayes

Messrs. Heflin, Mayo, and Balles, Alternate Members of the Federal Open Market Committee

Messrs. Morris, Kimbrel, and Clay, Presidents of the Federal Reserve Banks of Boston, Atlanta, and Kansas City, respectively

Mr. Holland, Secretary
Mr. Broida, Deputy Secretary
Messrs. Altmann and Bernard, Assistant Secretaries
Mr. Hackley, General Counsel
Mr. O'Connell, Assistant General Counsel
Mr. Partee, Senior Economist
Mr. Axilrod, Economist (Domestic Finance)
Messrs. Bryant, Gramley, Green, Hersey, and Hocter, Associate Economists
Mr. Holmes, Manager, System Open Market Account

Mr. Melnicoff, Deputy Executive Director, Board of Governors
Mr. Coyne, Special Assistant to the Board of Governors
Mr. Chase, Associate Director, Division of Research and Statistics, Board of Governors
Messrs. Keir, Pierce, Wernick and Williams, Advisers, Division of Research and Statistics, Board of Governors
Mr. Pizer, Adviser, Division of International Finance, Board of Governors
Mr. Wendel, Chief, Government Finance Section, Division of Research and Statistics, Board of Governors
Mrs. Rehanek, Open Market Secretariat Assistant, Office of the Secretary, Board of Governors
Mrs. Sherman, Secretary, Office of the Secretary, Board of Governors

Mr. Leonard, First Vice President, Federal Reserve Bank of St. Louis
Messrs. Eisenmenger, Debs, Parthemos, Taylor, Scheld, and Andersen, Senior Vice Presidents, Federal Reserve Banks of Boston, New York, Richmond, Atlanta, Chicago, and St. Louis, respectively
Messrs. Bodner and Doll, Vice Presidents, Federal Reserve Banks of New York and Kansas City, respectively
Mr. Davis, Adviser, Research and Statistics, Federal Reserve Bank of New York
Mr. Feldberg, Secretary and Assistant Counsel, Federal Reserve Bank of New York
Mr. Kaminow, Research Officer and Economist, Federal Reserve Bank of Philadelphia
Mr. Sandberg, Manager, Acceptance and Securities Departments, Federal Reserve Bank of New York
Mr. Bisignano, Economist, Federal Reserve Bank of San Francisco
Mr. Miller, Economist, Federal Reserve Bank of Minneapolis

By unanimous vote, the minutes of actions taken at the meeting of the Federal Open Market Committee on November 20-21, 1972, were approved.

The memorandum of discussion for the meeting of the Federal Open Market Committee on November 20-21, 1972, was accepted.

Chairman Burns noted that he and Mr. Bryant had recently returned from a trip to Europe, where they had attended the January Basle meeting and had held certain other conversations. He asked Mr. Bryant to comment on developments at the Basle meeting.

Mr. Bryant observed that, at their session on the afternoon of Sunday, January 7, the governors had continued the discussion of interest rate developments begun at their December meeting, on which Mr. Daane had reported to the Committee a month ago. The dominant impression he carried away was that the European central banks remained preoccupied with their inflationary problems and with possible policy measures to cope with those problems. As the members knew, short-term interest rates had risen markedly in Europe during the fall; the increases were particularly sharp in Germany, the United Kingdom, and France. Initially, the rate uptrend may have primarily reflected rising economic activity, but later it also reflected policy-tightening moves by monetary authorities. He had concluded from the general drift of the discussion at Basle that the shift toward greater monetary restraint might not have fully run its course. That had seemed particularly evident for Germany; indeed, the German Federal Bank had raised its discount rate again a few days after the Basle meeting. But the feeling seemed general at Basle that European interest rates might have to rise further to help moderate growth in monetary aggregates and credit demands.

It might be useful, Mr. Bryant continued, for him to report briefly on the comments by Chairman Burns at the Sunday afternoon session and the responses made by others. After reviewing developments in the real economy and in financial markets in the United States, Chairman Burns took note of the rise in European interest rates. He remarked that to some extent those rate increases were unavoidable and salutary, but that they also were a source of some concern. He went on to review the problems of economic stabilization in the United States, noting the importance of having the Economic Stabilization Act extended beyond its present expiration date of April 30, 1973. He observed that, while interest rates in the United States might well rise further as a result of market pressures, it was not likely that U.S. policy makers would deliberately seek higher interest rates for the purpose of limiting outflows of funds. Specifically, he noted that the Federal Reserve certainly did not want to see the United States undergo a credit crunch or recession in 1973 or 1974, and that it may not wish to take policy actions on balance of payments grounds if those actions would also create an undesired restriction of the domestic expansion. He expressed the hope that in formulating their own stabilization programs European policymakers would keep those considerations in mind; in particular, he suggested that they might want to place more emphasis on fiscal policy as well as wage and price policy and not lean quite so much on monetary policy.

Mr. Bryant noted that Mr. Zijlstra had picked up Chairman Burns' theme in his own remarks on the policy mix in European countries, and that he also had echoed some of the Chairman's sentiments about the need for the Europeans to avoid placing too great a burden on monetary restraint. However, comments by others disclosed some of the political constraints facing European policymakers. Many of the governors present were pessimistic about the prospects for adequate fiscal action in their countries, and with few options remaining, they expected that they would still have to rely primarily on monetary policy. That was the basis for his impression that monetary restraint might not as yet have run its full course in Europe.

An important question, Mr. Bryant remarked, was how the European authorities were likely to react if international rate relationships or other factors resulted in substantial flows of funds from the United States to Europe. It seemed to him that the authorities in most, if not all, of the affected countries were likely to tighten their capital controls. Chairman Burns and he had been told, for example, that in Germany and Switzerland existing controls on inflows of capital were judged to be fairly effective and that if necessary they probably could be tightened further. A similar attitude seemed to prevail in France. One might have doubts--as he did--about the effectiveness of such restrictions in the face of very strong incentives for movements of funds, but the authorities were nevertheless likely to rely on them.

Mr. Bryant observed that he would not say much about the U.S. balance of payments this morning; the staff was reevaluating the analysis of the outlook it had offered in connection with the chart show at the November meeting of the Committee, and it would be presenting the results of that reevaluation at the February or perhaps the March meeting. He might comment, however, on the attitudes towards the U.S. payments balance that were implied in remarks at the Sunday afternoon session of the governors and in some other conversations. In general, the Europeans' attitudes were very relaxed. They seemed to be focusing on the relative firmness of the dollar in exchange markets during recent months, and not to be carefully assessing recent data and reaching informed judgments about the prospects for improvement in the underlying balance. For example, they tended to place much more stress on the recent large increase in foreign purchases of U.S. equities than on the steep rise in November in the U.S. foreign trade deficit. His own view was that, while improvement was likely this year and next, the amount of improvement needed was very great indeed and the pace at which it would be accomplished was likely to be quite slow. It seemed to him that that prospect was not fully appreciated in Europe. He found the relaxed attitude of the Europeans to be disturbingly short-sighted, particularly since it was highly unlikely that the existing calm atmosphere in foreign exchange markets would persist throughout the year.

Chairman Burns said he might elaborate on Mr. Bryant's final comment. In the course of extensive conversations he had held during the trip in various European capitals--not only with central bankers but also with political leaders--he had found little sense of urgency about international monetary reform. It seemed to him that a number of factors were contributing to that situation. First, the dollar was firm and exchange markets were calm. Secondly, officials in the member countries of the European Community were preoccupied at present with the difficult problems associated with the entry of three new members. Third, there was a growing awareness that economic developments in any one European country were more heavily dependent on developments elsewhere in Europe than on those in the United States; the view that events in the United States were decisive for their own economies was much less firmly held by Europeans today than it had been a few years ago. Finally, and by no means of least importance, a number of European countries were faced with serious domestic political problems of their own. Obviously, where there was no effective government or the government was preoccupied with domestic concerns, no decisions could be expected on major international questions. It seemed clear that some time would have to elapse before conditions in those countries would be conducive to basic decisions on international monetary reform. While he was rather unhappy about the situation, it was necessary to face the fact that such decisions are not likely to be reached quickly.

Mr. Brimmer asked whether Chairman Burns was less optimistic now than he had been, say, around the end of the year, about the prospects for progress toward international monetary reform by the time the International Monetary Fund held its annual meeting in Nairobi next autumn.

The Chairman replied affirmatively. During his discussions in Europe he had stressed the need for making progress toward monetary reform, and he still expected that something would be accomplished by the time of the Nairobi meeting--if only because the various government leaders probably would be reluctant to come to the meeting without having achieved any agreements at all. Earlier, however, he had hoped that all of the basic political decisions would have been made before that meeting, so that--while the technical experts might still have to spend 12 or 18 months working out detailed arrangements--discussions among political leaders would no longer be required. He now considered that hope unduly optimistic.

Mr. Daane noted that at a 3-day meeting to be held in Paris next week the deputies of the Committee of 20 would be looking closely at the role of reserve assets, including gold and SDR's. Despite the rather discouraging situation with respect to attitudes that the Chairman had described, the U.S. representatives planned to press the U.S. views already submitted calling for the use of objective indicators, particularly reserves, in an effort to keep those proposals alive and to develop further momentum for them. As he had indicated at the December FOMC meeting, the deputies' group was large and rather cumbersome, and there were marked differences of view among its members.

Chairman Burns referred to Mr. Daane's comment regarding U.S. views and noted that the Sunday evening session at the Basle meeting had been devoted to a discussion of this country's proposals for international monetary reform. He had spent a good deal of time during the session in clarifying the proposals, since it was evident that the governors present were imperfectly informed about them and were laboring under certain misconceptions. The governors might eventually decide that they did not agree with the U.S. proposals, but any objections they had should no longer be based on misunderstandings.

In general, the Chairman continued, before agreements can be reached there must be mutual understanding, and before there can be understanding there must be extensive discussion. He hoped that members of the Federal Reserve family who were going abroad would familiarize themselves with the paper setting forth the U.S. proposals so that they could be messengers not only of goodwill but also of understanding. The paper did involve some problems of interpretation--as often was the case with an initial statement--and Mr. Daane and he, as well as Mr. Bryant and other staff members, would be happy to answer any questions that might arise concerning the intended meaning of particular passages.

Before this meeting there had been distributed to the members of the Committee a report from the Special Manager of the System Open Market Account on foreign exchange market conditions and on Open Market Account and Treasury operations in foreign currencies for the period December 19, 1972 through January 10, 1973, and a supplemental report covering the period January 11 through 15, 1973. Copies of these reports have been placed in the files of the Committee.

In supplementation of the written reports, Mr. Bodner made the following statement:

> As Mr. Bryant has indicated, the monetary screws were tightened another turn in a number of countries over the course of the last month but there was little change in exchange market conditions. Year-end adjustments and their unwinding have dominated the markets until the last couple of days, and with one or two exceptions, rates are little different from 4 weeks ago. The recent Federal Reserve discount rate increase

was followed by some hardening in Euro-dollar rates and a firming of the dollar. It has been interpreted in the European press as pointing toward a further tightening of U.S. policy.

Perhaps the most significant development with respect to the exchange markets per se was the January 1 reentry of Italy into full participation in the EC currency arrangements. The special exemption granted to the Italians, which had allowed them to support the lira through sales of dollars, was not renewed, and since January 1 the lira has been supported through sales of the strongest EC currencies, namely the Belgian franc and Danish kroner. One result of this was a sharp drop in the rate for the lira vis-a-vis the dollar which also pulled down the Belgian franc and Danish kroner rates. This has not produced any immediate market problems and intervention has been modest. Should the lira come under significant pressure, however, the potential is there for the same sorts of problems that we saw prior to the floating of sterling last summer. More immediate has been the effect on our ability to buy Belgian francs. We have continued to acquire francs on a daily basis, but we have not been able to increase the rate of acquisition, as I indicated at the last meeting we hoped to do, because our purchases of francs tend to push the franc up vis-a-vis the lira and to risk forcing additional intervention in lira by the Belgians. Consequently, the Belgians have not only been reluctant to see us increase our purchases of francs but, in fact, have asked that we cut back. In connection with this swap debt, the Committee will recall that at the last meeting I reported that we had received authorization from the Treasury to offer medium-term dollar-denominated notes to the Belgians. This proposition was discussed at the January Basle meeting but the Belgians were not receptive. Their position essentially was that they want to reduce their present uncovered dollar holdings and that they could not accept a nonguaranteed dollar-denominated investment in lieu of such a reduction. Despite these developments we have, as I noted earlier, continued to make some progress in reducing our Belgian debt; during this period we paid off another $25 million, bringing the debt down to $400 million.

The situation with respect to our Swiss franc indebtedness is still less satisfactory. Year-end adjustments and a general tightening of domestic liquidity resulted in a rise in the Swiss franc rate which put it above the level at which the Swiss were agreeable to our buying francs, with the result that in the past month we have paid off only $5 million. Moreover, liquidity conditions in Switzerland are expected to remain very tight at least through January. In fact, the Swiss National Bank already has offered to do swaps with their banks to cover end-of-January positions in the hope that they will be able to avoid taking in any dollars spot. Thus, the near-term outlook is not too encouraging.

This obviously is not a very satisfactory situation. I think it might be helpful for the Committee, as background in assessing this position, if I reviewed very briefly the techniques that we have used in the past to liquidate swap commitments. Essentially, we have employed five methods:

(1) Purchases in the market or directly from foreign central banks when flows of funds reversed and market conditions permitted such purchases. The bulk of System swap indebtedness over the years was repaid in this fashion.

(2) On occasion direct purchases were made from a foreign central bank even though the market situation had not turned around. These operations were possible mainly because nonmarket transactions had resulted in a decline in the dollar holdings of the central bank and it was prepared to rebuild its position through direct transactions with us.

(3) On a number of occasions when swaps did not prove reversible in the short run, the U.S. Treasury took over the debt through the issuance of medium-term securities denominated in the currency of the creditor.

(4) At times the Treasury drew on the IMF to provide the System with currencies needed for swap repayments.

(5) In some cases in which the market situation did not turn around and there appeared little prospect that it would, final settlement on swap drawings was made by the sale of reserve assets--mainly gold and SDR's, and on occasion other foreign currency balances.

> As the Committee is aware, alternatives 3, 4, and 5 are not now available to us. Alternative 2, that is, direct purchases from the foreign central bank, is open in principle, but both of our present creditors hold large uncovered dollar positions which they are anxious to reduce. In the case of Switzerland there may still be the possibility of arranging for some direct transactions but the most recent developments are not particularly encouraging in that respect. Consequently, we have been forced to rely on the first alternative, purchases in the market. In a situation in which the United States continues to run very substantial payments deficits, and both of our creditors are in surplus, liquidation of swap drawings through the market obviously is going to be a slow process. On the other hand, I think it should be remembered that in the period since August 1971, despite the continuing massive U.S. deficit and the unavailability of alternative means of settlement, we have been able to cut our debt almost in half to the present level of $1,565 million. The fact that these five techniques are the only ones we have used in the past, of course, does not necessarily mean that we are limited to them in the future, but so far neither we nor our colleagues abroad have been able to come up with alternative methods that do not ultimately involve one of these five approaches.

In reply to a question by Mr. Brimmer, Mr. Bodner said the discussion with the Belgians at the January Basle meeting of the possibility of their purchasing dollar-denominated notes from the U.S. Treasury was the most recent conversation on that question, but not the first. It had been thought that the Belgians might be interested in buying such notes in order to earn a higher yield on their dollar holdings. However, they felt that they could not make any investment which would imply that they were willing holders of the dollars at the present time, when they were in fact anxious to reduce their dollar position. Also relevant was the fact that the Belgians expected to be receiving more dollars in connection with final settlement on the lira intervention.

> By unanimous vote, the System open market transactions in foreign currencies during the period December 19, 1972, through January 15, 1973, were approved, ratified, and confirmed.

Mr. Bodner then reported that eight of the System's swap drawings on the National Bank of Belgium--accounting for $325 million of the $400 million total still outstanding--would mature for the sixth or seventh time in the period from February 2 through February 23. He hoped that it would be possible to make further progress in repaying the drawings during that period, but it seemed clear that renewals would still be required. Also, all of the System's outstanding drawings in Swiss francs would mature for the sixth time in the period February 9-13; they included two drawings on the Swiss National Bank totaling $565 million, and one drawing on the Bank for International Settlements of $600 million. Since each of the three swap lines in question had been in continuous use for more than one year, specific Committee action to authorize renewal of the drawings was required under the terms of paragraph 1(D) of the foreign currency authorization.

> By unanimous vote, renewal for further periods of 3 months of the eight System drawings on the National Bank of Belgium, the two drawings on the Swiss National Bank, and the drawing on the Bank for International Settlements maturing at various dates in the period February 2-23, 1973, was authorized.

The Chairman then called for the staff report on the domestic economic and financial situation, supplementing the written reports that had been distributed prior to the meeting. Copies of the written reports have been placed in the files of the Committee.

Mr. Partee made the following statement:

> The economic data available so far for December look a little less ebullient than in other recent months. Thus, nonfarm employment rose only marginally further last month, although the unemployment rate remained at the reduced 5.2 per cent level of November. The rise in industrial production is indicated to have slowed a little from the 12 per cent pace of the four preceding months. And the advance report on retail sales shows little further gain last month, though the weekly data had seemed to indicate a stronger pattern.
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> I would not want to point to these developments, however, as evidence that the pace of economic resurgence is moderating. First, the statistics in each case are preliminary, and might well be revised upward as has frequently been the case during the last half year or so. Second, earlier gains in all of the measures had been exceptionally large, so that the fourth-quarter averages for all--employment, output and retail sales--showed unusually large advances from the third quarter. Third, other indicators of activity, including new orders and order backlogs in durable goods manufacturing,

the amount and pattern of change in business inventories, and the behavior of the money stock, suggest growing underlying strength in the economy. Finally, qualitative information such as is contained in the red book[1] clearly points to a continued strengthening in business attitudes and plans.

Indeed, the business sector is now likely to provide the new major source of stimulus in the over-all performance of the economy. The recent Commerce-SEC survey of 1973 capital spending plans indicates a 13 per cent increase for the year, notably more than reported by the various private surveys conducted last fall. The projected rise appears amply supported thus far by the recent increases in output of and orders for business equipment and by the rising volume of contract awards for commercial and industrial building. As for inventories, the book value of stocks has been rising more rapidly since last August, but the over-all ratio of stocks to sales has continued to decline. In manufacturing, inventories of finished goods have actually fallen over the last 3 months, while purchased materials and goods in process have continued to rise. And there are more frequent reports of slower deliveries and developing imbalances between orders and supplies.

Such considerations have led us to increase slightly our projections for business fixed investment and rates of inventory accumulation over the year ahead. Business capital spending is now expected to rise 15 per cent for the year as a whole, and inventory accumulation to accelerate to a $16 billion annual rate by the fourth quarter of the year. These changes, along with the associated increases in income and consumption, raise the projected level of GNP for the year by $4-1/2 billion, and for the fourth quarter of 1973 by $7 billion. The growth in real output is still projected to slow as the year progresses, but it averages 5.7 per cent over the next four quarters. And because of the slightly faster growth in real output, the over-all unemployment rate is now expected to decline to 4.7 per cent by the fourth quarter.

1/ The report, "Current Economic Comment by District," prepared for the Committee by the staff.

The improvement in resource utilization implied by this projection is all to the good, but obviously it implies a using-up of most of the slack by the end of the year. Capacity utilization in manufacturing is estimated to rise only to the low eighties on the present index, but as noted at earlier meetings, measurement problems and difficulties in meeting current anti-pollution standards makes this index suspect. In any event, the availability of competent labor probably constitutes the limiting factor on output, and the projected decline in the unemployment rate for adult males--from 3.6 per cent this past quarter to slightly under 3.0 per cent by late 1973--suggests the development of a fairly taut labor market for experienced workers generally. Already, many of the District reports in the red book refer to shortages or tightness in the availability of skilled or qualified labor.

In these circumstances, it is especially disquieting to see the acceleration in wage rates that has taken place in recent months. Average hourly earnings in the private nonfarm sector, adjusted for overtime and interindustry shifts in manufacturing, rose at a 7.8 per cent annual rate in the August-December period. This was considerably faster than in the earlier months of the year--faster even than in the period preceding the August 1971 freeze--and it was very widely distributed by lines of activity. We have no good explanation for the speed-up, except to note that it was associated with a period of rapid over-all employment growth. But with labor markets expected to continue to strengthen, and with the stabilization program moving to a largely voluntary guidelines basis, the possibility exists that there may now be a persisting speed-up in the wage advance, extending to non-union as well as union workers. This would not be inconsistent with prior cyclical experience.

The recent upsurge in farm product prices is also disquieting, to say the least. It seems to me obvious that these increases will be passed on to the retail level in the weeks and months ahead and that the result will be an acceleration in the food price rise over at least the first part of 1973. Disproportionate increases in the price of food have been the main failure that the wage-price restraint program has had to face during the past year. Under the new program, food processors and retailers continue subject to mandatory controls, but they may pass on increases in raw agricultural product prices and in some other costs. Therefore, an accelerated rise in food prices is quite possible, and I am afraid that this would tend to discredit the whole Phase III program. It would certainly enter into workers' demands with respect to new wage agreements.

At this point, it is impossible to foresee how effective the Phase III program will prove to be. Prenotification and reporting requirements are substantially eased, a sizable part of the economy has been exempted from the program altogether, and there is an easing in the profit margin and price justification rules that previously have applied. But a voluntary program, forcefully administered, could still have a considerable influence on wage and price decisions, particularly where they involve big unions and big companies and tend to be of a pace-setting character. It is important to recognize, also, that the power to order rollbacks, and to subject individual industries to new mandatory standards, is retained by the Cost of Living Council. And the general 5-1/2 per cent guideline on "permissible" wage increases is to be continued, unless or until it is modified with the advice of the new Labor-Management Advisory Committee.

Nonetheless, it is hard to escape the conclusion that the new program is considerably looser than the old. There now appears to be latitude for a great many individual wage and pricing decisions to be biased on the higher side, so that average rates of increase in these measures are likely to accelerate, even if the major situations are still subject to effective constraints. The much less comprehensive reporting requirements also expose us to the risk that inflationary decisions will be taken and become facts of life before they receive public attention. We have not yet taken the new program into account in our formal economic projections, but I feel confident that it will lead us to add marginally to average rates of increase in employee compensation, profits, and prices.

> Under these circumstances, and with the economy showing great underlying strength, it seems to me more important than ever that aggregate demand management policies provide for a posture of firm and continuing restraint. We will be learning the details of the Administration's budget proposals before the end of this month, pending which the projection assumes NIA expenditures broadly consistent with unified budget outlays of $250 billion in fiscal 1973 and $270 billion in fiscal 1974. For monetary policy, the projection continues to assume a growth rate in M_1 of 6 per cent. This, of course, is well below the 8-1/2 per cent rate that actually materialized during the second half of 1972.

In reply to a question by Mr. MacLaury, Mr. Partee said the projected rate of unemployment for adult males, at 3 per cent or less late this year, would be somewhat lower and would represent a somewhat tighter labor market than in mid-1965, although the over-all unemployment would be about the same as at that time. The rate for males 25 years of age or more would be considerably below 3 per cent while the rate for those 20 to 24 years of age would be higher than 3 per cent.

Mr. Morris observed that it would be helpful to him and to other members of the Committee if Chairman Burns gave his appraisal of Phase III of the economic stabilization program that had been announced on January 11.

The Chairman commented that the official description of Phase III of the stabilization program had highlighted the voluntary or self-administered features, but he would emphasize other aspects of the program. Foremost, the new Labor-Management Advisory Committee would have the participation of the labor leaders who had abandoned the Wage Board, and that was a most constructive and hopeful development. Secondly, the Cost of Living Council retained a "big stick" in its authority to establish mandatory standards in particular industries, and if necessary, that stick would be used. All controls other than those on rents remained in effect. Rent controls had been eliminated in part because vacancy rates had risen. To be sure, prenotification of price increases was no longer required. Also, businesses had a somewhat greater degree of freedom in setting prices: the profit margin rule remained as a general guide, but alternatively, a business might raise prices to reflect increased costs without regard to its profit margin if its average rise in prices did not exceed 1.5 per cent a year.

Concerning wages, Chairman Burns continued, he had felt that the guideline needed to be reduced if progress was to be made in curbing inflation. However, it was necessary to obtain the participation of labor leaders in the new Advisory Committee, and it would not have been possible to do so if the guideline had been reduced in advance. In view of the unfavorable prospects for food prices, a near-term reduction in the wage guideline was most unlikely. In the period ahead, the important issue concerned the way the new structure of the stabilization program would be used to curb wage increases in the series of new contract negotiations, and a test would not be long in coming. With respect to the whole program, he was hopeful; but he shared some of Mr. Partee's skepticism that it would remain as tight as it had been.

In response to a question by the Chairman, Mr. Partee noted that important contracts involving the New York printers might be reopened shortly. The Rubber Workers' contracts began to expire in April, and at about the same time a new contract would have to be negotiated with the Chicago local of the Teamsters. In May the Electrical Workers would begin negotiations. Much later, in September, contracts involving the United Automobile Workers would expire.

Mr. Coldwell inquired about the staff's current estimate of the amount of overwithholding of 1972 Federal income taxes that would be refunded in the early months of this year.

Mr. Partee replied that the net effect that the new withholding schedule would have on refunds and final payments combined, as compared with a year earlier, was now estimated at

$8 billion. That was about $1 billion less than had been estimated earlier, but it was still a very substantial amount.

Mr. Winn inquired whether it was not more likely that Phase III of the stabilization program would operate to reduce rather than to raise profits.

In response, Mr. Partee commented that institutional rigidities might cause price increases to lag behind wage increases, inducing a temporary squeeze on profit margins. Over the past year, however, profits had expanded significantly less than the econometric model had indicated, which at least suggested the possibility that profits and profit margins had been limited by the controls. To the extent that was the case, efforts to restore profit margins were to be expected wherever the latitude existed. In that connection, firms with sales below $50 million were not required to keep records of price changes, or of their impact on profit margins, for possible scrutiny by the agents of the Cost of Living Council.

Mr. Mayo asked Chairman Burns whether he thought Phase III would make his task as Chairman of the Committee on Interest and Dividends easier or more difficult, and he asked for the Chairman's evaluation of the prospects for extension of the Economic Stabilization Act.

The Chairman replied that the task of the Committee on Interest and Dividends would be more difficult--perhaps very much more so. He was presently reappraising the role of that Committee. With respect to the Economic Stabilization Act, he thought it would be extended--after a considerable amount of debate. He had been concerned about the possibility of enactment of a new provision calling for mandatory ceilings on interest rates, but that now appeared unlikely.

In reply to a question by Mr. Balles, Chairman Burns affirmed that the Committee on Interest and Dividends' concern with respect to interest rates remained centered on administered rates and not market rates, and thus there was no potential conflict with the role and functions of the Federal Open Market Committee.

Mr. Brimmer observed that a number of deferred wage increases provided for in contracts negotiated a year or two ago would take effect during the course of this year, and both the number of workers involved and the size of some of the increases were substantial. He inquired about the impact of those increases on the outlook for the average rise in wages this year.

In response, Mr. Wernick remarked that deferred wage increases in 1973--increases that took effect in the second and third years of contracts--generally were not as large as those in 1972. In the case of contracts that contained cost-of-living provisions, however, average wage increases this year would depend on the behavior of prices. It was of great importance for wage developments in 1973 that the number of workers covered in contracts to be negotiated was substantially larger than in 1972 and that many of the negotiations were in important industries.

Mr. Partee added that a number of contracts that had been negotiated during Phase II contained provisions for renegotiation in the event of termination of the controls program, but the President's Executive Order establishing Phase III specifically declared such provisions inoperative as unreasonably inconsistent with the goals of the stabilization program. With reference to his earlier statement that there now appeared to be greater latitude for wage decisions to be biased on the higher side, he had in mind the nonunion situations involving clerical and other office workers as well as skilled and nonskilled production workers in manufacturing. Increases in wages in these cases had been subject to the general guideline under Phase II and they remained so under Phase III, for the present, but it seemed to be a widespread interpretation--in the press and elsewhere--that the guideline no longer applied to workers employed by firms whose workforce numbered less than 1,000.

Chairman Burns remarked that he had learned from some well informed observers that labor union leaders were counting on achieving wage settlements about 1 percentage point above the present guideline. He asked Mr. Wernick whether he had heard anything about the leadership's objectives.

Mr. Wernick replied that he had not heard of any general standard to be applied to the upcoming negotiations. The dominant theme was that the unions would attempt to negotiate "reasonable" settlements, and what was reasonable would depend on the particular case.

Mr. Heflin commented that he had the impression from the red book and also from conversations with the Richmond Bank's directors and with businessmen generally in the Fifth District that shortages of labor and other supply bottlenecks had become serious problems in a number of industries. In some cases, shortages of materials were being attributed to the workings of Phase II controls over prices and profits. Noting that the green book[1/] had not dealt with the subject, he asked Mr. Partee for his assessment of the possible impact of labor and materials shortages on the chances for achievement of the staff projections for total real output.

1/ The report, "Current Economic and Financial Conditions," prepared for the Committee by the Board's staff.

Mr. Partee replied that he too had been impressed by the number of Districts that had mentioned labor shortages and supply bottlenecks. As far as the statistics were concerned, the sharp decline over the autumn months in the unemployment rate for males 25 years of age and over also suggested that some labor supply problems might be developing. Generally, however, the statistics on unemployment and capacity utilization were not available in sufficient detail to permit a very good appraisal of the limitations that the available supply of labor and materials might impose on growth in total output throughout 1973.

As he had observed at previous meetings, Mr. Partee continued, business managers encountering persistent difficulties in association with rising rates of resource use would seek solutions to their problems. With respect to labor, the solution would take the form of some geographic widening of the search into areas of greater unemployment, resulting in some movement of workers, and it also would take the form of training programs to equip the available labor to perform the necessary tasks. Accordingly, it was possible for real output to grow at an average rate of 5.7 per cent from the fourth quarter of 1972 to the fourth quarter of 1973. However, that might be about as much growth as could be achieved, and as the year progressed, more and more bottlenecks would become visible. The staff projections, incidentally, did not allow for any major work stoppages that might occur during the year.

Mr. Morris commented that the rate of growth in the labor force as well as the current rate of unemployment needed to be considered in appraising the potential growth in output. The over-all unemployment rate, at 5.2 per cent in December, was lower than in early 1963 when the preceding business expansion was at a comparable stage, but the labor force had been growing more rapidly in the recent period. If the rate of growth remained more rapid, it would constitute some degree of offset to the lower unemployment rate.

In response, Mr. Partee noted that the staff projections suggested an increase of 1.7 million in the civilian labor force from the fourth quarter of 1972 to the fourth quarter of 1973. That was about 800 thousand less than in the preceding year, when Vietnam veterans entered the labor force in large numbers, but it was still 500 to 600 thousand above the annual rate of increase in the early 1960's. Accordingly, the projected unemployment rate declined less in relation to the projected rate of increase in output than it otherwise would.

In response to a question by Mr. Brimmer, Mr. Wernick observed that in the period ahead growth in the labor force would be concentrated among young men to a much greater degree than in the mid-1960's. While that might suggest that more training would be required to absorb them into the work force, they were probably better educated than comparable age groups in past periods.

Mr. Kimbrel observed that labor shortages had also been developing in the Sixth District. Nevertheless, he was as much or more concerned that businessmen seemed to have become convinced that inflation was inevitable. Their impression of the recent course of monetary policy had contributed to that view, although hopefully the Chairman's speech at the American Economic Association convention in late December and last week's decision to increase the discount rate had had beneficial effects. Businessmen were also concerned about the course of fiscal policy: while they believed in the sincerity of the Administration's efforts to limit over-all Federal spending to $250 billion in this fiscal year, they noted that every announcement to close a military installation or to reduce spending for agricultural programs or to cut subsidies for housing was met with objections from members of the Congress.

Given their belief in the inevitability of inflation, businessmen were likely to offer less resistance to wage and price increases. The consequences could be considerable in the Sixth District which had a relatively large number of firms that did not have to maintain wage and price records under the rules of Phase III.

Chairman Burns observed that, according to a table in the green book, average hourly earnings in a number of industries had increased sharply from November to December. In mining, average earnings had risen at an annual rate of 30 per cent. He asked whether a large number of anniversary increases had gone into effect in that period.

In response, Mr. Partee noted that after the wage-price freeze ended and Phase II began in mid-November 1971, a number of postponed wage increases went into effect almost immediately, and a strike in the coal mining industry was also terminated at about the same time. That probably altered the timing of some subsequent increases and distorted the data for December 1972. Partly for that reason, the staff tended to analyze changes in hourly earnings over periods of several months. In any case, the staff would provide a more detailed explanation of the December data.

Chairman Burns asked the staff to consider and make recommendations for policies that might help to improve control over food prices during the next 6 months and to influence the behavior of wage rates.

Turning to the Federal fiscal outlook, the Chairman observed that he had been hopeful that the Congress would reform its procedures for dealing with the budget so as to establish some over-all control on expenditures. Now, however, he was convinced that such reform would not occur in the near future.

Before this meeting there had been distributed to the members of the Committee a report from the Manager of the System Open Market Account covering domestic open market operations for the period December 19, 1972, through January 10, 1973, and a supplemental report covering the period January 11 through 15, 1973. Copies of both reports have been placed in the files of the Committee.

In supplementation of the written reports, Mr. Holmes made the following statement:

> The monetary aggregates expanded rapidly over the period since the Committee last met, exceeding the tolerance ranges for RPD's, M_1, and M_2. Open market operations, as a result, were used to hold back non-borrowed reserve growth, although through much of the period even-keel considerations involved in the Treasury's long-term bond offering inhibited

the Desk from pressing as hard as otherwise would have been desirable. By the end of the period, however, the Desk was seeking a degree of reserve restraint that was expected to result in a Federal funds rate of 5-3/4 to 5-7/8 per cent, the latter rate being the top of the range of tolerance for that rate set by the Committee at the last meeting.

The debt markets reacted in a mildly unfavorable fashion to the discontinuation of most mandatory wage and price controls on the assumption that it would be more difficult to restrain wage and price increases under a voluntary program. The extent to which Phase III controls succeed, or fail to succeed, in bringing about adequate restraint will do much to shape the market's attitude about the future course of interest rates. The market's reaction to Friday's change in the discount rate was almost nonexistent, with most market participants viewing the rise to 5 per cent as having been long overdue. There is a fair amount of uncertainty in the market, however, as to how much firmer monetary policy may have to become during the Phase III period. Desk operations in the period ahead are apt to be closely scrutinized by the market as it tries to assess whether the discount rate rise was just a delayed reaction to a rise in market rates or whether it may be a signal of a general firming of policy.

Short-term interest rates generally backed up only a few basis points yesterday, while prices of coupon issues were mixed, as encouraging reports on peace negotiations tended to offset any potential impact of the discount rate increase. In yesterday's regular Treasury bill auction, average rates of 5.28 and 5.54 per cent were established for the new 3- and 6-month bills, up 19 and 24 basis points from the rates established in the auction just preceding the last Committee meeting. During the period, good investor demand--part of it seasonal--tended to restrain the upward pressure on bill rates stemming from the rise in the Federal funds rate, a substantial amount of foreign selling, and the reluctant supply of reserves by the Desk.

The Treasury's innovative auction of a long-term bond early this month generated more interest from Government securities dealers and other professionals than had been expected. It had been anticipated that most dealers would be quite cautious in bidding in an auction in which all awards were to be made at a uniform "stop-out" price. In fact, aggressive dealer bids tended to shut out long-term investors, who had been thought to have enhanced interest in this type of auction. A uniform price of 99-1/2 was established for the 6-3/4 per cent bonds, but the oversupply in dealer hands put pressure on the new issue which closed last night at 98-29/32 where it yielded 6.85 per cent compared to the original yield of 6.795. The downward drift in the price of the new issue was cushioned to some extent by purchases by a Treasury investment account and continued buying of other coupon issues by foreign accounts. While enough distribution of the new issue has been accomplished to free the System from even-keel constraints, there are still sizable blocks that have yet to find a final resting place. Other tests of the Dutch-auction technique will be needed before a judgment can be formed as to the value of this technique in the Treasury's debt management kit. The first one certainly did not turn out quite as expected.

Looking ahead, the Treasury will be announcing on January 31 a refunding of February 15 maturities of which $4.8 billion are held by the public. Even-keel considerations will thus come into play as we near the end of January. Accordingly, if the Committee decides to restrain growth of the aggregates--in light of the rather strong advance indicated in the blue book[1/]--the Desk should be quite prompt to move to a less accommodative reserve-supply posture.

The System holds about $1.9 billion of the maturing February issues. I would plan to roll this amount over into whatever new issue or issues the Treasury offers in a proportion similar to that expected from public subscription.

1/ The report, "Monetary Aggregates and Money Market Conditions," prepared for the Committee by the Board's staff.

Open market operations were constrained by even-keel considerations over much of the period, but the System became an increasingly reluctant supplier of nonborrowed reserves as the period progressed, particularly when banks added to reserve availability through heavy borrowing at the discount window. The holiday period brought its own problems as the long Christmas and New Year weekends appeared to cause banks difficulties in their reserve management strategy. Reserve projections again turned out to be highly unreliable, with massive misses over 2 weekends. As a result the Desk again had to rely heavily on temporary injections and withdrawals of reserves, with \$3.8 billion of matched sale-purchase agreements and \$3.6 billion of repurchase agreements entered into through last night. With the money market tightening this morning and the funds rate moving up to 6-1/2 per cent, the Desk has injected a large amount of reserves.

Looking ahead, I should note that the narrowed range of tolerance for RPD growth and the aggregates contained in the blue book will, as noted there, be likely to call for somewhat greater movement of the Federal funds rate in the period between Committee meetings. Given the difficulties in projecting the appropriate relationships between RPD's, the aggregates, and the Federal funds rate, the risks of conflict between objectives may well be increased. This may require more consultation between regular Committee meetings than has been the case heretofore. I should also note--for what it is worth--that the New York Bank forecast for M_1 growth in January is only 2 per cent, well below the Board staff's 7 per cent. For the first quarter as a whole, however, the New York forecast is a little stronger than the Board staff's 7-1/2 per cent. I would assume, given the size of money growth in recent months, that the Committee would prefer to ignore any temporary shortfall from its longer-term growth path, if we should be fortunate enough to have one.

Mr. Daane asked Mr. Holmes whether he thought it would be feasible to conduct open market operations with narrower ranges specified for both the funds rate and the aggregates without scheduling more frequent consultations of the Committee. He recalled that Mr. Holmes' response to a similar question at an earlier meeting had been that the Committee had been fortunate in not encountering conflicts between its objectives and it should not expect its good fortune to persist. With respect to the immediate situation, he asked what the implications might be for the funds rate and other interest rates if operations to slow the rate of growth in the aggregates were undertaken promptly and continued until the start of even keel.

Mr. Holmes replied that narrowing the ranges for the aggregates would increase the probabilities of encountering conflicts among the Committee's objectives relatively early in the intermeeting period and thus would increase the probabilities of the need for Committee consultations between regular meetings. With respect to the second question, the effect on the funds rate and other short-term interest rates would depend on the degree of restraint the Committee wished to pursue. The main point was that operations to restrain growth would need to be accomplished over the next 10 days, prior to the start of even keel.

Chairman Burns observed that if the Committee widened the range for the funds rate at the same time that it narrowed the ranges for the aggregates, the probabilities of a need for intermeeting consultations might well be reduced.

Mr. Mitchell asked Mr. Holmes whether the Desk had injected a large volume of reserves that morning--as he had reported--because of a concern about the influence of a 6-1/2 per cent funds rate on the market that day or a concern about its influence on the average funds rate for the statement week.

In response, Mr. Holmes said he was concerned primarily with the effect on the weekly average. Given the strength in the aggregates, he thought the Desk should be moving the funds rate toward the upper end of the specified range of tolerance, and it had been aiming at a rate of 5-3/4 per cent to 5-7/8 per cent. At the same time, however, he would be concerned about the effect that a sharp rise in the rate would have on market attitudes if the Desk showed no willingness to resist the rise.

Mr. Mitchell then asked whether the Desk's ability to pursue the Committee's objectives had been hampered by the money market banks' large volume of borrowings at the discount window.

Mr. Holmes replied that early in the period since the last meeting the Desk had wanted to achieve some modest firming--despite the Treasury financing--but it had experienced difficulty in keeping the funds rate up because some banks preferred to borrow at the discount rate rather than to borrow at the higher rate for Federal funds. That was not the situation in the current week, however, because some banks that had borrowed heavily over the preceding 2 weeks now appeared to have decided to avoid the discount window in the current week on the grounds that they might wish to use it again 2 weeks later.

In response to questions by Messrs. Mitchell and Daane, Mr. Holmes observed that a rise of as much as 50 basis points in the funds rate over the 10-day period before the start of even keel would be a rather substantial change. Nevertheless, he was not sure that a rise of much less than that would go very far toward slowing the rate of growth in the aggregates.

Mr. Mitchell remarked that the funds rate had moved up about 100 basis points in a relatively short period in the late spring and early summer of 1971 in conjunction with System efforts to slow the rate of growth in the aggregates. With respect to the period ahead, therefore, he wondered why 50 basis points was regarded as the largest increase that might be tolerated.

In response, Mr. Holmes noted that there were only 2 weeks in the period immediately ahead before the start of even keel, and the even-keel period would extend to the middle of February. Consequently, any rise in the funds rate before the next Committee meeting could not be spread over the 4-week period.

Chairman Burns observed that even keel did not mean absolute rigidity of rates, especially when the Treasury was engaged in financings with the frequency that it would be in the current period. The funds rate could inch up during an even-keel period.

In response to additional questions, Mr. Holmes said if the Treasury should decide to use the auction technique in the forthcoming financing, even-keel constraints on open market operations would be relaxed. In the auction, nevertheless, the price of the issue or issues would be determined on the basis of the market's current assessment of monetary policy. To make a sudden or sharp shift in monetary policy just after the auction would be to change the rules of the game to the disadvantage of both the market and the Treasury. Alternatively, if the Treasury did not use the auction technique and monetary policy shifted just after the issues were priced, the financing could well be a failure. How much tightening might be accomplished during an even-keel period was difficult to forecast, and it was risky to depend on achieving any. It was better to get the new money market conditions established in advance of a Treasury financing so that the market would have a chance to adjust. With respect to the period immediately ahead, a rise in the funds rate even to 5-7/8 or 6 per cent in the wake of the recent increase in the discount rate would be interpreted by the market as a move toward further restraint.

Mr. Coldwell noted that the Treasury had used the auction technique in its financing around the turn of the year, and he asked why even keel had been so much of a constraint on System operations. Also, he inquired whether less of a constraint might have resulted in a better initial distribution of the issue between dealers and investors.

Mr. Holmes replied that the Treasury had issued a long-term security--the first in a long time--which required much greater caution in System operations than if the issue had been, for example, a 2-year note. With respect to the issue's distribution, the dealers might have backed away from the offering altogether, with adverse consequences for its success, had there been an atmosphere of much more uncertainty in the market on the eve of the auction.

Mr. Brimmer observed that if the Treasury were going to innovate in its financing operations, as it had in the recent financing, even keel could become more than the traditional kind of constraint on open market operations. Noting that the blue book had suggested that a relatively conventional exchange offering seemed most likely in the forthcoming financing, he asked whether Mr. Holmes had a view as to the Treasury's likely course.

Mr. Holmes said the Treasury was not likely to innovate in its next financing. With respect to the traditional options, he did not think the Treasury had yet focused on the choice.

Mr. Bucher remarked that since November 1 the Federal funds rate had risen about 60 basis points but that yields on long-term securities had changed little. That was a very favorable record--especially from the political point of view--and he asked what the prospects were that it would continue.

Mr. Holmes replied that, although less reaction in long-term than in short-term rates was to be expected, the long-term rates were unlikely to remain stable in the period ahead unless they benefited from especially good news with respect to Federal Government expenditures and a cease fire in Vietnam. Such factors as a large volume of corporate internal funds and a relatively light calendar of offerings of municipal securities might mitigate the upward pressures on long-term rates, but some rise was likely.

By unanimous vote, the open market transactions in Government securities, agency obligations, and bankers' acceptances during the period December 19, 1972, through January 15, 1973, were approved, ratified, and confirmed.

Chairman Burns remarked that before calling for Mr. Axilrod's report on prospective monetary developments, he would make some observations about the recent record. While the behavior of the monetary aggregates in December had been disappointing, it had to be viewed in the perspective of a longer period of time; monthly figures were not reliable indicators of developments. Over the year from the third quarter of 1971 to the third quarter of 1972, M_1 grew 5.6 per cent. In the same period real GNP and the current dollar value of GNP grew 7.2 per cent and 10.1 per cent, respectively. From the fourth quarter of 1971 to the fourth quarter of 1972, M_1 grew 7.2 per cent while real and nominal

GNP--according to calculations based on staff estimates for the fourth quarter of 1972--grew 7.8 per cent and 10.9 per cent, respectively. Over the half year from the second to the fourth quarter of 1972, M_1 grew at an annual rate of 7.3 per cent and real and nominal GNP grew at rates of 7.6 per cent and 10.1 per cent, respectively. In all three periods, growth in M_1 was less than that in real GNP and very much less than that in nominal GNP.

The Chairman went on to say that on the basis of the newly revised monetary statistics that appeared in an appendix table in the blue book prepared for today's meeting, rates of monetary growth differed somewhat from those he had cited. Growth in M_1 was 6.2 per cent rather than 5.6 per cent over the four quarters to the third quarter of 1972 and 7.5 per cent rather than 7.2 per cent over the four quarters to the fourth quarter of last year. In both cases, monetary growth was still less than growth in real GNP. However, over the half year from the second quarter to the fourth quarter of last year, the annual rate of growth in M_1 was now 7.7 per cent rather than 7.3 per cent, and it was thus a little higher rather than a little lower than the rate of growth in real GNP in the same period.

Continuing, Chairman Burns observed that the record he had cited was a reasonable performance. Nevertheless, monetary growth had been too rapid, especially in the latest 2 months.

Performance had not been better in part because of the Committee's procedures. The ranges of tolerance specified for growth in the aggregates were too wide. Had the ranges been narrower--and, consequently, the upper limits lower--conflicts between the specifications adopted for the aggregates and for the funds rate constraint probably would have occurred. In that event, the Committee would have had to consult between meetings and might have changed its policy. In view of that, the ranges for the aggregates contained in the blue book prepared for today's meeting were narrower than they had been in the past. That might provide the Committee with an opportunity to come closer to achieving its targets for monetary growth.

Mr. Axilrod made the following statement on prospective monetary developments:

> If the Committee should decide today to bring growth in the aggregates down into ranges something like those specified for alternatives B or C, it appears to us that money market conditions would be likely to tighten further over the next few weeks. If this happened, one question that may arise would be whether over-all credit market conditions, and banks and other financial institutions, will adjust smoothly to constraints on bank reserves that result in a Federal funds rate of about, say, 6 to 6-1/4 per cent or a little above.
>
> Following the seasonal lull in the latter part of December and early January, capital markets are once again being tested by new corporate and municipal bond issues. Rather prompt syndicate termination of two recent private issues and the decline in price of the new Treasury bond following the auction indicated some

nervousness in markets, influenced by the viscissitudes of Vietnam peace negotiations and also the money supply. But these developments do not yet suggest--I would say--any fundamental reappraisal that the outlook for longer-term bonds has become significantly more bearish, particularly given the renewal once again of prospects for peace.

The technical condition of capital markets appears good at this point. Despite some residual floating supply of the new 20-year Treasury bond, U.S. Government security dealers have a sizable net short position in securities maturing in over 5 years. Thus, they are well hedged. In corporate and municipal markets, the calendars for January and February remain quite moderate, and well below year-ago levels.

I do not mean to be suggesting that long-term markets will not adjust upwards in yield should Friday's discount rate action be followed by a noticeable further firming of money market conditions. I think that long-term interest rates would rise, but at the moment--given the current demand outlook and the position of dealers--I doubt that any rise would have strong, cumulative aspects or give the appearance that a credit crunch might be in the making. And the extent of any near-term upward adjustment in bond yields may, of course, be dampened if peace negotiations are successful or if, over time, monetary policy appears to be keeping growth in the aggregates to a relatively modest pace.

Assuming psychological factors influencing long-term rates are not more unfavorable than now, and may even become more favorable, the chief danger to the stability of credit markets comes from the institutional side. Again, I do not think that this represents an immediate threat. But there are some cautionary signs that should be mentioned.

Deposit growth at nonbank thrift institutions, though remaining generally ample, did slacken in the fourth quarter. I would expect some further erosion in growth if short-term market rates advance further, given current ceiling interest rates on deposits, although placement of income tax refunds in savings during the next 2 months may provide a temporary fillip.

Some erosion may also be expected in flows of savings into banks as market rates advance. If demand deposit growth is held down as well, and with U.S. Government deposits likely to be draining funds, net, from banks over the next few months, bank credit expansion--as measured by the proxy--may well slow considerably from the 11-1/2 per cent rate of 1972. With business loan commitments high, and take-downs expected to be at least as rapid as over the past few months, banks will need to cut back on other loans and investments, and to bid aggressively for CD funds.

Thus, one can see that institutional adjustments, particularly by banks, could add to rate pressures in short-term markets and also in longer-term markets. But these upward rate adjustments are likely to be kept within reasonable bounds, and the flow of funds is not likely to fall off drastically in an environment of somewhat tighter money market conditions. However, if the funds rate were to move persistently above the 6-1/4 to 6-1/2 per cent level, the sustainability of such elements in the financial picture as time deposit ceiling rates at banks and other institutions may come into question.

The conditions described for credit markets and financial institutions are, it seems to me, an argument for moving cautiously, but not too cautiously, in open market operations. The flow of savings into institutions is still strong enough, and the liquidity of corporations and individuals ample enough, to suggest that there is some cushion to adjust smoothly to interest rate increases.

As to the timing of open market operations, the Treasury announcement on January 31 of terms for the mid-February refunding means that practically all of any money market tightening that turns out to be required has to be accomplished over the next 2 weeks. If money market conditions do tighten further in that period, there are some odds that little further tightening might develop. The material we have looked at in preparing the blue book gives contradictory signals, but some of our models did indicate that past interest rate increases are sufficient to begin to have a significant slowing effect on money demand in the spring and summer of 1973. That may or may not be of any comfort, but at least to me it suggests that the Committee at this point need not necessarily view any tightening, should it evolve, of money market conditions over the period immediately ahead as the first stage of a progressive tightening.

Mr. Coldwell observed that in his view the fundamental forces of economic expansion were gathering momentum and the monetary aggregates were growing at an excessive pace. While, as the Chairman had said, the monthly figures for the monetary aggregates were not dependable indicators, many of the people who followed monetary developments were influenced by the monthly statistics, and the Committee had to consider that. For the period ahead, one issue deserving attention was the rate at which credit demands developed. Credit demands of the private sector and of the Federal Government would be strong, and flows of funds from the United States to other countries might be a complicating factor. At the same time, a rise in interest rates--including a slow advance in long-term rates--was likely.

Continuing, Mr. Coldwell said the ranges of tolerance for the aggregates should be narrowed and the range for the funds rate widened. As he had suggested at previous meetings, the Desk could intervene less in the market and allow the funds rate to fluctuate more freely and still would be able to hold the weekly average within the specified range.

With respect to policy, Mr. Coldwell commented that it was necessary to limit reserve injections and slow the rate of growth in the aggregates, especially now that the controls on wages and prices had been weakened, at least superficially. If interest rates rose further in consequence, that was a necessary price of limiting monetary stimulation to economic activity. About once every 8 or 10 years the Committee had the opportunity to contribute toward an equilibrium of growth with greater economic stability, and he hoped the Committee would act to moderate the pace of expansion and avoid another round of inflation.

Mr. Brimmer observed that while month-to-month fluctuations in the aggregates might be large, monetary growth over the past few months had been substantial. In the months ahead, the demand for money was likely to expand further, and even though the rate of monetary growth might recede, it was not likely to recede enough to provide an offset to the December bulge. Given the strong prospects for economic activity that Mr. Partee had described and the recent change in the economic stabilization program, now was the time to adopt lower targets for rates of growth in the monetary aggregates and deliberately bring about a higher level of short-term interest rates. Taking note of Mr. Holmes' remark that a rise in the funds rate above 5-7/8 per cent to 6 per cent immediately would lead the market to conclude that the increase in the discount rate had been more than a passive adjustment to market rates, he suggested that the Committee should decide to encourage market participants to perceive that increase as indicative of a change in the posture of monetary policy.

Mr. Brimmer went on to say, with reference to Chairman Burn's remarks on rates of growth in M_1 and in real and nominal GNP, that he would stress the time lag in the relationship. Although he did not know how long it might be, there was a substantial lag between policy actions affecting the rate of growth in the monetary aggregates and the impact of those actions on output and employment. Actions taken today should be viewed as affecting developments 6 to 9 months in the future. Moreover, the recent rates of monetary growth, which had been well above the Committee's targets, had to be taken into account. An effort should be made to compensate for those high rates, and he noted that Mr. Axilrod had suggested that it could be done without creating a credit crunch. Higher interest rates now had to be accepted as a by-product of monetary restraint.

Mr. Eastburn remarked that he would agree with Chairman Burn's observation that monetary growth had been too fast. That was especially the case for 1972 as a whole, and in coming months it was necessary, to the extent possible, to compensate for the excessive rate of growth. Although he favored the longer-run monetary growth rates of alternative B of the draft directives,[1] represented by an annual rate of growth between 5 and 6 per cent for M_1, he favored lower rates in the short run in an effort to avoid exceeding the target again.

Continuing, Mr. Eastburn observed that the reasons for exceeding the targets no doubt were complicated, but as he had argued at the last meeting, the Committee's method of operation was a contributing cause. Reliable information on the behavior of the aggregates was not available early enough in the inter-meeting period to provide a basis for a shift in money market conditions to the degree consistent with achievement of the Committee's targets. Because there was always some doubt about the significance of the first week's data, there was a tendency to wait a week or two for confirmation, and by that time it was no longer possible for the funds rate to move up sufficiently--especially if there should be a constraint on the amount the rate should move in a single week.

That problem, Mr. Eastburn went on to say, was particularly relevant in the period immediately ahead because of even keel. By the time reliable information concerning the aggregates became available, the Treasury would be in the market. To get

1/ The alternative draft directives submitted by the staff for Committee consideration are appended to this memorandum as Attachment A.

the funds rate up sufficiently, therefore, it would be necessary to give primary emphasis to the funds rate rather than to the aggregates. Specifically, the funds rate should be moved up as rapidly as possible to 6-1/4 per cent. During the remainder of the intermeeting period--if even keel permitted--it should be moved up further toward 6-1/2 per cent. If shortfalls in growth in the aggregates occurred, they would be welcome offsets to the recent excesses.

Mr. Holmes commented that because of the uncertainty surrounding the monetary statistics for any one week, it had generally been understood that they should not be taken as a basis for operating decisions. As a result, the response to excessive strength in the aggregates was likely to be delayed. On the other hand, there were frequent occasions when one week's statistics suggested strength that subsequently disappeared when the data were revised, and clearly it would have been a mistake to have based decisions on the original figures.

Mr. Balles remarked that he agreed with much that Messrs. Brimmer and Eastburn had said about the need for lower rates of monetary growth. The net result of Phase III might well be more rapid rates of rise in wages and in prices and thus a heavier burden on monetary policy to contain inflationary pressures.

At the same time, evidence of a very strong economy was accumulating rapidly, and some observers foresaw boom conditions approaching. In view of the lag with which monetary policy affected the course of economic activity, expansion in the monetary aggregates at rates above those that had been specified at recent meetings was a source of concern. The objective of slowing monetary growth from the third quarter to the fourth quarter of 1972 had not been achieved. Now, it would be better if any errors that occurred were in the direction of shortfalls.

Continuing, Mr. Balles noted Chairman Burn's expressed concern to avoid a credit crunch from developing this year and said the chances of a crunch occurring became greater when the aggregates were allowed to grow too rapidly, thereby creating the necessity for extremely restrictive action later on. Monetary history suggested that the main cause of large swings in policy was the failure to take early action to slow the rate of monetary growth because of a desire to have a slow and gradual upward adjustment in interest rates. At the present time, it would be better to take the risk--if that was what it was--of a rise in short-term interest rates in order to hold monetary growth down to a rate that was consistent with the containment of inflationary pressures.

At this point, Chairman Burns invited Mr. Partee to give his views concerning appropriate monetary policy.

Mr. Partee said he would make three points about appropriate policy, two of which were concerned with longer-run strategy and one with short-run strategy. At the meeting on December 19, he had suggested that the Committee consider reducing its longer-run target for monetary growth to an annual rate of 5 per cent in M_1 because the economic outlook was strong and deviations from the staff's GNP projections were more likely to be on the high side than on the low side. Since then nothing had occurred to alter his opinion. On the contrary, the basis for it had been strengthened by the larger-than-expected rate of monetary growth in the closing month of the year. In the economy, the announcement of Phase III was probably the most important development since the last meeting. But the apparent relaxation of the wage and price controls should not be taken as calling *per se* for a more restrictive monetary policy. In fact, it might necessitate a somewhat faster rate of monetary growth to finance the desired growth in real output under conditions of greater cost-push inflation than would have prevailed with tighter controls. Because of the relaxation of the controls, however, it was even more important to avoid exceeding the committee's targets for monetary growth.

Secondly, Mr. Partee observed, monetary growth at a 5 per cent rate over the next 6 months or so--given the anticipated strength in the economy--would surely be accompanied by higher interest rates. Whatever the political and public relations problems that higher interest rates might bring, they would provide a necessary constraint in the economic situation that was developing. In view of rapidly rising business expenditures for plant and equipment, expansion in business demands for inventories, and continued strength in residential construction, the interest cost of financing expenditures might well need to be higher. Of course, the rise in rates should be orderly and gradual.

Finally, Mr. Partee said, the situation in his view placed a high priority on the need for an immediate reduction in the rate of monetary growth--a reduction that would make clear to all observers that the high rate in December, and in the fourth quarter as a whole, was an aberration. Monetary growth should be slowed both because of the unfavorable psychological effects of continued rapid growth and because of the need to compensate for the excesses that had occurred. To achieve the objective, the funds rate might have to rise considerably. Unless clear evidence developed that the monetary aggregates were growing at rates well below those expected, he would be prepared to see a rise of as much as 50 basis points, from 5-3/4 per cent to 6-1/4 per cent or a little higher, in the 2 weeks before even keel. The market would interpret that as a clear indication of markedly tighter conditions. To apply the terminology of the past, doubts in the conduct of open market operations over this period should be resolved on the side of restraint.

Mr. Leonard commented that he would associate himself with the remarks that had been made by Messrs. Balles and Eastburn. He then asked whether even keel, which was a frustrating complication in monetary control, would be with them forever. Noting that Secretary of the Treasury Shultz was a market-oriented economist, he wondered whether the Treasury and the System had recently analyzed the costs and benefits of even keel. He asked whether even keel, if it were to be continued indefinitely, might be redefined to mean reasonable stability in monetary growth rather than in interest rates.

In response, Mr. Holmes observed that prices of securities in the market were crucial to financing the public debt, and in the very short run, changes in growth rates of the aggregates and in prices of securities were not closely related. At issue was the fundamental central banking relationship of the Federal Reserve System to the Treasury. When treasuries were unable to finance government debt in the market, central banks inevitably had to do the job.

Mr. Axilrod commented that given human nature, even keel in some form would always exist. To define it in terms of the aggregates might require prior announcement of the targets for rates of monetary growth, but difficulties in financing the debt nevertheless would develop. Concerning the effects of even keel, his own research, and other research as well, indicated that over longer periods of time the constraint had not interfered significantly with the System's ability to pursue its objectives--even in periods when the Treasury was in the market with the frequency that it would be this year. Monetary policy had not always been appropriate, but that had not been because of even keel.

In the most recent Treasury financing, Mr. Axilrod added, even keel had been the most severe constraint on System operations in his memory. The question, however, was whether its effects would be permitted to persist. The record of the past suggested that perhaps they would not.

Mr. MacLaury remarked that a definition of even keel in terms of the behavior of the aggregates would be unworkable. With respect to the longer-run effects of even keel on the pursuit of System objectives, his reading of history, like Mr. Axilrod's, suggested that the constraint had not been a real inhibition, although at times it had been an excuse. It was especially significant that during the latest Treasury financing--when even keel had posed an unusually severe constraint because the Treasury had used a novel technique to auction a long-term bond--the funds rate had risen to the top of the specified range of tolerance. As for the period ahead, the Committee could instruct the Desk to tighten money market conditions in advance of the even-keel period.

Mr. Robertson commented that even keel would remain a necessity, whether the Committee liked it or not. However, there was no need for it to be adhered to rigidly, and in fact, it had not been.

Mr. Mayo observed that Secretary Shultz had made important strides toward greater use of the auction technique in Treasury financings--which was evidence of the influence of market-oriented economics--and thereby had reduced the importance of the even keel as a constraint on System operations.

Mr. Mitchell noted that the money supply had grown at an annual rate of 13 per cent in December and 8.8 per cent in the fourth quarter, according to the revised statistics, but he remarked that he did not have a feeling of certainty, as some other Committee members did, about what was really happening and about the need to direct operations toward sharply reducing the rate of monetary growth. In 1971 the Committee had decided that monetary growth needed to be slowed sharply from a high rate and the System had raised the funds rate 250 basis points in just a few months only to lower it again by even more than 250 basis points. Concerning interpretation of the money supply statistics, apparently 1 percentage point of the rate of growth in the fourth quarter was accounted for by Treasury disbursements for revenue sharing. Another influence, as the blue book had pointed out, was the strong economic expansion toward the end of last year, which stimulated transactions demands for money. Moreover, the changes in Regulation J effected in early November may have been a factor. The staff had attempted to assess the impact of the regulatory changes, but in his view, the staff had asked the wrong question and consequently had received the wrong answer. Altogether, there was a fair chance that the rate of monetary growth in December was an aberration.

Nevertheless, Mr. Mitchell continued, the annual rate of growth in M_1 had been as high as 8-1/2 per cent over the second half of 1972, and it was a question whether that was appropriate. There was, unfortunately, a widespread dogma--believed by some members of the Committee as well as by representatives of the press and the public--that monetary growth ought to be at a rate of 5 or 6 per cent. To affect expectations, therefore, it would be necessary to slow growth to a rate consistent with the dogma, which also was unfortunate. At one time, a 4 per cent rate of growth had been considered appropriate, and on one occasion a Congressional committee had asserted that the rate should be between 2 and 6 per cent. He was not convinced that 5 or 6 per cent was the appropriate long-term rate, and he would be very cautious about selecting one.

Mr. Mitchell went on to say that his position was not especially inconsistent with some of the views that had already been expressed. He could accept the specifications of alternative B of the draft directives. However, the Committee should not now make a conspicuous move toward a more restrictive policy. The rate of growth in real GNP was projected to slow throughout the current year, and for the near term, developments would be dominated by the Treasury refunds of taxes overwithheld in 1972 and by fiscal policy. Moreover, there were a number of external considerations--including the objectives of the Committee on Interest and Dividends--that suggested a cautious approach. With respect to narrowing the ranges for the aggregates, reductions in the upper limits of the ranges would pose no problems. However, even if the rate of monetary growth should drop sharply, reserve-supplying operations should not be directed toward raising the rate of growth.

Chairman Burns remarked that his comments on narrowing the ranges specified for the aggregates were concerned with general procedures. At the appropriate time, he would suggest that the lower limits of the ranges be reduced.

Mr. Treiber said policy should move further in a restrictive direction. Concerning the language of the proposed directive, he was in agreement with the general paragraphs of the draft and preferred alternative C for the operational paragraph, calling for bank reserve and money market conditions that would support considerably slower growth in monetary aggregates over the months ahead. He preferred specifications generally between those of alternatives B and C--specifically, a 6-month target of 4-1/2 to 5-1/2 per cent and a January-February range of tolerance of 6 to 8 per cent for the rate of growth in M_1, and a range of 5-3/4 to 6-1/4 per cent or 6-1/2 per cent for the Federal funds rate, with the objective of raising the rate to 6 per cent quite promptly. If growth in the aggregates appeared to be strong, the funds rate should continue to move up within the specified range, but given the imminence of even keel, it seemed unlikely that the funds rate would exceed 6-1/4 per cent. On the other hand, should the rate of growth in the aggregates appear to slow, the funds rate should not be pushed down within the range.

Mr. MacLaury commented--with reference to Chairman Burns' remarks on the relative rates of growth in money and GNP--that he had found it difficult to understand why monetary growth during the late summer and autumn had been so slow in relation to the developing strength in economic activity, and he had concluded that a large increase in the rate of monetary growth was in prospect. In his view, the sharp rise in monetary growth in December was not an aberration, although he would not have predicted a rate as high as the one recorded; if there was an aberration, it was the lower rates of growth in the preceding months. Moreover, judgments about the relationship between growth in the money supply and growth in GNP had to allow for some secular rise in the income velocity of money.

Because of the rise in velocity, expected growth in the money supply was less rapid than that in both current dollar and real GNP. In the period ahead, the rise in short-term interest rates that had already occurred might slow the expansion in the demand for money, as Mr. Axilrod had said. However, that effect was likely to be weak in relation to the expansive influence that economic growth would have on the demand for money.

Continuing, Mr. MacLaury noted that the blue book projections suggested that monetary growth was likely to be moderate in January but then relatively rapid in February. That prospective pattern created a risk that the Committee would attach more weight to the data for January as they became available than to the projections for February, with the result that the provision of reserves might not be restricted sufficiently and the Federal funds rate not moved up high enough.

With respect to the Committee's targets and specifications, Mr. MacLaury observed that the important elements were the upper limits of the ranges for the aggregates in the January-February period and the maximum funds rate for the interval until the next meeting. Like Mr. Brimmer, he believed that the Committee should conduct its operations so as to indicate to the market that a change in the posture of monetary policy had been initiated with the increase in the discount rate. Accordingly, he would specify an upper limit of 6 per cent for the January-February annual rate of growth in M_1. Although that target was unlikely to be achieved, its specification would assure that the funds rate would move up sufficiently to slow the rate of growth in the aggregates in later months. For the funds rate, he would specify an upper limit of 6-3/8 per cent for the period until the next meeting of the Committee.

Mr. Morris said the situation confronting the Committee was somewhat unusual and called for a change in strategy. The rate of monetary growth, most seemed to agree, had been excessive. In the period immediately ahead, with only 10 days before the start of even keel, the usual procedure of basing operating decisions on the behavior of incoming data for the aggregates could result in a delay of a month in taking steps to reduce the growth rates in the aggregates. Consequently, it would be desirable to depart from the usual procedure for a month and to instruct the Manager to move the funds rate up to 6-1/4 per cent in advance of the Treasury's announcement of its next financing. The market would interpret such a course of action as a further move toward restraint, which would be a constructive development in the present situation.

Mr. Winn observed that one concern in making policy decisions for the period ahead was the difficulty in determining what had gone wrong in the recent past. His reading of the record for the past 6 months suggested that revenue sharing and some other special factors had been foreseen as significant influences on the behavior of the aggregates, and yet developments had differed from expectations. Secondly, like Mr. Eastburn, he was concerned that the lag in the availability of reliable information on the behavior of the aggregates tended to have an unfavorable effect on operations. Finally, he was concerned about the possibility of generating excessive swings in the growth rates in the aggregates; a low rate of growth following a rapid rate would not necessarily yield a satisfactory average rate. Therefore, he would prefer to aim at bringing the growth rates in the aggregates down closer to the Committee's long-run targets and not attempt to compensate for the recent overshoots.

Mr. Heflin remarked that he agreed with Mr. Partee's policy views and, like Mr. Morris, thought some immediate action was necessary to bring about a reduction in the growth rates in the aggregates. At the same time, like Mr. Mitchell, he thought the Committee should not react too strongly because the interpretation of the statistics was subject to some uncertainty. On the basis of statements made by Messrs. Axilrod and Holmes, he would judge that a funds rate in a range of 5-3/4 to 6-1/4 per cent was feasible.

Mr. Daane said he disagreed with the view, which many had expressed, that the real problem confronting the Committee was the need to reduce the rate of growth in the monetary aggregates. In his view, too much meaning was being attached to short-run gyrations in the money supply, which were unexplainable. Moreover, he did not believe that a close, quarter-to-quarter relationship existed between changes in the money supply and growth in real or nominal GNP. In any case, it was doubtful that much could be done in the short period before even keel--barring disruptive increases in interest rates--toward achieving the objective of reducing the rates of growth in the aggregates.

Continuing, Mr. Daane remarked that the real problem beyond the growth rates in the aggregates was the specter of acceleration in the rate of inflation. The important issue for the Committee was the System's posture with respect to that problem. The System ought to do all that it possibly could, and it could have an important effect on interest rates and on expectations as well as on the behavior of the aggregates. However, it had to be recognized that monetary policy had its limitations--that it could not compensate for inadequacies in fiscal policy, in the wage and price controls, or in other areas.

Mr. Daane went on to say that he was led to the view that the System in its operations should resolve doubts on the side of restraint. Using more of the terminology of the past, he would say that the Manager should probe toward somewhat more restraint up to and through the even-keel period, and the market would see and understand the System's behavior. With that kind of instruction in mind, he would favor alternative B with the operational paragraph altered to say, "To implement this policy, while taking account of the forthcoming Treasury financing and possible credit market developments, the Committee seeks to achieve somewhat more restrictive bank reserve and money market conditions."

Mr. Robertson observed that in early 1972 the Committee had made public its decision to place primary emphasis on RPD's as its operating handle, while continuing to consider interest rate and other developments. Most of the time since then, however, the Committee had continued to place emphasis on the Federal funds rate, which in his view, was mistaken. The monetary aggregates had grown too rapidly, and now it was necessary to take decisive action to reduce the rates of growth in order to avoid a regeneration of an inflationary psychology. Interest rates were bound to rise, but the Committee could not allow interest rates to be the determinants of its policy. The Committee might establish a limit to the change in the funds rate between meetings, but reaching the limit should be the occasion for further consultations.

With respect to the period immediately ahead, Mr. Robertson said he would expect the funds rate to reach 6-1/4 per cent before the start of even keel. For the whole period until the next meeting, he would set an upper limit of 6-1/2 per cent. Although he did not expect the rate to rise above 6-1/4 per cent, that level should not be a constraint on the efforts to reduce growth in the aggregates. He favored the specifications for the aggregates of alternative B. However, only the upper limits to the specified ranges were important; any shortfalls should be accepted as offsets to the recent overshoots. Concerning the language of the operational paragraph, either alternative B or C was acceptable.

Mr. Mayo commented that in 1971 and 1972 the Committee had encountered difficulties in its efforts first to raise the rate of monetary growth when it was too low and then to reduce it when it was too high. Once again, the lags between System operations in the market and their effects on the aggregates were a potential problem. Monetary policy should make its contribution to the control of inflation, but it would not be desirable to pursue that objective in the 10 days before the start of even keel to an extent that money market rates rose sharply and caused undue concern in the market. Some constraint on the rise in the funds rate was necessary. He favored alternative B for the directive, although he would not object to setting the upper limit for the funds rate at 6-3/8 per cent rather than 6-1/4 per cent, as Mr. MacLaury had suggested. Like Mr. Daane, however, he would prefer to probe toward more restraint rather than to establish the funds rate at the upper limit of the range in advance of the start of even keel.

Mr. Bucher observed that from his reading of various newspapers in recent days he had concluded that public concern about the prospects for inflation had increased substantially. Although Administration statements concerning fiscal policy had been encouraging over the past few months, they really did not warrant great optimism about the outcome. The announcement of Phase III, and the emphasis given to its voluntary features, had contributed to the widespread concern.

Continuing, Mr. Bucher remarked that the financial markets currently were in a better position than at many other times to weather a significant increase in the funds rate without unduly large effects on long-term rates. As the Committee was aware, the long-term rates--and especially rates on mortgages and long-term consumer loans--were of great public and political concern. While monetary policy alone could not do the whole job of dampening inflation, it could do more at this point without significant risk of causing a downturn. As Mr. Partee had said, there were important psychological effects of the course of action taken at this time.

Mr. Sheehan said he had been worried for some time that legislation to extend the economic stabilization program might include mandatory controls on interest rates, and he suggested that a significant rise in the prime rate might increase the risk of such controls. Apart from that, he recalled a comment by John Galbraith to the effect that the Federal Open Market Committee was a group of honorable gentlemen who sat down once a month and decided how much to tighten credit. On many occasions since joining the Committee a year ago, and again today, he found himself in a position of opposing a move toward much tighter money.

Continuing, Mr. Sheehan noted Mr. Bucher's comments regarding increased concern about inflationary prospects, and he remarked that members of the Committee had not suggested that it should be a cause for reducing the 6-month target for monetary growth from the 5 to 6 per cent range adopted at the December meeting. The December bulge in growth in the aggregates might be regarded as a cause for reducing the target, but that would be to over-react to one month's figures. Like Mr. Winn, he did not understand the causes of the December bulge--or, for that matter, of the bulge last July. Applying a lesson learned in his experience with piloting ships and aircraft, he felt that abrupt changes in course might cause serious strains. Accordingly, he would associate himself with the views that had been expressed by Messrs. Mitchell and Daane.

Chairman Burns said he had begun the Committee's discussion of monetary developments and policy by commenting on the relative rates of change in the money supply and GNP in order to suggest that the sharp rise in the monetary aggregates in recent weeks ought not to cause undue alarm, and it was clear that members of the Committee were not unduly alarmed. Nevertheless, the Committee clearly desired to move toward further monetary restraint, and he shared that desire. As Mr. Daane had suggested, monetary policy could not compensate for all the inadequacies in fiscal policy and the wage and price program and for all mistakes in the private sector, but monetary policy had a role to play and it could compensate to some degree.

The Chairman then said he would suggest certain targets and operating instructions for consideration by the Committee. He proposed that the longer-run targets adopted at the December meeting be retained. Annual rates of growth over the first half of 1973 would be 5 to 6 per cent for M_1, 6 to 7 per cent for M_2, 4 to 5 per cent for the bank credit proxy, and 6 to 7 per cent for RPD's. With respect to operating instructions to the Desk, a fairly visible move toward restraint was desirable in view of the recent behavior of the aggregates. Therefore, he suggested taking the ranges of tolerance for the aggregates for January-February specified under alternative C in the blue book and adjusting them in the following way: in each case the upper limit of the range would be reduced by one-half of a percentage point and the lower limit would be reduced substantially. Accordingly, the ranges of tolerance for annual rates of growth over the January-February period would be 4-1/2 to 10-1/2 per cent for RPD's, 3 to 7-1/2 per cent for M_1, and 4 to 9 per cent for M_2. For the Federal funds rate, he suggested a range of tolerance in the daily average for statement weeks between those of alternatives B and C--namely, 5-3/4 per cent to 6-3/8 per cent. Those specifications represented a move in the direction of restraint. A rise in interest rates was likely but not inevitable; operations would continue to be influenced by the behavior of the aggregates.

Mr. Mitchell asked, with respect to the upper limit of 6-3/8 per cent for the funds rate, whether the Chairman was suggesting that the Desk probe toward that level immediately.

In reply, Chairman Burns said he would not want to see the Desk take steps that would firm money market conditions on the first day after the Committee's meeting, thereby giving clear signals that might benefit market participants; he preferred to maintain a degree of uncertainty about the course of policy. If the figures becoming available on Wednesday and Thursday suggested that growth in the monetary aggregates was still strong, the Desk should take prompt and vigorous action to tighten money market conditions. Should monetary growth appear to be less strong, the Desk could take a more relaxed approach in probing toward tighter conditions.

With respect to even keel, the Chairman observed that when he had come to the Board he had neither understood nor approved of the constraint. Gradually, he had been persuaded that the concept had substance, but only when it was applied rather loosely. Thus, it was possible for the Desk to probe in one direction or the other even during a period of even keel. On that basis, he could accept it on the grounds that the ability of the Treasury to finance its debt in the market was the foundation of all credit in the country.

Mr. Brimmer remarked that he would like to see the funds rate rise to a range of 6 to 6-1/4 per cent by the start of the even-keel period.

Chairman Burns commented that it was likely that the funds rate would rise to that range by that time.

Mr. Holmes observed that if the incoming data tended to confirm current estimates of rates of growth in the aggregates, the funds rate would rise to the 6 to 6-1/4 per cent range prior to even keel. The only proviso had to do with member bank borrowings; if borrowings were very heavy, it might not be possible to move the funds rate up.

Mr. Coldwell observed that he could accept the Chairman's formulation of the targets and specifications. In the period ahead, it was especially important that the effort to restrain the rate of growth in the aggregates proceed right on through the even keel period, unless exceptional difficulties arose. Also, he would hope that Desk operations would not be too responsive to daily fluctuations in the funds rate.

Mr. Eastburn asked how much of an increase in the funds rate might be tolerable over the next 2 weeks, assuming that incoming data continued to suggest strong rates of growth in the aggregates.

Chairman Burns commented that if the Committee adopted his formulation of the targets and specifications, Desk operations would move the funds rate toward 6-3/8 per cent. If some significant development caused the Desk to hesitate in such operations, that would be an occasion for a Committee consultation.

Mr. Holmes observed that, given strength in the aggregates, it would be relatively easy to conduct operations in a way that would raise the funds rate to 6-1/4 per cent, but there was less certainty about 6-3/8 per cent.

Mr. MacLaury asked whether the mid-point of the ranges that the Chairman had specified for the aggregates had any significance and how the Desk would be expected to operate in the event that the January-February average rate of growth in M_1 appeared to be in the higher part of the 3 to 7 per cent range but still short of the upper limit.

In response, Chairman Burns said the mid-point of the ranges had absolutely no significance. If the January-February average rates of growth appeared to be in the higher part of the range, the Manager would move the funds rate up.

Mr. Holmes agreed that he would interpret the instructions in the manner the Chairman had described.

Chairman Burns then proposed that the Committee vote on a directive consisting of the staff's draft of the three general paragraphs and alternative B of the operational paragraph, on the understanding the the directive would be interpreted in accordance with the specifications he had described.

By unanimous vote, the Federal Reserve Bank of New York was authorized and directed, until otherwise directed by the Committee, to execute transactions for the System Account in accordance with the following current economic policy directive:

The information reviewed at this meeting suggests that real output of goods and services expanded much more rapidly in the fourth quarter than in the third quarter, and the unemployment rate declined. Wage rates have increased more rapidly in recent months than earlier in the year. Consumer prices rose considerably again in November. Wholesale prices of farm and food products advanced sharply in December but those of industrial commodities increased little. On January 11 the President announced Phase III of the economic stabilization program, which has among its major objectives a further reduction in the rate of inflation. The over-all deficit in the U.S. balance of payments has remained substantial in recent months, and U.S. merchandise imports rose more than exports in November.

Growth in the narrowly and broadly defined money stock was exceptionally rapid in December, after having been moderate on average during the preceding 4 months. In recent weeks interest rates on both short- and long-term securities have risen moderately. Effective January 15, Federal Reserve discount rates were raised one-half of a percentage point to 5 per cent.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions consonant with the aims of the economic stabilization program, including further abatement of inflationary pressures, sustainable growth in real output and employment, and progress toward equilibrium in the country's balance of payments.

To implement this policy, while taking account of the forthcoming Treasury financing and possible credit market developments, the Committee seeks to achieve bank reserve and money market conditions that will support slower growth in monetary aggregates over the months ahead than occurred in the second half of last year.

Secretary's note: The specifications agreed upon by the Committee, in the form distributed following the meeting, are appended to this memorandum as Attachment B.

Chairman Burns noted that on January 5, 1973, there had been distributed a document, dated the previous day, entitled "Final Report on Committee's Rules and Regulation." This report had been prepared by a staff committee consisting of Messrs. Hackley (Chairman), Broida, and Debs which had been appointed by Chairman Burns pursuant to a decision by the Committee on March 21, 1972, that it would be desirable to have a review made of the Committee's By-Laws, Rules regarding Organization, Procedure, and Availability of Information, and general Regulation relating to Open Market Operations of Federal Reserve Banks. The staff committee's assignment was to develop recommendations for whatever technical changes might be appropriate in the light of developments since the documents were last revised.

In its report the staff committee had indicated that its recommendations were based on the principle that documents of the kind under consideration should provide a meaningful general description of the basic organization, procedures, and operating methods of the FOMC, formulated in a manner that was informative to the public and that avoided unnecessary duplication. In accordance with this principle it recommended that the present By-Laws be rescinded and that the present Rules of Organization, Rules of Procedure, and Regulation relating to Open Market Operations of Federal Reserve Banks be revised substantially, in a manner indicated. The staff committee concluded that no substantive changes were needed in the Rules Regarding Availability of Information, but it recommended a few technical and editorial changes in the interest of accuracy and to conform to the style of the other Rules. Finally, the staff committee recommended that the documents in question be routinely included among those circulated to the members of the FOMC for review shortly before the organization meeting in March of each year.

Chairman Burns asked whether there were any objections to the recommendations of the staff committee, and none was heard.

Mr. Hackley noted that the desirability of a few minor technical changes in the proposed new documents had been brought to the attention of the staff committee following the distribution of its report. He suggested that the staff committee be authorized to introduce those changes in the final texts. He also suggested that the modifications in the Regulation and the various Rules be made effective February 1, 1973. Such a date would allow ample time to prepare the material for publication in the Federal Register.

There was general agreement with Mr. Hackley's suggestions.

By unanimous vote, the Committee's By-Laws were rescinded.

By unanimous vote, the Committee's Regulation Relating to Open Market Operations of Federal Reserve Banks was revised, effective February 1, 1973, to read as follows:

REGULATION RELATING TO OPEN MARKET OPERATIONS OF FEDERAL RESERVE BANKS

SECTION 270.1 - AUTHORITY

This Part is issued by the Federal Open Market Committee (the "Committee") pursuant to authority conferred upon it by sections 12A and 14 of the Federal Reserve Act (12 U.S.C. §§ 263, 355).

SECTION 270.2 - DEFINITIONS

(a) The term "obligations" means Government securities, U. S. agency securities, bankers' acceptances, bills of exchange, cable transfers, bonds, notes, warrants, debentures, and other obligations that Federal Reserve Banks are authorized by law to purchase and sell.

(b) The term "Government securities" means direct obligations of the United States (i.e., U. S. bonds, notes, certificates of indebtedness, and Treasury bills) and obligations fully guaranteed as to principal and interest by the United States.

(c) The term "U. S. agency securities" means obligations that are direct obligations of, or are fully guaranteed as to principal and interest by, any agency of the United States.

(d) The term "System Open Market Account" means the obligations acquired pursuant to authorizations and directives issued by the Committee and held on behalf of all Federal Reserve Banks.

SECTION 270.3 - GOVERNING PRINCIPLES

As required by section 12A of the Federal Reserve Act, the time, character, and volume of all purchases and sales of obligations in the open market by Federal Reserve Banks are governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country.

SECTION 270.4 - TRANSACTIONS IN OBLIGATIONS

(a) Each Federal Reserve Bank shall engage in open market operations under section 14 of the Federal Reserve Act only in accordance with this Part and with the authorizations and directives issued by the Committee from time to time, and no Reserve Bank shall decline to engage in open market operations as directed by the Committee.

(b) Transactions for the System Open Market Account shall be executed by a Federal Reserve Bank selected by the Committee. The participations of the several Federal Reserve Banks in such Account and in the profits and losses on transactions for the Account shall be allocated in accordance with principles determined by the Committee from time to time.

(c) In accordance with such limitations, terms, and conditions as are prescribed by law and in authorizations and directives issued by the Committee, the Reserve Bank selected by the Committee is authorized and directed -

(1) To buy and sell Government securities and U. S. agency securities in the open market for the System Open Market Account, and to exchange maturing securities with the issuer;

(2) To buy and sell bankers' acceptances of the kinds made eligible for purchase under Part 202 of this chapter [Regulation B] in the open market for its own account;

(3) To buy Government securities, U. S. agency securities, and bankers' acceptances of the kinds described above, under agreements for repurchase of such obligations, in the open market for its own account; and

(4) To buy and sell foreign currencies in the form of cable transfers in the open market for the System Open Market Account and to maintain for such Account reciprocal currency arrangements with foreign banks among those designated by the Board of Governors of the Federal Reserve System under § 214.5 of this chapter [Regulation N].

(d) In accordance with such limitations, terms, and conditions as are prescribed by law and in authorizations and directives issued by the Committee, the Reserve Bank selected by the Committee (or, if that Bank is closed, any other Federal Reserve Bank) is authorized and directed, for its own account or the System Open Market Account, to purchase directly from the United States such amounts of Government securities as may be necessary from time to time for the temporary accommodation of the Treasury Department.

(e) The Federal Reserve Banks are authorized and directed to engage in such other operations as the Committee may from time to time determine to be reasonably necessary to the effective conduct of open market operations and the effectuation of open market policies.

By unanimous vote, the Committee's Rules of Organization were revised, effective February 1, 1973, to read as follows:

RULES OF ORGANIZATION

SECTION 1 - AUTHORITY

These rules are issued by the Federal Open Market Committee (the "Committee") pursuant to the requirement of section 552 of Title 5 of the United States Code that every agency shall publish in the Federal Register a description of its central and field organization.

SECTION 2 - COMPOSITION OF COMMITTEE

(a) Members. - The Committee consists of the seven members of the Board of Governors of the Federal Reserve System (the "Board") and five representatives of the Federal Reserve Banks, each of whom is a President or a First Vice President of a Reserve Bank.

(b) Reserve Bank representatives. - The representatives of the Federal Reserve Banks, and an alternate for each representative, are elected by the boards of directors of the Reserve Banks in accordance with section 12A of the Federal Reserve Act (12 U.S.C. § 263) for terms of one year commencing on March 1 of each year. Prior to the first meeting of the Committee on or after March 1 of each year, each member of the Committee representing the Federal Reserve Banks shall cause a record of his election and of the election of his alternate to be forwarded to the Secretary of the Committee. If any question is raised as to the election or eligibility of a member or alternate, the Committee determines such question before such member or alternate participates in a meeting of the Committee. In the event a member is absent from a meeting of the Committee, his alternate, in attending the meeting, shall have the same status as the member for whom he is serving. If a member or alternate ceases to be a President or First Vice President of a Reserve Bank, a successor may be chosen in a special election by the boards of directors of the appropriate Reserve Bank or Banks and such successor serves until the next annual election.

(c) Oath of Office. - Each member of the Committee and each alternate take the same oath of office as that prescribed by statute to be taken by officers of the United States.

SECTION 3 - CHAIRMAN AND VICE CHAIRMAN

At its first meeting on or after March 1 of each year, the Committee elects a Chairman and a Vice Chairman from among its membership. The Chairman presides at all meetings of the Committe and performs such other duties as the Committee may require. The Vice Chairman performs the duties of the Chairman in the absence of the Chairman. In the absence of both the Chairman and the Vice Chairman of the Committee, the Vice Chairman of the Board acts as Chairman of the Committee; and, in the absence of the Chairman and the Vice Chairman of the Committee and the Vice Chairman of the Board, the member of the Board present with the longest service as a member of the Board acts as Chairman of the Committee.

SECTION 4 - STAFF

(a) Selection of staff officers. - At its first meeting on or after March 1 of each year, the Committee selects, from among the officers and employees of the Board and the Federal Reserve Banks, the following staff officers to serve until the first meeting on or after March 1 of the next following year: Secretary, Deputy Secretary, and one or more Assistant Secretaries; General Counsel and one or more Assistant General Counsel; and Economists, one or more of whom may be designated as Senior or Associate Economists or given titles reflecting their areas of particular specialization.

(b) Secretary and Deputy and Assistant Secretaries. - The Secretary keeps minutes of actions and records of discussions at all meetings of the Committee; he maintains a complete record of the actions taken by the Committee upon all questions of policy relating to open market operations; and he records the votes taken in connection with the determination of open market policies and the reasons underlying each such action. He has custody of such minutes and records, and he performs such other duties as the Committee may require. In the absence of the Secretary of the Committee, the Deputy Secretary or an Assistant Secretary acts as Secretary pro tem.

(c) Economists. - The Economists prepare for the use of the Committee and present to it such information regarding business and credit conditions and domestic and international economic and financial developments as will assist the Committee in the determination of open market policies, and they perform such other duties as the Committee may require.

(d) General Counsel and Assistant General Counsel. - The General Counsel furnishes such legal advice as the Committee may require. In the absence of the General Counsel, an Assistant General Counsel acts as General Counsel pro tem.

(e) Filling of vacancies. - At any meeting the Committee may fill any vacancy in the offices described in this section.

(f) Other staff assistance. - The services of any officers and employees of the Board and the Federal Reserve Banks are made available and are utilized by the Committee as required.

SECTION 5 - MANAGER AND SPECIAL MANAGER

The Committee selects a Manager of the System Open Market Account and a Special Manager for Foreign Currency Operations for such Account, both of whom shall be satisfactory to the Federal Reserve Bank selected by the Committee to execute open market transactions for such Account, and both of whom serve at the pleasure of the Committee. The Manager and Special Manager keep the Committee informed on market conditions and on transactions they have made and render such reports as the Committee may specify.

By unanimous vote, the Committee's Rules regarding the Availability of Information were amended, effective February 1, 1973, to read as follows:

RULES REGARDING AVAILABILITY OF INFORMATION

SECTION 271.1 - AUTHORITY

This Part is issued by the Federal Open Market Committee (the "Committee") pursuant to the requirement of section 552 of Title 5 of the United States Code that every agency shall publish in the Federal Register for the guidance of the public descriptions of the established places at which, the officers from whom, and the methods whereby, the public may obtain information, make submittals or requests, or obtain decisions.

SECTION 271.2 - DEFINITIONS

(a) "Information of the Committee". - For purposes of this Part, the term "information of the Committee" means all information coming into the possession of the Committee or of any member thereof or of any officer, employee, or agent of the Committee, the Board of Governors of the Federal Reserve System (the "Board"), or any Federal Reserve Bank, in the performance of duties for, or pursuant to the direction of, the Committee.

(b) "Records of the Committee". - For purposes of this Part, the term "records of the Committee" means rules, statements, opinions, orders, memoranda, letters, reports, accounts, and other papers containing information of the Committee that constitute a part of the Committee's official files.

SECTION 271.3 - PUBLISHED INFORMATION

(a) Federal Register. - To the extent required by sections 552 and 553 of Title 5 of the United States Code, and subject to the provisions of §§271.5 and 271.6, the Committee publishes in the Federal Register, in addition to this Part,

(1) a description of its organization;

(2) statements of the general course and method by which its functions are channeled and determined;

(3) rules of procedure;

(4) substantive rules of general applicability, and statements of general policy and interpretation of general applicability formulated and adopted by the Committee;

(5) every amendment, revision, or repeal of the foregoing; and

(6) general notices of proposed rule making.

(b) Policy record. - In accordance with section 10 of the Federal Reserve Act (12 U.S.C. § 247a), each annual report made to Congress by the Board includes a complete record of the actions taken by the Committee during the preceding year upon all matters of policy relating to open market operations, showing the votes taken and the reasons underlying such actions.

(c) Other published information. - From time to time, other information relating to open market operations of the Federal Reserve Banks is published in the Federal Reserve Bulletin, issued monthly by the Board, in such Board's annual report to Congress, and in announcements and statements released to the press. Copies of issues of the Bulletin and of annual reports of the Board may be obtained upon request.

SECTION 271.4 - RECORDS AVAILABLE TO THE PUBLIC ON REQUEST

(a) Records available. - Records of the Committee are made available to any person, upon request, for inspection or copying in accordance with the provisions of this section and subject to the limitations stated in §§ 271.5 and 271.6. Records falling within the exemptions from disclosure set forth in section 552(b) of Title 5 of the United States Code and in § 271.6 may nevertheless be made available in accordance with this section to the fullest extent consistent, in the

Committee's judgment, with the effective performance of the Committee's statutory responsibilities and with the avoidance of injury to a public or private interest intended to be protected by such exemptions.

(b) Place and time. - In general, the records of the Committee are held in the custody of the Board, but certain of such records, or copies thereof, are held in the custody of one or more of the Federal Reserve Banks. Any such records subject to this section will be made available for inspection or copying during regular business hours at the offices of the Board in the Federal Reserve Building, 20th and Constitution Avenue, Washington, D. C., 20551, or, in certain instances as provided in paragraph (c) of this section, at the offices of one or more designated Federal Reserve Banks.

(c) Obtaining access to records. - Any person requesting access to records of the Committee shall submit such request in writing to the Secretary of the Board. In any case in which the records requested, or copies thereof, are available at a Federal Reserve Bank, the Secretary of the Board may so advise the person requesting access to the records. Every request for access to records of the Committee shall state the full name and address of the person requesting them and shall describe such records in a manner reasonably sufficient to permit their identification without undue difficulty; and such person shall pay a fee in an amount based upon $5 per hour for the time required to locate such records and prepare them for inspection plus 10 cents per standard page for any copying thereof.

SECTION 271.5 - DEFERMENT OF AVAILABILITY OF CERTAIN INFORMATION

(a) Deferred availability of information. - In some instances, certain types of information of the Committee are not published in the Federal Register or made available for public inspection or copying until after such period of time as the Committee may determine to be reasonably necessary to avoid the effects described in paragraph (b) of this section or as may otherwise be necessary to prevent impairment of the effective discharge of the Committee's statutory responsibilities. For example, the Committee's current economic policy directive adopted at each meeting of the Committee is published in the Federal Register approximately 90 days after the date of its adoption; and no information in the records of the Committee relating to the adoption of any such directive is made available for public inspection or copying before it is published in the Federal Register or is otherwise released to the public by the Committee.

(b) Reasons for deferment of availability. - Publication of, or access to, certain information of the Committee may be deferred because earlier disclosure of such information would

(1) interfere with the orderly execution of policies adopted by the Committee in the performance of its statutory functions;

(2) permit speculators and others to gain unfair profits or to obtain unfair advantages by speculative trading in securities, foreign exchange, or otherwise;

(3) result in unnecessary or unwarranted disturbances in the securities market;

(4) make open market operations more costly;

(5) interfere with the orderly execution of the objectives or policies of other Government agencies concerned with domestic or foreign economic or fiscal matters; or

(6) interfere with, or impair the effectiveness of, financial transactions with foreign banks, bankers, or countries that may influence the flow of gold and of dollar balances to or from foreign countries.

SECTION 271.6 - INFORMATION NOT DISCLOSED

Except as may be authorized by the Committee, information of the Committee that is not available to the public through other sources will not be published or made available for inspection, examination, or copying by any person if such information

(a) is exempted from disclosure by statute or executive order;

(b) relates solely to internal personnel rules or practices or other internal practices of the Committee;

(c) relates to trade secrets or commercial or financial information obtained from any person and privileged or confidential;

(d) is contained in inter-agency or intra-agency memoranda or letters, including records of deliberations and discussions at meetings of the Committee and reports and documents filed by members or staff of the Committee that would not be routinely available to a private party in litigation with the Committee;

(e) is contained in personnel, medical, or similar files (including financial files) the disclosure of which would constitute a clearly unwarranted invasion of personal privacy; or

(f) is contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of any agency responsible for the regulation or supervision of financial institutions.

Except as provided by or pursuant to this Part, no person shall disclose, or permit the disclosure of, any information of the Committee to any person, whether by giving out or furnishing such information or copy thereof, by allowing any person to inspect, examine, or reproduce such information or copy thereof, or by any other means, whether the information is located at the offices of the Board, any Federal Reserve Bank, or elsewhere, unless such disclosure is required in the performance of duties for, or pursuant to the direction of, the Committee. Any person who may be denied access to records of the Committee may, within 5 days thereafter, file with the Committee a written request for review of such action.

SECTION 271.7 - SUBPOENAS

(a) Advice by person served. - If any person, whether or not an officer or employee of the Committee, of the Board, or of a Federal Reserve Bank, has information of the Committee that may not be disclosed by reason of § 271.5 or § 271.6 and in connection therewith is served with a subpoena, order, or other process requiring his personal attendance as a witness or the production of documents or information upon any proceeding, he should promptly inform the Secretary of the Committee of such service and of all relevant facts, including the documents and information requested and any facts that may be of assistance in determining whether such documents or information should be made available; and he should take action at the appropriate time to inform the court or tribunal that issued the process, and the attorney for the party at whose instance the process was issued, if known, of the substance of this Part.

(b) Appearance by person served. - Except as disclosure of the relevant information is authorized pursuant to this Part, any person who has information of the Committee and is required to respond to a subpoena or other legal process shall attend at the time and place therein mentioned and decline to disclose such information or give any testimony with respect thereto, basing his refusal upon this Part. If, notwithstanding, the court or other body orders the disclosure of such information, or the giving of such testimony, the person having such information of the Committee shall continue to decline to disclose such information and shall promptly report the facts to the Committee for such action as the Committee may deem appropriate.

By unanimous vote, the Committee's Rules of Procedure were revised, effective February 1, 1973, to read as follows:

RULES OF PROCEDURE

SECTION 272.1 - AUTHORITY

This Part is issued by the Federal Open Market Committee (the "Committee") pursuant to the requirement of section 552 of Title 5 of the United States Code that every agency shall publish in the Federal Register its rules of procedure.

SECTION 272.2 - FUNCTIONS OF THE COMMITTEE

The procedures followed by the Committee are designed to facilitate the effective performance of the Committee's statutory functions with respect to the regulation and direction of open market operations conducted by the Federal Reserve Banks and with respect to certain direct transactions between the Reserve Banks and the United States. In determining the policies to be followed in such operations, the Committee considers information regarding business and credit conditions and domestic and international economic and financial developments, and other pertinent information gathered and submitted by its staff and the staffs of the Board of Governors of the Federal Reserve System (the "Board") and the Federal Reserve Banks. Against the background of such information, the Committee takes actions from time to time to regulate and direct the open market operations of the Reserve Banks. Such policy actions ordinarily are taken through the adoption and transmission to the Federal Reserve Banks of regulations, authorizations, and directives.

SECTION 272.3 - MEETINGS

(a) Place and frequency. - The Committee meets in Washington, D. C., at least four times each year and oftener if deemed necessary. Meetings are held upon the call of the Chairman of the Board or at the request of any three members of the Committee. Notices of calls by the Chairman of the Board to other members are given by the Secretary of the Committee in writing or by telegram. Requests of any three members for the calling of a meeting shall state the time therefor and shall be filed in writing or by telegram with the Secretary who shall forthwith notify all members of the Committee in writing or by telegram. When the Secretary has sent notices to all members of the Committee that a meeting has been requested by three members and of the time therefor, a meeting is deemed to have been called. If, in the judgment of the Chairman, circumstances require that a meeting be called at such short notice that one or more members cannot be present in Washington, such members may participate in the meeting by telephone conference arrangements.

(b) Alternates. - Whenever any member of the Committee representing Federal Reserve Banks shall find that he will be unable to attend a meeting of the Committee, he shall promptly notify his alternate and the Secretary of the Committee in writing or by telegram, and upon receipt of such notice the alternate shall advise the Secretary whether he will attend such meeting.

(c) Quorum. - Seven members (including alternates present and acting in the absence of members) constitute a quorum for the transaction of business; but less than a quorum may adjourn from time to time until a quorum is in attendance.

(d) Attendance at meetings. - Attendance at Committee meetings is restricted to members and alternate members of the Committee, the Presidents of Federal Reserve Banks who are not at the time members or alternates, staff officers of the Committee, the Manager and Special Manager, and such other advisers as the Committee may invite from time to time.

(e) Meeting agendas. - The Secretary, in consultation with the Chairman, prepares an agenda of matters to be discussed at each meeting and the Secretary transmits the agenda to the members of the Committee within a reasonable time in advance of such meeting. In general, the agendas include approval of minutes of actions and acceptance of memoranda of discussion for previous meetings; reports by the Manager and Special Manager on open market operations since the previous meeting, and ratification by the Committee of such operations; reports by Economists on, and Committee discussion of, the economic and financial situation and outlook; Committee discussion of monetary policy and action with respect thereto; and such other matters as may be considered necessary.

SECTION 272.4 - COMMITTEE ACTIONS

(a) Actions at meetings. - Actions are taken at meetings of the Committee except as described below.

(b) Actions between meetings. - Special circumstances may make it desirable in the public interest for Committee members to consider an action to modify an outstanding Committee authorization or directive at a time when it is not feasible to call a meeting. Whenever, in the judgment of the Chairman, such circumstances have arisen, the relevant information and recommendations for action are transmitted to the members by the Secretary, and the members communicate their votes to the Secretary. If the action is approved by a majority of the members, advice to that effect is promptly given by the Secretary to the members of the Committee and to the Reserve Bank selected to execute transactions for the System Open Market Account. All communications of recommended actions and votes under this paragraph shall be in writing or by telegram; provided that, in exceptional cases when that is not feasible, such communications may be made orally, either in person or by telephone, and the Secretary shall cause a written record to be made without delay. An action taken between meetings has the force and effect of an action at a meeting; provided, however, that if a meeting is held before the execution of any operations pursuant to the action, the action is null and void unless it is ratified and confirmed by the Committee at such meeting.

(c) Delegations of authority. - In special circumstances, the Committee may delegate authority to take an action, subject to such instructions or guidelines as the Committee deems proper. Such delegations of authority may be made to the Chairman; to a subcommittee consisting of the Chairman and the Vice Chairman of the Committee and the Vice Chairman of the Board (or in the absence of the Chairman or of the Vice Chairman of the Board the members of the Board designated by the Chairman as alternates, and in the absence of the Vice Chairman of the Committee his alternate); or to any other member or members of the Committee. An action taken pursuant to such a delegation of authority has the force and effect of an action taken by the Committee.

(d) Effective date. - Committee action ordinarily is made effective as of the time it is taken because the nature of the subject matter and the action taken is such that the public interest and the proper discharge of the Committee's responsibilities so require. Occasionally, however, the Committee may specify that an action is to be effective at some different time.

SECTION 272.5 - NOTICE AND PUBLIC PROCEDURE

There ordinarily is no published notice of proposed action by the Committee or public procedure thereon, as described in section 553 of Title 5 of the United States Code, because such notice and procedure are impracticable, unnecessary, or contrary to the public interest.

It was agreed that the next meeting of the Federal Open Market Committee would be held on Tuesday, February 13, 1973, at 9:30 a.m.

Thereupon the meeting adjourned.

Secretary

ATTACHMENT A

January 15, 1973

Drafts of Current Economic Policy Directive for Consideration by the Federal Open Market Committee at its Meeting on January 16, 1973

GENERAL PARAGRAPHS

The information reviewed at this meeting suggests that real output of goods and services expanded much more rapidly in the fourth quarter than in the third quarter, and the unemployment rate declined. Wage rates have increased more rapidly in recent months than earlier in the year. Consumer prices rose considerably again in November. Wholesale prices of farm and food products advanced sharply in December but those of industrial commodities increased little. On January 11 the President announted Phase III of the Economic Stabilization Program, which has among its major objectives a further reduction in the rate of inflation. The over-all deficit in the U.S. balance of payments has remained substantial in recent months, and U.S. merchandise imports rose more than exports in November.

Growth in the narrowly and broadly defined money stock was exceptionally rapid in December, after having been moderate on average during the preceding 4 months. In recent weeks interest rates on both short- and long-term securities have risen moderately. Effective January 15, Federal Reserve discount rates were raised one-half of a percentage point to 5 per cent.

In light of the foregoing developments, it is the policy of the Federal Open Market Committee to foster financial conditions consonant with the aims of the Economic Stabilization Program, including further abatement of inflationary pressures, sustainable growth in real output and employment, and progress toward equilibrium in the country's balance of payments.

OPERATIONAL PARAGRAPHS

Alternative A

To implement this policy, while taking account of the forthcoming Treasury financing and possible credit market developments, the Committee seeks to achieve bank reserve and money market conditions that will support some moderation of growth in monetary aggregates over the months ahead from the pace in the second half of last year.

Alternative B

To implement this policy, while taking account of the forthcoming Treasury financing and possible credit market developments, the Committee seeks to achieve bank reserve and money market conditions that will support slower growth in monetary aggregates over the months ahead than occurred in the second half of last year.

Alternative C

To implement this policy, while taking account of the forthcoming Treasury financing and possible credit market developments, the Committee seeks to achieve bank reserve and money market conditions that will support considerably slower growth in monetary aggregates over the months ahead than occurred in the second half of last year.

ATTACHMENT B

January 16, 1973

Points for FOMC guidance to Manager in implementation of directive		Specifications (As agreed, 1/16/73)
A. Longer-run targets (SAAR): (first and second quarters combined)	M_1	5 - 6%
	M_2	6 - 7%
	Proxy	4 - 5%
	RPD's	6 - 7%
B. Short-run operating constraints:		
1. Range of tolerance for RPD growth rate (January-February average):		4-1/2 - 10-1/2%
2. Ranges of tolerance for monetary aggregates (January-February average):	M_1	3 - 7-1/2%
	M_2	4 - 9%
3. Range of tolerance for Federal funds rate (daily average in statement weeks between meetings):		5-3/4 - 6-3/8%
4. Federal funds rate to be moved in an orderly way within range of toleration		
5. Other considerations: account to be taken of Treasury financings and credit market developments.		

C. If it appears that the Committee's various operating constraints are proving to be significantly inconsistent in the period between meetings, the Manager is promptly to notify the Chairman, who will then promptly decide whether the situation calls for special Committee action to give supplementary instructions.