79th Annual Report 1992

Board of Governors of the Federal Reserve System

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Letter of Transmittal

Board of Governors of the
Federal Reserve System
Washington, D.C., April 16, 1993

The Speaker of
The House of Representatives

Pursuant to the requirements of section 10 of the Federal Reserve Act, I am pleased to submit the Seventy-Ninth Annual Report of the Board of Governors of the Federal Reserve System.

This report covers operations of the Board during calendar year 1992.

Sincerely,

Chairman

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Part 1

Monetary Policy and the U.S. Economy in 1992

Introduction

Economic activity accelerated over the course of 1992, and the rise in real gross domestic product during the year cumulated to more than 3 percent, the largest increase since 1988. Inflation continued to trend lower in 1992, with many broad measures of price change showing increases that were among the smallest of recent decades.

Although the rise of real GDP in 1992 was far from robust by the standards of past cyclical upswings in activity, it was a much larger gain than many analysts—both inside and outside government—had thought likely, given the extraordinary headwinds with which the economy had to contend. Chief among the influences restraining growth were budgetary stresses at all levels of government, widespread structural changes in the business sector, both in defense-related industries and elsewhere, exceptional caution among financial intermediaries, and ongoing efforts by businesses and households to strengthen their finances by restricting the growth of their indebtedness. Adding still further to the drag on the economy in 1992 was the sluggish performance of foreign industrial economies, a number of which still were struggling at year-end to regain forward momentum.

The force of the headwinds seemed greatest in the first half of the year. In the second half, their power appeared to abate somewhat. In addition, a number of important sectors—housing, consumer durables, and business fixed investment—continued to benefit in the second half from the substantial easing of money market conditions that had been implemented over time by the Federal Reserve.

With the firming of the economy, employment turned up in 1992, but the rate of job growth was relatively sluggish. The structural adjustments undertaken by large businesses were accompanied in many cases by permanent cutbacks in employment. More generally, businesses were able to meet their output objectives through hefty increases in productivity, thereby limiting the need for additional workers. The unemployment rate rose in the first half of 1992 in conjunction with a surge in the share of the working-age population in the labor force but turned down thereafter as labor force participation fell back. The unemployment rate in December was 7.3 percent, almost half a percentage point below the peak rate of June, but still a little above the level of a year earlier.

Price developments remained favorable in 1992. The rise in the consumer price index over the four quarters of the year amounted to 3.1 percent, essentially matching the low rate achieved in the previous year. Consumer energy prices turned back up in 1992, but the prices of other goods and services that enter into the CPI generally rose less rapidly than they had in 1991. The success in keeping inflation in check, while restoring growth, had highly salutary effects on financial markets and on the process of financial reconstruction, the continuing progress of which is essen-

NOTE. The discussion here and in the following two chapters is adapted from *Monetary Policy Report to the Congress Pursuant to the Full Employment and Balanced Growth Act of 1978* (Board of Governors, February 1993). Data cited are those available as of mid-March 1993.

tial to the achievement of renewed and sustainable prosperity.

The hesitant pace of the economy evident in incoming information throughout much of 1992, along with notable weakness in the monetary and credit aggregates and steady gains against inflation, prompted the Federal Reserve to ease monetary conditions three times, bringing short-term rates down another full percentage point over the year. The discount rate was reduced to 3 percent, and short-term rates generally closed the year at their lowest levels since the early 1960s.

Long-term rates also fell, on balance. At times, the declines in long-term rates were limited by concerns about prospective federal budget deficits and about the possibility that inflation might begin to move higher as the expansion proceeded. However, notable decreases in long rates were registered in late 1992, as inflation remained subdued and as statements by the incoming Administration suggested that it might seek only limited near-term fiscal stimulus and were giving serious consideration to proposals aimed at making substantial cuts over time in the federal budget deficit. The trade-weighted foreign exchange value of the dollar in terms of the other Group of Ten currencies appreciated on balance over the course of 1992. The dollar benefited from the improved performance of the U.S. economy relative to conditions in other industrial countries.

Growth of the monetary aggregates slowed in 1992 despite an acceleration in nominal spending and income. For the year, M2 advanced 1.8 percent, below the 2½ percent lower end of its target range. M3 also came in under its 1 percent to 5 percent target range, growing only 0.3 percent. The Federal Reserve did not make greater efforts to boost growth to within these ranges because, as the year went on, it became increasingly clear that slow growth of the broad money aggregates did not indicate that financial market conditions were impeding the expansion of spending and income. In fact, growth of nominal GDP, which accelerated to 5.7 percent from 3.5 percent in 1991, exceeded that of M2 by nearly 4 percentage points in 1992 and that of M3 by nearly 5½ percentage points. Not only did data on spending itself show a firming trend over the year, but narrow money (M1) and reserves expanded rapidly—suggesting to some that liquidity was quite ample—and the growth of debt, while restrained, was considerably in excess of that of the broader monetary aggregates.

The faster rise of nominal GDP in 1992 was fueled by spending that was financed largely outside banks and other depositories, whose liabilities constitute the lion's share of the monetary aggregates. Spurred in part by advances in equity prices and by declines in longer-term interest rates, businesses and households strengthened their balance sheets by raising funds in bond, mortgage, and equity markets and repaying bank loans and other short-term debt. This shift in the focus of financing efforts toward the capital markets, a process that had been evident in 1991 as well, helped to redress financial distortions that had accompanied the preceding buildup of debt and the rapid rise of some asset prices in the 1980s.

The low level of credit demanded from depositories meant that these institutions did not need to seek large volumes of deposits. As a consequence, rates paid on deposits were adjusted downward rapidly as short-term market rates declined. Savers, reacting to the lower deposit rates and to attractive returns on bonds and equity, shifted funds from M2 deposits into the capital markets. One notable aspect of this shift toward the capital markets was the purchase of bond and stock mutual funds, which are not included in the monetary aggregates and which together experienced record inflows in 1992. In addition, with consumer loan rates falling by less than deposit rates, households apparently used M2 assets to repay consumer debt or restrain its growth. The combination of rate incentives, desires to strengthen balance sheets, and the greater availability at low transaction cost of a broadened array of savings vehicles beyond traditional deposits appear to have distorted, at least for a time, the traditional relationship between levels of M2 and M3 assets and given levels of spending.

Although growth of M2 and M3 was very weak in 1992, M1 growth accelerated to 14.3 percent, the second fastest annual increase recorded in the official series, which begins with 1959. This pickup owed in part to the expansion of aggregate spending, but it mainly reflected the tendency for rates on liquid deposits to adjust downward less rapidly than those on time deposits. In response, savers shifted substantial volumes of funds from maturing time deposits to NOW accounts. In addition, businesses boosted their demand deposits substantially. To support this growth in transactions deposits, the Federal Reserve added substantial volumes of reserves in 1992. Total reserves increased 20 percent last year, and the monetary base, which includes currency outstanding as well as reserves, increased 10.4 percent, the highest rate ever registered in the official series.

The decisions of households and businesses to strengthen their balance sheets also affected debt growth in 1992, although not as much as the broad monetary aggregates. In total, the debt of nonfinancial sectors expanded 4.9 percent in 1992, somewhat faster than in 1991 but still just above the lower end of its monitoring range. With debt growing less rapidly than aggregate income and with declines in market interest rates allowing higher-cost debt to be rolled over at lower rates, households and businesses made substantial further progress in reducing debt-service burdens over the course of the year.

Some of the financial and economic adjustments that were evident in the economy in 1992 seemed likely to extend into 1993 and perhaps beyond. At year-end, government spending for defense appeared likely to continue on a path of sharp decline. More broadly, balance sheet repair and business restructuring seemed to be still in progress at year-end, and near-term prospects for the foreign industrial economies were far from encouraging. The degree to which these, and other, developments might restraint growth in the coming year remained somewhat uncertain.

This uncertainty notwithstanding, however, the economy clearly ended the year 1992 on stronger footing than it had been on at the start of the year. The improvement in household and business finances over the course of 1992, together with the ongoing efforts of businesses to enhance efficiency, seemed to augur well for sustained expansion of the economy in 1993 and beyond. In addition, the considerable progress that had been made in bringing down inflation provided another of the essential underpinnings for sustained growth of real living standards.

Looking ahead to 1993, the aim of the Federal Reserve will be to promote financial conditions that will help to maintain the greater momentum that the economy developed in 1992, while consolidating the trend toward lower inflation. But, achieving a satisfactory economic performance both in 1993 and over the long run will depend on government policies in many areas other than monetary policy. The most important, perhaps, is the direction of fiscal policy. The new Administration and the Congress have an opportunity to make a fresh start in coming to grips with the federal government's long-standing budgetary problems. Credible action to reduce the prospective size of future budget deficits would likely yield a direct and meaningful payoff in the form of reduced federal demands on national saving, leading in turn to lower long-term interest rates than would otherwise prevail, increased capital investment, and higher living standards. ■

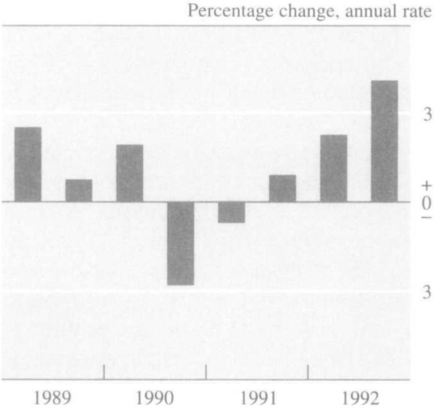
The Economy in 1992

The economy began to exhibit renewed firmness in 1992, overcoming a host of impediments that were working to retard the growth of activity. With the strengthening of growth in the second half, to an annual rate of more than 4 percent, the rise in real GDP over the year cumulated to 3.2 percent, the strongest gain since 1988. Employment also picked up in 1992, but rather slowly; the unemployment rate rose further in the first half of the year but thereafter followed a course of gradual decline. Inflation continued to trend lower over the year.

The growth of household and business expenditures picked up appreciably in 1992. Households began to spend more freely on motor vehicles and other goods, and their purchases of homes also strengthened, spurring additional gains in residential construction. Businesses began investing more heavily in new equipment; much of the gain went for computers and other electronic equipment embodying new technologies. Business outlays for nonresidential construction declined, on net, over the year, but by a much smaller amount than in 1991. In total, the final purchases of households and businesses rose about 4½ percent in real terms in 1992, after declining in each of the two previous years; the gain was the largest in eight years. By contrast, governments at all levels continued to be burdened by huge budget deficits in 1992, and for a second year their combined purchases of goods and services changed little in real terms. In addition, export growth was slowed by weakness of activity in several foreign industrial economies; despite improvement in the second half, the rise in real exports of goods and services over the year, 5 percent, was the smallest gain since 1985. Meanwhile, the faster growth of domestic spending pushed up the growth in imports of goods and services to 9½ percent in 1992.

Further progress was made in reducing inflation last year. The consumer price index excluding food and energy—a measure widely used in gauging the underlying trend of inflation—increased about 3½ percent over the four quarters of 1992; this was a full percentage point less than the increase during 1991. The total CPI rose about 3 percent over the four quarters of 1992, almost the same as in the previous year; energy prices, which had fallen sharply in 1991, turned up slightly this past year, while increases in food prices were quite small for the second year in a row. Except for 1986, when the CPI was pulled down by a collapse of world oil prices, the increases of the past two

Real GDP



The data are seasonally adjusted and come from the Department of Commerce.

years are the smallest in a quarter century.

The Household Sector

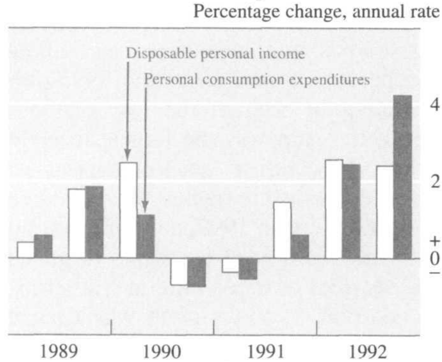
The financial condition of households improved in 1992. Income growth picked up a little in the aggregate, the strains on household balance sheets eased a bit, and the spirits of consumers brightened markedly toward year-end. Growth in consumer spending followed a stop-and-go pattern through midsummer, but the gains thereafter were steadier and fairly sizable overall. Spending for residential investment also advanced over the year, by a considerable amount in total.

The aggregate wealth of households appears to have increased further during 1992. The value of households' financial assets rose moderately, and the value of residential real estate also moved up, on average. On the liability side, households remained cautious in taking on new debt in 1992, and the burden of carrying debt continued to ease because of restrained growth in the volume of debt outstanding and further reductions in interest rates, which facilitated the ongoing substitution of new, lower-cost debt for old, higher-cost obligations. The incidence of households experiencing loan-repayment difficulties diminished over the year.

Income growth picked up moderately in 1992. Wages and salaries rose nearly 4½ percent in nominal terms, after a gain of only 2¼ percent in 1991. In addition, proprietors' incomes benefited from the strengthening of economic activity, and, with corporate profits on the rise, the dividends paid to shareholders more than reversed the decline of the previous year. Transfer payments, which had soared as the economy softened in 1990 and 1991, continued to grow rapidly in 1992. By contrast, interest income trended sharply lower, as the rates of return on household deposits and other financial assets fell further. Total after-tax income got a temporary boost in 1992 from an adjustment of federal tax withholdings that took effect at the start of March. With inflation low, real disposable personal income increased nearly 2½ percent over the year—not a large gain by past cyclical standards, but nonetheless the biggest since 1988.

Real personal consumption expenditures rose about 3¼ percent over the four quarters of 1992, after essentially no gain over the two previous years. For a considerable part of 1992, the increases in spending were interspersed with stretches of sluggishness. A surge in consumer expenditures early in the year was followed by listlessness during the spring, and a second jump in spending around midyear was followed by still another bout of slow growth during the summer. However, the last few months of the year brought fairly sizable advances, boosting the growth of consumption expenditures to a rate of about 4¾ percent in the fourth quarter.

Real Income and Consumption

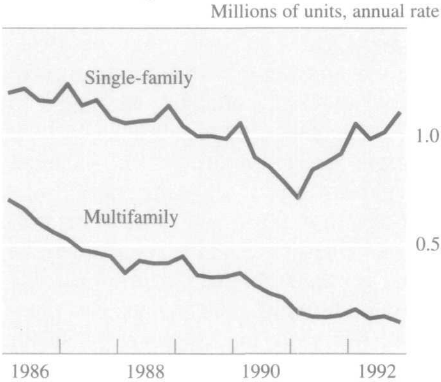


The data are seasonally adjusted and come from the Department of Commerce.

Consumer expenditures for motor vehicles increased 8½ percent over the four quarters of 1992. A large portion of the gain came in the fourth quarter, when sales of new vehicles were boosted by special promotional incentives and, apparently, by a growing perception among consumers that better economic conditions lay ahead. More than likely, some fundamental support for sales came from the replacement needs of persons who had put off buying new vehicles during the recession and the early phases of the recovery.

Spending picked up during the second half of 1992 for many items other than motor vehicles, with notable gains in categories in which an element of discretion typically enters into households' purchasing decisions. Real outlays for furniture and household equipment rose at an annual rate of about 15 percent in the second half of 1992, and real expenditures for apparel climbed at more than a 10 percent rate. In total, spending for consumer durables other than motor vehicles grew almost 10 percent in real terms over the four quarters of 1992, after declining in each of the two previous years. Real outlays for nondurables, which also had fallen in both 1990 and 1991, rose more than 3 percent in the latest year. Real expenditures for services increased about 2 percent during 1992, slightly faster than in other recent years.

Private Housing Starts



The data are seasonally adjusted and are from the Department of Commerce.

The personal saving rate (the share of disposable income not used for consumption or other outlays) rose moderately in the first half of the year, when concerns of households about the prospects for the economy apparently led them to adopt more cautious attitudes toward spending. The rate then turned down in the second half of the year as consumers began to spend more freely. The fourth-quarter rate was slightly below the average for 1992 but well within the range of quarterly observations seen over the past several years.

Real outlays for residential investment rose almost 15 percent during 1992, climbing to a fourth-quarter level nearly 24 percent above the recession low of early 1991. Most of the 1992 rise in residential investment came in the form of increased construction of single-family housing units, which benefited from the further net reduction in mortgage interest rates over the course of the year. Outlays for home improvements, which make up about one-fifth of total residential investment, also increased in 1992, after declining in each of the three previous years; repair of the damage caused by Hurricane Andrew accounted for part of that gain. By contrast, multifamily housing remained depressed; high vacancy rates and unfavorable demographic trends continued to be big obstacles to new construction activity in that portion of the market.

As with consumer spending, the gains in single-family housing activity tended to come in intermittent bursts through much of 1992. Sales of new homes surged early in the year, weakened in the spring, surged again during the summer, and then flattened out in the fourth quarter; on net, the increase over the year amounted to about 15 percent. Mortgage interest rates, although lower than in 1991, exhibited some mild swings during 1992, and these swings appear to have contributed to the fluctuations in home sales. Proposals early in the year for a tax credit for first-time homebuyers also may have affected the timing of purchases to some degree.

Construction activity in the single-family sector also had its ups and downs in 1992, influenced by unusual weather patterns as well as by the fluctuations in sales. Even so, the trend over the year as a whole was decidedly upward, and the average level of starts in the fourth quarter was about 20 percent above that of a year earlier.

Nonetheless, by the fourth quarter of 1992, starts in the single-family sector had retraced only part of the decline that took place in the late 1980s and early 1990s. Strong impetus for recovery was provided by the declines in mortgage interest rates, which were considerably lower in 1992 than they were in 1986, when single-family starts were at their most recent annual peak. However, a number of other developments continued to retard the recovery of housing activity. Uncertainties about job prospects no doubt deterred some buyers from taking advantage of the lower rates on home mortgages. More broadly, demographic trends in 1992 were less favorable to growth in the demand for single-family housing than were the trends of the mid-1980s. The declines in house prices in a number of regions in recent years—and the more general lack of any real price appreciation to speak of—also may have affected demand to some extent; certainly, housing was no longer viewed by potential buyers as the sure-fire, high-yield investment that it was once thought to be.

Builders, for their part, remained a little cautious in 1992, as did the lenders who finance new construction. More often than in the past, houses tended to be started only when a buyer was lined up; eagerness to build in anticipation of future sales was not widely apparent.

In the multifamily sector, the number of units started in 1992 was about 75 percent below the peak rates of the mid-1980s; the sector accounted for only 6 percent of total residential investment in 1992. The overbuilding that had occurred in the multifamily sector in the mid-1980s led to high vacancy rates that stymied activity thereafter. In that regard, only limited progress was made in reducing vacancy rates for multifamily rental units in 1992, despite the greatly diminished level of new construction. Declines in the population of young adults continued to hold down the speed at which the excess supply of space could be worked off.

The Business Sector

The past year brought moderate increases in activity in the business sector of the economy. Production, sales, and orders rose, on net, over the year, and business profits continued to swing back up from the recession lows of 1991. Many businesses continued to undertake major structural changes designed to cut costs and enhance efficiency; the changes were manifest both through reorganization of existing operations and through investment in new technologies. Businesses also continued to shore up their finances, trimming away debt and building equity. Financial pressures persisted in the business sector in 1992, but, in general, they seemed to become less acute as the year progressed.

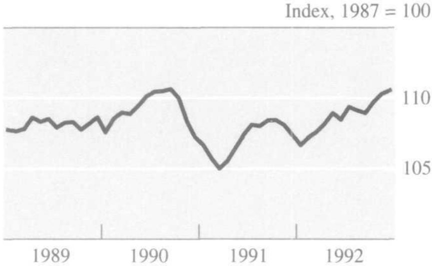
Industrial output rose more than 3 percent from December 1991 to December 1992. Production fell in the first month of 1992 but then picked up, rising about ½ percent per month from February through May. During the summer, the expansion of activity seemed to be losing momentum; orders and shipments fell slightly, on net, from May to August, factory inventories backed up a little, and industrial production essentially flattened out over a four-month stretch. However, orders and shipments began moving up once again in September, and they increased considerably in the fourth quarter. Industrial production also picked up once again in the fourth quarter, rising at an annual rate of about 7 percent over the final three months of the year.

Business profits, which had taken a turn for the better late in 1991, improved further during 1992. The operating profits earned by nonfinancial corporations from their domestic operations rose 18 percent from the final quarter of 1991 to the third quarter of 1992, and a further gain seemed implicit in the available data for the fourth quarter. (An actual estimate of fourth-quarter profits was not published by the Department of Commerce until late March, after this REPORT had gone to press.) Profits of these firms were lifted, in part, by further increases in the volume of output. In addition, tight control over costs led to increases in profits per unit of output. Unit labor costs of nonfinancial corporations rose only slightly from the start of the current economic expansion to the third quarter of 1992, and net interest costs declined sharply over this period because of lower interest rates and restraint in the use of debt. The domestic profits of financial corporations were strong in the first half of 1992 but were severely depressed in the third quarter by the unprecedented losses that insurance companies suffered in the wake of Hurricane Andrew; in the absence of the hurricane, profits in the financial sector would have increased in the third quarter.

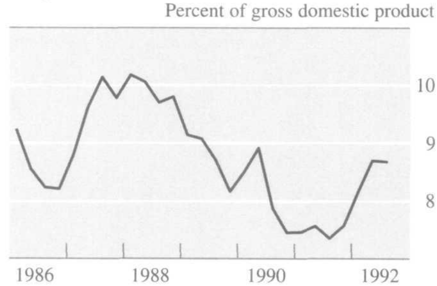
The economic condition of smaller companies also seemed to improve somewhat in 1992. The estimated rise in the profits of nonfarm proprietors over the year was the largest annual gain since the mid-1980s; increases had been relatively small over the three previous years.

The net income of farm proprietors turned back up in 1992 after a moderate decline in 1991. Farm output rose to a record high in 1992, with strong gains for both crops and livestock. Prices, meanwhile, lagged year-earlier levels through much of 1992, but most of that

Industrial Production



Corporate Profits before Taxes



Profits of nonfinancial corporations from domestic operations, with adjustments for inventory valuation and capital consumption, divided by GDP of nonfinancial corporate sector.

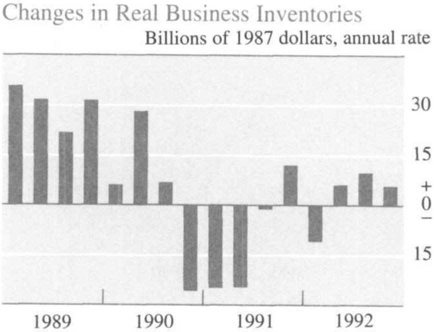
slippage in farm prices already had taken place by the start of the year; the average level of farm prices in December 1992 actually was about the same as that a year earlier. Farm production expenses were little changed for a second year as farm operators, like their nonfarm counterparts, continued to maintain tight control over costs.

Business investment in fixed capital rose about 8 percent in real terms during 1992, more than reversing the decline of the previous year. Spending for equipment increased in each quarter of 1992, and the gains cumulated to about 12½ percent by the fourth quarter; with spare capacity still extensive in most industries in 1992, much of the gain in equipment spending over the year probably was a result of the desire of businesses to modernize their operations. Meanwhile, nonresidential construction spending, which had plunged 14 percent in 1991, fell by a much smaller amount in 1992—2¾ percent according to the estimate in the latest GDP report.

Increased spending for computers was at the forefront of the rise in equipment outlays in 1992. In terms of annual averages, the nominal outlays for office and computing equipment rose nearly 17 percent; the gain in real terms was much greater still, as technological advances and competitive market conditions combined to continue driving down the price of real, effective computing power. Businesses also boosted their outlays for telecommunications equipment, especially in the second half of 1992. Spending for motor vehicles strengthened in 1992, and investment in industrial equipment edged up after three years of decline. Spending for aircraft traced out a volatile pattern during 1992 and, for the year as a whole, was down only moderately from the high level of 1991; at year-end, however, the prospects for such spending did not seem encouraging, given the losses that had been experienced by airline companies and the related cancellations and stretch-outs of orders that had been reported.

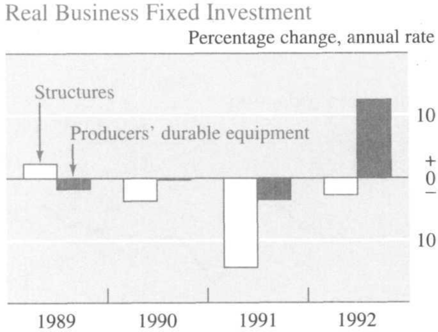
The moderate decline in nonresidential construction outlays during 1992 reflected some widely divergent trends across the various types of construction activity. Spending for new office buildings fell sharply further during the year, to a fourth-quarter level that was more than 60 percent below the peak of the mid-1980s. In addition, real outlays for industrial structures declined in 1992 for the second year in a row, influenced, no doubt, by the current high levels of unused industrial capacity and by the

Changes in Real Business Inventories



Total nonfarm sector. The data are seasonally adjusted and come from the Department of Commerce.

Real Business Fixed Investment



The data are seasonally adjusted and come from the Department of Commerce.

ongoing trend toward tighter control of inventories and concomitant reductions in needed storage space. Annual outlays for oil and gas drilling also fell further in 1992; a rise in drilling in the year's final quarter probably was prompted mainly by a year-end phaseout of certain tax incentives, although some drillers may also have been responding to an upturn in natural gas prices over the year.

Other types of construction activity fared better in 1992. Spending for commercial structures other than office buildings moved up over the year, after sharp declines in both 1990 and 1991, and the outlays of utilities rose appreciably, boosted by environmental requirements as well as by further moderate additions to capacity. Increases in construction spending also were reported for various types of institutional structures, such as hospitals.

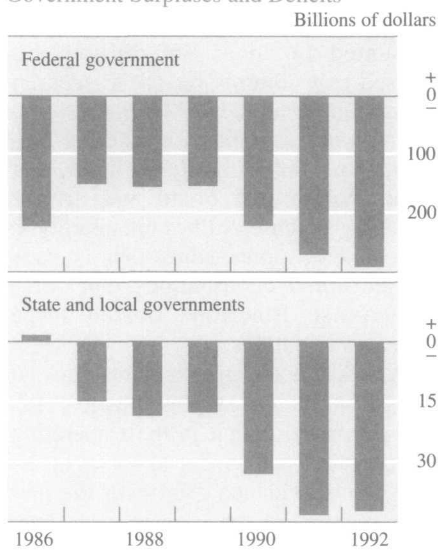
The Government Sector

Government purchases of goods and services, the portion of government spending that is included in GDP, increased slightly in real terms over the course of 1992, after declining slightly during 1991. Federal purchases fell about ¾ percent in real terms over the year, as a further decline in real defense purchases more than offset a small increase in real nondefense purchases. State and local purchases of goods and services increased about 1½ percent during 1992, a rise slightly larger than in 1991 but still well below the rates of increase seen through much of the 1980s.

Governments at all levels continued to be plagued by severe budgetary imbalances in 1992. At the federal level, the unified budget deficit rose about $20 billion in fiscal year 1992, to a level of $290 billion. With the economy gradually strengthening, the rate of increase in federal receipts picked up a little, to 3½ percent, from only 2¼ percent in fiscal 1991. However, spending once again rose faster than receipts; total federal outlays were up 4½ percent in fiscal 1992, after a rise of nearly 5¾ percent in the previous fiscal year.

The rates of growth in total spending in 1991 and 1992 may well understate the degree of upward momentum in federal outlays in those years. In 1991, total spending was held down considerably by a convention used in the federal budget to account for the flow of contributions to the United States from its allies in the Gulf War. Those contributions were counted as negative defense outlays rather than additions to receipts. Additional contributions from the allied countries were received in fiscal year 1992, but they were much smaller than

Government Surpluses and Deficits



The data on the federal government are for fiscal years. They are on a unified budget basis and are from the Department of the Treasury.

The data on state and local governments are for operating and capital accounts on a national income accounts basis and are from the Department of Commerce.

in 1991. Another important factor at work in 1992, however, was a delay in funding the activities of the Resolution Trust Corporation, which kept the 1992 outlays for deposit insurance programs much lower than they otherwise would have been.

Excluding the outlays for deposit insurance and the effect of the allied contributions on reported levels of defense spending, federal expenditures rose about 6½ percent in nominal terms in fiscal year 1992, after an increase of nearly 9 percent in fiscal year 1991. Spending for entitlements, especially those related to health care and income support, continued to grow very rapidly in 1992. In the health area, federal outlays for Medicaid increased nearly 30 percent, and spending for Medicare rose 14 percent. Spending for income security was boosted in 1992 by further large increases in unemployment benefits and food stamp disbursements. In dollar terms, the combined rise in outlays for health care and income security amounted to about $60 billion. Increased expenditures for social security added almost another $20 billion.

Combined spending for all other programs rose only slightly in fiscal year 1992. Within that broad and diverse grouping, defense outlays fell sharply in nominal terms, once adjustment is made for the allied contributions, but some nondefense functions posted large increases in outlays.

State and local governments saw no relief from budgetary pressures in 1992. The combined deficit in their operating and capital accounts, net of social insurance funds, widened a bit over the first three quarters of the year, reversing the small improvement that had been achieved in the latter part of 1991. As is true at the federal level, a rapidly rising level of mandated transfer payments to individuals for health and income support was at the core of the budget difficulties of many states and localities; in nominal terms, transfer payments in the fourth quarter were about 16 percent above the level of a year earlier.

Construction spending by state and local governments picked up in 1992. According to preliminary data, the real gain in these outlays amounted to 3 percent over the four quarters of the year. Spending for highways increased considerably in 1992, and outlays for buildings other than schools were strong in the first half of the year. Construction of educational facilities, which had been boosted in previous years by increases in the school-age population, rose further in 1992, but the increase was small, both in absolute terms and relative to the gains in most other recent years.

Growth in other major categories of state and local expenditures was restrained. Compensation of employees, which accounts for more than half of total state and local expenditures, increased 1½ percent in real terms over the four quarters of 1992; in nominal terms, the rise over the year amounted to about 4¾ percent, similar to that of 1991 but much less than the nominal increases seen in the years before 1991. Restraint on wage growth was widespread in the state and local sector in 1992, and although total employment in the sector grew a little faster than in 1991, hiring freezes, furloughs, and layoffs continued to be reported in some hard-pressed jurisdictions. State and local purchases of durable and nondurable goods—such things as equipment and supplies—apparently grew little in real terms over the course of 1992. Real purchases of services from outside suppliers apparently edged down for the third year in a row.

Many states and localities have implemented tax increases in recent years in an effort to bolster receipts. In addition, grants-in-aid from the federal government have been rising rapidly, and, in 1992, improvement in the economy helped boost receipts to some degree. In total, state and local receipts rose 7¾ percent in annual average terms in 1992, outpacing the growth of nominal GDP by a considerable amount. However, for the third year in a row, the increase in receipts fell short of the annual rise in nominal expenditures, which amounted to more than 8 percent in 1992.

Labor Market Developments

The labor market remained relatively sluggish in 1992. Some large companies continued to undergo major restructurings or reorganizations, and these changes led in many cases to permanent work force reductions at those firms. More generally, businesses remained hesitant to take on new workers, even as the recovery progressed. The still-sluggish pace of output growth in the first half of the year tended to limit labor requirements during that period. Later on, when firms started to expand output more rapidly, they were able to do so without making major long-term hiring commitments. Needs for additional workers were met, in many cases, through use of temporary-help firms, rather than through permanent additions to companies' own payrolls.

Nonetheless, the tilt of the overall employment trend was positive, rather than negative as it had been in 1990 and 1991. Payroll employment, a measure that is derived from a monthly survey of business establishments, was up about 600,000 during 1992. The number of jobs in manufacturing fell further in 1992, but not as much as in either of the two previous years. In addition, employment in construction changed little in 1992, after two years of sharp decline.

About 900,000 new jobs were created in the service-producing sector of the economy in 1992. The number of jobs in retail trade turned up a little, on net, after dropping about one-half million over the two previous years. Also, firms that provide services to other businesses recorded strong employment growth in 1992; more than likely, these firms were the ones that benefited most from the tendency of businesses to purchase labor and services from other firms rather than hire additional workers of their own. Employment in health services, which had remained on a strong upward trend right through the recession, continued to grow fairly rapidly in 1992.

The employment measure that is derived from the monthly survey of households was stronger than the payroll measure in 1992; it showed an increase of about 1½ million in the number of persons holding jobs and by year-end had moved back close to the previous cyclical peak of mid-1990. Reasons for the stronger performance of the household series are not entirely clear. Differences in coverage between the household survey and the payroll survey accounted for only a small part of the 1992 gap, and at year-end other possible explanations were little more than conjecture.

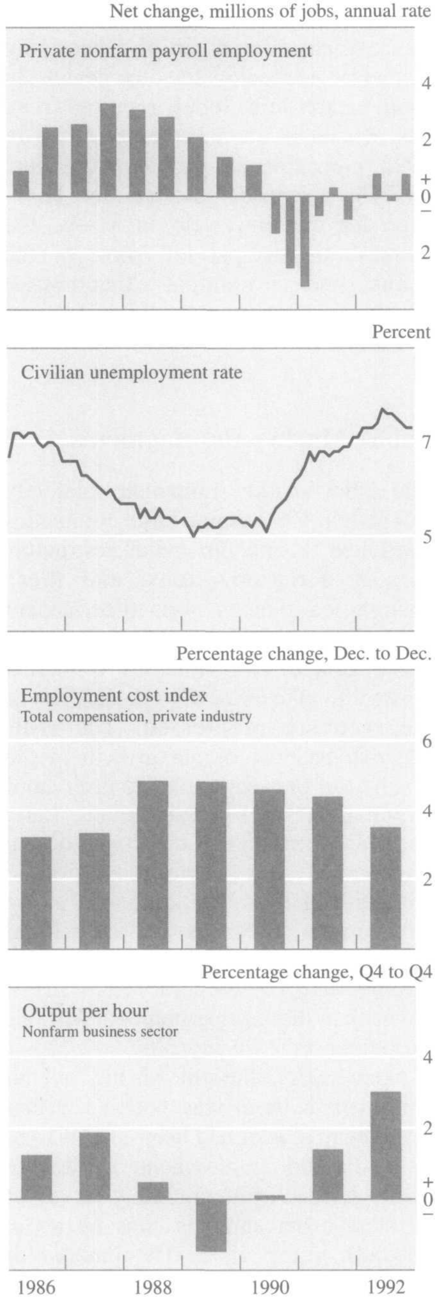
The number of unemployed persons increased in the first half of 1992, to a peak in June of nearly 9.8 million. Job losses—many of them apparently permanent—continued to mount in the first half of the year, and new job opportunities did not open up fast enough to fully absorb either those workers or others entering the work force for the first time. As a result, the unemployment rate rose more than ½ of a percentage point in the first half of the year, to a June level of 7.7 percent.

The second-half outcome was more favorable. The number of unemployed persons declined about one-half million from June to December, and the unemployment rate moved down over that period, to a level of 7.3 percent at year-end. Some of the workers who had been laid off temporarily were recalled in the second half of the year. In addition, the number of unemployed workers not expecting to be recalled—the so-called permanent job losers—also declined; presumably, these workers either found new jobs elsewhere in the economy or dropped out of the labor force altogether. A similar story applied to unemployed new entrants, a category of jobless workers whose ranks were a little thinner at the end of 1992 than they had been at midyear.

In the aggregate, the civilian labor force—the sum of those persons who are employed and those who are looking for work—rose sharply in the first half of 1992 but changed relatively little thereafter. Its level in December was up 1¾ million from that of a year earlier. The labor force participation rate—the proportion of the working-age population that is in the labor force—fell over the second half of the year, reversing part of its first-half rise.

Against a backdrop of slack in labor markets and in the context of reduced inflation, the rate of rise in workers' hourly compensation continued to slow in 1992. The employment cost index for private industry (a measure of labor cost that includes wages and benefits and covers the entire nonfarm business sector) increased 3½ percent from December of 1991 to December of 1992. The index had risen nearly 4½ percent in the previous twelve-month period, and as recently as mid-1990 its twelve-month rate of change had exceeded 5 percent. The employment cost index for wages and salaries increased only 2.6 percent

Labor Market Conditions



The data are from the Department of Labor.

during 1992; this was the smallest annual rise ever reported in this measure, which dates back to 1975. The rate of rise in the cost of benefits provided by firms to their employees also slowed in 1992, but the size of the increase—5¼ percent—was still relatively large. Many firms, both large and small, continued to be pressured by the rising cost of medical care for their employees and by the increased cost of workers compensation insurance; the difficulty of bringing these costs under control may well have been a serious deterrent to increased hiring in 1992.

Despite the further slowdown in nominal compensation per hour in 1992, the purchasing power of an hour's labor appears to have risen in real terms, as the nominal increase in hourly wages and benefits, as measured by the employment cost index, outpaced the rise in consumer prices for the second year in a row. Real compensation, computed in this manner, had declined sharply in 1990, and the increase in 1989 had been barely positive.

Sustained increases in real living standards depend ultimately on advances in the productivity of the work force, and on that score the economy performed well in 1992. Output per hour worked in the nonfarm business sector jumped more than 3 percent over the year, the largest annual gain since 1975. A portion of this large rise was a reflection of normal cyclical tendencies, but longer-range improvement in productivity growth also appeared to be in progress. The jump in output per hour in 1992, combined with the slowing of compensation gains, held the increase in unit labor costs to just 0.4 percent.

Price Developments

The consumer price index rose 3.1 percent over the four quarters of 1992, virtually the same as the increase in the previous year. Energy prices, which had fallen in 1991, turned up a little in 1992, but price increases elsewhere in the economy were generally smaller than those of the previous year. The limited rise in labor costs in 1992 was one important factor exerting restraint on the rate of price increase. In addition, the cost of materials used in production rose only moderately over the year, as did the prices of goods imported from abroad. Although inflation expectations, as reported in various surveys of consumers and business officials, remained a step or so above actual inflation rates, they too appear to have moved lower over the year. Their levels toward year-end were about in line with—or, according to some surveys, less than—the lower bound of the range of inflation expectations reported during the 1980s.

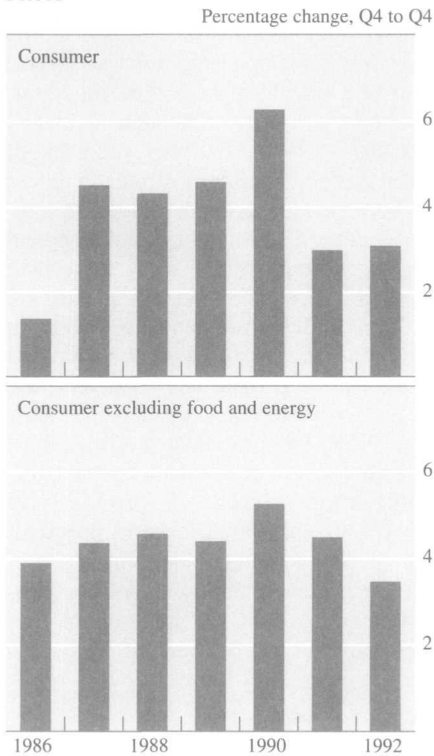
The CPI for food increased a bit less than 1¾ percent in 1992, about the same amount as in 1991. Not since the 1960s had there been a two-year period in which the cumulative increase in food prices was so small. This low rate of food price inflation in 1991 and 1992 was, in part, a reflection of the same factors that were working to pull inflation down in other parts of the economy. In addition, food prices were restrained by favorable supply conditions in the farm sector. Meat production rose further in 1992, and the output of crops soared. Dryness in some regions imparted temporary volatility to crop prices in late spring. Thereafter, growing conditions turned exceptionally favorable and remained so through the summer and into early autumn. Unusually wet conditions in some regions later on in the autumn apparently made only a small dent in the eventual size of the harvest.

The rise in consumer energy prices over the four quarters of 1992 amounted to about 2½ percent. The previous year, energy prices had fallen 8 percent. With no major supply or demand shocks springing up in world oil markets in 1992, the price of West Texas intermediate stayed in the relatively narrow trading range of about $18 to $23 per barrel. At the retail level, price changes for petroleum products were mixed in 1992; the price of gasoline rose about 3 percent, while fuel oil prices declined moderately. The CPI for natural gas rose nearly 5 percent in 1992, considerably more than in other recent years. Although much of that rise in gas prices came in the second half of the year in the wake of supply disruptions caused by Hurricane Andrew, prices of gas at the wellhead had already moved up considerably before the hurricane hit, apparently in response to a somewhat tighter supply–demand balance than had existed over the previous year or so.

The CPI excluding food and energy rose 3.4 percent over the four quarters of 1992, a percentage point less than it had risen in 1991. The slowdown was widespread among the various categories of goods and services that are included in this measure of core inflation. The rate of rise in the cost of shelter—the single most important category in the CPI, with a weight equal to more than one-fourth of the total—slowed further in 1992; rents for both apartments and houses apparently were damped by the large amount of vacant housing that was available in many parts of the country. The prices of other services that are included in the CPI—which collectively make up another one-fourth of the total index—also slowed appreciably in 1992; nonetheless, their overall rate of increase remained relatively high. The costs of medical care services and tuition continued to rise much faster than prices in general in 1992, and airfares rebounded from their 1991 decline. The CPI for commodities other than food and energy rose 2½ percent during 1992, after an increase of more than 4 percent over the four quarters of 1991. Price increases for this broad category of goods were restrained by the cost and price developments in manufacturing: Unit labor costs in manufacturing actually declined in 1992, and the producer price index for finished goods rose less than 2 percent.

After falling sharply from mid-1990 to the end of 1991, the prices of industrial commodities generally changed little, on balance, during 1992. By the end of 1992, however, prices for some industrial metals had begun to tilt up, consistent with the pickup in the pace of

Prices



For all urban consumers. The data are seasonally adjusted and are from the Department of Labor.

industrial expansion toward year-end. The prices of lumber and plywood—following a path considerably different from that of most other commodities—rose substantially during 1992. The surge in prices of these products appeared to be a reflection of the uptrend in single-family housing construction, weather-related supply disturbances in some timber regions, and adjustment of the logging industry to environmental restrictions that had been implemented in some areas of the country. Prices of some other wood products, such as pulp, also rose sharply at the producer level in 1992.

The increases in prices of these raw materials showed through to some extent to broader measures of producer prices. For example, the producer price index for intermediate materials excluding food and energy—a price index that encompasses a wide range of production materials—rose 1 percent during 1992 after declining about ¾ percentage point over the four quarters of 1991. From an economywide perspective, however, the pickup in materials prices in 1992 was not sufficient to dominate the deceleration in labor costs, which account for a far greater share of total production costs in the economy. ■

Monetary Policy and Financial Markets in 1992

Federal Reserve policy in 1992 was directed at promoting and extending the recovery from the 1990–91 recession in the context of continued progress toward price stability. Designing and implementing constructive monetary policies continued to be exceptionally difficult. As in the previous couple of years, economic activity was held back to an unusual degree by the efforts of households, nonfinancial businesses, and some key providers of credit to the economy, including commercial banks, to strengthen their balance sheets. These forces tended to alter the normal relations between financial flows—particularly those reflected in movements in M2 and M3—and the behavior of the economy. Under the circumstances, the Federal Reserve had to take a flexible approach to the use of money and credit aggregates as intermediate policy targets; specifically, in light of evidence that expansion in economic activity was being financed to an unusual extent in capital markets rather than through banks and other depositories, the System tolerated shortfalls of M2 and M3 from their target ranges.

The Federal Reserve judged it appropriate to ease reserve conditions on three occasions in 1992, when financial and economic data suggested that the economy might be losing momentum. The extent of the easings last year was considerably less than in 1991, however, as the underlying trend of the economy overall was more positive. Partly as a result of the cumulative effect of the monetary easings of recent years, economic activity accelerated in 1992 to its fastest pace since 1988. This pickup was achieved even as various measures of inflation evidenced further slowing, with the "core" inflation rate falling to levels last seen in the early 1970s. Thus, 1992 was a year not only of financial repair, but also of improved aggregate economic performance in the United States.

The Implementation of Monetary Policy

The year 1992 began with short-term interest rates at their lowest levels in more than a quarter of a century, following a series of actions by the Federal Reserve in the latter part of 1991 that reduced the discount rate and the level around which the federal funds rate was expected to trade to 3½ percent and 4 percent respectively. Long-term rates were also at lower levels, reflecting the policy actions and a weakening of economic activity in the final quarter of 1991.

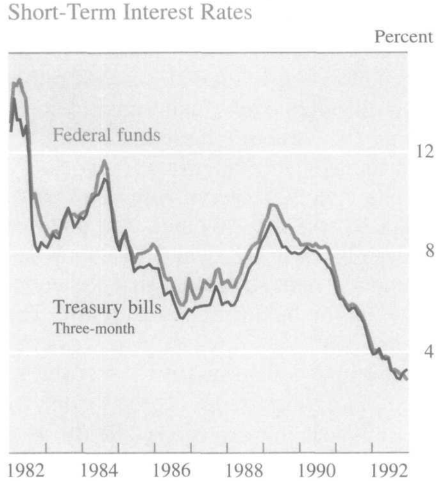
Evidently in the expectation that these rate cuts would revive the recovery, the stock market began the year with strong upward momentum, and the dollar appreciated. However, other evidence that the economy was picking up remained scanty in the initial part of 1992, despite the significant monetary stimulus already in place and the positive developments in equity and capital markets. Apart from rising housing starts, a phenomenon in part related to special weather and tax factors, the economy appeared sluggish in the first few weeks of 1992, and confidence levels were low. Spending by households and businesses was seemingly being restrained by efforts to strengthen financial positions, and banks had done little to reverse the substantial tightening of lending standards that occurred in 1990 and 1991. In view of the still-tentative nature of the recovery and the solid progress against inflation that had been made to that point, the Federal Open Market Committee at its first meeting of 1992 instructed the Manager of the Open Market Account at the Federal Reserve Bank of New York to remain especially alert to evidence that money market conditions might need to be eased before the next scheduled meeting of the Committee. Such a policy stance biased toward ease had prevailed over much of 1991.

M2 and M3, which had posted moderate gains in January, surged in February, partly because of stronger income growth and earlier sharp declines in short-term interest rates and partly because of special factors—above-average tax refunds and a jump in mortgage refinancing, which resulted in funds being held temporarily in demand deposits. Underlying money growth remained very weak, however, and well below that consistent with expectations based on the historical relationship of money with income, deposit rates, and market interest rates. In March, as the influence of the special factors abated, M2 flattened out, and M3 contracted.

News on the economy became more upbeat as the first quarter progressed. Retail sales and housing starts strengthened, industrial production turned up, and the confidence of businesses and households improved, as did the quality of their balance sheets. The signs of recovery and a market view that prospects for further near-term monetary ease had faded caused long-term interest rates to increase during this period, and the dollar rose on foreign exchange markets as well. Private interest rates rose less than rates on Treasuries, likely reflecting perceived reductions in the riskiness of private debt as the economy strengthened coupled with concerns about enlarged Treasury demands on credit markets stemming from discussions of possible fiscal stimulus. Areas of weakness in the economy remained, however—some attributable to the substantially overbuilt commercial real estate sector and some to the transition to a smaller defense sector. In addition, the backup in long-term interest rates threatened to slow the pace of balance sheet adjustment and to damp spending for housing, consumer durables, and business investment. Meanwhile, the outlook for exports clouded.

In early April, the System eased reserve conditions again. The action was taken on indications that the monetary aggregates, already at the bottom of their target ranges after their sluggish performance in March, were contracting, that the pace of economic expansion might be slowing once again, and that inflation was continuing to recede.

Short-Term Interest Rates



The data are monthly averages.

The federal funds rate is from the Federal Reserve.

The rate for three-month Treasury bills is the market rate on three-month issues on a coupon-equivalent basis and is from the Department of the Treasury.

Short-term interest rates fell more than the ¼ percentage point drop in the trading level of the federal funds rate, as market participants judged the economy

Reserves, Money Stock, and Debt Aggregates

Annual rate of change in percent, based on seasonally adjusted data except as noted[1]

Item	1989	1990	1991	1992				
				Year	Q1	Q2	Q3	Q4
Depository institution reserves[2]								
Total	−.4	2.2	8.7	20.2	23.4	14.9	9.3	27.9
Nonborrowed	4.6	2.4	9.2	20.4	19.3	16.7	6.0	34.5
Required	−.2	1.8	9.4	20.4	23.5	15.4	9.9	27.4
Monetary base[3]	4.0	9.4	8.2	10.4	9.1	7.8	10.5	12.9
Concepts of money[4]								
M1	.6	4.3	8.0	14.3	15.5	10.6	11.6	16.8
Currency and travelers checks	4.8	10.9	8.3	9.1	7.2	6.7	11.1	10.3
Demand deposits	−2.9	−.6	3.3	18.0	21.6	13.4	13.3	19.6
Other checkable deposits	1.0	3.6	12.5	15.4	16.9	11.3	10.8	19.3
M2	4.7	4.0	2.8	1.8	3.2	.3	.8	2.7
Non-M1 components	6.2	3.9	1.1	−2.6	−1.1	−3.4	−3.2	−2.8
MMDAs, savings, and small-denomination time deposits	3.8	2.8	.9	−2.3	−1.6	−2.5	−2.8	−2.2
General-purpose and broker–dealer money market mutual fund assets	30.6	11.4	4.2	−5.2	−3.0	−6.6	−7.5	−4.1
Overnight RPs and Eurodollars (n.s.a.)	−8.5	3.4	−6.8	1.7	18.5	−27.8	15.3	2.3
M3	3.7	1.8	1.1	.3	1.9	−.6	.1	−.2
Non-M2 components	−.3	−6.5	−6.2	−6.6	−4.1	−4.9	−3.6	−14.3
Large-denomination time deposits	5.4	−9.7	−13.0	−16.3	−17.6	−16.9	−17.9	−17.1
Institution-only money market mutual fund assets	17.7	21.9	33.5	18.2	33.0	24.0	32.8	−19.3
Term RPs (n.s.a.)	−13.3	−12.4	−20.2	7.8	−11.2	16.5	2.6	23.1
Term Eurodollars (n.s.a.)	−23.3	−13.6	−10.7	−22.6	−27.0	−24.0	−19.5	−28.5
Domestic nonfinancial sector debt	8.1	6.9	4.3	4.9	4.2	5.7	4.9	4.4
Federal	7.2	10.3	11.0	10.7	10.0	14.4	10.7	6.0
Nonfederal	8.4	5.9	2.2	3.0	2.3	2.8	2.9	3.8

1. Changes are calculated from the average amounts outstanding in each quarter. Annual changes are measured from Q4 to Q4.

2. Data on reserves and the monetary base incorporate adjustments for discontinuities associated with regulatory changes in reserve requirements.

3. The monetary base consists of total reserves; plus the currency component of the money stock; plus, for all quarterly reporters, and for all weekly reporters without required reserve balances, the excess of current vault cash over the amount applied to satisfy current reserve requirements. For further details, see the Federal Reserve's H.3 Statistical Release.

4. M1 consists of currency in circulation excluding vault cash; travelers checks of nonbank issuers; demand deposits at all commercial banks other than those due to depository institutions, the U.S. government, and foreign banks and official institutions, less cash items in the process of collection and Federal Reserve float; and other checkable deposits, which consist of negotiable orders of withdrawal and automatic transfer service accounts at depository institutions, credit union share draft accounts, and demand deposits at thrift institutions.

M2 is M1 plus savings deposits (including money market deposit accounts); small-denomination time deposits (including retail repurchase agreements), from which have been subtracted all individual retirement accounts (IRAs) and Keogh accounts at commercial banks and thrift institutions; taxable and tax-exempt general-purpose and broker–dealer money market mutual funds, excluding IRAs and Keogh accounts; wholesale overnight and continuing-contract repurchase agreements (RPs) issued by commercial banks and thrift institutions net of money fund holdings; and overnight Eurodollars issued to U.S. residents by foreign branches of U.S. banks worldwide net of money fund holdings.

M3 is M2 plus large-denomination time deposits at all depository institutions other than those due to money stock issuers; institution-only money market mutual funds; wholesale term RPs issued by commercial banks and thrift institutions net of money fund holdings; and term Eurodollars held by U.S. residents at all banking offices in Canada and the United Kingdom and at foreign branches of U.S. banks worldwide net of money fund holdings. For further details, see the Federal Reserve's H.6 Statistical Release.

n.s.a. Not seasonally adjusted.

sufficiently weak to make further near-term monetary easing moves likely. The easing buoyed the stock market, but long-term rates showed a limited response and remained well above year-end levels.

In the weeks following the April easing, news on the economy was mixed, but positive on balance. Single-family housing starts, which had contracted in March, fell considerably further in April, and retail sales were little changed on balance between February and April. However, nonfarm payroll employment and industrial production continued to expand. Weakness in the monetary aggregates persisted into April, but concerns on this front were allayed to some degree by evidence that this weakness was importantly related to the ongoing rechanneling of credit away from depository institutions and into capital markets, and by expectations that this rechanneling and other financial restructuring would continue to damp money growth considerably more than economic activity. Moreover, the restraint that balance sheet restructuring was exerting on spending was seen as likely to abate in view of the considerable progress that by then had been made in that regard, both by borrowers and by depository institutions, as banks added rapidly to capital. At its mid-May meeting, the Committee determined that its bias toward ease in assessing possible intermeeting policy changes was no longer appropriate.

However, data that became available in the weeks after the mid-May meeting suggested that the forces restraining economic expansion continued to be quite strong. The contraction of consumer credit accelerated, and bank loans more generally began to decline. With the forces that had been constraining money growth intensifying, all three monetary aggregates contracted in June.

Nonfinancial data confirmed that the economy remained slack. Although both nonfarm payroll employment and industrial production increased in May for the fourth straight month, the unemployment rate rose sharply because of a rising labor force participation rate. Moreover, homebuying and retail sales, other than of automobiles, slowed from the pace earlier in the year, and demand for U.S. exports was held down as growth in some foreign industrial countries slowed or turned negative while other countries struggled to recover from their downturns in 1991 or remained in recession.

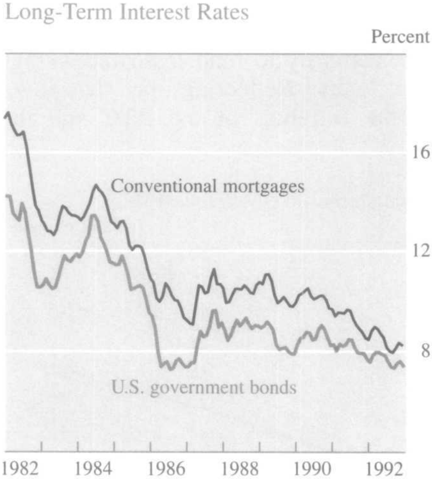
With the tenor of incoming economic news having become distinctly negative, long-term Treasury rates, which had been little changed during most of May and June, turned down around midyear, although they remained above year-end lows. In light of these developments, and with the downward trend in inflation continuing, the System reinstated its bias toward ease at its midyear meeting. Immediately after that meeting, on July 2, with evidence of a weakening economy confirmed by a further rise in the unemployment rate, to 7¾ percent in June, the Federal Reserve reduced both the discount rate and the federal funds rate by ½ percentage point, to 3 percent and 3¼ percent respectively. Banks lowered their prime rate, also by ½ percentage point, to 6 percent, leaving its unusually wide spread over market rates intact.

Long-term interest rates fell in July in response to the employment data and the monetary easing, and they moved down further into early August as the incoming economic news continued to be poor. The drop in yields brought long-term rates to the lowest levels since the early 1970s, and the dollar continued to retreat from the higher levels reached in April.

In early September, after another weak labor market report and in the context of contracting industrial production and positive but weaker-than-expected expansion in the monetary and credit aggregates, reserve conditions were eased further and the federal funds rate fell to around 3 percent. Shorter-term market rates dropped on this action, bringing them to the neighborhood of zero in real terms. Despite the poor economic news and expectations that further easing moves were in the offing, long-term interest rates, which had initially declined after the September action, drifted back up on renewed concerns that weakness of the economy might prompt significant fiscal stimulus, thereby enlarging the size of the federal budget deficit.

Throughout the late summer and early fall, policy was conducted against a background of tension in foreign exchange markets; a strong deutsche mark had caused several European countries to raise interest rates sharply to preserve fixed exchange rate relationships with the exchange rate mechanism of the European Monetary System at a time when aggregate demand in these countries was slowing or sluggish. The dollar continued to decline into early September but then began to firm. The rise in long-term rates contributed to the reversal, as did actions by several European countries to devalue their currencies, in some cases dropping out of the ERM, and to lower their interest rates.

Long-Term Interest Rates



The data are monthly averages.

The rate for conventional mortgages is the weighted average for thirty-year fixed-rate mortgages with level payments at major financial institutions and is from the Federal Home Loan Mortgage Corporation.

The rate for U.S. government bonds is their market yield adjusted to thirty-year constant maturity by the Treasury.

With short-term interest rates in the United States lower, the monetary aggregates continued to expand in September. The implications of the strength of M2 were difficult to assess, however, because it reflected to an uncertain degree the impact of mortgage refinancing on demand deposits as well as strong foreign demands for U.S. currency. Stronger income also appeared to be contributing to money growth, as private employment edged up and the unemployment rate declined in September. Nevertheless, the outlook for the economy remained uncertain. Final demand seemed weak and was being met in part through higher imports, holding down industrial production and employment, and business and consumer sentiment remained relatively depressed.

In these circumstances, the Committee established a strong bias toward ease at its early October meeting. However, an improvement in economic indicators immediately after the meeting, along with evidence of some strength in M2 and bank credit, stayed any further easing actions. Because anticipation of further easing had been built into the structure of interest rates, short-term rates backed up after the meeting. Rates also rose at the long end, responding to growing expectations that fiscal stimulus could follow the upcoming presidential election, as well as to the indications of improved economic performance.

Evidence of greater economic strength continued to accumulate in a variety of indicators of production and spending during the fourth quarter. Although this news initially put further upward pressures on longer-term interest rates, these increases were slowed and then reversed as the better economic prospects, along with statements and actions of the incoming Administration, began to be viewed as reducing the likelihood of outsized fiscal stimulus. Also helping to lower longer-term rates was continuing good news on inflation.

With the better economic news, the Federal Reserve kept reserve conditions and short-term interest rates unchanged toward year-end, and the Committee at its December meeting decided to move back to a symmetric policy stance. Reflecting the improved economic outlook, a stock market rally developed that rivaled in strength the rally at the beginning of the year, and the dollar rose further.

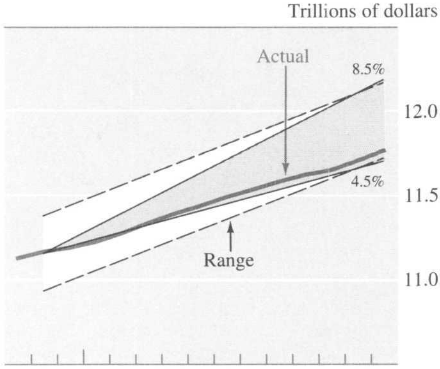
Although the monetary aggregates strengthened a bit in the fourth quarter, the depressing effects of balance sheet restructuring continued to be important, a fact that became clearer once the hard-to-measure temporary boost to deposits deriving from higher mortgage refinancing abated after October. The velocities of both M2 and M3 rose significantly further in the final quarter of the year, contributing to the exceptional velocity increases posted by both measures for the year as a whole.

Monetary and Credit Flows

Credit flows were damped again in 1992, and money growth was exceptionally weak. Despite an appreciable pickup in nominal GDP growth last year, the broad monetary aggregates decelerated further, and expansion of the nonfinancial debt aggregate picked up by only a small amount. As had been the case in the previous couple of years, considerable efforts in key sectors of the economy to improve balance sheets had a significant restraining effect on credit growth and, especially, on money growth—indeed, a much greater effect than on spending itself. Growth of the debt of nonfinancial borrowers other than the federal government amounted to about 3 percent in 1992, only ¾ percentage point more than in 1991. Households restrained their borrowing in 1992, in part by limiting the accumulation of financial assets, and businesses curbed their credit needs by financing spending out of cash flow and equity issuance.

The expansion of federal debt slowed slightly to a still-rapid 10¾ percent, held down by the lack of activity by the Resolution Trust Corporation (RTC) after April, when it exhausted its legislative authority to fund losses at savings and loans. Reflecting the slowdown in the activities of the RTC and the

Total Domestic Nonfinancial Debt



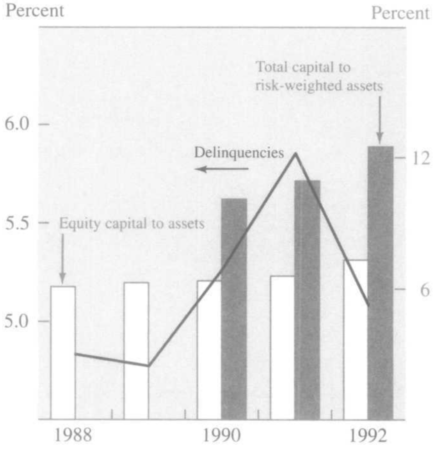
The range was adopted by the FOMC for the period from 1991:Q4 to 1992:Q4.

improving health of depositories, federal outlays attributable to deposit insurance activity fell from around $50 billion in 1991 to nil in 1992. The total nonfinancial debt aggregate expanded about 5 percent in 1992, a rate that was near the lower end of the Committee's monitoring range.

The sluggishness in credit and money growth in 1992 appeared to represent mainly weak demand rather than any new tightening of credit supply terms. At banks, loan flows were depressed, and, in the absence of appreciable credit demands, bank asset growth mainly took the form of security acquisitions.

Some observers have argued that the shift to government securities in 1992 and other recent years was motivated by the Basle risk-weighted capital standards, which require capital against loans but not against many government securities. However, the effect of these standards appears to have been relatively minor. As in 1990 and 1991, banks that had already achieved adequate capital positions were the major purchasers of U.S. Treasury and agency securities in 1992, and loan flows were depressed at these banks as well. Moreover, other regulatory factors may have contributed to a reduction in the willingness of banks to take deposits and make loans; these factors included rising deposit insurance premiums and tighter regulations and requirements of the laws governing banks and thrift institutions in recent years. A similar pattern of asset growth concentrated in government securities occurred at credit unions, which are not subject to the Basle capital standards. Although loan growth at banks generally remained lackluster in 1992, it did strengthen in the final quarter of the year as the economy began to expand more rapidly. At the same time, the growth of bank holdings of government securities, which had been very rapid all year, slowed in the fourth quarter.

Capital Ratios and the Loan Delinquency Rate at Commercial Banks



To be sure, the pickup of bank lending toward year-end seemed primarily related to stronger demand. Banks gave little indication in Federal Reserve surveys that they had begun to ease the tighter lending standards and terms that they had put in place in 1990 and 1991, and the unusually wide spread of the prime rate over market rates persisted. Nonetheless, banks did seem better positioned to meet increases in demand thanthey had been a few years earlier. Not only has their liquidity improved with the acquisition of government securities, but banks have made substantial progress in improving capital positions, including leverage ratios—which are unaffected by asset composition. Banks' profits and their debt and equity issuance reached record levels in 1992. Moreover, the quality of banks' assets showed some scattered signs of improvement; the delinquency rate for bank loans, though still high, began to turn down, as did the rate of charge-offs.

Other financial intermediaries also have taken steps to strengthen balance sheets, and the availability of credit from these lenders also remained somewhat constrained in 1992—though probably not more than in 1991. Life insurance companies, having suffered from an abundance of bad loans, remained saddled with poor-quality commercial real estate loans in 1992. Such firms limited their acquisitions primarily to high-quality, easily marketable assets; thus, as in 1991, some medium-sized, below-investment-grade companies found credit from life insurance companies difficult to obtain in 1992. Some business finance companies also experienced high and rising levels of nonperforming loans, many of which were secured by commercial real estate, with effects on the willingness of these lenders to make new loans.

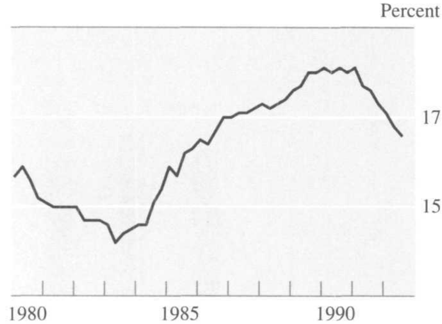
Downgradings of the manufacturing parents of automobile sales finance companies led to some increases in their funding costs in 1992. However, the downgradings had little or no effect on the cost or availability of consumer credit, as these finance companies increased the volume of loans they securitized. The availability of credit at thrift institutions likely improved a bit in 1992. Reflecting the declines in interest rates, profits of private sector savings and loan associations reached a record level, sustained by a wide spread between interest earned on assets and the cost of funds as well as by a decline in the industry's still high level of troubled assets.

Weak credit demand and constraints on some sources of supply produced generally restrained borrowing in each major nonfinancial sector other than the federal sector. Overall household borrowing accelerated but remained moderate, as demand was depressed by insecurity about employment as well as by efforts to restructure balance sheets. Declines in mortgage rates were accompanied by a pickup in the growth of mortgage debt outstanding; the volume of mortgage refinancings increased considerably. Some of the proceeds of mortgage refinancings likely were used to pay down higher-cost consumer credit. Consumer credit also was held down in 1992 by the tendency of households to pay down high-cost debt using funds that otherwise would have been held in low-yielding deposits.

With the pace of debt accumulation by the household sector damped, and with rates on consumer debt falling and mortgage debt being refinanced at lower rates, the ratio of debt-servicing payments to household income declined considerably further in 1992. Other indicators of financial stress also improved somewhat. Consumer loan delinquency rates mostly fell over the year, although they remained at relatively high levels. Home mortgage delinquency rates also declined in 1992; by year-end, they had moved back down to near their prerecession levels and were around the low end of the range of the 1980s.

Business debt grew only slightly in 1992 as internally generated funds exceeded investment spending. Taking advantage of the strong stock and bond markets, nonfinancial corporations

Debt Service of the Household Sector



Percentage of disposable personal income. Debt service is a staff estimate of scheduled payments of principal and interest on home mortgages and consumer debt.

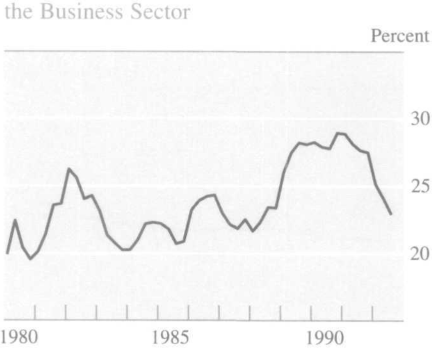
stepped up their equity issuance and refinanced large volumes of longer-term debt at more favorable rates. In part, the proceeds of these issues were used to pay down short-term debt, particularly bank loans, thereby lengthening liability structures.

The hospitality of the capital markets extended even to lower-graded business borrowers, which issued substantially more bonds than in other recent years. Overall public gross bond issuance by nonfinancial corporations was well above the 1991 level. Likewise, gross equity issuance by nonfinancial corporations also rose from the already high pace of 1991 and was four times that of the late 1980s and early 1990s. As a result of debt refinancing and sales of equity, corporate net interest payments as a percentage of cash flow fell sharply for a second year. As declining interest rates allowed firms to reduce debt burdens, and as the economy advanced, corporate debt ratings began to improve and quality spreads narrowed.

The state and local sector also benefited from interest rate declines in 1992. Large amounts of state and local debt were refinanced, including a large volume that was called. Net debt growth of state and local debt continued to be moderate, however, as the sector's spending remained constrained.

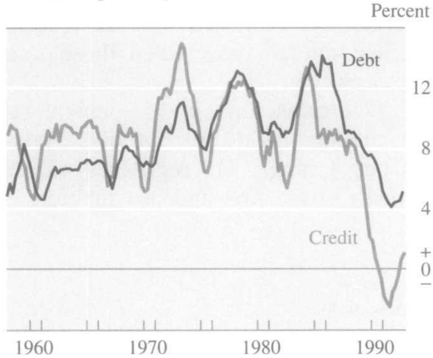
Although balance sheet restructuring damped credit flows and spending in 1992, its greatest impact was on the monetary aggregates, as an unusually high proportion of spending again was financed outside depositories, whose liabilities make up the bulk of the monetary aggregates. Some spending was supported through sources other than borrowing—for example, by issuing equity or restraining the accumulation of liquid assets. Depository credit expanded last year, after two years of contraction, but its share of total nonfinancial debt continued to shrink, as borrowers concentrated their credit demands in long-term securities

Net Interest Payments of
the Business Sector



Percentage of cash flow plus net interest payments. Cash flow is depreciation (book value) plus retained earnings (book value).

Changes in Debt of
the Domestic Nonfinancial Sector
and in Depository Credit



Domestic nonfinancial debt covers borrowing by households, farm businesses, nonfarm noncorporate businesses, corporate nonfinancial businesses, state and local governments, and the federal government.

Depository credit is the sum of credit market funds advanced by savings institutions and commercial banks.

The percentage changes are four-quarter moving averages. They are calculated by first subtracting the level at the end of the previous quarter from the level at the end of a given quarter (flow) and dividing by the level at the end of the previous quarter. The quarterly percentage changes are then used in computing four-quarter moving averages.

markets—bonds for corporations and fixed-rate mortgages for households.

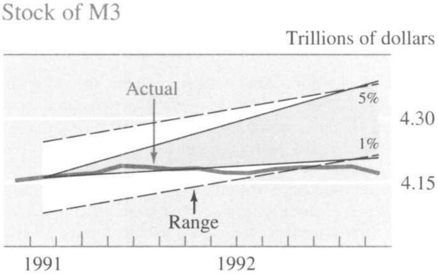
The sluggish expansion of depository credit was echoed in M3, which comprises most—though not all—of the instruments depositories use to finance their credit extensions. In fact, growth of M3 slowed last year to ¼ percent despite the pickup in depository credit, as depositories relied much more on equity issuance and sales of subordinated debt, which are not in M3. Large time deposits at banks and thrift institutions fell rapidly. The tendency for spending to be financed outside of depositories, along with the latter's reliance on non-M3 funds, produced a sizable increase in M3 velocity in 1992—at a rate far above that of other recent years. The rise in velocity of M3 would have been even greater had it not been for strong inflows into institution-only money funds over the first three quarters of the year. The attractiveness of these funds increases when short-term interest rates are falling, a phenomenon caused by the fact that the funds do not mark to market, so that their yields tend to exceed market rates when those rates are declining.

M2 increased about 1¾ percent last year, below the 2½ percent lower end of its target range. M2 registered modest growth in the first and last quarters of the year but was about flat over the middle quarters. The underlying weakness of money growth appeared to stem from several important factors, many of which were related to the unattractiveness of holding funds in M2 assets relative to other possible uses of savings.

Contributing to the relative attractiveness of nonmonetary assets was the rapidity with which banks adjusted down offering rates on retail deposits as market rates declined in 1992. Banks' unaggressive pricing of deposits reflected substantial paydowns of bank debt by households and businesses, which kept loan demand low and banks' need for funds to finance them quite limited. In addition, banks and thrift institutions were discouraged from going after deposits by the rising cost of issuing deposits to make loans; among the factors accounting for this increase were increases in deposit insurance rates and higher capital ratios occasioned by market and regulatory forces.

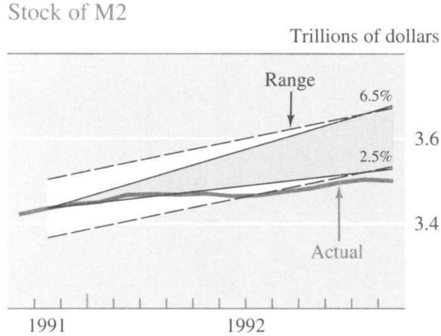
The prompt declines and low level of deposit rates combined with several other factors to induce savers to cut back on holdings of assets in M2. One important influence was the unprecedented steepness of the yield curve, which pulled deposit funds into capital

Stock of M3



The range was adopted by the FOMC for the period from 1991:Q4 to 1992:Q4.

Stock of M2



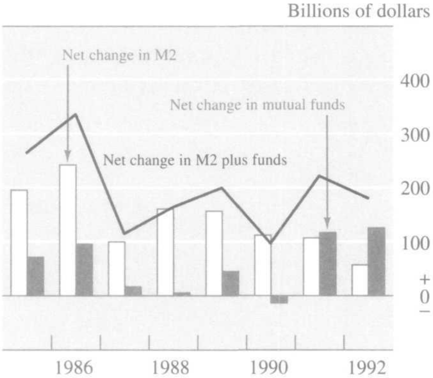
The range was adopted by the FOMC for the period from 1991:Q4 to 1992:Q4.

markets. An important channel for accomplishing this portfolio shift was mutual funds, which experienced record inflows in 1992. Not only were yields on these funds attractive, but the funds had become increasingly available through banks and thrift institutions. Assets in bond and equity mutual funds (apart from those held by institutions and those in IRA and Keogh accounts) increased $125 billion in 1992, up from $117 billion in 1991 and an average of $30 billion over the previous five years. The years 1991 and 1992 were the first ever in which increases in mutual fund assets exceeded increases in M2.

Money growth also was weakened by the tendency of consumer loan rates to move downward less rapidly than deposit rates. As a consequence, households faced a considerable interest rate incentive—particularly after taking account of changes in the tax deductibility of consumer interest payments—to use funds from deposit accounts to pay down debt or to limit its accumulation. In fact the rise in consumption in 1992 was accompanied by an unusually small increase in debt and was financed in part by reducing or limiting holdings of financial assets.

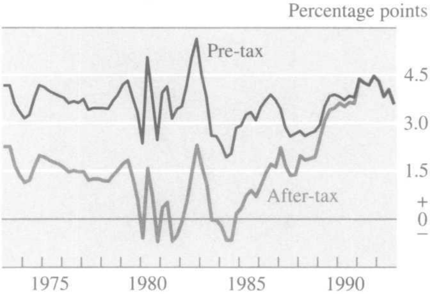
The cuts in bank deposit rates were particularly evident for larger (and presumably more interest sensitive) accounts and at longer maturities. Small time deposits ran off throughout the year. Some of these funds appeared to flow into more-liquid deposit accounts, as rates on small time deposits fell faster than those on savings and checkable deposits. General purpose and broker–dealer money market mutual funds (MMMFs) also contracted over the year, despite the yield advantage these assets offered vis-à-vis other money market rates in an environment of declining yields. This contraction appeared to be another reflection of the attractiveness of bond and equity funds and other capital market instruments. MMMFs grew in October and November, however, in a reversal that perhaps reflected reactions to capital losses in bond funds resulting from the rise in long-term rates in September and October.

Changes in M2 and in Assets of Stock and Bond Mutual Funds



Mutual fund data have been adjusted to exclude institutional holdings and IRA and Keogh balances; for 1992 the adjustment is an estimate.

Spreads between Pre-Tax and After-Tax Rates on Auto Loans and Rate Paid on Small Time Deposits

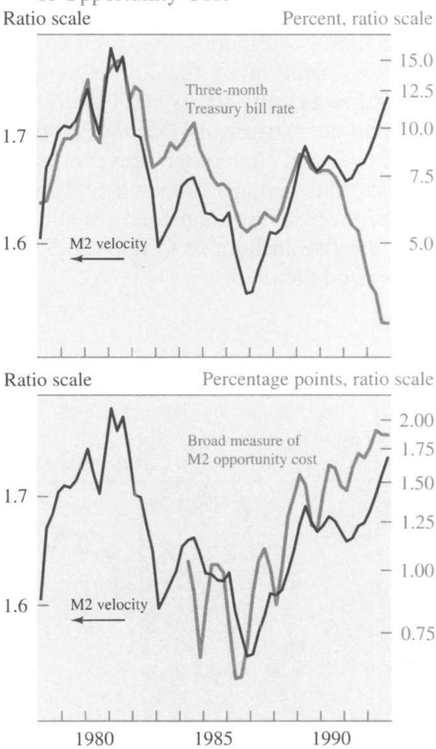


The auto loan rate is the forty-eight-month rate. The small time deposit rate is for maturities of two and one-half years and longer. The marginal federal tax rate is based on John J. Seater, "On the Construction of Marginal Federal Personal and Social Security Tax Rates in the U.S." *Journal of Monetary Economics*, vol. 15 (January 1985), pp. 121–35.

The overall effect of the unusual forces that influenced M2 in 1992 were summed up by the behavior of its velocity, the growth of which accelerated for the second year in a row, to nearly 4 percent, despite the continued sharp downward trend in short-term interest rates. In previous decades, M2 velocity and short-term rates had moved together in a reasonably predictable way (upper panel of chart on M2 velocity and measures of opportunity cost). This seemingly predictable relationship was the result of changes in deposit rates lagging behind changes in market rates: When short-term rates fell, deposit rates declined by a lesser amount, providing an incentive for savers to shift assets from market instruments to deposits, thereby depressing M2 velocity. However, because of the unusual configuration of forces discussed above, these incentives to hold M2 did not follow their usual pattern in either 1991 or 1992. Instead, a combination of the steep yield curve, sluggish adjustment of loan rates, and other factors *decreased* the incentive to hold M2, forestalling the developments that normally would have been seen in a period of rapidly falling short-term interest rates. In other words, the opportunity cost of holding M2—the earnings given up—actually widened in 1992, rather than narrowing as had happened in the past when market interest rates fell; that divergence from past patterns helps to explain why M2 velocity rose atypically (bottom panel of chart).

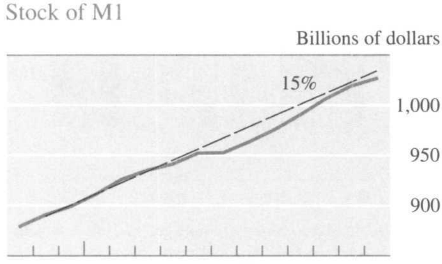
Another indication of the unusual behavior of M2 velocity in 1992 was provided by the performance of the Board staff's P* model in predicting inflation. The model is premised on reasonably stable M2 velocity over time and is used to predict the price level and inflation rates that are consistent with M2 growth. In situations where the velocity of M2 is rising atypically, slow

M2 Velocity and Indicators of Opportunity Cost

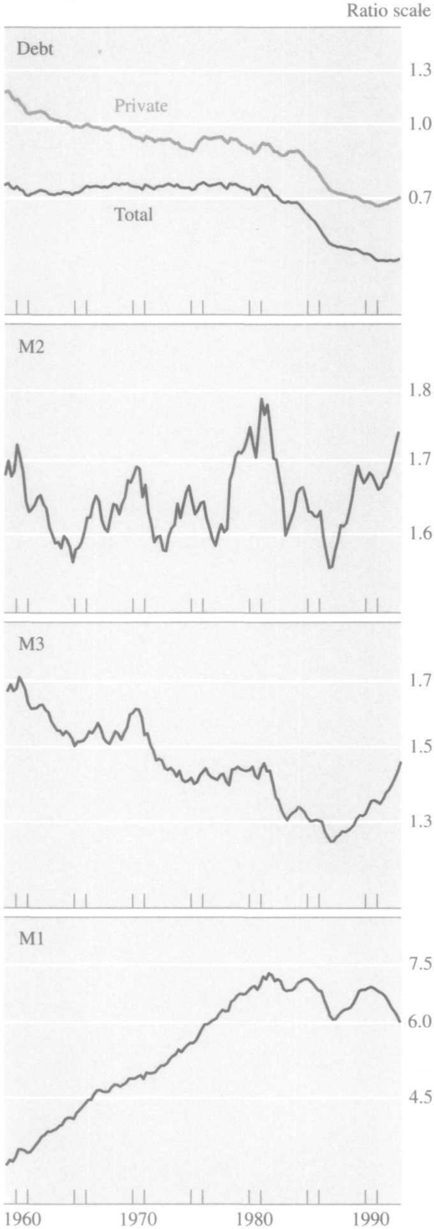


The broad measure of opportunity cost is the difference between a weighted average of competing rates and a weighted average of rates paid on components of M2. The competing rates are those on three-month and five-year Treasury securities and after-tax rates on auto loans. The indicators of opportunity cost are two-quarter moving averages.

Stock of M1



Velocity of Debt and Money



The velocity of each quantity is the ratio of gross domestic product, measured in current dollars, to the stock of the quantity. The data are quarterly averages.

growth of M2 would be associated with a lesser degree of disinflationary pressure than would be predicted by the P* model, which assumes normal velocity behavior. That, in fact, was what happened in 1992, when the model, using actual M2 growth as an input, underpredicted inflation.

The growth of M2 that did take place during 1992 was entirely attributable to its currency and transactions deposit components, as M1 growth surged to about 14¼ percent. Although this strength of M1 was in part a reflection of the pickup in aggregate income growth in 1992, it stemmed mainly from declines in both short- and long-term interest rates. Long-term rate declines prompted large volumes of mortgage-rate refinancings, particularly in the first and last quarters. Because a large portion of prepayments are held in demand deposits until the mortgage servicer remits the funds, the level of demand deposits is temporarily boosted by mortgage refinancings. Falling short-term rates boosted demand deposits by lowering the opportunity cost of holding them and by increasing the amount of deposits businesses needed to hold under compensating balance arrangements. In addition, NOW accounts were boosted by funds shifted from small time deposits, as rates on the latter fell faster than those offered on the former. Growth in NOW accounts accelerated in 1992 from the already brisk pace of 1991, and demand deposits posted the largest increase since at least 1959.

To accommodate the growth in transactions deposits associated with the process of easing reserve conditions, the Federal Reserve supplied large volumes of new reserves in 1992. Total reserves grew at around 20 percent, more than twice the rate of increase in 1991. Currency growth also was rapid, in part because of shipments abroad, and as a consequence the monetary base increased 10½ percent last year—the highest growth rate in the Board's official series, which extends back to 1959. ■

International Developments

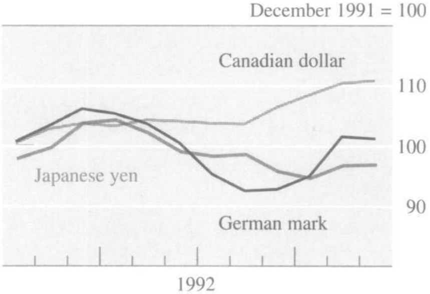
Expectations of economic recovery in the major foreign industrial countries during 1992 were not realized. Despite measures taken in some countries to boost spending and stimulate activity, real gross domestic product in the foreign G-10 countries increased by a disappointing ¼ percent.[1] In Japan and western Germany, strong first-quarter performances gave hope that late-1991 slumps had been temporary, but activity decelerated sharply thereafter. Economic activity also weakened during the year in France and Italy, while the United Kingdom showed scant signs of recovery. Among the major foreign industrial countries, only Canada experienced a pickup in growth, which was supported partly by the U.S. recovery.

By contrast, economic growth during 1992 was robust in many developing countries, particularly in the Middle East (which continued to rebound after the Gulf War) and Asia. Results in Latin America were mixed; economic reforms boosted growth in several countries, but political distractions dampened activity in Brazil. In Mexico, the pace of activity remained solid, but it was slower than in 1991.

Sluggish economic activity in many markets for U.S. exports contributed to a larger U.S. merchandise trade deficit in 1992. The growth rate of U.S. exports was only about half that of U.S. imports, which were boosted by the early effects of the domestic economic recovery. Largely because of an improvement in net service receipts, however, the current account deficit widened by less than the trade deficit after adjusting for 1991 and 1992 cash transfers associated with the Persian Gulf war.

The value of the dollar rose about 5½ percent from December 1991 to December 1992 in terms of a trade-weighted average of the other G-10 currencies. The dollar's appreciation was nearly the same after adjustment for changes in consumer price levels here and abroad, as consumer price inflation in the United States exceeded a trade-weighted measure of the average rate of inflation in the foreign G-10 countries by only about ¼ percentage point. The value of the dollar measured against the mark gained slightly more than 1 percent; in terms of the yen, it deteriorated about 3 percent. The rise in the weighted average value of the dollar mainly

Exchange Value of the Dollar versus Selected Currencies



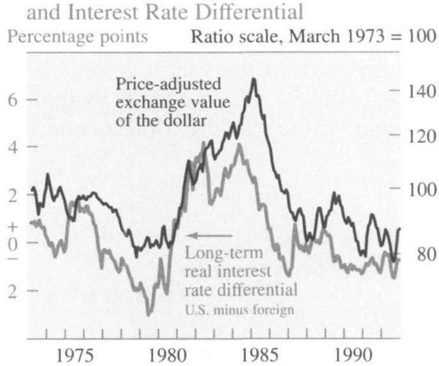
Foreign currency units per dollar. The data are monthly.

1. The Group of 10 consists of Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Sweden, Switzerland, the United Kingdom, and the United States. Unless otherwise indicated, growth rates and inflation rates are calculated from the fourth quarter of 1991 to the fourth quarter of 1992, and averages for groups of countries are weighted by the countries' gross domestic products as valued after adjusting for differences in the purchasing power of their currencies.

mirrored sharp depreciations in several European currencies and to a lesser extent the Canadian dollar.

Over the first three months of 1992, the dollar appreciated and U.S. long-term interest rates rose amid expectations that an economic recovery would take hold in the United States during the year. Over the summer, however, when the U.S. recovery proved halting and U.S. long-term interest rates moved back down, the movement in the dollar's value reversed course. At the same time, continuing growth in the German monetary aggregates at rates above Bundesbank targets and rising inflation prompted the Bundesbank to maintain a stringent monetary stance, boosting the mark's value versus the dollar. Authorities in the other countries in the European Monetary System supported the value of their currencies in terms of marks by holding interest rates high in spite of laggard economic activity.

Exchange Value of the Dollar
and Interest Rate Differential



The exchange value of the U.S. dollar is its weighted average exchange value in terms of the currencies of the other Group of 10 (G-10) countries using 1972–76 total trade weights. Price adjustments are made using relative consumer prices.

The interest rate differential is the rate on long-term U.S. government bonds minus the rate on comparable foreign securities, both adjusted for expected inflation estimated by a thirty-six-month moving average of actual consumer price inflation or by staff forecasts where needed.

The data are monthly.

Before rebounding, the value of the dollar in terms of most European currencies fell to levels well below those at which it had begun the year.

In the fall, arrangements in Europe governing exchange rates both within and outside the European Monetary System came under severe stress, with the result that some currencies were devalued and others were allowed to float. In addition, the Bundesbank allowed German interest rates to fall somewhat. These adjustments contributed to an appreciation of the dollar that was already gaining momentum from renewed indications of recovery in the United States.

Net intervention in marks by foreign central banks was of unprecedented size in 1992 as a result of exchange rate pressures in Europe. Net intervention in dollars by fifteen major central banks amounted to sales of about $9 billion. U.S. intervention was moderate in 1992, with sales of $200 million for yen and purchases of about $1,270 million for marks. U.S. monetary authorities also exchanged about $6 billion equivalent of marks for dollars directly with the Bundesbank.

Foreign Economies

All major industrial countries operated below potential in 1992, some considerably so, and inflation continued to moderate. Average consumer price inflation in the foreign G-10 countries was only 2½ percent in 1992, almost 1½ percentage points below the inflation rate recorded in 1991. Effects on prices in 1992 from the depreciation of currencies in the United Kingdom, Italy, and Canada were small. Wages also decelerated in most foreign industrial countries. The leading exception to the generally disinflationary pattern abroad was western Germany, where inflation remained in the neighborhood of 3¾ percent and contributed to the reluctance of German monetary authorities to ease more rapidly.

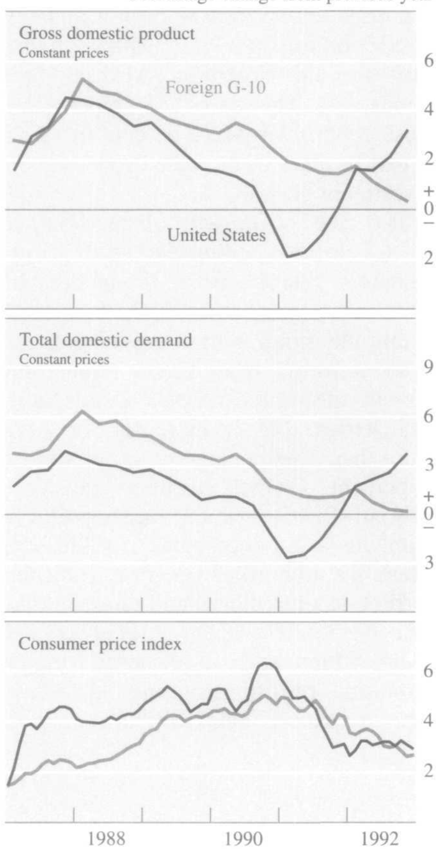
Labor-market conditions deteriorated during 1992 in the major industrial countries. Unemployment rates moved up across Europe, reaching 10½ percent in the United Kingdom and France. The unemployment rate in Canada exceeded 11¾ percent in late 1992, although thereafter signs emerged that Canada's long upward trend in unemployment might have peaked. The west German unemployment rate also moved up, although only to 7¼ percent, a level still below historical peaks. In Japan, the unemployment rate remained below 2½ percent, but more sensitive indicators suggested a slackening of labor market conditions.

The main factors that contributed to the generally disappointing performance of demand abroad were high levels of real interest rates in Europe, continued adjustment in spending by households and enterprises so as to reduce high levels of debt, a reduced pace of lending in some countries, and worries about financial-sector problems, especially in Japan and Scandinavia.

Growth in major monetary aggregates abroad generally remained subdued in 1992, with the important exception that in Germany M3 increased 8¾ percent, a rate well outside the Bundesbank's target range. Money market conditions nonetheless eased in several key countries, including Japan and, late in the year, Germany, as decelerating demand provided room for authorities to let short-term interest rates decline. Japanese short-term interest rates moved down about 2¼ percentage points, and the official discount rate was cut twice by a total of 1¼ percentage points. German authorities also allowed short-term interest rates to ease after mid-year, from a peak of about 9¾ percent to near 8½ percent. In other countries, pressures in foreign exchange markets required authorities to keep short-term interest rates above desired levels, particularly when those pressures intensified in the fall. The September departure of sterling and the lira from the exchange rate mechanism of the Euro-

GDP, Demand, and Prices

Percentage change from previous year



Data for the foreign G-10 countries are weighted by the countries' GDP as valued after adjusting for differences in the purchasing power of their currencies; the data are from foreign official sources.

Data for the United States are from the Departments of Commerce and Labor.

For GDP and domestic demand, the data are quarterly; for consumer prices, the data are monthly.

pean Monetary System allowed the United Kingdom and Italy to lower short-term interest rates, but rates in France (which held the franc in the exchange rate mechanism) were kept high and finished the year up about 75 basis points. A declining trend in Canadian short-term interest rates was temporarily reversed in the autumn; interest rate increases were intended to relieve downward pressure on the Canadian dollar that was related in part to political uncertainties.

In 1992 the combined current account surplus of the foreign G-10 countries widened about $30 billion, to nearly $40 billion. This change was more than accounted for by a $44 billion increase in Japan's surplus as Japanese domestic demand slowed. Much of the change represented a widening of Japan's bilateral surpluses with European and Asian trading partners. Lower inflation in France improved French competitiveness and helped move the current account into surplus. By contrast, current account positions in both the United Kingdom and Italy deteriorated because of their weakening competitive positions and softening demand in their European markets; the German current account deficit also widened slightly.

The current account deficit of developing countries as a group improved from $80 billion in 1991 to $59 billion in 1992. A decline in the collective trade surplus was more than offset by an improvement in net services that was due in part to lower international interest rates. Net transfers also shifted in favor of the developing countries because the large war-related transfers in 1991 from Saudi Arabia and Kuwait to industrial countries were not repeated in 1992. The deterioration of the trade balance was traceable to weak external demand and a decline in commodity prices; both factors limited export earnings while imports were being spurred by strong growth in real output in many developing countries. The current account surplus of the newly industrializing economies of Asia was about $13 billion in 1992, essentially unchanged from the previous year. A decline of $5 billion in the surplus of Taiwan was offset by increased surpluses in Hong Kong and Singapore and a smaller deficit in Korea. By contrast, the combined current account deficit of fourteen heavily indebted developing countries rose from $17 billion in 1991 to $30 billion in 1992.[2] Much of this shift was in Argentina, Mexico, and Venezuela. The value of imports by these countries rose 30 percent in 1992, in part because of increased spending on investment goods.

The rate of growth of real output in developing countries as a group increased sharply, from 3¼ percent in 1991 to 5¾ percent in 1992.[3] However, within the group, output growth was far from uniform; it fell below population growth rates in the Western Hemisphere and Africa, but it increased in Asia more than 1 percentage point, to almost 7 percent. Growth declined considerably in Brazil—which faced political problems—and moderately in Mexico, where the authorities sought to limit the current account deficit and reduce inflation further. However, Argentina and Chile, which have implemented major economic reform programs in recent years, registered gains in real output of

2. The countries are Argentina, Bolivia, Brazil, Chile, Colombia, Côte d'Ivoire, Ecuador, Mexico, Morocco, Nigeria, Peru, Philippines, Uruguay, and Venezuela.

3. The growth of output in developing countries is calculated by comparing measures of total annual output rather than fourth-quarter output.

6½ percent or more, as did Venezuela.[4] The most dramatic acceleration in output was in the Middle East, where growth rebounded from around zero in 1991 to 10 percent in 1992 as the region recovered from the Gulf War. Real output was also particularly robust in China, where the rate of expansion is estimated to have been nearly 13 percent in 1992, compared with 7 percent in 1991.

During 1992, both Brazil and Argentina made progress toward normalizing relations with foreign creditor banks to whom they are in substantial arrears. In July, Brazil reached preliminary agreement with its bank creditors on a debt-reduction package, which will be implemented in 1993 if the country makes further progress toward macroeconomic stabilization. Argentina and its bank creditors signed an agreement in December to reduce the country's external debt in 1993.

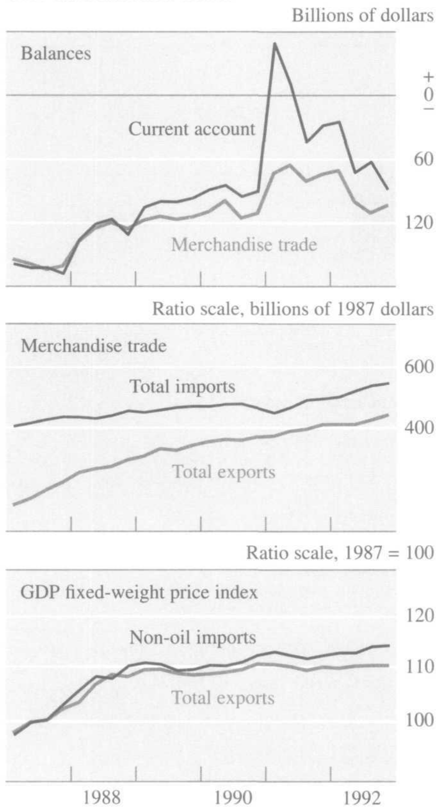
U.S. International Transactions

The U.S. merchandise trade deficit, measured on a balance-of-payments basis, widened to $96 billion in 1992, compared with $73 billion in 1991. Imports rose nearly twice as fast as exports as economic recovery gained some momentum in the United States, while growth in many U.S. export markets was sluggish. Early in the year, the deficit narrowed somewhat when a drop in oil prices lowered the value of imports. After the first quarter, however, the deficit widened sharply: Imports expanded strongly during the second and third quarters, while export growth remained subdued until late in the year.

4. Argentina's reforms not only stimulated rapid growth but brought inflation below 20 percent, compared with about 85 percent in 1991 and more than 1,300 percent in 1990.

The U.S. current account worsened substantially more than the trade account, moving from near balance in 1991 to a deficit of nearly $60 billion in 1992. However, abstracting from one-time cash transfers associated with the Gulf War (they reduced the current account deficit by $42 billion in 1991, but by only $1 billion during 1992), the current account weakened less than the trade account largely because of increased net service receipts. U.S. armed forces purchased fewer services abroad, and foreign reinsurers made

U.S. International Trade



The data are quarterly, seasonally adjusted at annual rates, and come from the Department of Commerce. The 1992 data are preliminary.

substantial payments on claims for hurricane damage in the United States.

U.S. merchandise exports rose 6½ percent in real terms over the four quarters of 1992. Most of the increase occurred in the second half of the year, and the largest gains were in computer exports. Other nonagricultural exports increased 3½ percent in real terms, about half the rate reached in 1991; among these items, machinery (other than computers) and automotive products accounted for most of the strength. Among agricultural products, wheat, soybeans, meat, and dairy products were exported in significantly larger quantities in 1992; overall, the volume of agricultural exports rose 9 percent over the four quarters of the year. The biggest gains in the value of U.S. exports were made in trade with the developing countries in Asia and Latin America where fairly strong economic growth took place. The value of exports to Japan and to European countries declined.

Merchandise imports expanded more than 10 percent in real terms during 1992. Two categories accounted for a significant portion of that rise: oil and computers. The quantity of imported oil

U.S. International Transactions[1]

Billions of dollars, seasonally adjusted

Transaction	Year		Quarter				
			1991	1992p			
	1991	1992p	Q4	Q1	Q2	Q3	Q4
Merchandise trade, net	−73	−96	−19	−18	−25	−28	−26
Exports	416	439	108	108	107	110	114
Imports	489	535	126	125	132	138	140
Services, net	45	55	13	14	13	16	13
Receipts	164	178	43	45	44	45	45
Payments	118	123	30	31	31	29	32
Investment income, net	16	10	2	4	2	3	1
Direct investment, net	53	49	12	14	12	13	11
Portfolio investment, net	−37	−39	−10	−9	−10	−9	−10
Unilateral transfers, private and government, net	8	−31	−4	−7	−8	−7	−10
Current account balance	**−4**	**−62**	**−7**	**−6**	**−18**	**−16**	**−22**
Private capital flows, net	−23	32	−9	−6	25	6	7
Bank-related capital, net (outflows, −)	−18	47	*	11	10	22	4
U.S. net purchases (−) of foreign securities	−45	−49	−11	−9	−8	−14	−18
Foreign net purchases (+) of U.S. securities							
Treasury securities	16	35	1	−1	10	5	21
Corporate and other non-Treasury bonds	26	35	7	8	12	7	8
Corporate stocks	9	−5	−2	−3	−1	−4	4
U.S. direct investment abroad	−27	−35	−12	−16	−7	−4	−9
Foreign direct investment in United States	11	−4	6	−4	5	−3	−3
Other corporate capital flows, net	5	8	2	7	4	−3	n.a.
Foreign official assets in United States (increase, +)	18	40	13	21	21	−7	5
U.S. official reserve assets, net (increase, −)	6	4	1	−1	1	2	2
U.S. government foreign credits and other claims, net	3	−1	*	*	*	*	*
Total discrepancy	−1	−13	2	−8	29	15	8
Seasonal adjustment discrepancy	0	0	1	5	1	−7	*
Statistical discrepancy	−1	−13	2	−13	−30	22	8

1. Details may not sum to totals because of rounding.
*In absolute value, greater than zero and less than $500 million.

n.a. Not available. p Preliminary.
SOURCE. Department of Commerce, Bureau of Economic Analysis.

rose 13 percent over the four quarters of 1992 as U.S. consumption of petroleum products recovered from depressed levels in 1991 and as domestic oil production resumed a downward course. Measured in constant dollars, imports of computers (including peripheral equipment and parts) jumped nearly 50 percent in 1992. U.S. domestic sales of computers became strong beginning in the summer; they were fueled by price wars and by a push on the part of U.S. businesses to take advantage of improvements in software by upgrading desktop microcomputers. Most of these sales were in lower-technology equipment—items that are often imported. Imports of products other than oil and computers rose 6 percent in real terms in 1992 as domestic demand in the United States picked up. Major sources were developing countries in Latin America and Asia, especially China.

The substantial U.S. current account deficit in 1992 was more than matched by recorded net capital inflows, so the statistical discrepancy was negative. By contrast, in 1991 the current account, capital account, and statistical discrepancy all had been close to zero.

As shown in the table, substantial inflows were recorded for both official and private capital. Foreign official holdings in the United States increased $40 billion, more than twice as much as in 1991. Substantial inflows were recorded from both industrial and other countries.

The net flow of private capital reversed in 1992, reaching an inflow of about $32 billion. Banks more than accounted for these net inflows, and foreign-related banks were a particularly important factor. They used the funds to help finance a continued general expansion of their assets in the United States. In 1991, by contrast, foreign-based banks had relied more heavily on large time deposits issued in the United States and less on inflows from abroad to finance asset growth.

Although securities transactions also contributed to the net inflow of capital in 1992, strong two-way gross flows again emphasized the widening scope for cross-border financial transactions. Foreigners added substantially to their holdings of U.S. government and corporate bonds, although they were net sellers of U.S. equities. U.S. net purchases of foreign stocks and bonds were large; in fact, the pace of foreign bond issues in the United States set a record.

U.S. direct investment abroad was strong again in 1992. Outflows to Latin America and Asia grew, and outflows to Europe were again substantial. By contrast, foreign direct investment in the United States remained depressed at a level close to zero, compared with the peak of almost $70 billion, reached in 1989. Merger and acquisition activity in the United States has declined since the 1980s, and foreign investors in particular may have been discouraged in 1992 by the disappointing returns on much recent foreign investment in the United States.

Foreign Currency Operations

U.S. monetary authorities intervened in foreign exchange markets on a moderate scale in 1992. In late January and early February, during a period when the dollar was appreciating relative to the yen, the Federal Reserve System and the Treasury's Exchange Stabilization Fund, cooperating with foreign authorities, purchased Japanese yen worth $200 million, of which $50 million was for the account of the Federal Reserve. As the dollar depreciated sharply during July and August, particularly in terms of the German mark, U.S. authorities purchased $1,270 million for marks in cooperation with foreign authorities. The proceeds of these operations were split evenly between the accounts of the Federal Reserve and the Treasury. U.S. authorities also exchanged $6,177 million of marks for dollars directly with the Bundesbank, including $3,705 million of marks from System balances. These transactions were made to bring U.S. and German balances of foreign currencies more nearly in line with current needs. On April 2 the Exchange Stabilization Fund purchased $2 billion equivalent of marks that had been warehoused with the System. No warehoused balances were outstanding from that date through the end of the year.

At year-end, the System held $21,514 million of foreign currencies valued at current exchange rates, almost entirely in marks and yen. The System realized $804 million in profits on sales of foreign currency during 1992 and recorded a translation loss of $1,882 million on foreign currency balances. There was no activity on the Federal Reserve swap network during the year. ■

Monetary Policy Reports to the Congress

Given below are reports submitted to the Congress on February 19 and July 20, 1992, pursuant to the Full Employment and Balanced Growth Act of 1978.

Report on February 19, 1992

Monetary Policy and the Economic Outlook for 1992

When the Federal Reserve presented its midyear monetary policy report to Congress last July, a moderate economic upturn was under way. Consumer spending and housing activity had risen considerably since the winter, bolstered by the decline in oil prices, by a rebound in consumer confidence in the wake of the allied victory in the Persian Gulf conflict, and by lower interest rates. Inventories had been trimmed appreciably, orders were rising, and businesses, while still cautious, had begun to increase employment and production. The key monetary aggregates had accelerated and were around the middle of their 1991 target ranges. With the stance of monetary policy seemingly conducive to an upturn in economic activity, the Federal Reserve, after having progressively reduced pressures on reserve positions earlier in the year, maintained a more neutral money market posture in the spring and early summer.

As the year wore on, however, the incipient recovery lost its momentum. Consumer spending turned down, and business and consumer sentiment began to erode. Inventories at wholesale and retail trade establishments began to increase relative to sales, inducing a new outbreak of production adjustments and layoffs that continued through year-end. Although the economy—as measured by its real gross domestic product—continued to grow in the second half of the year, the pace of expansion was only marginally positive.

The faltering of the recovery process apparently owed to a variety of forces, some of which were operating well before the oil price shock of 1990 tipped the economy into recession. In a sluggish economy and amid unexpectedly weak asset values—particularly in real estate—deteriorating financial positions of debt-laden households and corporations further damped credit demands and aggregate spending. Financial intermediaries, chastened by their negative experience with earlier loans, became more hesitant about extending new credit; the resultant tighter lending standards deepened the slowdown in economic activity and inhibited the subsequent recovery. In the government sector, where deficits remained large, not only at the federal level but also in many state and local jurisdictions, efforts to curb spending and increase revenues constituted a further drag on aggregate demand in the short run.

Inflation, meanwhile, moved down over the second half of 1991. Weak demand reduced pressures in both labor and product markets, and, after some acceleration of wages and prices in 1989 and 1990, an underlying disinflationary trend has now been established. Important in this process has been a reduction in inflation expectations, visible not only in a variety of survey data but also in the behavior of securities markets.

With actual and prospective inflationary pressures easing, economic activity flagging, and the broader monetary aggregates weakening and growing near the bottom of their target ranges, the Federal Reserve resumed easing money market conditions in the second half of the year. As a result, the federal funds rate fell from 5¾ percent in July to 4 percent by year-end, and most other short-term rates followed suit; the discount rate was also reduced over this period, from 5½ percent to 3½ percent, the lowest rate in nearly thirty years. Long-term interest rates, which had failed to respond to declines in money market rates in the early months of the year, came down significantly in the latter part of 1991, partly in response to the easing in inflationary expectations. Although long-term rates have backed up some in recent weeks, they remain appreciably below the levels of last summer. The decline in rates has helped reduce the financial burdens of highly leveraged households and corporations, which have taken this opportunity to refinance mortgages and to replace existing debt with new lower-cost bonds. Lower interest rates also have contributed to an increase in stock prices, inducing firms to boost equity issuance and to pay down debt, further strengthening their balance sheets. With the decline in U.S. interest rates, the foreign exchange value of the dollar has largely reversed the upward movement that had occurred earlier in the year.

The unusually slow growth of the key monetary and credit aggregates last year was, to a degree, indicative of the continuing restraint on private credit usage and spending. The aggregate debt of domestic nonfinancial sectors—abstracting from federal government debt, which continued to grow briskly—expanded only 2¾ percent in 1991, the slowest advance in decades, and below the pace of nominal GDP; households, nonfinancial businesses, and state and local governments all retrenched, curbing spending and borrowing in order to buttress deteriorating financial positions.

The weakness in the monetary aggregates M2 and M3 reflected not only subdued overall credit usage but also a continued decline in the share of credit intermediated by depositories. With the thrift industry contracting further, commercial banks exercising caution in their credit extensions, and borrowing demand concentrated in longer-term instruments, depository credit continued to shrink as a share of overall credit extensions. As a result, the velocity of M3—a monetary aggregate that comprises most of the liabilities used by depositories to fund credit growth—increased again in 1991, as M3 grew only 1¼ percent, near the bottom of its target range. Depository restructuring also restrained M2, which grew in line with nominal GDP despite a steep drop in short-term market interest rates; ordinarily such a drop would have been expected to depress the velocity of this aggregate. Banks, eager to improve capital positions, reduced deposit rates more than loan rates, increasing the incentive for households to pay down debt rather than to accumulate monetary assets. Less aggressive pursuit of retail accounts by depositories also led investors to switch into other financial assets, such as bond and stock mutual funds.

Ranges for Growth of Monetary and Debt Aggregates[1]

Percent

Aggregate	1990	1991	1992
M2	3–7	2½–6½	2½–6½
M3	1–5	1–5	1–5
Debt[2]	5–9	4½–8½	4½–8½

1. Change from average for fourth quarter of preceeding year to average for fourth quarter of year indicated. Ranges for monetary aggregates are targets; range for debt is a monitoring range.

2. Domestic nonfinancial sector.

Flows into these funds helped finance credit that had formerly been intermediated by depositories, facilitating shifts to longer-term borrowing and reducing the adverse effects of any retrenchment by banks and thrifts on the cost and availability of credit to many borrowers. However, some types of lending that are not so easily rechanneled—such as construction loans and credits to small and lower-rated businesses—have been curtailed, and a number of borrowers now face more stringent credit terms.

Monetary Objectives for 1992

In formulating its objectives for monetary policy for 1992, the Federal Open Market Committee has sought to promote a sustainable upturn in economic activity while continuing to build upon the hard-won gains against inflation that have already been made. The task of translating these objectives into specific ranges for money and debt continues to be complicated by the ongoing restructurings of depositories and by the evolving attitudes toward credit on the part of borrowers and lenders. The Committee believes that the rechanneling of credit flows away from depository institutions could well continue to produce slower growth in the broad monetary aggregates than normally would be associated with a given path for nominal GDP.

Taking account of these effects, the Committee has deemed the ranges for 1992 tentatively adopted last July as appropriate for achieving its objectives. The target range for M2 growth in 1992 is 2½ percent to 6½ percent, unchanged from 1991. Demands for M2 relative to income would be damped if, as seems likely, banks and thrifts continue to reduce deposit rates in lagged response to the decline that has occurred in market rates. These deposit-rate reductions could be especially large if credit continues to be channeled outside depositories; in this case, relatively modest growth in M2 would be adequate to support a satisfactory outcome for the economy. On the other hand, as the balance sheets and capital positions of depositories continue to improve, banks and thrifts may adopt a generally more accommodative posture with respect to credit extensions and would therefore have greater need for retail deposits. In that event, somewhat faster growth of M2 would be appropriate.

On balance, the Committee's M2 range for 1992 allows room for a variety of developments in the intermediation process and thus in the behavior of monetary velocity. Flexibility in interpreting M2 within its range is particularly important at this time, in light of the ongoing and unpredictable shifts in the patterns of credit usage and financial intermediation that likely will continue to buffet our financial system. Looking ahead to future years, the Committee also recognizes that the range for M2 growth may eventually have to be lowered in order to put in place the monetary and credit conditions consistent with price level stability.

The target range for M3 growth in 1992 remains at 1 percent to 5 percent. Although credit growth is expected to pick up somewhat in 1992, in line with a firming of economic activity, much of this credit likely will be financed outside the depository system. The thrift industry is expected to contract further as activity by the Resolution Trust Corporation continues apace, and banks, faced with continued—though moderating—pressures on capital positions, will still be somewhat hesitant to expand. At the same time, additional households are likely to refinance adjustable-rate mortgages with fixed-rate obligations that can easily be securitized, and corporations will probably continue to turn to equity markets and long-term bonds rather than bank loans. As a result, depository funding needs are likely to remain damped relative to the pace of economic activity, and the velocity of M3 should consequently rise further.

The monitoring range for the aggregate debt of domestic nonfinancial sectors for 1992 is 4½ percent to 8½ percent, also unchanged from 1991. Federal government borrowing is expected to remain heavy in 1992, given the large budget deficit. Debt growth in nonfederal sectors, however, should remain fairly subdued relative to economic activity as borrowers and lenders alike maintain a cautious approach to leverage, in part because of a desire to make further repairs to damaged balance sheets.

Economic Projections for 1992

Although the long-standing structural problems that aborted the fledgling recovery last summer clearly are being addressed, the speed of their resolution—and the associated restraint on economic growth—is quite difficult to gauge, augmenting the usual uncertainties in assessing the economic outlook. On the whole, however, the members of the Board of Governors and the Reserve Bank presidents believe that, with the easing of monetary conditions to date providing considerable impetus to the economy, the most likely outcome is for a moderate reacceleration of activity over 1992. At the same time, they anticipate that the trend toward price stability, which now appears to be rooted more securely, will be sustained through this year.

The forecasts of most of the governors and presidents for growth of real gross domestic product are in a range of 1¾ percent to 2½ percent measured from the fourth quarter of 1991 to the fourth quarter of 1992. With employers likely to be cautious about hiring until they are fully persuaded of the sustained vitality of the upturn, gains in employment are expected to come slowly. Thus, only a small improvement in the unemployment rate is anticipated this year, with the central tendency of projections being a range of 6¾ percent to 7 percent for the fourth quarter of 1992. With regard to inflation, the central tendency range for the CPI increase this year is 3 percent to 3½ percent. These forecasts are, in general, very similar to the projections presented by the Administration in the fiscal year 1993 budget. Indeed, the Administration's forecast for nominal GDP is well within the Committee's central tendency range and thus appears to be quite consistent with the FOMC's monetary ranges.

In their early February discussion of the economic outlook, the Board members and Reserve Bank presidents observed that the effects of recent job losses and weak consumer confidence are likely to restrain activity in the near term. Under the circumstances, the Board members and Bank presidents stressed that economic developments need to be monitored closely to guard against the possibility that the economy might falter. Nonetheless, the monetary stimulus already in train is expected to provide effective support for economic growth this year, and in this regard the early indications of a marked pickup in residential real estate activity and a rise in retail sales are a particularly favorable sign.

It is also expected that the drags on growth from disruptions in credit supply and from the restructuring of household and business balance sheets will begin to lessen over the year. As noted above, this is obviously an area of substantial uncertainty. However, as household and corporate debt loads diminish in an environment of stronger economic activity, and as lower interest rates continue to ease financing burdens of borrowers, consumers and businesses should be poised to participate more fully in the economic expansion. Moreover, the problems of credit availability that have plagued the economy over the past couple of years should begin to ease in 1992 as the economic recovery takes hold and lenders become more confident about extending credit.

Nonetheless, the pace of expansion this year is expected to remain weaker than in previous business cycle recoveries. In large part, this expectation reflects some still-unresolved economic and financial imbalances in particular segments of the economy. The persistent overhang of space in office and other commercial buildings undoubtedly will inhibit new construction in that sector for some time. In addition, the budgetary constraints that have capped government spending are likely to linger; a good many states and localities are finding that budget gaps are reopening despite the spending cuts and tax increases they instituted last year. Meanwhile, the external sector is expected to have a relatively neutral net influence on domestic production this year; foreign demand—particularly from Mexico and developing countries in Asia—should continue to boost export growth, but the anticipated pickup in domestic purchases is likely to draw in additional imports as well, limiting the potential for further substantial improvement in the trade balance.

Only a minority of Board members and Reserve Bank presidents foresee a smaller increase this year in the overall CPI than the 3 percent rise experienced in 1991. But the pickup in inflation suggested by the 3 percent to 3½ percent central tendency range is deceptive: the underlying trends in price movement are more favorable. The CPI was held down to a substantial degree last year by the unwinding of the energy price shock that followed Iraq's invasion of Kuwait in August 1990, and further sharp declines in energy prices do not appear likely in the current environment. However, an ongoing deceleration in prices is evident for a wide range of other goods and services, and with inflationary tendencies under considerable restraint from several factors—including further moderation in labor cost growth, continued slack in industrial product markets, and small increases in import prices—"core" inflation is expected to move down appreciably in 1992. Indeed, this trend should carry into 1993—a pattern

Economic Projections for 1992

Item	FOMC members and other FRB presidents: Range	FOMC members and other FRB presidents: Central tendency	Administration	MEMO 1991 actual
Percent change, fourth quarter to fourth quarter[1]				
Nominal GDP	4–6	4½–5¾	5.4	3.2
Real GDP	1½–2¾	1¾–2½	2.2	.2
Consumer price index[2]	2½–3½	3–3½	3.1	2.9
Average level, fourth quarter (percent)				
Unemployment rate[3]	6¾–7¼	6¾–7	6.8	6.9

1. From average for fourth quarter of 1990 to average for fourth quarter of 1992.

2. All urban consumers

3. Percentage of civilian labor force.

that bodes well for the achievement of a balanced, sustained economic expansion.

The Performance of the Economy in 1991

The year 1991 began with the U.S. economy in the midst of recession. Activity had contracted sharply after the jump in oil prices that followed Iraq's invasion of Kuwait in August 1990, and this weakness spilled into the first quarter with further reductions in production and employment. By the spring, however, economic data indicated that the decline in economic activity had bottomed out. The rapid conclusion of the Persian Gulf war boosted consumer confidence, and the reversal of the earlier runup in oil prices and the cumulative effects of declining interest rates were providing support for an increase in household spending. Indeed, construction of single-family homes had already turned up noticeably by April, and consumer spending posted a moderate rise in the second quarter. Although businesses continued to liquidate inventories at a fairly rapid pace, industrial production grew steadily from April through July, and hiring activity increased.

However, the pickup in the economy evident from April to July failed to develop any momentum, as the thrust to domestic demand initiated by the end of the Gulf war dissipated during the summer. The absence of a more robust recovery likely reflected the drag on aggregate demand from some longer-term economic and financial adjustments. For example, imbalances long evident in the commercial and multifamily construction sectors damped enthusiasm for new projects, and ongoing difficulties in the financial sector continued to restrain credit availability; these influences undoubtedly muted the stimulus that normally would have been forthcoming from the decline in interest rates. Fiscal restraint evident at all levels of government weighed on aggregate demand in a way not typically observed in previous economic cycles. Significant restructurings of operations in a number of sectors had the effect of retarding employment and income growth, at least in the short run. And concerns about debt-servicing burdens as well as about economic prospects sustained a reluctance on the part of businesses and consumers to borrow and increase spending.

Despite their cautious planning, some businesses experienced inventory backups in the late summer and fall, necessitating another round of production adjustments. In part, the impact of these adjustments was felt abroad as businesses cut back their imports of foreign goods. However, domestic adjustments were evident as well, and, apart from atypical weather patterns that temporarily increased the demand for electricity, industrial production was flat over the second half of the year. The sluggish pace of activity in the industrial sector was joined by weakness in other parts of the economy, and overall, the nation's real gross domestic product is estimated to have risen a scant ¼ percent at an annual rate in the fourth quarter of last year. In the labor market, layoffs proliferated once again, and the civilian unemployment rate rose to 7.1 percent at the end of 1991.

The deterioration in both industrial activity and nonfarm employment extended into this year, with factory production down sharply in January and private payrolls edging beneath the low of last April. On the other hand, housing market activity appears to have picked up somewhat since the beginning of the year, and nominal retail sales rose about ½ percent in January.

Inflation slowed in 1991, with consumer prices up 3 percent over the year, much less than the 6 percent rise posted during 1990. In part, the slowing in inflation reflected the sharp drop in oil prices early in the year; consumer energy prices in December were 7½ percent below their level at the end of 1990, with the decline concentrated in the first quarter of the year. Food price inflation also moderated considerably, amounting to only 2 percent last year after three years of increases in excess of 5 percent.

Even apart from food and energy, inflation now appears to be on a downward trend. To be sure, there were sizable increases in the CPI excluding food and energy early in the year, as higher federal excise taxes and a pass-through of the sharp rise in energy prices boosted prices for a variety of goods and services. With the subsequent reversal in oil prices and no further major tax hikes, however, price pressures eased visibly beginning in the spring. On balance, the CPI excluding food and energy rose less than 4 percent at an annual rate in the second half of 1991, well below the 5 percent pace of 1990. Labor cost pressures also diminished last year, although substantial increases in health care expenses remained a problem for employers. As measured by the employment cost index, nominal compensation per hour rose about 4½ percent over 1991, somewhat less than the increases recorded in each of the three previous years.

Household Spending—Consumption and Residential Construction

With household finances adversely affected by job losses and declining real incomes, real consumer spending rose just ¼ percent over the year, the same as in 1990. At the beginning of the year, consumer purchasing power already had been sapped by the rise in energy prices and by declines in employment. And although the retreat in oil prices then in progress and an improvement in consumer confidence following the end of the Gulf war provided a boost to spending in the spring, the failure of the recovery to take hold and concerns about financial prospects and debt burdens restrained spending in the second half of the year. On balance, real consumer outlays edged down between July and December, retracing part of the rise that had occurred during the spring and early summer.

The weakness in consumer spending over the past year was particularly evident for durable goods. A sharp drop in motor vehicle purchases accounted for much of the overall decline in spending on durables; indeed, the level of motor vehicle sales in 1991, at 12¼ million units, was the lowest since 1983. Outlays for other durable goods were down slightly over the year, after a 1½ percent decline in 1990. As with total spending, purchases of other durables picked up somewhat in the spring and early summer, but then fell in the fourth quarter as consumers retrenched. Spending on nondurable goods also declined last year, with expenditures, especially for apparel, down sharply in the fourth quarter. In contrast, outlays for services continued to trend up at a pace similar to that registered in the two previous years.

The patterns of change among the components of consumer spending—particularly the steep decline in outlays for "big ticket" durable goods—underscore the role of household balance sheet concerns in restraining economic growth last year. Household debt burdens rose substantially during the 1980s, when consumers stepped up spending on motor vehicles and other consumer durables, often financing their purchases with credit. In some parts of the nation, this spending boom spread to residential real estate as well, with the associated borrowing, which was often predicated on expectations of rapidly rising family incomes, adding further to the financing burdens of households. As income growth weakened over the past year and a half, consumers struggled to meet the monthly obligations on their accumulated debt and apparently deferred some discretionary spending in the process. This financial stress also was evidenced by an increase in delinquency rates for consumer and mortgage loans last year to levels comparable to those experienced in the previous two recessions.

A renewed pessimism on the part of households may also have contributed to the reluctance of consumers to step up spending over the latter part of 1991. As noted previously, consumer confidence, which was quite low at the beginning of the year, rose markedly upon the conclusion of the Gulf war. However, as it became apparent that the anticipated recovery in the economy was not materializing and announcements of layoffs resumed, confidence turned down, dropping especially sharply toward the end of the year. In January 1992, the Survey Research Center's index of consumer sentiment stood at the levels of last winter, while the Conference Board's confidence index was below that seen in the 1981–82 recession. Many analysts observed that consumers appeared to be more apprehensive than normally might be expected, given the broad macroeconomic circumstances—for example, the unemployment rate has remained well below that reached in the early 1980s—suggesting that concerns about longer-run economic prospects may have contributed to the heightened anxiety among households last fall.

After dropping sharply in January, housing starts posted a moderate recovery over the remainder of the year, fueled by a reduction in mortgage rates to their lowest levels since the 1970s. Sales of new and existing single-family homes rose over the year, with the pickup in demand reportedly especially pronounced from first-time buyers. Reflecting the strengthening in demand, the excess supply of unsold new homes diminished, and the pace of single-family housing starts moved above 900,000 units at an annual rate by the fourth quarter, an increase of more than 16 percent from a year earlier. Nevertheless, production was well below that of earlier years, and, despite the upturn in activity, the single-family housing market remains softer than would be expected given recent mortgage rates and the rising number of households of prime homebuying age. Continued lender caution about granting land-acquisition and construction loans reportedly has damped production in some locales. However, given the absence of significant price pressures in the housing market, restraint on the demand for single-family homes, stemming from weak income growth, concerns about employment prospects, and poor conditions for home selling, likely has been a more prominent influence on homebuilding than have supply constraints.

In the multifamily housing market, an excess supply of vacant units and restraints on credit availability continued to depress construction last year. Starts of multifamily units fell about 30 percent over the twelve months of 1991, and the number of starts during the year was the lowest since the 1950s. There have been numerous reports of restrictive lending practices damping activity in this sector. However, vacancy rates for rental units remain exceptionally high—and rents soft—suggesting that in many areas new projects might well be of questionable economic viability. Until market supplies begin to tighten discernibly, activity in this segment of the market is unlikely to show appreciable improvement.

Business Spending—Investment in Inventories and Fixed Capital

In early 1991, the investment climate was dominated by the effects of the decline in the demand for business output and the jump in energy prices during the second half of 1990. With profit margins down sharply and inventory imbalances emerging in a number of sectors, businesses reduced production and employment substantially between October 1990 and March 1991. Cutbacks in the motor vehicle sector were especially sharp over that period, although output of most other types of goods and materials turned down as well.

By the spring, inventories generally were better aligned with sales, and operating profits, while still low, had turned up. As a result, the improvement in aggregate demand in the second quarter was accompanied by an increase in business output, and industrial production rose an average 0.7 percent per month from April to July. Despite the firming in sales, businesses remained cautious, and inventory levels continued to decline through midyear.

In late summer, however, final demand slackened, and after seven months of decline, business inventories accumulated at a substantial rate from September through December. The rise in inventories was centered in wholesale and retail trade, and inventory–sales ratios there moved into ranges that appeared undesirably high in light of carrying costs and expected sales. A portion of the accumulation appeared to consist of goods ordered from abroad; indeed, a partial reaction to the overhang may have been visible in the sharp drop in nonoil imports in November. Nonetheless, retailers evidently also reduced orders from domestic suppliers, contributing to the sluggish pattern of manufacturing output in the fourth quarter. By January of this year, factory production had dropped back to its level of a year earlier, and the operating rate in industry was back down to levels that, prior to last winter, had not been seen since the brief industrial slump of 1986.

Business investment in fixed capital fell 7 percent in real terms over the four quarters of 1991. As is typical during recessions, spending was inhibited by weak profits, a rise in excess capacity, and uncertainty regarding the outlook for sales. However, investment outlays last year also were depressed by a desire on the part of many businesses to reduce debt burdens and by a continued oversupply of office and other commercial space. Even adjusting for cyclical considerations, last year's weak pace of investment appeared to extend the relatively slow rate of capital formation evident for some time. The capital stock in the nonresidential business sector, net of depreciation, has risen about 2¾ percent at an annual rate over the past decade—down from 3¾ percent annually during the previous decade. In part, this pattern has owed to a shift toward shorter-lived assets—such as computers—that depreciate more quickly. However, such outlays, by generating a relatively high flow of capital services per dollar of investment, have cushioned the impact on productivity of the slowing pace of capital formation. Even so, the quantity of investment, which has also been depressed by large federal budget deficits and the resulting low level of national saving, has been inimical to productivity growth and thus to the advance of living standards.

Real spending for equipment fell 3¼ percent over 1991, as outlays plunged in the first quarter and showed only limited improvement on net over the remainder of the year. The strongest area in investment spending was computers, for which real outlays increased more than 40 percent at an annual rate over the second half of the year; these gains were driven by new product introductions and by the substantial price cuts offered by computer manufacturers. In contrast, business investment in other types of equipment generally declined, on balance, over the year. Outlays for industrial equipment continued to deteriorate as excess capacity limited expansion in the manufacturing sector, and business purchases of motor vehicles dropped off sharply. In addition, domestic orders for commercial aircraft plunged after midyear as a number of domestic airlines trimmed investment plans. Although the large backlog of unfilled orders that still remains should sustain production and shipments for some time, the slackening in demand indicated by the sharp downturn in aircraft orders suggests that the growth surge in this sector may have run its course.

Nonresidential construction plummeted 15 percent in real terms over the four quarters of 1991. The contraction was broadly based, but especially large declines in outlays were evident for office buildings and other commercial structures. Despite the sharp cutbacks in construction in recent years, prices of existing commercial properties have continued to fall, contributing to the substantial stress evident in the financial sector. Of course, the fundamental problem is the space overhang from the earlier overbuilding; the vacancy rate for office buildings nationwide was still close to 20 percent at the end of the year. However, a lack of liquidity in this market—in particular, the reluctance of lenders to finance acquisitions of commercial properties—has made the adjustment still more difficult. Such problems are especially acute in the market for office buildings, where appraised values have declined nearly 30 percent since 1985 and where lenders and developers generally have shown little interest in new projects. For other commercial structures—primarily shopping centers and warehouses—the outlook is slightly less downbeat, with the data on new contracts and building permits suggesting that the steepest declines may have already occurred. Spending for industrial structures also generally declined over the year, as low rates of capacity utilization curtailed plans for new factory construction. Petroleum drilling activity, meanwhile, dropped sharply in response to the decline in oil prices.

Federal banking regulators have taken a number of steps to ensure that supervisory pressures do not unduly restrict real estate lending. The agencies have, for example, addressed issues relating to accounting and appraisal, to make sure that illiquid real estate exposures are evaluated sensibly and consistently. And, they have issued guidance to examiners—and simultaneously to bankers—emphasizing that banks should not be criticized for renewing loans to creditworthy borrowers whose real estate collateral has fallen in value—even when the banks need to build up capital or reduce loan concentrations over time. However, with so adverse a supply–demand imbalance in the property market, lenders understandably have remained reluctant to bear the risks of real estate exposures.

The Government Sector

Budgetary pressures were widespread in the government sector in 1991. At the federal level, the unified budget deficit increased to $269 billion in fiscal year 1991, up $48 billion from the 1990 deficit. In large part, the rise in the deficit was attributable to the slowdown in economic activity, which reduced tax receipts and increased outlays for income-support programs such as unemployment insurance and food stamps. However, as in 1990, the fiscal 1991 deficit also was affected by special factors: A pickup in net outlays for deposit insurance added to the deficit, while one-time contributions from our allies to defray the costs of Operations Desert Shield and Desert Storm reduced it. Excluding deposit insurance and these foreign contributions, the 1991 deficit totaled $246 billion.

On the revenue side, federal tax receipts rose just 2 percent in fiscal 1991, the smallest increase in many years. The slowing in receipts largely stemmed from weak nominal income growth; indeed, personal income tax payments in 1991, which accounted for nearly half of total receipts, were about the same as in 1990 despite changes in tax provisions that were projected to raise $16 billion in new revenues.

Meanwhile, spending rose nearly 6 percent in fiscal 1991. Part of the $71 billion increase in nominal federal outlays reflected the slightly more rapid pace at which the Resolution Trust Corporation resolved insolvent thrift institutions last year. In contrast, outlays were reduced by allied contributions to the Defense Cooperation Account. These contributions, which are scored as negative outlays in the budget accounts, exceeded the outlays made in 1991 for U.S. involvement in the conflict; the excess will be put toward the replacement of munitions in 1992 and beyond. Excluding deposit insurance and contributions of allies, outlays rose about 9 percent in fiscal 1991. Spending for health programs continued to rise rapidly, elevated by large increases in health care costs and in outlays for the medicaid program. Among other entitlement programs, outlays for social security and other income-support programs, which together account for one-third of total federal spending, rose more than 11 percent in fiscal 1991, reflecting substantial increases in the number of beneficiaries. In contrast, declining interest rates reduced the growth of interest payments on the federal debt. Defense outlays—excluding foreign contributions—were up 5½ percent from fiscal year 1990 to fiscal year 1991, as the additional U.S. outlays for the Persian Gulf conflict were only partially offset by the spending cuts enacted in the 1990 budget agreement and in previous years.

Federal purchases of goods and services, the portion of federal spending that is included directly in GDP, fell 3¼ percent in real terms over the four quarters of 1991. Defense purchases jumped sharply early in the year to support operations in the Persian Gulf, but declined substantially over the remainder of the year as the effects of scheduled cuts in defense outlays were augmented by a dropoff in purchases for Desert Storm; on net, defense purchases were down about 4½ percent last year. In contrast, nondefense purchases were up slightly in 1991; increases for law enforcement, space exploration, and health research offset a drawdown in inventories held by the Commodity Credit Corporation.

The fiscal position of state and local governments, which had deteriorated sharply in 1990, remained poor in 1991. The deficit in the combined operating and capital accounts (excluding social insurance funds) narrowed to $34 billion in the third quarter of 1991 from a high of nearly $47 billion in the fourth quarter of 1990; the shrinkage of this deficit represents the first major improvement since 1984, when the state and local budget surplus peaked. Even so, relative to GDP, the deficit still is quite high on a historical basis. The credit quality of state and local government debt also continued to deteriorate last year, as illustrated by the downgrading of the general obligation debt of eight states by one rating agency; most of the rating changes were the direct result of budgetary imbalances.

The poor fiscal position of state and local budgets led to both severe restraints on spending and sizable tax hikes. Overall, real purchases of goods and services edged down over the four quarters of 1991. In nominal terms, total expenditures by these governments were up 4 percent last year, less than one-half the average pace in recent years. Receipts rose an estimated 7 percent over 1991, as numerous jurisdictions imposed a variety of new tax measures and federal aid to state and local governments—especially for medicaid—increased substantially. Nonetheless, many state and local governments continue to report revenue shortfalls and spending overruns for the current fiscal year, setting the stage for another round of budget-balancing measures ahead.

The External Sector

Measured in terms of the other Group of Ten (G-10) currencies, the trade-weighted foreign exchange value of the U.S. dollar appreciated 14 percent, on balance, from December 1990 to July 1991, reversing more than one-half of the decline that had occurred from the middle of 1989 to the end of 1990. In large part, the rise in the dollar over this period reflected the quick end to the Gulf war and expectations of a recovery in the U.S. economy, as well as developments in Eastern Europe that initially weighed on the German mark. However, as the U.S. economic recovery faltered in late summer and market participants viewed further easing actions by the Federal Reserve as more likely, the dollar again turned down, averaging in December 1991 only about 3 percent above its level in December 1990. The dollar rebounded somewhat in January on market perceptions of a diminished likelihood of an additional easing in U.S. interest rates and expectations that German authorities would not push their interest rates up further.

On a bilateral basis, the dollar rose 19 percent against the mark between December 1990 and July 1991, amid disappointment about the effect of German unification on German inflation and trade. During the second half of last year, German monetary policy tightened, and the dollar gave up much of its previous gains, finishing the year just 4 percent above its December 1990 level. Other currencies in the European Monetary System generally moved with the mark during 1991, although sterling slipped somewhat near year-end. The dollar declined about 4 percent on net against the yen in 1991, as increasing Japanese trade surpluses led to the view that an appreciation of the yen would be welcomed by the authorities.

The merchandise trade deficit narrowed to less than $75 billion in 1991, compared with $108 billion in 1990; the trade deficit last year was the smallest since 1983. An especially large decline in the deficit was registered early in the year, as the drop in oil prices sharply reduced the value of imports. In addition, trade flows during the first half of 1991 were influenced by the weakening of U.S. activity (which reduced demand for imports), by continued growth abroad (which boosted exports), and by the lagged effects of the decline in dollar exchange rates that had taken place in 1990. However, imports rose sharply in the third quarter, and the trade deficit widened somewhat in the second half of the year. The current account balance recorded a small surplus, on average, during the first three quarters of 1991, a sharp improvement from the $92 billion deficit in 1990. However, about half of that improvement resulted from cash grants from foreign governments to support operations in the Persian Gulf; excluding these transfers, the current account showed an average deficit of $48 billion at an annual rate over the first three quarters of 1991. The improvement in the current account (excluding transfers) was somewhat greater than that in the trade balance owing to a strengthening of net service receipts in such areas as travel, education, and professional services.

U.S. merchandise exports grew about 10 percent in real terms over the four quarters of 1991, tempering the production declines associated with the weakness in domestic demand. Exports rose fairly strongly in the second quarter, as high levels of investment in such countries as Germany and Japan boosted exports of computers and other capital equipment. Economic activity in the major foreign industrial countries weakened as the year wore on, however, and with a deterioration in the competitive position of U.S. companies following the appreciation of the dollar over the first half of the year, export growth slowed markedly in the third quarter. Exports surged again in the fourth quarter, led by sales of computers, aircraft, and other capital goods. However, some of the recent increase appears to represent a bunching of sales rather than an increase in economic activity abroad.

Merchandise imports excluding oil grew about 4 percent in real terms during 1991. Imports declined early in the year as weak domestic spending reduced the demand for foreign goods. As domestic demand in the United States turned up in the spring, imports—especially of automotive products, computers, and consumer goods—rose and remained strong through the summer. With the subsequent weakening in demand, however, some of the additional import volume apparently ended up on retailers' shelves. In response, U.S. businesses reduced orders from abroad, and import growth slowed sharply over the fourth quarter. The quantity of oil imports, which had plunged after the sharp rise in oil prices in the fall of 1990, generally moved up through the third quarter as refiners moved to rebuild inventories. However, oil import volumes turned down again in the fourth quarter, reflecting sluggish U.S. activity and unseasonably warm weather.

The sharp reduction in the recorded U.S. current account deficit in the first three quarters of 1991 was mirrored by changes in recorded capital inflows and the statistical discrepancy. The statistical discrepancy in the international accounts, which had jumped to $64 billion in 1990, declined to virtually zero in the first three quarters of 1991.

Inflows of official capital were about matched by outflows of private capital in the first three quarters of 1991. Net official inflows amounted to $16 billion despite net intervention sales of dollars in foreign exchange markets by the G-10 countries and a drawdown of reserves held in the United States by countries helping to cover the costs of Desert Storm; some countries also financed their contributions by borrowing and liquidating investments in the Euromarkets. Net private capital outflows were $18 billion in the first three quarters, largely accounted for by banks.

In part, these outflows reflected the increased net demand for funds in the Euromarkets associated with Desert Storm transfers. In addition, the elimination by the Federal Reserve of certain reserve requirements in December 1990 led some U.S. agencies and branches of foreign banks to increase their issuance of large time deposits in the United States and to reduce their reliance on borrowing from abroad.

Securities transactions in the first three quarters of 1991 reflected the continued internationalization of financial markets. Although the net inflow was modest, private foreigners added substantially to their holdings of U.S. stocks and bonds, while U.S. residents bought a large volume of foreign stocks and bonds. Reflecting interest rate developments that encouraged shifting from short- to long-term financing, both issues of foreign bonds in the United States and issues of Eurobonds by U.S. corporations were strong. Capital outflows associated with U.S. direct investment abroad also were sizable, as U.S. investors positioned themselves to take advantage of EC 1992 and participated in the privatization of previously state-owned enterprises in such countries as Mexico. In contrast, foreign direct investment in the United States was far below recent peaks; foreign takeovers of U.S. businesses declined, and reinvested earnings were depressed by the recession.

Labor Markets

Labor market conditions generally deteriorated in 1991, and the unemployment rate rose above 7 percent by the end of the year, the highest level since 1986. Employers had moved quickly to shed workers when the recession took hold during the second half of 1990, and this pattern continued into 1991, with nonfarm payroll employment down sharply over the first four months of the year. Economic conditions improved in the spring, and labor demand turned up for a time. However, the subsequent weakening in activity in the late summer led to a renewed bout of layoffs that has continued into early 1992, retracing the job gains recorded during the spring and summer.

The net job losses last year were widespread by industry and reflected both the cyclical weakness in labor demand associated with the recession and more fundamental efforts by many businesses to restructure operations and permanently reduce the size of their workforces. Employment in manufacturing, which began its decline in 1989, fell more than 400,000 over 1991 with most of the losses in the durable goods sector. The continued contraction in commercial building depressed construction employment despite the moderate recovery in residential housing demand. Efforts to restructure existing operations and to downsize workforce levels were evident in the finance, insurance, and real estate sector as well, where job losses last year stood in contrast to the past pattern of continued hiring during recessions. Employment in trade establishments also fell substantially over the year, pushed down by the decline in consumer spending and the high degree of financial distress among retailers. In contrast, employment in services continued to trend up over the latter part of the year, as steady gains in health services more than offset sluggish hiring in the more cyclically sensitive business and personal service industries.

Reflecting the substantial declines in output and employment over the past year and a half, the unemployment rate rose more than 1½ percentage points between July 1990 and December 1991. Moreover, the distribution of job losses was especially wide compared with previous episodes of rising unemployment. Increases in unemployment were broadly based across regions, industries, and occupations, and an unusually large proportion appeared to constitute permanent layoffs.

Nonetheless, the rise in the jobless rate has been less than in prior episodes of increasing unemployment. In part, the rise has been smaller because labor force growth has been unusually slow over the past two years. In particular, the labor force participation rate, which stood at about 66 percent at the beginning of this year, is ½ percentage point below its average during the first half of 1990. This decline in participation appears to contain some elements of a cyclical pattern: The number of discouraged workers rose over the year, and sizable increases in the number of retirees were reported, perhaps reflecting to some extent a spate of early retirement programs. However, the weak labor force growth of recent years may also represent a downshift in the trend rate of increase in labor supply that—if not offset by productivity gains—could translate into a reduction in the rate of trend potential output growth. In this regard, the composition of the corresponding increase in nonparticipants is, in part, a favorable long-term development. There has been a sharp rise in recent years in the number of individuals who have left the labor force in order to attend school. Although that increase may, to some degree, reflect declining opportunity costs associated with the poor job prospects of last year, recognition of the longer-term decline in relative wages among lower-skilled workers may also have played a role. As these individuals reenter the labor force upon completion of their schooling, their increased skills should boost labor productivity and potential output in future years.

Efforts to increase labor productivity have also intensified in the business community. If the aforementioned plans to reorganize corporate structures and to downsize the labor force requirements of existing operations are successful, the possible outcome is a significant improvement in the productivity trend, much as occurred in the manufacturing sector after the considerable compression of manufacturing organizations in the early 1980s. The performance of productivity, which rose about 1 percent for the nonfarm business sector in 1991, has been somewhat better than is typical in a weak economy. However, last year's advance came after a decline in 1989 and no change in 1990, and it is difficult at this stage to distinguish more fundamental changes in productivity trends from the apparent cyclical tendency last year for employers to reduce labor inputs aggressively in response to deteriorating sales.

With widespread layoffs and the unemployment rate rising throughout the year, the upward pressures on wages that had intensified between 1987 and mid-1990 diminished somewhat over 1991. As measured by the employment cost index, increases in hourly compensation for private nonfarm workers rose 4½ percent over the four quarters of 1991, down from more than 5 percent in the first half of 1990. The wage and salary component of hourly compensation, which rose 3 percent at an annual rate over the second half of last year, exhibited the most deceleration. Although employer costs for benefits have also decelerated from their mid-1990 peak, increases in benefit costs—at 6¼ percent in 1991—remained well above those for wages alone. Expenses for health insurance have continued to spiral upward despite considerable efforts on the part of employers to control costs by negotiating directly with providers and by increasing workers' share of health expenditures. Employer premiums for workers compensation insurance also rose sharply last year, reflecting both a swelling in the number of claims and the rapid pace of inflation of medical care costs.

Price Developments

Evidence that a significant slowing of inflation is under way mounted over 1991. The consumer price index rose 3 percent during the year, about half the rate of increase in 1990. A sharp swing in energy prices accounted for a major part of this deceleration. However, the elements of a more fundamental diminution of inflation moved into place: Labor cost increases moderated; expectations of inflation eased; and upward pressures from import prices and industrial raw material prices were virtually absent during the year.

Energy prices dropped sharply in 1991, mirroring the changes in oil prices over the year. The CPI for energy fell 30 percent at an annual rate in the first quarter of last year, as the sequence of events in the Middle East reduced the posted price of West Texas Intermediate crude oil from a peak of about $39 per barrel in October of 1990 to less than $20 by February of last year. Oil prices subsequently held near that level, but gasoline prices firmed somewhat during the summer as reduced imports and domestic refinery problems led to some tightness in inventories. However, these forces were offset by declines in natural gas and electricity rates, and energy prices changed little, on balance, in the second and third quarters. Price pressures again emerged in the fall as crude oil prices trended up in September and October on concerns about supplies from the Soviet Union. Since October, however, oil prices have retreated again, with the most recent quotes at about $18 per barrel. These latest reductions probably will show up at the retail level in the first quarter of 1992; indeed, the energy component of the producer price index fell nearly 3 percent in January, and other preliminary information points to sizable declines in both retail gasoline and heating oil prices.

The CPI for food rose just 2 percent over 1991, well below the increases of 5 percent to 5½ percent in the three previous years. In part, the subdued pace of food price inflation reflects an increased supply of livestock products. Beef production turned up last year in response to the strong prices that prevailed in the preceding few years, and supplies of pork and poultry rose sharply; in response, meat and poultry prices fell about 2 percent over the year. The deceleration in food prices also extended to food groups whose prices are influenced more by the cost of nonfarm inputs than by supply conditions in agriculture; for example, the increase in the price of food away from home last year was the smallest since 1964. Elsewhere, there were large monthly variations in prices for fruits and vegetables, as adverse weather conditions temporarily boosted prices in the first half of the year and prices for some fresh vegetables jumped toward the end of the year because of the whitefly infestation in California.

The consumer price index for items other than food and energy rose 4½ percent in 1991, about ¾ percentage point less than in 1990. The index was boosted early in the year by increases in federal excise taxes on cigarettes and alcoholic beverages and by an increase in postal rates. Price increases last winter also were enlarged by the pass-through of the rise in energy prices to a wide range of nonenergy goods and services. However, the subsequent decline in energy prices soon spread to the nonenergy sector, and except for an uptick during the summer associated with some bunching of price increases, this measure of core inflation moderated significantly over the remainder of the year.

Prices for nonenergy services decelerated considerably last year, rising 4½ percent after an increase of 6 percent in 1990. Reflecting weak real estate markets, rent increases slowed sharply, with both tenants' rent and owners' equivalent rent up less than 4 percent last year. The drop in interest rates pushed down auto financing costs more than 7 percent. And, after a brief spurt early in the year, airfares receded as energy costs fell and the weak economy cut into demand; more recently, however, airfares have turned up again as carriers have reduced the availability of and increased restrictions on low-end "super-saver" fares. In contrast, prices for medical care services rose 8 percent over the year, while tuition costs and other school fees were up nearly 10 percent.

The CPI for commodities excluding food and energy rose 4 percent in 1991, about ½ percentage point faster than in 1990. In large part, the more rapid rate of inflation in goods prices reflected the aforementioned hike in excise taxes and, despite weak sales, larger increases in prices for both new and used cars. However, a slowing in price increases was evident for a number of other goods, notably apparel, household paper products, and personal care items.

The easing of inflationary pressures has been even more evident at earlier stages of processing. The producer price index for finished goods edged down over 1991 after an average 5 percent annual rate of increase over the three preceding years; this index posted another small decline in January of this year. Falling prices for energy and consumer foods accounted for much of the overall deceleration last year. Even apart from food and energy, however, producer prices slowed to a 3 percent pace. Prices for intermediate materials excluding food and energy declined ¾ percent over the year, reflecting declining fuel and petroleum feedstock costs, an easing of wage pressures, and weak demand. The downturn in economic activity also depressed industrial commodity markets last year. After dropping sharply in the fourth quarter of 1990, spot prices for these commodities continued to decline gradually over most of 1991.

Monetary and Financial Developments in 1991

The principal objective of monetary policy this past year has been to help lay the groundwork for a sustainable expansion without sacrificing the progress against inflation that had already been set in motion. The Federal Reserve progressively eased money market conditions in 1991 amid signs of continued sluggish economic activity, weak growth in the broader monetary and credit aggregates, and diminishing inflationary pressures. A more generous provision of reserves through open market operations, coupled with five separate reductions in the discount rate—which now stands at its lowest level in nearly 30 years—brought the federal funds rate and most other short-term interest rates down about 3 percentage points over the course of the year. These actions, building on earlier easing efforts, pushed the federal funds rate down to 4 percent, its lowest sustained level since the 1960s and nearly 6 percentage points below its most recent peak in the spring of 1989.

The faltering of the economic recovery in the second half of 1991 owed in part to an unusually cautious approach to credit on the part of both borrowers and lenders. Efforts by debt-burdened households and businesses to pare debt in order to strengthen balance sheets that had been strained by the general slowdown in income and by declines in property values exerted further damping effects on credit demands and on aggregate spending. Faced with deteriorating asset values and pressures on capital positions, depositories and other lenders maintained tighter lending standards and were somewhat hesitant to extend credit. The more circumspect attitude toward credit and spending on the part of borrowers and financial intermediaries was manifest in the behavior of the aggregate debt of domestic nonfinancial sectors, which grew near the bottom of the Federal Open Market Committee's monitoring range despite burgeoning U.S. Treasury borrowing. Not only was overall credit growth subdued, but credit flows continued to be rechanneled away from depositories, reflecting the more restrictive lending standards at banks and thrifts as well as efforts by borrowers to make greater use of longer-term debt and equity in order to strengthen their balance sheets. Partly as a result, the monetary aggregates M2 and M3 also finished the year near the bottoms of their target ranges.

To prevent these forces from stifling the recovery, the Federal Reserve eased money market conditions aggressively in the latter part of the year. In light of weak aggregate demand and reduced inflationary potential, long-term interest rates—which had largely failed to respond to monetary easings earlier in the year—came down substantially toward the end of 1991. This decline prompted a flood of mortgage refinancings and additional corporate and municipal bond offerings, which helped reduce the financing burdens of nonfederal sectors. Lower interest rates also contributed to a major stock market rally, which induced firms to boost equity issuance and pay down debt, partially reversing the trend of the 1980s toward increased leverage that had severely stretched corporate balance sheets.

On the whole, the nation made considerable progress in strengthening its balance sheet in 1991. Less reliance on debt, greater use of equity, and lower financing costs have helped ease debt-servicing burdens for many financially troubled households and corporations. Although to date the trend toward deleveraging has exerted a restraining effect on aggregate spending, over time this trend should help put consumers, firms, and financial intermediaries on a sounder financial footing, paving the way for healthy, sustainable economic growth.

The Implementation of Monetary Policy

The Federal Reserve eased money market conditions several times in the first few months of 1991, extending the series of easing moves initiated in the latter stages of 1990. Against a backdrop of further declines in economic activity, abating price pressures, weakness in the monetary aggregates early in the year, and continuing credit restraint by banks and other financial intermediaries, a more expansive open market posture was adopted, in conjunction with two ½ percentage point reductions in the discount rate, to engender a 125 basis point decline in the federal funds rate over the first four months of the year. Short-term Treasury rates generally followed suit, and banks reduced the prime rate in three 50 basis point increments to 8½ percent.

Long-term interest rates, by contrast, were roughly unchanged on balance over the first few months of the year. At first, these rates fell somewhat in response to the continued downturn in economic activity and declining energy prices, especially in light of initial successes in the Gulf war that ensured an unimpeded flow of oil. Success in the initial phases of the war also prompted a brief dip in the exchange value of the dollar, as safe-haven demands that had been propping up the dollar's value in the face of falling interest rates in the United States dissipated.

In March, bond yields drifted up on the post-war rebound in consumer confidence and other evidence, particularly from the housing industry, that an economic upturn was at hand. The improving outlook for recovery also contributed to narrowing risk premiums on private securities, especially on below-investment-grade issues, which had reached very high levels in January. The debt and equity instruments of banks performed especially well over this period, responding to lower short-term interest rates and the likelihood that an economic rebound would help limit the deterioration in their loan portfolios. Moderate official support for the dollar, better prospects for a U.S. economic recovery, and a rise in U.S. long-term interest rates relative to those abroad, together with an uncertain economic and political situation overseas, especially in the Soviet Union, helped to reverse the dollar's slide on foreign exchange markets.

As evidence of a nascent economic recovery cumulated through the remainder of the spring and into early summer, interest rates and the dollar continued to firm, and quality spreads narrowed further. Although the increases in rates during this period were most pronounced at the long end of the maturity spectrum, short-term rates backed up a bit as well as prospects for additional monetary easings faded. Indeed, with the pace of economic activity apparently quickening, and with the broader monetary aggregates near the middles of their target ranges, the Federal Reserve held money market conditions steady, as the stimulus already in train seemed sufficient to support an upturn in aggregate spending.

As the summer passed, however, the strength and durability of the recovery appeared less assured. Aggregate spending, production, and employment began to falter, easing wage and price pressures. In addition, the broader monetary aggregates suddenly weakened dramatically, with M2 coming to a virtual standstill and M3 actually declining in the third quarter. The softness in the aggregates was symptomatic of a warier approach to spending and borrowing on the part of households and corporations, whose balance sheet problems were exacerbated by the stagnant economy. In addition, credit standards at financial intermediaries remained restrictive, and spreads between loan and deposit rates remained high by historical standards, reinforcing households' inclinations to pay down debt rather than to accumulate assets.

To help ensure that these forces did not imperil the recovery, the Federal Reserve moved to ease money market conditions further during the latter part of the year. Pressures on reserve positions were reduced slightly in August and again in September, with the latter move accompanied by a 50 basis point reduction in the discount rate. With the economic climate remaining stagnant, price pressures subdued, and the broader monetary aggregates still mired near the bottoms of their target ranges, the System's easing moves became more aggressive in the fourth quarter, culminating in a full 1 percentage point reduction in the discount rate on December 20. All told, these moves combined to drive the federal funds rate down from 5¾ percent in July to 4 percent by year-end. Most other short-term interest rates declined by similar magnitudes, and the prime rate was reduced by 2 percentage points, to 6½ percent.

The decline in short-term interest rates, in combination with flagging economic activity, depressed credit demands, and prospects for lower inflation, contributed to bringing long-term interest rates down significantly in the latter part of 1991. The thirty-year Treasury bond rate dropped about a percentage point over the second half of the year, and mortgage interest rates tumbled to their lowest levels in many years. Declining interest rates prompted a spate of mortgage refinancings, corporate and municipal bond offerings, and a major stock market rally, which propelled most indexes to record highs. Although monetary growth bounced back a bit in the fourth quarter, both M2 and M3 remained near the lower ends of their respective growth cones. The dollar, which had begun to lose ground in foreign exchange markets in the summer—when the weakness in money and credit raised the specter of additional easings of U.S. monetary policy—depreciated further in the fourth quarter as the economic situation deteriorated and the pace of policy easings quickened. Rising interest rates in Germany also put downward pressure on the foreign exchange value of the dollar. In January 1992, the dollar rebounded somewhat, reflecting an emerging view that interest rate declines in the United States and interest rate increases in Germany might have come to an end. The former view was also reflected in the U.S. bond market, where rates retraced a portion of their earlier declines, partly on brightening prospects for the U.S. economy but also on concerns that impending fiscal stimulus may increase federal government demands on credit markets.

Monetary and Credit Flows

Patterns of credit usage and financial intermediation, which began to shift even before the onset of the economic downturn, continued to evolve in 1991, distorting traditional relationships between overall economic activity and the monetary and credit aggregates.

These changes were evident in the behavior of the aggregate debt of nonfinancial sectors, which expanded 4¾ percent in 1991, leaving this aggregate near the bottom of its monitoring range. Robust growth in federal government debt, owing to the economic downturn and to additional outlays for federal deposit insurance, masked an even weaker picture for nonfederal debt. Households, nonfinancial corporations, and state and local governments accumulated debt at an anemic 2¾ percent rate in 1991, the slowest advance in decades and below even the sluggish growth rate of nominal GDP.

The small rise in nonfederal debt velocity last year runs counter to the pattern seen in the 1980s, when the accumulation of debt vastly outstripped growth in nominal GDP. The rapid buildup of debt in the 1980s was likely a result of the deregulation of interest rates and financial innovations, which combined to lower the cost of borrowing to households and businesses, spawning a surge in leveraging activity. Greater debt burdens may also have been accumulated under the assumption that nominal income growth would be sustained at the elevated pace of the mid-1980s and that the prices of assets purchased with credit would continue to climb.

In recent years, however, asset values and income growth have fallen short of these expectations. In particular, depressed commercial and residential real estate values, coupled with slower income growth, have eroded the net worth of some borrowers and severely strained the ability of highly leveraged households and corporations to service debt. These difficulties, in turn, have fed back on to the strength of the financial intermediaries that extended the credit. In an effort to bolster depleted capital positions, reduce financing burdens, and shore up weakened balance sheets, both borrowers and lenders have adopted a more chary attitude toward additional credit.

This more cautious approach to leverage has interacted with the sluggish pace of economic activity to restrain borrowing across nearly all sectors of the economy. Nonfinancial business sector debt, held in check by the decline in financing needs associated with weak aggregate demand and by efforts of debt-laden firms to restructure their balance sheets, grew only ½ percent in 1991. Taking advantage of a buoyant stock market, particularly in the latter part of the year, corporations turned to equity financing; net equity issuance for the year was positive for the first time since 1983, and the ratio of the book value of nonfinancial corporate debt to equity, which had soared in the 1980s amid a flurry of corporate restructurings, actually turned down in 1991. Firms also took advantage of lower interest rates to refinance higher-rate long-term bonds and to reduce uncertainty about their future financing burdens by substituting long-term debt for short-term borrowing. Overall, the mixture of less debt, more equity, and lower interest rates had a salubrious effect on the financial positions of many firms. Indeed, the ratio of interest payments to cash flow for all nonfinancial firms declined in 1991, reversing some of the runup seen in the late 1980s. Consistent with an improving financial picture and prospects of an economic rebound, quality spreads on corporate issues narrowed considerably from their peaks in early 1991, especially on below-investment-grade securities. In addition, downgradings of corporate bonds dropped sharply in the third and fourth quarters, although they still ran higher than the pace of upgrades.

Deleveraging was also evident in the household sector in 1991. Consumer credit declined as households reined in expenditures, curbed their accumulation of financial assets, and pared existing debt burdens. Households took advantage of declining interest rates, particularly in the fourth quarter, by refinancing outstanding mortgages; they also substituted home equity loans for installment

Growth of Money and Debt
Percent

Period	M1	M2	M3	Debt of domestic nonfinancial sector
Annually, fourth quarter to fourth quarter[1]				
1980	7.5	8.9	9.5	9.2
1981	5.4 (2.5[2])	9.3	12.3	9.9
1982	8.8	9.1	9.9	9.2
1983	10.4	12.2	9.9	11.3
1984	5.4	8.0	10.8	14.1
1985	12.0	8.7	7.6	13.8
1986	15.5	9.2	9.0	13.8
1987	6.3	4.3	5.9	10.4
1988	4.3	5.2	6.4	9.4
1989	.6	4.8	3.6	8.2
1990	4.2	3.8	1.7	6.9
1991	8.0	3.1	1.3	4.7
Quarterly (annual rate)[3]				
1991:1	5.2	3.5	3.3	4.5
2	7.4	4.3	1.8	4.0
3	7.5	1.1	−1.1	4.9
4	11.1	3.3	1.2	5.2

1. From average for fourth quarter of preceding year to average for fourth quarter of year indicated.

2. Adjusted for shift to NOW accounts in 1981.

3. From average for preceding quarter to average for quarter indicated.

debt and other consumer credit, which carry higher financing costs and are no longer tax deductible. By reducing their net accumulation of debt and refinancing a substantial volume of their remaining borrowings at lower rates, households were able to ease their financing burdens, reducing the ratio of scheduled debt payments to disposable personal income, which had risen sharply in the 1980s. Even so, loan delinquency rates rose through much of 1991, albeit to levels not out of line with what was seen in previous cyclical downturns. On the other side of the ledger, many households that had net creditor positions saw their interest incomes decline last year.

Faced with intensifying budgetary pressures and numerous downgradings, state and local governments also put only limited net demands on credit markets in 1991. The outstanding debt of this sector grew but 3 percent last year, the smallest increase in more than a decade. Gross issuance of municipal bonds was substantial, however, as states and localities moved to refinance debt at lower rates.

Efforts by borrowers to restructure balance sheets by substituting long-term debt and equity for short-term borrowing, along with more restrictive credit standards by some lenders and the closing and shrinkage of troubled thrifts, have affected the channels through which debt flows. In particular, in recent years there has been a major rerouting of credit flows away from depository institutions. The decline in the importance of depositories, when measured by the credit they book relative to the total debt of nonfinancial sectors, has been striking, and this trend was extended in 1991. Not only did the thrift industry continue to contract, as the direct result of RTC resolutions as well as the retrenchment of marginally capitalized institutions, but commercial banks cut back on their net credit extensions. Indeed, bank credit increased only 4 percent, not even enough to offset the continued runoff at thrifts. Weakness was particularly evident in bank lending, which shrank ¼ percent last year; banks' holdings of government securities, by contrast, expanded at a rapid clip.

Although the shifting composition of bank asset flows in 1991 was reminiscent of patterns seen in previous periods of languid economic activity, the magnitude of the downturn in loan growth last year was more pronounced than the usual experience. Apparently, loan growth was depressed not only by reduced credit demands, but also by a more restrained bank lending posture. Faced with deterioration in the quality of their assets, higher deposit insurance premiums, and more stringent requirements for capital, banks retrenched, adopting a more cautious attitude regarding credit extensions. Concerns about capital, especially in light of rising loan delinquency rates and mounting loan loss provisions, induced many banks to continue tightening lending standards through the early part of 1991 and to maintain fairly restrictive standards over the balance of the year.

A more prudent approach to capitalization and lending decisions is, in the main, a positive development that ultimately will result in strengthened balance sheets for the nation's depositories. Reflecting this improved outlook, prices of outstanding bank debt and equity increased markedly from their lows in late 1990 and early 1991, outperforming broader market indexes. Bank profits, benefiting from wide spreads between loan rates and deposit rates, also showed improvement relative to the depressed levels of recent years, although they remained low by broader historical standards.

To date, depository retrenchment appears to have had some restraining effects on aggregate borrowing. Of course, in some areas, much of the credit formerly extended by banks and thrifts has been supplanted by other intermediaries and by credit advanced directly through securities markets, at little if any additional cost to borrowers. For example, growing markets for securitized loans largely have filled the vacuum created by depository restraint in the areas of residential mortgage and consumer lending. Similarly, many large businesses have turned to stock and bond markets to meet credit needs and to restructure balance sheets, reducing their reliance on banks as well. Both banks and thrifts have cut back on other types of lending that can less easily be rechanneled, however, including construction and nonresidential real estate loans, loans to highly leveraged and lower-rated borrowers, and loans to small and medium-sized businesses. Other financial intermediaries, including life insurance companies, have been afflicted by some of the same balance sheet problems plaguing depositories and have also curbed their lending to these sectors. As a result of the pullback in credit supplies, these borrowers now face somewhat more stringent borrowing terms.

As in 1990, the retrenchment of banks and thrifts and the associated redirection of credit flows away from depositories continued in 1991 to have profound effects on the broad monetary aggregates and their traditional relationships with aggregate economic activity. M3, which comprises most of the liabilities used by banks and thrifts to fund credit expansion, has been most affected by the reduced importance of depository credit in funding spending. The velocity of this aggregate, which declined through much of the 1980s, has trended up in recent years; this trend continued in 1991, as M3 rose only 1¼ percent, well below the pace of nominal GDP, leaving this aggregate near the bottom of its target range.

In the first few months of the year, M3 showed surprising strength, boosted in part by a firming of its M2 component, which benefited from declining interest rates. The most important single factor contributing to strong M3 growth in the early part of 1991, however, was the rebirth of the market for "Yankee CDs"—large time deposits issued by foreign banks in the United States. After the 3 percent reserve requirement against nonpersonal time deposits and net Euroborrowings was lifted at the end of 1990, foreign banks showed a distinct preference for funding with such instruments, rather than borrowing from their overseas affiliates or in the federal funds or repurchase agreement markets. Domestic depositories, by contrast, faced with high and rising U.S. deposit insurance premiums, exhibited no inclination to alter their funding strategies in favor of large time deposits.

The surge in Yankee CD issuance, which totaled nearly $40 billion over the first quarter, began to taper off a bit as the year progressed, revealing the underlying weakness in M3. After slowing somewhat in the second quarter, this aggregate contracted at a 1¼ percent annual rate in the third quarter, reflecting feeble loan demand in a tepid economy as well as the restructuring of depositories. The Resolution Trust Corporation played a direct role in damping M3 growth by taking assets formerly held by thrifts and funded with M3 deposits onto its own books and financing them with Treasury securities. Although M3 rebounded a bit in the fourth quarter, in line with some firming of bank credit, its growth remained subdued.

The effects of depository restructuring on M2 remain imperfectly understood. In the past, the velocity of M2 has tended to move in tandem with changes in a simple measure of the opportunity cost of holding this aggregate—that is, with changes in the returns on alternative short-term investments relative to those available on assets included in M2. Typically, when the opportunity cost of holding M2 declines as decreases in money market interest rates outpace drops in yields on deposits, holdings of M2 strengthen relative to expenditures—and velocity drops. In recent years, however, this relationship appears to have broken down, with the velocity of M2 holding up despite a steep, persistent drop in this measure of opportunity cost. This was particularly evident in 1991, when M2 expanded at about the same pace as nominal GDP despite a significant decline in such opportunity costs. M2 finished the year near the bottom of its target range and much weaker than would be expected on the basis of historical relationships among income, interest rates, and the public's appetite for monetary assets.

In the early months of the year, M2 growth accelerated somewhat from its lackluster pace of late 1990. Narrowing opportunity costs generated substantial inflows to liquid deposits, particularly those in M1, which more than offset continued runoffs in small CDs. Money growth also was temporarily boosted by strong foreign demands for U.S. currency as a safe haven during the crisis in the Persian Gulf. Through May, M2 growth remained broadly consistent with the general configuration of opportunity costs and income, and near the middle of its target range.

M2 began to slow in June, however, and stalled in the third quarter, despite expansion in nominal income and further declines in opportunity costs. Growth in this aggregate resumed in the following quarter, fueled by a surge in transactions deposits owing to additional declines in opportunity costs, but inflows to M2 remained fairly weak, and this aggregate ended the year only a little above the bottom of its target range.

Although the unusual behavior of M2 relative to income and opportunity costs has not been fully explained, it surely is related to the restructuring of financial flows and to the downsizing of the banking system. With inflows of M2 deposits apparently tending to be more than sufficient to fund weak depository credit growth, banks and thrifts seem to have pursued additional retail deposits less aggressively than in the past. Although rates offered on these deposits did not, until very recently, fall unusually rapidly in response to declining market interest rates, depositories seem to have acted in other ways to reduce the cost of funds, including adjustments in advertising and marketing strategies that would not show up in traditional measures of opportunity costs. In addition, by keeping deposit rates very low relative to loan rates, partly in an attempt to bolster profit margins while shrinking their balance sheets, depositories provided households with a greater incentive to finance spending by holding down the accumulation of M2 assets rather than by taking on new debt. This incentive likely reinforced the impetus to borrowing restraint stemming from household concerns about their own balance sheets.

The slowdown in M2 growth, particularly in the third quarter, also appears to have been related to the configuration of returns on financial assets. Yields on small time deposits and money market mutual funds largely tracked the downward path of market interest rates, falling to their lowest levels since the deregulation of deposit rates and prompting significant outflows from these components of M2. Although some of these funds shifted into the liquid deposit components of M2—whose offering rates responded slowly, as they normally do, to the declines in market interest rates—a portion of these funds appear to have left the aggregate. The primary lure seems to have been the stock and bond markets, which offered higher returns, in part because of the steep upward slope of the yield curve. Indeed, inflows to stock and bond mutual funds were robust throughout 1991, and especially since midyear, when investors seemed particularly intent on reaching for higher yields by lengthening the maturity of their portfolios. Depositories, faced with weak loan demand and pressures on capital positions, seemed disinclined to compete aggressively for these funds by offering competitive rates on longer-term CDs.

The rapid pace of activity by the Resolution Trust Corporation also likely depressed M2 growth in the third quarter, as it did throughout the year. The abrogation of existing retail CD contracts and the disruption of long-standing depositor relationships often attending resolutions of failed thrift institutions may have encouraged investors to reshape their portfolios, substituting nonmonetary financial assets for M2 deposits.

Despite sluggish income growth, M1 expanded 8 percent in 1991, the swiftest advance since 1986. Unlike M2, this aggregate has responded to declining market interest rates about as would be expected given historical relationships. M1 was boosted by large inflows to NOW accounts, whose offering rates responded very slowly, until the end of the year, to declining market interest rates. Falling rates also brought new life to demand deposits, as compensating balances to pay for bank services surged. Demand deposits likely benefited as well from the pickup in mortgage refinancings, because the proceeds from mortgage prepayments are sometimes housed temporarily in demand accounts. Rapid growth in currency, owing in part to continued strong foreign demands, also contributed to the strength in M1, as well as in the monetary base, which increased 8¼ percent last year.

Report on July 20, 1992

Monetary Policy and the Economic Outlook for 1992 and 1993

Economic activity has increased on balance since the beginning of the year, but rather hesitantly in recent months, and inflationary pressures have continued to abate. Against this backdrop, and with money and credit exhibiting renewed weakness in the second quarter, the Federal Reserve has eased money market conditions twice—in April and again in early July. The descent of domestic interest rates, which began in 1989, has now carried nominal yields on many market instruments to the lowest levels in two or three decades.

In mid-February, when the Board presented its last semiannual report on monetary policy to the Congress, the economy seemed to be struggling to regain forward momentum. Growth had come almost to a standstill in the final quarter of 1991, and, while a hint of improvement was evident in some of the indicators that were available in mid-February, convincing signs of a strengthening of activity had not yet appeared. Moreover, in looking ahead at that time, growth seemed likely to continue to be retarded by the still incomplete resolution of major structural adjustments in a variety of sectors, financial and nonfinancial. Chief among those structural impediments were persistent problems in commercial real estate markets, budgetary stress at all levels of government, a downsizing of the defense industry, exceptional caution among financial intermediaries, and ongoing efforts of businesses and households to reduce the level of their indebtedness.

At the same time, however, considerable impetus to activity was thought to be already in train, partly as a result of the substantial easing of money market conditions that the System had implemented in the second half of 1991. Among other effects, the decline in short- and long-term interest rates was reducing debt-servicing obligations and was facilitating needed balance sheet restructuring by borrowers and lenders. In assessing the situation as of last February, the Board members and Reserve Bank presidents recognized that the uncertainties in the outlook were unusually large, but they believed that a moderate pickup in output from the especially sluggish pace of the fourth quarter of 1991, coupled with further improvement in underlying price trends, was the most likely prospect in 1992.

In the event, economic growth did move back into a moderate range in the first quarter of 1992. After keeping a tight grip on their expenditures during the holiday shopping season, consumers stepped up their spending sharply in early 1992; simultaneously, purchases of new houses soared, spurred in part by lower mortgage interest rates. An unusually mild winter also helped to buoy activity in January and February. Although businesses were able to accommodate much of the burst in spending through a drawdown of inventories, the rise in demand sparked a rebound in industrial output. Consumer sentiment, which had deteriorated in late 1991 and early 1992, began to tilt back up in late winter and early spring, and business executives expressed greater optimism. Economic growth, as measured by the annualized rate of change in real gross domestic product, moved up to 2¾ percent in the first quarter, the largest quarterly gain in more than three years.

The strength in final demand that seemed to be emerging in the early part of the year does not appear to have carried through the second quarter, however. Households, restrained by a soft labor market and the lack of significant gains in real income, clamped down on their spending after the burst early in the year; real consumption expenditures appear to have grown little, if at all, in the second quarter, and new home sales fell steadily from February through May. In addition, exports, which, over the past several years, had been an area of strength in the economy, showed little growth over the first five months of 1992. Although manufacturers boosted production in April and May, they tended to do so more by stretching the hours of their workers, rather than by adding employees to their payrolls. Declines in production became evident in the industrial sector in June, as firms apparently moved quickly to forestall unintended inventory accumulation. In the labor market, the data for May and June showed a disturbing rise in the unemployment rate, to a level of 7.8 percent. On the whole, the growth of total output in the economy likely was positive again in the second quarter—as it had been in each of the four preceding quarters. But, as the Federal Reserve had anticipated at the start of the year, the drag from ongoing structural adjustments has remained heavy.

Inflationary forces have been muted this year. Prices accelerated somewhat in the first quarter, but that flare-up proved to be short-lived, as increases in the consumer price index were small, on average, in the second quarter. The "core" rate of inflation, as measured by the change in the CPI excluding food and energy, averaged 3.8 percent at an annual rate in the first six months of 1992; this rate of rise was a little lower than the average rate of increase during 1991, and it was considerably less than the increase seen during 1990. With inflation expectations down appreciably from recent highs, and with firms striving to reduce their costs on all fronts, a trend toward gradual reduction in the rate of price increase appears to be well established at the present time.

Growth in the broad measures of money was quite weak in the second quarter, leaving both M2 and M3 in June below the lower bounds of their annual ranges. Measured from its average level in the fourth quarter of 1991, M2 increased at an annual rate of 1½ percent through June, while M3 edged down at a rate of ¼ percent over that same period. As is discussed in more detail below, the sluggishness of money during this period seemed to be more a reflection of changing patterns of finance than of restraint on nominal income growth. Still, private credit growth also was relatively slow, and, in the context of renewed softness in the incoming data on spending and production, the weakness in both money and credit added to concerns about the ongoing strength of the expansion.

In this environment, the System eased money market conditions slightly in April and implemented a reduction of ½ percentage point in the discount rate on July 2, along with a commensurate further easing of money market conditions. In total, short-term interest rates have declined about ¾ of a percentage point since the beginning of the year. Longer-term rates backed up early in the year as the economic expansion appeared stronger than many people had expected, raising market concerns about a revival of inflationary pressures. However, in recent months many bond and mortgage rates have retraced their earlier increases. Broad indexes of stock prices have remained close to record levels. In foreign exchange markets, the weighted average value of the dollar, in terms of the currencies of other Group of Ten (G-10) countries, appreciated until early March, but recent depreciation, occasioned primarily by a less robust outlook for the U.S. economy, has left the dollar somewhat below its 1991 year-end level.

Declining interest rates in recent years have contributed to sizable reductions in debt-service obligations, as both long- and short-term debt has been rolled over or refinanced at lower rates. In addition, lower long-term rates and high price-earnings ratios on stocks have encouraged businesses to reduce the interest rate risk and the uncertainty associated with short-term funding by relying more heavily on issuance of long-term debt and equity. Households also have taken advantage of lower rates to refinance existing debt, especially mortgages. In addition, over-leveraged households, facing uncertain income and employment prospects and wide spreads between rates charged on consumer credit and yields on monetary assets, have moved to limit debt growth.

The resulting improvements in the financial conditions of households and businesses are evident in several indicators: Delinquencies on consumer loans and home mortgages have declined, ratings for a number of firms have been upgraded, and yield spreads have narrowed on private fixed-income securities relative to Treasury obligations. Of course, not all parties have benefited from lower interest rates; households holding short-term deposits have experienced a sizable decline in interest income. On balance, however, lower interest rates have helped households and businesses strengthen their balance sheets, thereby building a firmer financial foundation for future economic expansion.

Efforts to return to more sustainable leverage positions have contributed to slow expansion of the debt of nonfederal sectors in the first half of this year. Heavy borrowing by the federal government has kept total debt expanding at the lower end of the Federal Open Market Committee's (FOMC) monitoring range of 4½ to 8½ percent, based on current estimates. Depository credit remains especially weak, reflecting not only muted private loan demands, but also continued caution among depositories. Commercial banks no longer appear to be tightening their nonprice terms of lending, but the degree of credit restraint remains substantial and spreads between loan rates and the cost of funds remain unusually wide. Bank capital positions have improved substantially over the past year; nonetheless, banks are likely to continue working to bolster capital, partly as a consequence of incentives contained in the FDIC Improvement Act.

The contraction of depository credit has been mirrored by the meager advance in the monetary aggregates. This is seen clearly in M3, which includes most of the liabilities banks and thrift institutions use to fund loans and other assets. But M2 has also been affected. Banks and thrift institutions have not actively pursued deposit funding in light of weak loan growth, and retail deposit rates have fallen considerably over the course of the year. Consumers consequently have sought higher-yielding assets outside M2, including those in the capital market where—despite the greater risks involved—returns have appeared more attractive. In addition, given the wide deposit–loan rate spreads, some M2 holders likely have opted to pay down debt rather than to hold monetary assets.

The rechanneling of credit flows away from depositories and the associated sluggish money growth have not been entirely benign; many borrowers face higher costs and stricter terms of credit now than in the past at given levels of market interest rates. Nonetheless, weakness of the monetary aggregates has not been associated with a similar degree of restraint on aggregate demand. Indeed, growth in nominal spending has considerably outpaced that of M2 and M3; put differently, both monetary aggregates appear to have registered sizable increases in their income velocities in the first half of the year. The rise in M2 velocity is particularly notable, given the marked drop in short-term interest rates in the latter part of 1991. Ordinarily, velocity tends to fall for a time after a decline in short-term rates.

Monetary Objectives for 1992 and 1993

In reviewing the annual ranges for the monetary aggregates in 1992, the Committee noted the substantial uncertainties created by the unusual behavior of M2 and M3 velocity thus far this year. If portfolio shifts ebb and more normal relationships of depository credit to spending begin to emerge, growth of the monetary aggregates within the existing ranges would be consistent with the Committee's objectives for making progress toward price stability and fostering economic growth. However, it is unclear whether the forces giving rise to the unusual behavior of the aggregates will wane in coming months or continue unabated. Faced with these uncertain-

Ranges for Growth of Monetary and Debt Aggregates[1]

Percent

Aggregate	1991	1992	Provisional range for 1993
M2	2½–6½	2½–6½	2½–6½
M3	1–5	1–5	1–5
Debt[2]	4½–8½	4½–8½	4½–8½

1. Change from average for fourth quarter of preceding year to average for fourth quarter of year indicated. Ranges for monetary aggregates are targets; range for debt is a monitoring range.

2. Domestic nonfinancial sector.

ties, the Committee chose to retain the 2½ to 6½ percent range for M2 and the 1 to 5 percent range for M3 announced earlier this year for 1992.

The Committee also reaffirmed the existing 1992 monitoring range for the aggregate debt of domestic nonfinancial sectors. The more cautious attitudes toward borrowing that have damped credit growth this year, and the improving balance sheets of borrowers, should lay the groundwork for sustained economic expansion in years to come.

The ongoing structural changes in the financial system and the tentative nature of the recovery greatly complicated the task of choosing ranges for the coming year. The Committee recognized that the range for M2 probably would need to be reduced at some point to be consistent with the Federal Reserve's long-run objective of reasonable price stability. However, pending further analysis of the recent relationship of money stock movements to income and interest rates, the Committee chose to carry forward the 1992 ranges for the monetary aggregates and debt as provisional ranges for 1993.

Economic Projections for 1992 and 1993

The members of the Board of Governors and the Reserve Bank presidents, all of whom participate in the discussions of the Federal Open Market Committee, generally believe that the most likely scenario for the economy in the second half of 1992 is one in which real GDP increases at a moderate pace and job growth is sufficient to impart a downward tilt to the unemployment rate. In 1993, output growth is expected to pick up slightly further from the 1992 pace, bringing additional small reductions in the unemployment rate. Inflation will likely hold to a gradual downward trend over the next year and a half.

In quantifying their views of the prospects for economic growth, the Board members and Reserve Bank presidents ended up with forecasts that are somewhat stronger than those made in February. A large majority of them see the most likely outcome for this year as being one in which real gross domestic

Economic Projections for 1992 and 1993

Item	FOMC members and other FRB presidents	
	Range	Central tendency
	1992	
Percent change, fourth quarter to fourth quarter[1]		
Nominal GDP	5–6¼	5¼–6
Real GDP	2–3¼	2¼–2¾
Consumer price index[2]	3–3½	3–3½
Average level, fourth quarter (percent)		
Unemployment rate[3]	7–7½	7¼–7½
	1993	
Percent change, fourth quarter to fourth quarter[1]		
Nominal GDP	4½–7	5½–6¼
Real GDP	2½–3½	2¾–3
Consumer price index[2]	2½–4	2¾–3¼
Average level, fourth quarter (percent)		
Uunemployment rate[3]	6½–7¼	6½–7

1. From average for fourth quarter of 1990 to average for fourth quarter of 1992.

2. All urban consumers.

3. Projections are for civilian labor force.

product rises 2¼ percent to 2¾ percent over the four quarters of 1992; the central tendency of the forecasts for 1993 spans a range of 2¾ to 3 percent. With regard to the unemployment rate, the central tendency of the governors' and Bank presidents' forecasts for the fourth quarter of 1992 covers a range of 7¼ to 7½ percent, as compared with the second-quarter average of 7½ percent; the corresponding central tendency range for the final quarter of 1993 is 6½ to 7 percent.

The achievement of the projected GDP growth will depend in part on the progress in resolving the various structural adjustments noted earlier. In general, the Board members and Reserve Bank presidents believe that these structural problems will continue to exert negative drag on the economy in coming quarters, but that their force will gradually lessen. On that score, some of the recent trends have been encouraging. In the market for commercial real estate, which has been the most striking area of weakness in the economy in recent quarters, downward pressures on the prices of existing properties seem to have begun to diminish, and the rate of decline in new construction appears to be slowing. In addition, businesses and households also have made considerable progress in strengthening their finances, and even though that improvement evidently has not yet generated more expansive attitudes toward spending and investing, such a shift probably will be forthcoming at some point. An obvious risk in the outlook is that these, and the other, structural adjustments could persist with greater intensity than is anticipated; but, alternatively, a faster resolution of the structural problems—and a stronger pickup of the economy—is not out of the question either.

The governors and Bank presidents expect the rise in the consumer price index over the four quarters of 1992 to end up in the range of 3 to 3½ percent. Although an increase of this magnitude is to the high side of that realized in 1991, inflation rates were held down last year by the unwinding of the oil price shock that had occurred in 1990. Core inflation this year is expected to be lower than it was in 1991, and most Board members and Reserve Bank presidents believe that sustained progress toward the containment of costs and a further easing of inflation expectations will keep the trend rate of price increase on a course of gradual slowing next year as well. With neither food nor energy prices anticipated to depart in any meaningful way from the broad trends of inflation, the total CPI is also expected to slow in 1993, to a range of 2¾ to 3¼ percent, according to the central tendency of the FOMC participants' forecasts.

Earlier this year, in the *Economic Report of the President* and the Budget, the Administration issued forecasts that showed nominal GDP growth in 1992 and 1993 that falls within the ranges anticipated by Federal Reserve officials. Consequently, there would appear to be no inconsistency between the System's plans for monetary policy and the short-term goals of the Administration.

Looking more toward the long term, the prospect of a sustained period of declining inflation, together with a resolution of the many structural problems that currently afflict the economy, suggests the opportunity for substantial economic gains and a broadening prosperity. The Federal Reserve, for its part, can best contribute to the achievement of those objectives by keeping its sight firmly on the long-run goal of price stability. But the longer-range progress of American living standards will depend on more than monetary stability. Sound fiscal policies and an open world trading system are essential if we are to enhance capital formation and achieve the greatest possible productivity of our human and physical resources.

The Performance of the Economy in 1992

After coming almost to a standstill in the final quarter of 1991, economic activity showed more vitality in the early part of 1992. Buoyed by a surge in final sales, real gross domestic product rose at an annual rate of 2¾ percent in the first quarter. Growth evidently slowed considerably in the second quarter; in that period, signs of softness began to surface once again in a number of the indicators. Most notably, industrial production and payroll employment turned down in June, after four months of increases, and, with an influx of jobseekers into the labor market, the civilian unemployment rate moved up sharply toward midyear, to a June level of 7.8 percent—about ¾ of a percentage point above the rate at the end of 1991.

The first-quarter surge in final sales was largely a reflection of a firming of demand in the domestic economy. Consumer spending strengthened markedly in the opening months of the year, housing starts and home sales jumped, and business fixed investment increased for the first time in several quarters. In the second quarter, domestic demand appears to have risen further, but, on the whole, at a slower pace than in the first quarter. By contrast, the external sector of the economy, which had contributed appreciably to growth of the economy in 1990 and 1991, has provided little or no impetus to activity this year; exports have been limited recently by the continued sluggishness of many foreign industrial economies, and imports appear to have moved up after a couple quarters of flatness.

Although price movements were erratic from month to month in the first half of 1992, there was ample evidence that the underlying processes of disinflation still were at work. Wage increases moderated further, and productivity increases also contributed importantly to the containment of costs. The twelve-month change in the consumer price index excluding food and energy, a rough gauge of the underlying rate of inflation in the economy, dropped below the 4 percent mark; as recently as the first quarter of 1991, that measure had been running as high as 5½ percent. The total CPI rose only 3 percent over the twelve months ended in June, held down by small increases in food and energy prices over that twelve-month period.

The Household Sector

Indicators of the economic health of households were mixed in the first half of 1992. Households continued to make gradual progress in reducing their debt burdens in the first half of the year, and the incidence of financial stress seemed to diminish. However, neither income nor wealth displayed the degree of vigor needed to sustain strength in household expenditures.

When the year began, consumer spending was a major question mark in the economic outlook. Consumer outlays for goods had weakened appreciably in the final quarter of 1991, and consumer confidence, which had gone into an alarming plunge during the autumn, continued to soften into early 1992. But—such pessimism notwithstanding—consumers pushed expenditures up at a very rapid pace in January and raised them further in February; although spending softened in March, the rise in real consumption expenditures for the first quarter as a whole amounted to 5 percent at an annual rate, the strongest quarterly advance in four years. Purchases of durable goods rose briskly, and solid gains were also recorded for a wide range of nondurables. Given the size of those increases—and with housing sales also rising sharply in the early part of the year—it seemed for a time that the forces of expansion might be gathering considerable strength.

However, the first-quarter surge did not carry over into the spring. Indeed, it appears that real consumption expenditures probably were little changed in the second quarter as a whole. Nevertheless, a bright spot in the recent spending data has been the firmness of motor vehicle sales. After bottoming out in January at an annual rate of about 12 million units, the sales of cars and light trucks rebounded to a rate of about 12½ million units in the next three months and then moved up further to a level of 13¾ million units in June. Although a portion of the recent strength in auto sales apparently is a reflection of increased business investment in motor vehicles, it also seems likely that households that have put off buying new cars and trucks in the past couple of years are now entering the market in greater numbers.

Real disposable personal income fell after the oil price shock of 1990 and then turned up in the spring of 1991. Growth since then has been positive in each quarter, but a bit erratic and, on average, relatively slow. The level of real income in the first quarter of this year was about 2 percent above the recession low of a year earlier; the average for April and May was up less than 2 percent from the level of a year ago. Growth of wage and salary income has remained sluggish this year, and interest income has continued to decline. By contrast, government transfer payments to individuals have continued to grow rapidly in recent quarters, buoyed, in part, by a rise in unemployment benefits. Starting in March, disposable income also was lifted by a change in tax withholding schedules that altered the timing of tax payments to some extent, delaying a portion of those payments until 1993.

A combination of restrained debt growth and lower interest rates has led to reductions in the debt-servicing burdens of households, although, measured relative to income, the repayment burden still is relatively high by historical standards. The incidence of financial stress among households also appears to have eased somewhat in the most recent quarters for which data are available. Delinquency rates on consumer loans and home mortgages, which rose sharply from mid-1990 to mid-1991, turned down in the second half of last year and declined further in the first quarter of 1992.

Real outlays for residential investment have been rising since the start of 1991. The first-quarter gain—11¾ percent at an annual rate—took outlays to a level close to 10 percent above that of a year earlier. Even so, spending gains over the year ended in the first quarter of 1992 recouped less than half of the sharp decline of the preceding four quarters.

For a brief time early this year, residential investment seemed to be picking up considerably more momentum. In the latter part of 1991, mortgage interest rates had dropped to their lowest levels in more than fifteen years, and the sales of new single-family houses, which had already been moving up at the end of last year, surged in January and remained strong in February. Reacting to the rise in demand—and aided by an unusually mild winter—builders boosted the pace of single-family housing starts to the highest seasonally adjusted level in two years. In March, however, sales of new homes plummeted, and they weakened further in April and May. Starts also retreated; the number of single-family units started in the second quarter was 6 percent below the first-quarter average.

Several factors have affected the recent patterns of the housing indicators. The mild winter weather evidently permitted some starts to be undertaken a bit sooner than they otherwise would have been. In addition, a substantial backup of mortgage interest rates after January undoubtedly cut into demand to some degree; rates on thirty-year fixed-rate conventional mortgages rose from about 8¼ percent in mid-January to 9 percent by March and remained above 8½ percent until June. Discussion of a possible tax credit for first-time homebuyers also appears to have raised demand temporarily.

Moreover, the recovery in housing activity probably has continued to be retarded to some degree by negative influences that were evident in 1991. A significant number of potential homebuyers are being deterred by concerns about jobs and incomes. Others now view the purchase of a home as being a riskier, less attractive investment than it once seemed, owing to the sharp declines seen in house prices in some regions in recent years and to the lack of much price appreciation more generally. High vacancy rates and unfavorable demographic trends continue to be formidable obstacles to recovery in the multifamily sector. By contrast, an increasingly favorable factor is the improved affordability of housing: Lower mortgage interest rates—in part a reflection of the less inflationary environment of recent years—have substantially reduced the size of the monthly payment associated with the purchase of a home, measured relative to personal income. In that regard, the latest round of cuts in mortgage interest rates, to the lowest level since 1973, appears to have stimulated some pickup in real estate activity very recently.

The Business Sector

When the year began, the business sector of the economy was still in the process of adjusting to the sluggishness of demand and the mild backup of inventories that had emerged in the second half of 1991. Industrial production, which had declined in the final two months of last year, fell further in January; assemblies of motor vehicles dropped sharply in that month, and cutbacks in output were reported in other industries as well. Those production cuts, coupled with the January surge in household spending, led to a reduction in business inventories, clearing away most of the excess stocks that had accumulated in the final four months of 1991.

Industrial production turned up in February, and, with orders and shipments trending up, additional gains followed in each of the next three months. Assemblies of motor vehicles rose considerably during this period and, by May, were at the highest level since the fall of 1990; although assemblies were reduced by a small amount in June, automakers have announced plans to step up assemblies in the third quarter. Production of consumer goods other than motor vehicles also increased moderately over the four-month period beginning in February; a small portion of those gains was reversed in June, however. Bolstered by strong gains in the production of office and computing equipment, output of business equipment (other than motor vehicles) rose in each month from February through June.

Manufacturing and trade inventories, measured in real terms, fell further in February. Thereafter, inventories appear to have risen somewhat, on net. In manufacturing, the level of inventories at the end of May was relatively low, compared to the level of sales. But, in parts of the trade sector, stocks may have been slightly higher than desired, and with household demand looking sluggish once again, some businesses may have felt it appropriate to pull back a bit on orders for additional merchandise, triggering the production adjustments that were evident in June.

Business profits, which came under considerable pressure during the recession, began rising noticeably in the latter part of 1991 and increased sharply in the first quarter of 1992. The before-tax economic profits of all U.S. corporations jumped 12½ percent in the first quarter and were at the highest level since the first half of 1989. The profits of financial corporations have been boosted by sharp reductions in interest expenses and by a strengthening of their loan portfolios. The economic profits of nonfinancial corporations from their domestic operations also have been rising; in the first quarter of 1992, these profits, on a pre-tax basis, were more than 20 percent above their quarterly low of late 1990. That rise in profits was the result of small increases in volume, a moderate increase in the margin over unit labor costs, and substantial reductions in net interest expenses.

Stress has continued to be evident this year in several industries—notably retailing, airlines, and commercial real estate. Overall, however, corporate balance sheets have been strengthening. Issuance of equity by nonfinancial corporations has been outstripping share retirements in recent quarters, after several years in which the balance ran markedly in the other direction. In addition, the growth of business debt has remained sluggish this year, as internal sources of funds have proved to be large enough to finance a subdued level of business investment. Lower bond yields have enabled firms to replace higher-cost debt and have encouraged a shifting out of short-term liabilities. Among farm businesses, income has dropped back from the relatively high levels of 1989 and 1990, and farmers have cut back on their investment in machinery and equipment. However, farmers' balance sheets appear to be considerably stronger at this point than they were in the mid-1980s, when the sector went through an extended period of severe financial stress.

Business fixed investment turned up in the first quarter of this year, after declining in each quarter from late 1990 to the end of 1991. Real outlays for equipment increased moderately in the first quarter, and business investment in new structures turned up, after five quarters of sharp declines. The second-quarter indicators that are in hand suggest that equipment spending probably increased enough to raise total real business fixed investment further in that period.

The first-quarter rise in equipment spending amounted to about 3½ percent at an annual rate. Increased outlays for computers and related devices more than accounted for the first-quarter gain; spending for that type of equipment has been rising briskly since mid-1991, boosted by product innovations, extensive price-cutting by computer manufacturers, and the ongoing efforts of businesses to achieve efficiencies through the utilization of new information-processing technologies. By contrast, spending for aircraft, which had been strong in 1990 and for most of 1991, has weakened substantially since last autumn; a first-quarter uptick in those outlays retraced only a small part of the fourth-quarter plunge. Business outlays for motor vehicles were down moderately in the first quarter, but they appear to have firmed in the second quarter. Spending for all other types of equipment, roughly half of which is industrial machinery, was down further in the first quarter in 1992, but at a much slower pace than in 1991. In total, equipment investment appears to be exhibiting the traditional lagged response to changes in aggregate economic activity, the recent pickup being supported by the rise in profits and increased cash flow.

Real outlays for nonresidential structures rose at an annual rate of 2½ percent in the first quarter. Investment in industrial structures was up for the second quarter in a row, and increases also were reported for utilities, private educational facilities, and hospitals and institutions. However, spending for gas and oil drilling fell further in the first quarter, and the outlays for construction of office buildings continued to decline.

In total, the first-quarter level of spending for offices and other commercial structures was about 40 percent below the level of two years earlier, but there are tentative indications that the steepest part of this protracted decline may now be over. Although spending for the construction of office buildings has continued to fall rapidly this year, the outlays for commercial structures other than offices—a category that includes such things as warehouses, shopping malls, and other retail outlets—have changed little, on net, over the past several months. In addition, there are indications that the rate of decline in prices of existing commercial properties has slowed, and transactions in commercial real estate reportedly have picked up in some areas of the country this year.

The Government Sector

Government purchases of goods and services—the part of government spending that is included in gross domestic product—increased at an annual rate of 3 percent in real terms in the first quarter of 1992, after declining about 1½ percent over the four quarters of 1991. Federal purchases, which fell 3 percent last year, rose at an annual rate of about 1 percent in the first quarter; nondefense purchases moved higher, and the decline in defense purchases was smaller than those seen in previous quarters. State and local purchases, which had declined slightly over the course of 1991, were boosted in the first quarter of 1992 by a surge in the outlays for structures.

Budgetary problems continue to confront many governmental units. At the federal level, the unified budget deficit over the first eight months of fiscal 1992—the period from October to May—totaled $232 billion; this total was about $56 billion larger than the deficit recorded in the first eight months of the previous fiscal year. Federal receipts in the current fiscal year are up only 1 percent from the same period of a year earlier, while outlays have climbed about 7½ percent. On the receipts side of the ledger, the income taxes paid by individuals have been damped by slow income growth, and, despite a pickup recently, the revenue from corporate profits taxes has been weak for the fiscal year to date. Receipts from excise taxes have risen considerably this fiscal year, but these do not account for a very large share of total federal revenue.

The sharp rise in federal spending this year partly reflects a diminished flow of contributions to the United States from our allies in the Gulf War; these contributions are counted as negative outlays in the federal budget, and their shrinkage therefore translates into a rise in recorded outlays. By contrast, spending has been held down this year by a reduction in outlays for deposit insurance programs. This reduction stems, in part, from delays in funding the activities of the Resolution Trust Corporation (RTC), the federal agency that is responsible for cleaning up the problems of insolvent thrift institutions.

Excluding the allied contributions and the spending for deposit insurance programs, federal outlays have risen about 5½ percent this fiscal year. Federal financing of health care has continued to rise at a very rapid pace in fiscal 1992; grants to states for Medicaid, the fastest growing category in the health care budget, are running more than 30 percent above the level of a year ago. In addition, slow growth of the economy and actions taken to extend unemployment benefits have pushed federal spending for income support programs sharply higher, and outlays for social security have been boosted by cost-of-living adjustments and increases in the number of beneficiaries. Combined federal spending for other functions has risen only slightly in nominal terms this fiscal year. The mix of this spending is changing, however. Outlays for some nondefense functions—notably law enforcement, education, and health programs other than Medicaid—have risen fairly rapidly in fiscal 1992; outlays for defense have been cut back, even in nominal terms, once adjustment is made for the diminished flow of allied contributions.

Many state and local governments still are grappling with severe budgetary imbalances, and further progress toward correcting those imbalances was not evident in the first quarter of 1992. After four quarters in which state and local governments had managed to chip away steadily at the deep deficit in their combined operating and capital accounts, that deficit is estimated to have widened a little in the first quarter, to a total, excluding social insurance funds, of about $26 billion.

Last year's progress in reducing the combined state and local budget deficit was achieved partly through tax increases and partly through spending restraint. With deficits still large this year, legislators and administrators are facing yet another round of painful choices. Tax hikes have been implemented in some places this year, and efforts to curb spending appear to be widespread, even as the demands for many types of government services have continued to rise. Increases in the wages and benefits of state and local workers have slowed considerably in recent quarters, with wage freezes being imposed in some cases. Although state and local employment has risen a little in recent months, partly because of election activity, the cumulative growth in the number of state and local jobs over the past year has been quite sluggish, and some governments have furloughed workers temporarily in order to hold down expenditures. Against the backdrop of these widespread attempts to restrain spending, the substantial first-quarter rise in real state and local purchases may well have been a temporary bulge, rather than the harbinger of a renewed uptrend in state and local spending.

The External Sector

For the year to date, the foreign exchange value of the dollar, in terms of the currencies of the other Group of Ten (G-10) countries, has declined somewhat, on balance, from its level at the end of 1991. Appreciation early in the year has been offset by subsequent depreciation.

From its low point at the end of 1991, the dollar appreciated through about mid-March, reaching a level nearly 9 percent above where it was at year-end. The dollar was lifted during this period by data pointing to increasing strength in the recovery of U.S. economic activity, which also worked to raise U.S. long-term interest rates relative to those in other countries. From mid-March through April, exchange rates fluctuated in a fairly narrow range. Beginning in May, however, the dollar began to decline as long-term interest rates eased, and as of mid-July, it had more than reversed the rise earlier in the year. The market's reassessment of the prospects for a strong U.S. economic recovery appears to have been a major factor underlying the declines in both the dollar and long-term rates.

Developments abroad reinforced these factors. The dollar rose sharply against both the Japanese yen and the German mark early in the year. Signs of further weakening of economic growth in Japan and the decline of the Japanese stock market worked to depress the yen. Reports of a decline in German output in the fourth quarter of 1991 and increasing expectations that the Bundesbank would not move further toward tightening German monetary policy contributed to the weakness of the mark. Beginning in late April, the dollar started to decline against the yen and the mark. News of a substantial widening of Japan's current account surplus and a belief that the Group of Seven nations supported appreciation of the yen contributed to a turnaround in the dollar's exchange rate against that currency. In Germany, economic activity proved stronger than expected in the first quarter and, along with rapid money growth in that country, led both to a reevaluation of the prospects for an early easing by the Bundesbank and to a rise in the mark.

On balance, the dollar declined more than 3 percent against the mark and was little changed against the yen from the start of the year to mid-July. The dollar appreciated against the Canadian dollar; with Canadian real GNP flat in the fourth quarter of 1991 and posting only a small rise in the first quarter of this year, Canadian authorities eased interest rates and appeared to welcome the associated decline in their currency as a way to help stimulate economic activity. By contrast, the dollar depreciated moderately against the currencies of major developing countries over the first half of 1992, after adjustment for movements in relative price levels.

Prices of U.S. non-oil imports accelerated to a 6¼ percent annual rate of increase in the first quarter of 1992, more than double the rate of rise in the fourth quarter of 1991. The jump in import prices most likely reflected the lagged effects of the depreciation of the dollar that occurred during the latter part of 1991. Most of the price increase of the first quarter was reversed in April and May. The price of oil imports declined 15 percent in the first quarter in response to strong OPEC production and warmer-than-normal weather. However, that oil price decline was reversed in the second quarter in response to production restraint by Saudi Arabia and to indications that the Kingdom may be prepared to target prices at a somewhat higher level.

With growth of the U.S. economy still on a relatively slow track, real merchandise imports remained about unchanged in the first quarter, after only a small increase in the fourth quarter of 1991. Increases in imports of capital goods in the first quarter were about offset by declines in imports of consumer goods. Data for April and May show the quantities of imports of most categories of goods moving up noticeably from their first-quarter averages.

Export volume, which had climbed sharply in the final quarter of 1991, held around its fourth-quarter pace in the first five months of 1992. Despite its recent flatness, export volume in this five-month period was about 7½ percent above the level of a year earlier. The strongest growth in exports over the past year has been in capital goods, particularly to developing countries, reflecting strong investment demand in Latin America (especially Mexico), the Middle East, and in Asia. However, the general slowdown in growth in the major industrial countries last year, and the recessions in some countries, generally continued during the first half of 1992, depressing the growth of U.S. exports to these countries. At the same time, special factors that contributed to the strength in exports last year—notably the surge in investment demand in Latin America and replacement demands from the Persian Gulf countries after the war—have been less pronounced this year.

The merchandise trade deficit narrowed to an annual rate of $70 billion in the first quarter of 1992, slightly below the deficit recorded in the fourth quarter of 1991 and also a little below the 1991 average. The current account showed a deficit of $21 billion at an annual rate in the first quarter, compared with a deficit of $4 billion for calendar-year 1991. However, excluding unilateral transfers associated with Operation Desert Storm in both periods, the current account deficit in the first quarter—$23 billion at an annual rate—was about half the deficit seen in 1991. This improvement in current account transactions reflected a further widening of the substantial surplus on net service transactions (particularly in the areas of medical, educational, and other professional and business services) and an increase in net investment income receipts.

A large net capital inflow was recorded in the first quarter of 1992; foreign official holdings of reserve assets in the United States rose strongly, and private capital transactions showed a small net inflow. Within the private-sector accounts, the first quarter brought substantial capital outflows that were associated with U.S. purchases of foreign securities and increased direct investment abroad—particularly in intercompany debt flows to Canada and the United Kingdom. These outflows were largely offset by a sizable net capital inflow reported by banks, and by private foreign purchases of U.S. securities other than Treasury securities. Inflows associated with foreign direct investment in the United States amounted to less than $1 billion in the first quarter, down sharply from the average pace in recent years; acquisitions of U.S. businesses by foreigners fell sharply, and slow growth in the United States produced reduced earnings to be reinvested in this country. The net capital inflow in the first quarter exceeded the current account deficit by a wide margin, implying a substantial statistical discrepancy in the international accounts—$16 billion at a quarterly rate. The discrepancy in 1991 had amounted to only $1 billion over the year as a whole.

Labor Market Developments

Payroll employment, which had declined somewhat in the final quarter of 1991, fell further in January of this year. Thereafter, employment rose in each month from February through May, before turning down once again in June. In the private sector, the level of payroll employment in June was up only slightly from its level at the end of 1991, and it remained well below the prerecession peak of 1990.

The sectoral patterns of change in the number of workers on private payrolls continued to vary considerably in the first half of 1992. Employment at establishments that provide services to other businesses rose fairly briskly, especially in the period from February through May. Those gains seemed to be a reflection of a firming of activity in the business sector, but they also may have been symptomatic of businesses' hesitation to push aggressively into expansion; it appears that firms may simply have been turning temporarily to outside help, rather than committing themselves to the expansion of their own payrolls.

Elsewhere, employment in the health services industry continued to rise in the first half of 1992, but in many of the other major sectors employment either changed little or declined. The number of jobs in the construction business in the second quarter was about the same as in the final quarter of last year. Employment in retail trade was also about flat over that same period. In manufacturing, employment fell slightly over the first half of the year, with small declines reported across a wide range of industries.

In total, about 200,000 new jobs were created in the first half of 1992, according to the payroll data obtained from business establishments and governments. An alternative employment series, compiled from the monthly survey of households, showed the number of persons with jobs rising by a larger amount—about 850,000—over that same period. Although a complete accounting of the reasons for the recent disparity between these two surveys is not possible, one possibility is that the payroll survey might not be fully capturing job growth at newly created establishments. If that is the case, then actual employment growth in the first half of this year may have been somewhat stronger than the payroll data indicate, although it still was not comparable to the gains seen at a similar stage of previous economic recoveries.

Despite the rise in employment in the household survey, there were further sharp increases in the number of unemployed, and the civilian unemployment rate rose from 7.1 percent in December to a level of 7.8 percent in June. Unemployment rates moved up, on net, for most occupational and demographic groups during the first half of the year, with especially large increases for adult men and teenagers. Much of the rise in unemployment in the first half consisted of persons who had lost their jobs. In addition, unemployment was boosted by a rise in the number of persons who had entered or re-entered the labor force, but were unable to find jobs; this influence was especially pronounced in May and June, the two months in which most of the first-half rise in the unemployment rate occurred.

The civilian labor force—the sum of those persons who are employed and those who are seeking work but cannot find it—grew very rapidly in the first half of 1992—about 3 percent at an annual rate. However, this surge in the labor force follows a period in which labor force growth had been quite weak, and the percentage increase over the past year is much smaller—about 1½ percent. Moreover, with the labor force participation rate now back to its previous peak and the working-age population estimated to be rising rather slowly in coming quarters, it does not seem likely that labor force growth can be maintained at its recent pace for very long.

The softening of labor markets and easing of inflation expectations since mid-1990 has been reflected in a gradual, but persistent deceleration of labor compensation rates over the past couple of years. The twelve-month rate of change in the employment cost index for private compensation, after peaking at 5.2 percent in the first half of 1990, declined to 4.6 by the end of that year, slowed to 4.4 percent in 1991, and eased still further, to 4.2 percent in the twelve-month period that ended this past March. The annual rate of increase in straight-time wages has been running at less than 3½ percent in recent quarters. However, the cost of benefits that firms provide to their employees has continued to rise rapidly, propelled by the steep climb in the cost of medical insurance and by increases in payments for workers' compensation. Nonetheless, the slower rate of increase in nominal compensation per hour, coupled with a somewhat faster rate of deceleration in consumer prices, has been translating into increases in real hourly compensation.

Productivity has been picking up. In the first quarter of 1992, output per hour worked in the nonfarm business sector was 1.9 percent above the level of a year earlier, a four-quarter improvement last achieved in early 1988 when the economy was still growing rapidly. At the same time that employers have been cautious in expanding output, they have continued to move aggressively to economize on labor input, thus boosting output per hour. The increase in productivity, together with the slowing of hourly compensation, held the rise in unit labor costs to just 1.2 percent over the year ended in the first quarter of 1992, the smallest four-quarter increase in labor costs in eight years.

Price Developments

All the measures of aggregate price change show inflation to have eased substantially from its most recent peak. The 3 percent rate of rise in the consumer price index over the past year is roughly half the rate at which that index increased in 1990; swings in energy prices account for a sizable part of that slowdown, but most non-energy prices have slowed as well. A halving of the rate of price rise also is evident in the fixed-weight price index for gross domestic purchases, a measure that takes account of the prices paid by businesses and governments as well as those paid by consumers. Measures of price change that are related to domestic production (rather than to domestic spending) have slowed by smaller, but still appreciable, amounts. For example, the fixed-weight price index for gross domestic product, the broadest measure of price change for goods and services produced domestically, rose less than 3 percent over the four quarters ended in early 1992; that index had moved up at rates of 4 to 4½ percent in each year from 1988 to 1990.

Consumer energy prices have continued to fluctuate since the end of the Gulf War, but those fluctuations have been relatively subdued. Energy prices at the retail level fell early in 1992, influenced by the mildness of the winter, the further cut in U.S. industrial production early in the year, the persistence of sluggish growth in other industrial countries, and the high level of OPEC production. Later in the winter, however, energy prices began to firm. The upswing in U.S. industrial activity that began in February gave some lift to prices, as did the return to more normal weather patterns in late winter. Further impetus to prices came in the spring, with the apparent mid-May shift by Saudi Arabia toward somewhat greater production restraint than had been expected. In response to these developments, the spot price of West Texas intermediate moved up from a February low of about $18 per barrel to a level of more than $22 per barrel in June. The CPI for energy, basically following the lead provided by the oil markets, rose moderately in March, April, and May, and then jumped 2 percent in June. These increases more than reversed the declines seen early in the year. Even so, the CPI for energy in June was up only moderately from the level of a year earlier, most of the price swings of the past twelve months having essentially cancelled out. In the oil market, the price of West Texas intermediate has softened a little, on net, since June and recently has been in a range not much different from that of a year earlier.

Food prices have slowed considerably over the past year and a half. The CPI for food rose more than 5 percent in each year from 1988 to 1990. But last year they rose only 2 percent, and in the first half of this year, they changed little on net. A temporary runup in fruit and vegetable prices in late winter was reversed in the spring, and increases in the prices of other foods were small on average during the first half of the year. As of June the CPI for food was only 0.1 percent above the level of a year earlier.

The marked slowing of food prices since the end of 1990 is partly the result of declines in the prices received by farmers for their products. In addition, however, the food sector is being affected by forces similar to those that are shaping price trends in other parts of the economy: Demand growth has been relatively sluggish in the food sector, competition is intense in both food retailing and the fast food business, and increases in labor costs have been restrained. Price increases at grocery stores over the past year have been small even for those foods for which farm products account for only a small portion of value added, and the twelve-month rise in prices of food consumed away from home, a category dominated by nonfarm inputs, has been running in the lowest range since the mid-1960s.

The CPI excluding food and energy, which had increased at an annual rate of only 3 percent during the final three months of 1991, climbed at a rate of 4¾ percent in the first three months of 1992. The prices of non-energy services rose a little faster in the first quarter than they had in the latter part of 1991, and the prices of commodities other than food and energy, which had changed little in the fourth quarter, surged ahead at an annual rate of 5¼ percent. Apparel prices, which had declined in late 1991, moved up rapidly in the first quarter, and fairly large increases were reported for several other commodities. But, the first-quarter flare-up of price increases dissipated in the spring, as the annual rate of increase in the CPI excluding food and energy dropped to less than 3 percent over the three months ending in June. The price indexes for both commodities and services rose much less rapidly during this period than they had in the first quarter.

Looking beyond the many twists and turns that inevitably show up in the price data over any short period, the reports of recent months appear to be depicting a gradual, but broadly based, slowing in the trend of consumer prices. The twelve-month change in the CPI for services excluding energy, a category that has a weight of more than 50 percent in the CPI total, has dropped back about 2 percentage points since early 1991, to a pace of 4¼ percent; deceleration is evident for most types of services included in that total. A slower rate of price increase also has emerged across a broad range of CPI commodities, although, somewhat surprisingly, the slowing there has not proceeded as rapidly as in the markets for services.

A sustained easing of inflation pressures also is widely evident in the data on prices received by domestic producers. In June, the producer price index for finished goods other than food and energy was 2½ percent above the level of a year earlier; toward the end of the 1980s, this index had been moving up at more than a 4 percent rate. The prices received by producers of intermediate materials other than food and energy have risen less than ½ percent, on balance, over the past year; their cumulative increase over the past three years amounts to just 1¼ percent. The prices of industrial commodities, which tend to track roughly the contours of the business cycle, have firmed in the first half of this year, after sharp declines from the autumn of 1990 to the end of 1991; however, in the context of a still hesitant recovery, the recent firming of these prices has been relatively subdued compared with the increases seen during many past periods of stronger expansion in industrial activity.

Monetary and Financial Developments in 1992

Monetary policy in 1992 has continued to be directed toward the goal of securing a sustained economic expansion while making progress toward price stability. In furtherance of these objectives, the Federal Reserve this year has eased money market conditions twice—once in association with a cut in the discount rate—and lowered reserve requirements.

On balance, most signs from financial markets this year have been consistent with a moderate pace of expansion in economic activity, but also seemed to indicate questions about lasting gains in reducing inflation. Short-term real and nominal interest rates have declined to unusually low levels, and the yield curve has been extraordinarily steep while share prices have been at near-record levels—a pattern often associated with market expectations of a strengthening economy. In addition, the risk premiums on private credit instruments relative to Treasury obligations have narrowed, indicating growing market confidence in private borrowers and ample credit availability in securities markets. Households and businesses improved their balance sheets by constraining total debt growth, issuing equity, and refinancing costly existing debt with longer-term debt at lower rates. As a result of these actions and the decline in interest rates, borrowers have been successful in reducing the ratio of debt-service payments relative to income.

In contrast with the positive signals from other financial variables, the advance in the money and credit aggregates has been very subdued. M2 and M3 in June stood below the lower end of their annual growth cones, and the debt of domestic nonfinancial sectors was running at the lower end of its range. In part, the sluggish expansion of M2 and M3 seemed to be related to the actions of borrowers and lenders to restructure balance sheets and was not reflected in commensurate weakness in spending. Under pressure to improve their capital positions and earnings and facing weak loan demand from borrowers relying more heavily on longer-term debt from market sources, banks and thrift institutions have not been aggressively seeking to expand loan portfolios. In these circumstances, depositories have cut deposit rates substantially this year, and many customers have shifted their funds to alternative assets or applied their deposit balances toward debt repayment. These actions have resulted in appreciable increases in the velocities of the broad aggregates—a situation the FOMC has taken into account in assessing how much weight to place on slow growth in the aggregates in making policy decisions.

Implementation of Monetary Policy

Early in the year, economic releases and financial market indicators signaled an improvement in economic activity—consumer expenditures and confidence were up, M2 growth surged in late January and February, a wave of refinancing activity indicated households and businesses were successfully reducing debt-servicing costs, and the ebullient tone in the stock market anticipated even stronger economic fundamentals in the future. The Federal Open Market Committee noted these positive developments at its meetings during the late winter and spring, but in view of ongoing impediments to robust expansion—including still-strained balance sheets and limitations on credit availability—concluded that the recovery was still fragile. Recognizing the tentative nature of the recovery and confident that a disinflationary trend had been firmly established, the Committee remained especially alert in this period to the potential need for further easing of money market conditions if the economy failed to show continued improvement.

During the early months of the year, the bond market seemed to focus on the possibility of a strong recovery, and long-term interest rates backed up about ½ percentage point from early January through March. A robust recovery could rekindle upward price pressures and would produce stronger demands for credit. In addition, looming U.S. budget deficits and potential credit needs of countries undergoing the transition from centrally planned to market economies were seen as adding to upward pressure on interest rates in the future.

Despite the rise in long-term rates, corporate bond yields remained well below levels prevailing in recent years. Eager to refinance costly existing debt and to reduce the uncertainty and interest rate risk of short-term funding, many firms issued bonds and used a portion of the proceeds to pay down bank loans. Faced with tepid loan demand and continuing pressures on earnings and capital positions, banks lowered deposit rates promptly as market rates declined and did not raise them when intermediate and long-term market rates backed up in the first quarter. Households responded by shifting funds into nonmonetary assets and by paying down debt at the expense of deposit accumulation. Although these and other portfolio adjustments appeared to play a prominent role in the deceleration of M2, the possibility that income growth might also be slackening, perhaps due to tight lending terms at banks and the reluctance of businesses and households to borrow, could not be ruled out. Incoming data over the spring suggested only a modest further rise in economic activity after February, and given the Committee's concerns about the sustainability of the recovery, the Federal Reserve slightly eased the degree of reserve market pressure in mid-April. The federal funds rate declined to 3¾ percent, its lowest sustained trading level since the 1960s; other short-term rates generally followed suit, edging down about 25 basis points. Long-term rates registered little response to the policy action; the rate on the thirty-year Treasury bond was essentially unchanged in the days following the move.

The Federal Reserve's easing of reserve market pressure in April came only days after implementation of a previously announced reduction in reserve requirements. Reserve requirements are effectively a tax on depository intermediation; the cut in reserve requirements on transaction deposits from 12 to 10 percent was intended to reduce this burden on depositories and their customers and thereby to stimulate flows of credit. The effect on credit should come directly as sterile reserves are freed for lending and indirectly as increased earnings improve depository institutions' access to capital and their willingness to lend. This year's reduction in reserve requirements sparked little of the heightened volatility of the federal funds rate that ensued from the reserve requirement cut in 1990. In large measure, the smoother transition this year reflected the higher level of reserve balances available to cover daily clearing needs; balances have been boosted in recent months by a higher level of transaction deposits in concert with a sizable increase in bank clearing balances at the Federal Reserve.

Neither the April easing of reserve market pressure nor the cut in reserve requirements revived the broad monetary aggregates. Other financial indicators, however, suggested that the markets were anticipating continued economic expansion. Spreads on commercial paper and corporate bonds relative to Treasury rates continued to narrow, especially for less-than-prime issues, evidencing easier access to market sources of funds for businesses. Improvement in banks' capital positions placed them in a better position to meet loan demand, and many reported that they were no longer tightening credit standards. In addition, long-term interest rates edged down from their March peak, providing some stimulus to mortgage markets and debt restructuring. On balance, despite continued weakness in the broad monetary aggregates, many financial variables appeared to indicate that conditions conducive to a moderate economic expansion were in place.

Still, overall credit growth remained quite subdued, suggesting that some impediments to borrowing and spending remained, and M2 and M3 turned down further in June. In these circumstances, and with direct readings on the economy indicating some weakening relative to earlier in the year, the Federal Reserve in early July cut the discount rate ½ percentage point to 3 percent and allowed this reduction to show through as a similar-sized easing of money market conditions. Banks responded quickly to the policy actions, cutting the prime rate by ½ percentage point to 6 percent.

On balance, short-term rates generally have declined about ¾ of a percentage point this year. Long-term rates, after falling in recent months, have about returned to their lows of early January. The foreign exchange value of the dollar generally has tracked the course of long-term rates, appreciating from January through March and depreciating more recently. On a trade-weighted basis in terms of the currencies of the other G-10 countries, the dollar in mid-July stood at a level somewhat below its 1991 year-end level.

Monetary and Credit Flows

Overall credit flows have been damped this year, reflecting a moderate pickup in spending and efforts by borrowers to pare debt burdens. Although demands for credit by the federal government have been heavy, growth in the debt of other sectors has been lethargic, and, as a result, the total debt aggregate has remained around the lower bound of its annual range throughout much of 1992. Reacting to the difficulties that resulted from carrying heavily leveraged positions in a period of weak economic growth and to wide spreads between the cost of borrowing and the returns on holding financial assets—especially deposits—households and businesses have sought to reduce debt and restructure balance sheets. Total debt, including that of the federal sector, grew about in line with nominal GDP after many years in which debt growth exceeded income.

Along with limiting debt growth, borrowers have sought to strengthen their balance sheets by refinancing existing debt at lower rates. By issuing equity and refinancing debt, businesses have been successful in reducing debt-service burdens; the ratio of net interest payments to cash flow for businesses has declined appreciably this year. The decline in rates over the past year or so has been especially evident for high-yield bonds, indicating that lower-rated borrowers are regaining some of the access to capital markets lost during the credit distress in late 1990 and 1991. A substantial number of firms this year have been upgraded by rating agencies, reflecting improved economic prospects and the salutary effects of lower interest rates and stronger balance sheets on financial conditions.

Many households also have refinanced debt at more attractive rates. Mortgage refinancing began to increase late in 1991 and was very heavy early this year after mortgage rates fell sharply. Later, as mortgage rates backed up, mortgage refinancing applications subsided, but they remained brisk relative to recent years. Households evidently shared the view of businesses that long-term rates presented an opportunity to lock in attractive financing, and many opted to refinance with longer-term fixed-rate mortgages rather than risk future interest rate increases with adjustable-rate mortgages.

Just as for businesses, refinancings and debt reduction appear to have helped relieve the stress on household balance sheets. The ratio of household debt-service payments to personal disposable income has declined appreciably through May. Delinquencies on consumer loans, auto loans, and home mortgages have fallen this year as well. On the other hand, many households with financial assets substantially exceeding debt have seen their spendable income decrease as a result of lower interest rates. Some of the decline in interest rates compensates for lower inflation—the purchasing power of the principal invested is not falling as rapidly as in previous years—but real returns have declined as well, especially for short-dated assets.

State and local governments have exhibited a similar trend in credit demand; on net, total debt growth has been restrained, but gross issuance of bonds has ballooned as municipalities refinance existing debt. A substantial portion of the debt being refinanced likely was issued during the high interest rate episodes of the early 1980s.

Growth of Money and Debt

Percent

Period	M1	M2	M3	Debt of domestic nonfinancial sector
Annually, fourth quarter to fourth quarter[1]				
1980	7.5	8.9	9.5	9.3
1981	5.4 (2.5[2])	9.3	12.3	10.1
1982	8.8	9.1	9.9	9.3
1983	10.4	12.2	9.9	11.4
1984	5.4	8.0	10.8	14.2
1985	12.0	8.7	7.6	13.9
1986	15.5	9.2	9.0	14.1
1987	6.3	4.3	5.9	10.4
1988	4.3	5.2	6.4	9.4
1989	.6	4.8	3.6	8.1
1990	4.2	4.0	1.7	7.0
1991	8.0	2.8	1.2	4.4
Semiannually (annual rate)[3]				
1992:1	13.4	2.1	.2	4.5
Quarterly (annual rate)[4]				
1991:1	16.5	4.3	2.2	3.8
2	9.9	.0	−1.9	5.1

1. From average for fourth quarter of preceding year to average for fourth quarter of year indicated.
2. Adjusted for shift to NOW accounts in 1981.
3. From average for preceding quarter to average for quarter indicated.

Not only has total borrowing been muted, but banks and thrift institutions are accounting for a sharply decreasing share of the total. In fact, credit at depositories has declined over the past two and one-half years even as total credit in the economy continued to advance, and this pattern has left its imprint on the monetary aggregates and their velocities. Part of this rerouting of credit flows reflects the closure of insolvent thrift institutions; the RTC usually assumes the assets of closed thrift institutions and effectively finances them with Treasury obligations rather than deposits. Moreover, when the assets are later sold, depositories are not always the acquirers. The shift in credit flows away from depositories also reflects ongoing market and regulatory pressure on banks and thrift institutions to bolster earnings and capital. Responding to increased deposit insurance costs, to past and prospective loan losses, and to regulatory restrictions triggered as capital–asset ratios fall below the highest levels, depositories have maintained wide spreads between loan rates and deposit rates. The prime lending rate, for example, has remained unusually high relative to market rates and the depository cost of funds, and depositories have tightened nonprice terms of credit as well in recent years. On the deposit side, rates have fallen considerably as depositories have moved to limit balance sheet growth and bolster net interest margins.

Bank credit from the fourth quarter of 1991 to June managed only a 2¾ percent growth rate, slower than in 1991. Bank lending to businesses has contracted in 1992, leaving total loan growth at banks essentially flat. Overall, the contraction in bank business lending in 1992, which has been at an even faster pace than the decline in 1991, appears to reflect primarily weaker demand, as firms have opted to borrow directly in the market and have relied on strong increases in internal funds. Evidence from survey data indicates very little, if any, additional tightening of credit terms by depositories this year. However, the cumulative degree of tightening over the past two years remains substantial, and many banks apparently are still responding to concerns about the condition of borrowers, cumulative loan losses, and pressures to meet or exceed fully phased-in capital requirements. Foreign banks, which had been aggressively seeking new business in the recent past, have reined in balance sheet growth and have tightened the terms of lending this year by somewhat more than domestic banks.

With loans falling relative to deposits, banks have elected to expand their security investment portfolios, pushing the share of government securities in total bank credit to its highest level in twenty years. It seems likely that some of this increase represents banks taking advantage of the steep yield curve to improve earnings by funding these securities with short-term deposits bearing low interest rates. The sharp rise in bank security investments has also been spurred by capital considerations: Mortgage-backed securities issued by government sponsored enterprises (GSEs) are treated more favorably than the underlying loans by risk-based capital standards. As a result, many banks have sold a substantial share of their home mortgage loan portfolios to GSEs and replaced them with the securities issued by these same agencies.

Although continued loan losses and increased deposit insurance premiums have added to bank costs, bank profitability has improved. Earnings have been bolstered by wider net interest margins and some improvement in the quality of loan portfolios. The market has looked favorably on these developments, as gains on bank share prices this year have outstripped advances in broad stock price indexes.

Conditions in the thrift industry appear to have improved this year, at least for solvent institutions. Thrift institutions in fairly secure financial condition have experienced better profit trends analogous to those of banks, and share prices of better capitalized SAIF-insured institutions have fared well over the first half of this year. Still, the improved profit picture for a portion of the thrift industry has not implied any expansion in overall thrift balance sheets; total thrift credit is estimated to have contracted at a 3½ percent rate from the fourth quarter of 1991 to June. A large part of this contraction owes to the significant volume of RTC resolutions conducted through early April of this year. However, additional funds to cover losses have not been appropriated, bringing RTC resolutions to a halt after early April.

The limited growth in total bank and thrift balance sheets has carried important implications for the monetary aggregates. The velocities of the deposit components of the broader aggregates, M2 and M3, have tracked the upward trajectory of the velocity of total depository credit in recent years, and this trend has continued in 1992. M3, especially, has been hindered by the lack of growth of depository credit this year. This aggregate was essentially unchanged in June from its fourth-quarter 1991 level and fell below the 1 to 5 percent annual range set by the FOMC. With retail deposits expanding—if only sluggishly—and depository credit subdued, banks and thrift institutions have shed large time deposits and other managed liabilities. At branches and agencies of foreign banks, large time deposits (Yankee CDs), having decelerated sharply from last year's rapid growth, have been flat this year. Market concerns that lower Japanese stock prices had impaired the capital positions of Japanese banks evidently tarnished the appeal of Yankee CDs for some institutional investors. In response, U.S. branches and agencies of Japanese banks cut back issuance of Yankee CDs, shed liquid assets, and relied more heavily on funding in Eurodollar markets.

Institution-only money market funds were the only source of strength in the non-M2 portion of M3 during the first half of 1992. Investors capitalizing on the sluggish adjustment of money market fund yields to declining market rates accounted for much of the strength in money funds. In addition, some institutional investors, finding their resources augmented rapidly by inflows from former bank depositors, likely have parked some of the cash inflow in money market funds.

The implications of depository retrenchment and household balance sheet adjustments for longstanding empirical relationships between money and spending have been perhaps most pronounced for M2 growth. Despite the pickup in nominal income growth this year and very substantial stimulus from drops in short-term interest rates last year, M2 advanced at only a 1½ percent annual rate from the fourth quarter of 1991 to June, placing its June level below the lower bound of its annual range. The decoupling of the historical relationships among M2, GDP growth, and short-term interest rates is evident in the behavior of M2 velocity. M2 usually rises relative to income (its velocity falls) when market rates drop because rates on M2 deposits do not decline one for one with market rates, inducing portfolio shifts into M2 assets. But in recent months, M2 velocity has risen markedly despite a substantial decline in market rates and a standard measure of opportunity costs—the difference between short-term market rates and returns on M2 assets.

In this period of extraordinary retrenchment, depositories apparently have reduced deposit rates in ways not captured in standard measures of average deposit rates, and the pull of market alternatives has been stronger than is captured by comparisons of deposit rates to short-term market rates. For example, banks and thrift institutions appear to have made larger cuts in the relatively high rates offered to individuals with larger balances and in the rates offered on brokered deposits; holders of both types of accounts might be especially sensitive to rates on alternative investments. In addition, depositories have been particularly hesitant to compete for funds at intermediate and longer maturities. As a result, longer-term bank and thrift CDs have not been attractive investments for savers seeking to raise returns by moving out the upward sloping yield curve. In effect, depositories have used retail time deposits as managed liabilities in making balance sheet adjustments. The result has been large outflows of retail time deposits, with a relatively large portion of the outflow finding its way to higher-yielding, nonmonetary assets. Depositors, witnessing substantial declines in the rates on their accounts relative to market alternatives, apparently exited M2 in favor of stock and bond funds or direct equity and bond investments. Of course, in doing so, these depositors sacrificed the benefits of deposit insurance and accepted the risk of asset price fluctuations.

For a time, the depressing effects of depository retrenchment and investor portfolio shifts on M2 were obscured by the confluence of various special factors. Early in the year, demand deposits surged as lower rates required businesses to build up compensating balances and as mortgage servicers held larger balances during the mortgage refinancing boom. Later, the abrupt deceleration in M2 appeared related to the effects of tax flows and RTC resolutions. Federal nonwithheld taxes this year were weak relative to previous years, and this may have resulted in a smaller deposit buildup in March and April than could be anticipated by normal seasonal adjustment factors. In late March and early April, the RTC resolved a substantial number of institutions. In the past, a heavy volume of RTC resolutions has appeared to damp M2 growth for a month or two, apparently as acquiring institutions abrogate time deposit contracts and depositors take the opportunity to reallocate their portfolios in light of the current configuration of deposit rates and market rates. Thus the RTC resolutions in March and April likely played a role in slowing M2 growth during April and perhaps even in May.

As the weakness in M2 persisted, however, it became increasingly clear that these special factors were not the whole story. If the deceleration of M2 in March and April reflected evolving seasonal tax patterns, May and June should have witnessed an appreciable rebound in M2 growth. In fact, M2 continued to founder, leaving its level in June well below its February level and also below the lower bound of its annual range. Furthermore, RTC resolutions halted abruptly when additional funding for losses was not forthcoming. By June, M2 should have been largely free of RTC effects, but growth of M2 in June was, in fact, even weaker than in April and May. On balance, these special factors appeared to figure prominently in the month-to-month variations of M2 growth, but the overall advance of M2 this year was impeded by more fundamental forces.

These fundamental forces, involving balance sheet adjustments by depositories and money holders, appear to be boosting the velocity of M2. There is considerable uncertainty, however, about how long this process will persist, and whether it will permanently affect the equilibrium level or cyclical behavior of M2 velocity. One means of evaluating this question will be observations of the future performance of the P-star model in predicting inflation. This model is based on M2 per unit of potential output, normalized by equilibrium velocity, which had proved to be constant. Persistent underpredictions of inflation by this model would suggest that the rise in velocity relative to its historical average may be a more permanent phenomenon.

While highly interest-responsive depositors were tilting their portfolios toward capital market instruments, less rate-sensitive, more risk-averse households simply rolled over a portion of their maturing small time deposit holdings into more liquid M2 deposits, at little or no sacrifice in yield. In fact, while M2 growth overall this year has been moribund, growth in its liquid components has been robust and more in line with historical relationships to income and interest rates. M1, for example, has grown at a 12 percent pace through June, a rate well above its average during 1991 of 8 percent. Especially since the introduction of NOW accounts in the early 1980s, the demand for M1 has become quite interest sensitive, leading to wide fluctuations in the velocity of M1, and the drop in M1 velocity this year is consistent with that pattern. Foreign demands for U.S. currency have been more subdued this year, and currency growth has slowed a bit relative to the pace of 1990 and 1991. Even so, moderate growth in currency, together with the brisk advance in transaction deposits, has fueled growth in the monetary base of 7¾ percent from the fourth quarter of 1991 to June.

The unusual behavior of the velocity of M3 and, especially, of M2 this year has sparked renewed interest in alternative definitions of the monetary aggregates. Two alternatives that have received some attention are M2 plus stock and bond mutual funds and M2 plus institution-only money funds less small time deposits. Both alternative aggregates have grown substantially more rapidly than M2 in recent quarters. The former adds back into M2 the apparent destination of much of the recent outflows from M2; the latter subtracts the weakest component of M2—retail time deposits—to create a highly liquid aggregate, which behaves over time very much like M1. Both alternatives recently appear to have followed more closely historical relationships with income and opportunity costs than has M2. However, both show periods in the past in which their velocities have been highly variable and difficult to predict. The Federal Reserve is continuing to analyze these experimental monetary measures carefully. ■

Part 2

Records, Operations, and Organization

Record of Policy Actions of the Board of Governors

Regulation D (Reserve Requirements of Depository Institutions)

February 18, 1992—Amendments

The Board amended Regulation D, effective April 2, 1992, to lower reserve requirements on transaction accounts.

Votes for this action: Messrs. Greenspan, Mullins, Angell, Kelley, and Lindsey and Ms. Phillips. Absent and not voting: Mr. LaWare.

The Board reduced from 12 percent to 10 percent reserve requirements on net transaction accounts to reduce funding costs for depository institutions. It was hoped that the reduction would strengthen banks' financial condition, improve their access to capital markets, and put them in a better position to extend credit. The reduction was effective with the reserve maintenance period beginning April 2, 1992.

August 12, 1992—Amendments

The Board amended Regulation D to reduce the seasonal variation in required reserves and to improve the ability of depository institutions to manage their reserve balances.

Votes for this action: Messrs. Greenspan, Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips.

The Board amended Regulation D to shorten by two weeks the lag in the application of vault cash to reserve requirements. The change was effective with the reserve maintenance period beginning November 12, 1992.

The Board also amended the regulation to increase the amount of excesses or deficiencies in reserve balances that an institution can carry over from one reserve maintenance period to the next. Effective September 3, 1992, the amount of excess or deficiency that can be carried forward was increased from the greater of 2 percent or $25,000, to the greater of 4 percent or $50,000.

August 12, 1992—Amendments and Interpretations

The Board amended Regulation D and issued several interpretations to prevent the evasion of reserve requirements on transaction accounts.

Votes for these actions: Messrs. Greenspan, Mullins, Angell, and Kelley and Ms. Phillips. Votes against these actions: Messrs. LaWare and Lindsey.

The Board took several actions to preserve the integrity of reserve requirements, prevent erosion of the reserve base for transaction accounts, and maintain equitable competition among depository institutions. Included in those actions are amendments and interpretations that (1) change the definition of teller's checks to treat them as cashier's checks and include them as demand deposits subject to reserve requirements; (2) reclassify certain multiple savings accounts as transaction accounts and make them subject to reserve requirements under certain conditions; (3) reclassify certain linked time deposits as transaction accounts; (4) revise the definition of "cash items in process of collection" to clarify that matured bonds and coupons may be deducted from gross transaction accounts; (5) prohibit larger institutions from reducing their reservable liabilities by depositing funds with smaller banks and thereby generating a "due from" deduction; and (6) prohibit the netting of negative balances in individual trust accounts against positive balances in other trust accounts to lower reserve requirements.

Governors LaWare and Lindsey dissented from this action. They thought that the proposal affecting teller's checks inappropriately assessed reserve requirements against the seller of the checks. They believed that the payable-through bank should be assessed the applicable reserve requirement because that institution was likely to hold the transaction account on which the teller's check would be drawn. Governor Lindsey also disagreed with the proposed treatment of multiple savings accounts. He preferred alternative measures to prevent evasion of reserve requirements, particularly those that would permit the payment of interest on required reserve balances.

The revisions pertaining to teller's checks, cash items in process of collection, and trust accounts were effective December 22, 1992; the others were effective September 29, 1992.

Votes for these actions: Messrs. Greenspan, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips. Absent and not voting: Mr. Mullins.

November 18, 1992—Amendments

The Board amended Regulation D to increase the amount of transaction balances to which the lower reserve requirement applies and to increase the amount of reservable liabilities subject to a zero percent reserve requirement.

Under the Monetary Control Act of 1980, depository institutions, Edge Act and Agreement corporations, and U.S. agencies and branches of foreign banks are subject to reserve requirements set by the Board. Initially, the Board set reserve requirements at 3 percent of an institution's first $25 million in transaction balances and at 12 percent of balances above that amount. (Subsequently, the Board lowered the maximum reserve requirement to 10 percent.) The act directs the Board to adjust annually the amount subject to the lower reserve requirement to reflect changes in transaction balances nationwide. By the beginning of 1992, that amount was $42.2 billion. Recent increases in transaction balances warranted an increase of $4.6 million. The Board, therefore, amended Regulation D to increase to $46.8 million the amount of transaction balances to which the lower reserve requirement applies.

The Garn–St Germain Depository Institutions Act of 1982 established a zero percent reserve requirement on the first $2 million of an institution's reservable liabilities. The act also provides for annual adjustments to that exemption based on deposit growth nationwide. By the beginning of 1992, that amount had been increased to $3.6 million. Recent growth in deposits warranted an increase to $3.8 million in the amount of deposits subject to a zero percent reserve requirements, and the Board amended Regulation D accordingly.

The amendments are effective with the reserve computation period beginning December 22, 1992, for institutions that report weekly, and December 15, 1992, for institutions that report quarterly.

Regulation F (Limitations on Interbank Liabilities)

November 20, 1992—Adoption of New Regulation

The Board adopted Regulation F to limit the risk that the failure of a depository institution would have on insured institutions.

Votes for this action: Messrs. Greenspan, Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips.

The Board adopted the new Regulation F to implement provisions of the Federal Deposit Insurance Corporation Improvement Act of 1991 that require the Board to limit the risk that the failure of a large depository institution would pose for federally insured institutions. The new regulation requires that federally insured depository institutions, including banks, savings associations, and branches of foreign banks, adopt procedures to evaluate and control exposure to their correspondents. In addition, an insured institution must limit its overnight credit exposure to any institution that is not adequately capitalized to an amount not more than 25 percent of the institution's total capital. No regulatory limits have been established for correspondents that are at least "adequately capitalized," as that term is defined in the rule.

The new regulation is effective December 19, 1992, but provides for a phased implementation period over thirty months. Insured institutions must have internal policies and procedures in place by June 19, 1993. The regulatory limit on exposure to a correspondent that is not adequately capitalized would be set at 50 percent of an insured institution's total capital beginning June 19, 1994, and would be reduced to 25 percent on June 19, 1995.

Regulation H (Membership of State Banking Institutions in the Federal Reserve System)

September 14, 1992—Amendments

The Board amended Regulation H, effective December 19, 1992, to implement legislation requiring prompt corrective action when assisting financially troubled institutions.

Votes for this action: Messrs. Greenspan, Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips.

A section of the Federal Deposit Insurance Corporation Improvement Act of 1991 requires the Federal Reserve, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision to take prompt corrective action to resolve the problems of insured depository institutions, and it requires that such action minimize the long-term loss to the deposit insurance fund. The legislation created a framework that specifies the supervisory actions that the agencies must or should take, depending on the institution's placement in one of five categories of capital levels.

The Board implemented these requirements for state member banks by amending Regulation H. Among other provisions, the new rules establish capital measures and thresholds for the five categories of capital specified in the statute; establish procedures for providing banks with notice of a proposed supervisory directive; establish procedures for lowering a bank's rating if such a reclassification is based on factors other than capital; and provide a uniform schedule by which under-capitalized state member banks must file capital restoration plans and by which the Federal Reserve must review those plans.

Regulation H (Membership of State Banking Institutions in the Federal Reserve System) *and* **Regulation Y** (Bank Holding Companies and Change in Bank Control)

December 9, 1992—Amendments

The Board amended Regulations H and Y, effective March 9, 1993, to revise the capital adequacy guidelines regarding the treatment of intangible assets.

Votes for this action: Messrs. Greenspan, Mullins, Kelley, and LaWare and Ms. Phillips. Absent and not voting: Messrs. Angell and Lindsey.

The Federal Reserve and the other federal bank regulatory agencies have been attempting to develop more consistent treatment of intangible assets—other than goodwill—in the calculation of capital ratios. In connection with those efforts, the Board amended Regulations H and Y to revise the capital adequacy guidelines by specifying the types of intangible assets that can be included in tier 1 capital when calculating risk-based capital ratios and leverage ratios. Under the revised guidelines, all identifiable intangible assets other than goodwill, purchased mortgage-servicing rights, and purchased credit card relationships are to be deducted from capital. The amendments also establish quantitative limits on the amount of purchased mortgage servicing rights and purchased credit card relationships that can be included in tier 1 capital and specify the conditions under which those intangible assets can be included.

Pursuant to provisions in the Federal Deposit Insurance Corporation Improvement Act of 1991, the amendments require that organizations determine the fair market value and the book value of their purchased mortgage-servicing rights. The amendments provide criteria for determining those values.

The other bank regulatory agencies would adopt substantially similar guidelines for the organizations they supervise.

Regulation J (Collection of Checks and Other Items by Federal Reserve Banks and Funds Transfers through Fedwire) *and* Policy Statements on Measures for Reducing Payment System Risks

September 30, 1992—Adoption of Amendments and Issuance of Policy Statements

The Board amended Regulation J and issued two policy statements regarding fees to be charged and new posting procedures to be implemented to reduce risks in the payments system.

Votes for these actions: Messrs. Greenspan, Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips.

Under existing procedures for clearing and settling transactions on the Federal Reserve's payments system, institutions present items for payment throughout the business day and settle for the net amount of those transactions at the end of the day. The Federal Reserve, therefore, runs the risk that an institution using the payments system might fail during the day or otherwise be unable to settle for the checks presented during the day.

For some time now, the Board has had in place a program to reduce risks both in the Federal Reserve's payments and in private systems. The latter type of risk can arise in circumstances such as the failure of a participant on a private-sector transfer network to cover a net debit. That failure, in turn, could prevent the creditors of that participant from settling their own commitments and could have further repercussions in the payments system and the economy in general. The Board's program is designed to encourage risk-reducing behavior by payments system participants.

Recently, the Board decided that additional measures were needed and took three actions to reduce risks. The primary change is the introduction of a charge for average daily intraday (daylight) overdrafts in reserve or clearing accounts. The new daylight overdraft fee will be phased-in in three steps and will be assessed against an institution's average daily total of overdrafts. Fees of $25 or less during any two-week period would be waived.

To facilitate pricing, the Board also adopted new procedures for accurate measurement of daylight overdrafts. The Board also amended Regulation J to provide for intraday posting of debits for checks presented by the Federal Reserve Banks.

The daylight overdraft measurement procedures and the Regulation J amendment are effective October 14, 1993; the assessment of fees for daylight overdrafts will begin April 14, 1994.

Regulation K (International Banking Operations) *and* **Regulation Y** (Bank Holding Companies and Change in Bank Control)

April 2, 1992—Interim Rules

The Board amended Regulations K and Y to adopt interim rules to implement provisions of the Foreign Bank Supervision Enhancement Act of 1991 and the Federal Deposit Insurance Corporation (FDIC) Improvement Act of 1991.

Votes for these actions: Messrs. Greenspan, Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips.

Because the Foreign Bank Supervision Act was effective when enacted, the Board published for comment proposed implementing amendments and also adopted them as interim rules. That act included provisions that: (1) require foreign banks to obtain Board approval before establishing a branch, agency, commercial lending company, or representative office in the United States; (2) establish standards for entry by foreign banks; (3) allow termination of a foreign bank's U.S. office if a violation occurs; (4) require annual examinations of U.S. branches of foreign banks and permit the Federal Reserve to coordinate examinations of all U.S. operations of a foreign bank; (5) permit sharing of supervisory information with foreign bank regulators; (6) establish limits for state-licensed branches and agencies on lending to a single borrower; (7) require foreign banks to obtain Board approval before acquiring more than 5 percent of the shares of a U.S. bank; and (8) establish new restrictions on retail deposit-taking by branches and agencies of foreign banks.

The Board also approved adoption of an interim rule and publication for comment of an amendment to Regulation Y to implement provisions of the FDIC Improvement Act that govern bank holding companies and foreign banking organizations with operations in the United States. The rule specifies additional factors the Board will consider when reviewing applications to acquire a bank.

November 4, 1992—Amendments

The Board amended Regulations K and Y to implement provisions of the Foreign Bank Supervision Enhancement Act of 1991.

> Votes for this action: Messrs. Greenspan, Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips.

The Foreign Bank Supervision Enhancement Act provided uniform standards for entry by foreign banks into the United States and also strengthened supervision of their operations by U.S. banking regulators. Among other provisions, the act requires that any foreign bank that seeks to operate in the United States be subject to comprehensive supervision, on a consolidated basis, by supervisors in its home country.

Because the legislation was effective upon enactment, the Board adopted interim rules in April 1992 and also sought comment on those rules. The interim rules had outlined the standards and the factors that the Board would consider in determining whether an organization receives comprehensive and consolidated supervision in its home country. The rules also reviewed the other mandatory and discretionary standards for Board approval of applications by foreign banks to establish a branch, agency, representative office, or commercial lending company. In addition, the rules implement other provisions of the act relating to the Board's new regulatory and supervisory powers over the U.S. offices of foreign banks.

After completion of its review of the comments received on the interim rules, the Board amended Regulation K to adopt the rules in final form, with certain modifications to reflect those comments. The Board also amended Regulations K and Y to require that a foreign banking organization file an application under the Bank Holding Company Act if it proposes to acquire more than 5 percent of the shares of a U.S. bank or bank holding company. These amendments in the final rules were effective January 28, 1993. In addition, the Board amended Regulation Y, effective February 4, 1993, to specify two additional factors it will consider when reviewing foreign banking applications and to reflect the new requirement for an application from foreign banks that seek to acquire more than 5 percent of a U.S. banking organization.

Regulation O (Loans to Executive Officers, Directors, and Principal Shareholders of Member Banks) *and* **Regulation Y** (Bank Holding Companies and Change in Bank Control)

April 22, 1992—Amendments

The Board amended Regulation O to implement provisions in the Federal Deposit Insurance Corporation (FDIC) Improvement Act, to make technical revisions, and to clarify certain ambiguities in the rules. The Board also amended Regulations O and Y to implement certain reporting requirements imposed by the act. The amendments were effective May 18, 1992.

Votes for these actions: Messrs. Greenspan, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips. Absent and not voting: Mr. Mullins.

The FDIC Improvement Act modified in several ways the requirements concerning a bank's extensions of credit to its officials, including executive officers, directors, and principal shareholders and their related interests. One modification limits the aggregate amount of credit that a bank may extend to insiders. Another modification extends the aggregate lending limits to directors and their related interests.

A bank's aggregate lending limit generally is equal to the amount of its unimpaired capital and surplus. Because of the effect that such a limit might have on smaller banks, the Board established temporarily a higher limit for institutions that have less than $100 million in deposits. For such institutions, the limit would be up to 200 percent of unimpaired capital and surplus, provided the bank's board of directors passes a resolution to establish a limit higher than 100 percent. The higher lending limit would be in effect for a year. During that time the Board would assess the effect of the limitation on the ability of banks to attract directors and to serve community credit needs.

The Board also amended Regulations O and Y to implement certain reporting requirements of the FDIC Improvement Act pertaining to loans to executive officers and directors of certain bank holding companies, to make technical revisions, and to eliminate ambiguities.

Regulation Y (Bank Holding Companies and Change in Bank Control) *and* Rules of Procedure

April 22, 1992—Amendments

The Board amended Regulation Y to permit bank holding companies to engage in full-service brokerage and financial advisory activities and in certain leasing transactions; and revised an interpretative rule regarding advisory activities.

Votes for these actions: Messrs. Greenspan, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips. Absent and not voting: Mr. Mullins.

The Board amended Regulation Y, effective September 4, 1992, to include on the list of activities permissible for bank holding companies the provision of full-service securities brokerage activities to both institutional and retail customers; and the provision of financial advisory services regarding transactions such as mergers, acquisitions, and divestitures, as well as the structuring of loan syndications, interest rate swaps, and similar types of transactions. The permissible activities are subject to certain disclosure and other requirements.

The Board also expanded the list of permissible activities to allow holding companies to engage in the leasing of personal property, activities in which national banks are permitted to engage under the Competitive Equality Banking Act. The Board amended Regulation Y to permit a holding company to rely on up to 100 percent of the residual value of a leased property for recovering the holding company's leasing costs. The amendment imposes a limit on the volume of such leasing activities but permits holding companies to engage in an unlimited number of transactions in which they rely on residual values of up to 25 percent of the acquisition cost of the leased property for compensation of their full leasing costs. This amendment was effective May 14, 1992.

The Board also revised an interpretive rule, effective August 10, 1992, to permit a holding company or a nonbank subsidiary to act as an agent for customers in the brokerage of shares of an investment company to which the holding company or any of its subsidiaries provides investment advice. The revision also permits the provision of investment advice to customers regarding the purchase or sale of shares of an investment company to which a holding company affiliate provides investment advice. In both circumstances, certain disclosures must be made to address the potential conflicts of interest or the possible adverse effects.

June 19, 1992—Amendments

The Board approved several amendments to Regulation Y, effective June 29, 1992, as part of its efforts to reduce regulatory burden and simplify the applications process.

Votes for this action: Messrs. Greenspan, Mullins, Kelley, and Lindsey and Ms. Phillips. Votes against: None. Absent and not voting: Messrs. Angell and LaWare.

The Board revised several provisions of Regulation Y to streamline certain procedural requirements. Among other provisions, the amendments (1) increase the size of nonbank companies that can be acquired by bank holding companies under the fifteen-day expedited notice procedures, (2) increase the relative size of nonbank assets that holding companies may acquire in the ordinary course of business without Federal Reserve approval, and (3) define the criteria for determining when bank holding company applications may be waived in connection with certain bank mergers.

September 3, 1992—Amendments and Adoption of New Rule

The Board amended Regulation Y, revised its Rules of Procedure, and issued a new rule as part of its efforts to reduce regulatory burden and simplify the applications process.

Votes for these actions: Messrs. Mullins, Kelley, and LaWare and Ms. Phillips. Votes against: None. Absent and not voting: Messrs. Greenspan, Angell, and Lindsey.

The Board revised its Rules of Procedure and Regulation Y to reduce the number of times institutions must publish notice in local newspapers of certain applications filed with the Federal Reserve. Effective October 13, 1992, institutions need publish only once, instead of twice, notices of applications to become a member of the Federal Reserve, to establish a branch, to merge with or acquire another bank, or to become a bank holding company.

In a related action, the Board adopted a new rule, effective September 11, 1992, to exempt from the limitations of section 23A of the Federal Reserve Act certain transactions between affiliates of an insured depository institution, provided certain criteria are met. Section 23A limits the ability of institutionss to purchase assets from, or lend to, affiliates. The new rule exempts transactions that have been approved by an appropriate federal banking agency pursuant to the Bank Merger Act and thereby eliminates the need for duplicate federal applications.

Regulation Z (Truth in Lending)

July 29, 1992—Amendments

The Board adopted amendments to Regulation Z pertaining to home equity loans to bank officials.

Votes for this action: Messrs. Mullins, Kelley, LaWare, and Lindsey and Ms. Phillips. Absent and not voting: Messrs. Greenspan and Angell.

The Board amended Regulation Z to permit depository institutions to retain the right to demand payment of a home equity line of credit extended to their executive officers when required by federal law. The amendment resolved a discrepancy between the Home Equity Loan Consumer Protection Act and Regulation O (Loans to Executive Officers, Directors, and Principal Shareholders of Member Banks). The amendment is effective immediately; compliance is optional, however, until October 1, 1993.

Regulation CC (Availability of Funds and Collection of Checks)

January 15, 1992—Amendments

The Board amended Regulation CC, effective immediately, to implement provisions of the Federal Deposit Insurance Corporation (FDIC) Improvement Act of 1991.

Votes for this action: Messrs. Greenspan, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips. Absent and not voting: Mr. Mullins.

The FDIC Improvement Act amended the Expedited Funds Availability Act to allow banks to extend the holds that they place on checks under certain conditions. Accordingly, the Board adopted an interim rule for Regulation CC and also sought comment on the rule. The interim rule allows banks—on an exception basis—to extend the holds to "next-day" and "second day" availability and to allow one-time notices of exception holds in certain cases.

July 29, 1992—Amendments

The Board amended Regulation CC, effective September 14, 1992, to adopt an interim rule in final form.

Votes for this action: Messrs. Greenspan, Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips.

Regulation CC implements the Expedited Funds Availability Act, in part, by establishing schedules by which banks must make available to customers the funds deposited in their transaction accounts. The FDIC Improvement Act of 1991 amended provisions of the Funds Availability Act, and in January the Board had adopted an interim rule. Subsequently, it took final action by adopting the rule in final form. The revision to Regulation CC allows banks to extend the holds, on an exception basis, to "next-day" and "second-day" availability checks and allows one-time notices of exception holds, in certain cases. In addition, the amendments made permanent the availability schedules that had been in effect for deposits at nonproprietary automated teller machines and affirmed the administrative enforcement authority of federal regulatory agencies over U.S. offices and branches of foreign banks.

September 30, 1992—Amendments

The Board amended Regulation CC, effective January 3, 1994, to provide for same-day settlement of checks presented by private-sector banks.

Votes for this action: Messrs. Greenspan, Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips.

The Board amended Regulation CC to require that paying banks settle for checks presented to them by private-sector banks on the same day that the checks are presented, without imposing a presentment fee. Under the new rule, paying banks must settle for any checks presented on the same day they are presented, if the checks are presented by 8:00 a.m. local time, at the location designated by the paying bank. Settlement must be made by credit to an account at a Federal Reserve Bank by the close of business on the day presented. The provisions of the rule may be varied by agreement.

Regulation DD (Truth in Savings) *and* **Regulation Q** (Prohibition Against the Payment of Interest on Demand Deposits)

September 10, 1992—Adoption of New Regulation

The Board adopted a new Regulation DD to implement provisions of the Truth in Savings Act of 1991 and made conforming changes to Regulation Q.

Votes for this action: Messrs. Angell and Lindsey and Ms. Phillips. Votes against this action: Messrs. Mullins and LaWare. Absent and not voting: Messrs. Greenspan and Kelley.

The Truth in Savings Act is part of the Federal Deposit Insurance Corporation Improvement Act of 1991. One purpose of the Truth in Savings Act is to assist consumers in comparing deposit accounts offered by depository institutions. The act establishes certain disclosures that must be provided whenever a consumer requests the information or before an account is opened.

The new Regulation DD implements the requirements of the act and also provides explanations and sample disclosure forms to assist in compliance. Among other provisions, the new regulation (1) provides formulas for computing the required annual percentage yield to ensure a uniform method for calculating the return on accounts; (2) specifies the conditions under which institutions must disclose any fees imposed, the annual percentage yield, and other information; (3) limits the manner in which an institution may determine the balance on which interest is paid; and (4) establishes rules for advertising deposit accounts.

Although Board members were concerned about the compliance burden imposed by the legislation, a majority did not object to adoption of Regulation DD as the best measure for implementing the statutory requirements. Governors Mullins and LaWare, however, did not support adoption of the new regulation. Governor Mullins believed that the amount of detail in the regulation and accompanying model forms would interfere with an institution's operations, and he preferred that the amount of detail in the explanatory information be reduced. Governor LaWare thought that the burden of complying with the regulation would serve to reduce the amount of interest that institutions paid on deposits and the amount of service they provided.

In a related action, the Board approved conforming revisions to Regulation Q to delete advertising and disclosure requirements that were included in the new regulation and also changed the title of Regulation Q from "Interest on Deposits" to "Prohibition Against the

Payment of Interest on Demand Deposits."

The new regulation is effective September 21, 1992; compliance is optional, however, until March 21, 1993. After this action, the Congress amended the Truth in Savings Act to delay its effective date by three months. Accordingly, compliance is optional until June 21, 1993.

Policy Statements

January 21, 1992—Highly Leveraged Transactions

The Board discontinued use of the supervisory definition of highly leveraged transactions, effective after institutions submit their midyear 1992 financial reports, and made certain interim changes in reporting requirements, effective with the first-quarter statements.

Votes for this action: Messrs. Greenspan, Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips.

The Board, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation had adopted use of the definition of highly leveraged transactions for supervisory purposes in 1989, when leveraged buyouts were frequent. Besides providing guidance to examiners, the definition had encouraged financial institutions to structure highly leveraged financings in a manner consistent with the associated risks, to develop adequate internal controls, and to review mechanisms to monitor such transactions. Now, however, merger and acquisition activity has declined significantly, and the term no longer serves a useful purpose. Rather than revise the definition, the Board, along with the other two agencies, decided to discontinue supervisory use of the definition of highly leveraged transactions and to eliminate required reporting on such exposure by banking organizations after midyear. Until use of the term was discontinued, however, the agencies approved revisions to the definition that banks and bank holding companies should use for purposes of their financial reports for March 31, and June 30, 1992.

March 6, 1992—Community Reinvestment Act

The Board issued a policy statement noting the responsibility of financial institutions under the Community Reinvestment Act (CRA) to analyze the geographic distribution of their lending patterns.

Votes for this action: Messrs. Greenspan, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips. Absent and not voting: Mr. Mullins.

Under the CRA, financial institutions are required to serve the convenience and needs of the communities in which they are chartered, and supervisory agencies are required to assess an institution's record of meeting the credit needs of its entire community, including low- and moderate-income areas. Among the factors the agencies consider when making such assessments are (1) the extent to which an institution's board of directors participates in formulating policies and reviewing performance and (2) the distribution of the institution's credit extensions, applications, and denials throughout the delineated community.

The Board, along with the Federal Deposit Insurance Corporation, the Comptroller of the Currency, and the Office of Thrift Supervision, adopted a policy statement to emphasize the need for institutions to analyze the geographic distribution of their credit extensions as part of their CRA planning process and to ensure that potential borrowers are treated fairly and that all segments of the community are served appropriately. The statement also reviews the agencies' expectations regarding such lending and provides guidance regarding how best to meet those expectations.

October 28, 1992—Withdrawal from a Priced Service

The Board issued a policy statement, effective October 29, 1992, describing the criteria it would consider in deciding whether to withdraw from a priced service.

> Votes for this action: Messrs. Mullins, Angell, Kelley, LaWare, and Lindsey and Ms. Phillips. Absent and not voting: Mr. Greenspan.

The policy statement indicated that the Board would consider the following factors when assessing a request from one or more Federal Reserve Banks to discontinue the provision of a priced service: (1) whether other service providers are likely to provide an adequate level of the same service in the relevant markets(s) if the Federal Reserve withdraws from the service; (2) whether it is likely that users could obtain other substitutable services that can reasonably meet their needs, if other firms are not likely to provide an adequate level of the same service in the market(s); (3) whether withdrawal from the service would not have a material, adverse affect on the ability of the Federal Reserve to provide an adequate level of other services; (4) whether withdrawal would not have an adverse effect on the System's ability to discharge its other duties; and (5) whether there are no public benefits from continued provision of the service that outweigh the reasons for withdrawal. The statement also indicated that the Board would consider discontinuing a service line only when a Reserve Bank failed to achieve full cost recovery for a particular service line over the long run.

1992 Discount Rates

The Board approved one change in the basic discount rate during 1992, a reduction from 3½ to 3 percent in early July. The Board also approved numerous changes, including increases and decreases, in the rates charged for seasonal credit and for extended credit; rates for both types of credit are set on the basis of market-related formulas and exceeded the basic discount rate by varying amounts during the year.

The reasons for Board decisions are reviewed below. Those decisions were made in the context of the policy actions of the Federal Open Market Committee (FOMC) and the related economic and financial developments that are covered more fully elsewhere in this Report.

Basic Discount Rate

In December 1991 the Board approved a reduction of a full percentage point in the basic discount rate, to 3½ percent, and the FOMC also acted to reduce pressures on reserve positions. These policy easing moves, together with the ongoing effects of cumulatively sizable easing actions implemented earlier, were viewed as likely to have a positive effect on financial markets and to provide a basis for a rate of economic growth stronger than the quite sluggish pace experienced since the beginning of the current upturn in the spring of 1991.

The economic expansion picked up some momentum in the early months of 1992. Much of the impetus was supplied by an upswing in consumer spending and a sharp increase in purchases of new houses. In financial markets, interest rates fell considerably around the turn of the year, but most rates, including those on mortgages, subsequently came under appreciable upward pressure. By early spring, growth in final demand moderated as consumers appeared to respond to continuing weakness in labor markets and the absence of significant gains in real income. New home sales fell steadily after February, net exports weakened in the second quarter, and defense spending remained on a downtrend. On the positive side, wage and price increases seemed to be trending lower. After strengthening somewhat in the first quarter, the broad measures of money weakened markedly in the second quarter, and the growth of credit continued to lag.

In this environment, the FOMC eased pressures on reserve conditions slightly in April. In the weeks that followed, market interest rates fell appreciably, notably in short-term markets. During this period nearly all of the Reserve Banks recommended that the basic rate be maintained at its then current level, and the Board took no action on a proposed reduction of ½ percentage point that was pending at one Bank. Subsequently, on July 2, the Board approved a reduction in the basic rate from 3½ to 3 percent. Open market operations were directed toward allowing the full amount of the reduction to be reflected in money market interest rates.

Over the course of July and August, indicators of economic activity pointed to a continuing but quite sluggish expansion. Although growth in the broad measures of money picked up in August after declining in previous months, their expansion remained slow. Against this background, the FOMC implemented a slight further easing of reserve conditions in early September. Over the balance of the year, indications of renewed firmness in economic activity tended to multiply. Consumer spending picked up, especially toward year-end; housing demand grew somewhat further; and business purchases of capital equipment continued to rise at a brisk pace. However, growth in the broad measures of money and in nonfederal debt remained quite limited during the latter part of the year. Several Reserve Banks proposed a further reduction in the basic discount rate, to 2½ percent, during the September-to-December period, but the Board took no action on these proposals, and only one was still pending at year-end.

Structure of Discount Rates

The basic discount rate is the rate charged on loans to depository institutions for short-term adjustment credit, while flexible, market-related rates generally are charged on other types of credit. These flexible rates are adjusted periodically, subject to Board approval. Under the seasonal program, loans may be provided for periods longer than those permitted under adjustment credit to assist smaller institutions in meeting regular needs arising from a clear pattern of intra-yearly movements in their deposits and loans. Since its introduction on January 9, 1992, the flexible rate charged on seasonal credit has been closely aligned with short-term market rates and is never less than the basic rate applicable to adjustment credit.

A different flexible rate is charged on extended-credit loans, which are made to depository institutions that are under sustained liquidity pressure and are not able to obtain funds from other sources.

The rate for extended credit is 50 basis points higher than the seasonal rate and is at least 50 basis points above the basic discount rate. The first thirty days of borrowing on extended credit may be at the basic rate, but further borrowings ordinarily are charged the flexible rate. Exceptionally large adjustment-credit loans that arise from computer breakdowns or other operating problems that are not clearly beyond the reasonable control of the borrowing institution are assessed the highest rate applicable to any credit extended to depository institutions; under the current structure, that rate is the flexible rate on extended credit.

At the end of 1992 the structure of discount rates was as follows: a basic rate of 3 percent for short-term adjustment credit, a rate of 3.20 percent for credit under the seasonal program, and a rate of 3.70 percent for extended credit. During 1992 the flexible rate on seasonal credit ranged from a high of 4.15 percent to a low of 3.15 percent and that on extended credit ranged from a high of 4.65 percent to a low of 3.65 percent.

Board Votes

Under the provisions of the Federal Reserve Act, the boards of directors of the Federal Reserve Banks are required to establish rates on loans to depository institutions at least every fourteen days and to submit such rates to the Board of Governors for review and determination. Federal Reserve Bank proposals on the discount rate include requests to renew the formulas for calculating the flexible rates on seasonal and extended credit. Indicated below are the votes relating to the Board's decision to reduce the basic discount rate in early July. Votes relating to the reestablishment of existing rates or for the updating of market-related rates under the seasonal and extended credit programs are not shown. All votes taken during 1992 on discount rates were unanimous.

Effective July 2, the Board approved proposals by the directors of the Federal Reserve Banks of Boston, New York, Philadelphia, Richmond, Atlanta, Chicago, Minneapolis, Kansas City, Dallas, and San Francisco to reduce the basic discount rate from 3½ to 3 percent.

Votes for this action: Messrs. Greenspan, Angell, Kelley, LaWare, Lindsey, and Mullins and Ms. Phillips. Votes against this action: None.

The Board subsequently approved similar actions taken by the directors of the Federal Reserve Banks of Cleveland, effective July 6, and St. Louis, effective July 7, 1992. ■

Record of Policy Actions of the Federal Open Market Committee

The record of policy actions of the Federal Open Market Committee is presented in the ANNUAL REPORT of the Board of Governors pursuant to the requirements of section 10 of the Federal Reserve Act. That section provides that the Board shall keep a complete record of the actions taken by the Board and by the Federal Open Market Committee on all questions of policy relating to open market operations, that it shall record therein the votes taken in connection with the determination of open market policies and the reasons underlying each such action, and that it shall include in its annual report to the Congress a full account of such actions.

The pages that follow contain entries relating to the policy actions at the meetings of the Federal Open Market Committee held during the calendar year 1992, including the votes on the policy decisions made at those meetings as well as a résumé of the basis for the decisions. The summary descriptions of economic and financial conditions are based on the information that was available to the Committee at the time of the meetings, rather than on data as they may have been revised later.

Members of the Committee voting for a particular action may differ among themselves as to the reasons for their votes; in such cases, the range of their views is noted in the record. When members dissent from a decision, they are identified in the record along with a summary of the reasons for their dissent.

The policy record for each meeting is released a few days after the next regularly scheduled meeting and is subsequently published in the *Federal Reserve Bulletin*.

Policy directives of the Federal Open Market Committee are issued to the Federal Reserve Bank of New York as the Bank selected by the Committee to execute transactions for the System Open Market Account. In the area of domestic open market activities, the Federal Reserve Bank of New York operates under two sets of instruction from the Open Market Committee: an Authorization for Domestic Open Market Operations and a Domestic Policy Directive. (A new Domestic Policy Directive is adopted at each regularly scheduled meeting.) In the foreign currency area, the Committee operates under an Authorization for Foreign Currency Operations, a Foreign Currency Directive, and Procedural Instructions with Respect to Foreign Currency Operations. These policy instruments are shown below in the form in which they were in effect at the beginning of 1992. Changes in the instruments during the year are reported in the records for the individual meetings.

Authorization for Domestic Open Market Operations

In Effect January 1, 1992

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, to the extent necessary to carry out the most recent domestic policy directive adopted at a meeting of the Committee:

(a) To buy or sell U.S. Government securities, including securities of the Federal

Financing Bank, and securities that are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States in the open market, from or to securities dealers and foreign and international accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the System Open Market Account at market prices, and, for such Account, to exchange maturing U.S. Government and Federal agency securities with the Treasury or the individual agencies or to allow them to mature without replacement; provided that the aggregate amount of U.S. Government and Federal agency securities held in such Account (including forward commitments) at the close of business on the day of a meeting of the Committee at which action is taken with respect to a domestic policy directive shall not be increased or decreased by more than $8.0 billion during the period commencing with the opening of business on the day following such meeting and ending with the close of business on the day of the next such meeting;

(b) When appropriate, to buy or sell in the open market, from or to acceptance dealers and foreign accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the account of the Federal Reserve Bank of New York at market discount rates, prime bankers acceptances with maturities of up to nine months at the time of acceptance that (1) arise out of the current shipment of goods between countries or within the United States, or (2) arise out of the storage within the United States of goods under contract of sale or expected to move into the channels of trade within a reasonable time and that are secured throughout their life by a warehouse receipt or similar document conveying title to the underlying goods; provided that the aggregate amount of bankers acceptances held at any one time shall not exceed $100 million;

(c) To buy U.S. Government securities, obligations that are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States, and prime bankers acceptances of the types authorized for purchase under 1(b) above, from dealers for the account of the Federal Reserve Bank of New York under agreements for repurchase of such securities, obligations, or acceptances in 15 calendar days or less, at rates that, unless otherwise expressly authorized by the Committee, shall be determined by competitive bidding, after applying reasonable limitations on the volume of agreements with individual dealers; provided that in the event Government securities or agency issues covered by any such agreement are not repurchased by the dealer pursuant to the agreement or a renewal thereof, they shall be sold in the market or transferred to the System Open Market Account; and provided further that in the event bankers acceptances covered by any such agreement are not repurchased by the seller, they shall continue to be held by the Federal Reserve Bank or shall be sold in the open market.

2. In order to ensure the effective conduct of open market operations, the Federal Open Market Committee authorizes and directs the Federal Reserve Banks to lend U.S. Government securities held in the System Open Market Account to Government securities dealers and to banks participating in Government securities clearing arrangements conducted through a Federal Reserve Bank, under such instructions as the Committee may specify from time to time.

3. In order to ensure the effective conduct of open market operations, while assisting in the provision of short-term investments for foreign and international accounts maintained at the Federal Reserve Bank of New York, the Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York (a) for System Open Market Account, to sell U.S. Government securities to such foreign and international accounts on the bases set forth in paragraph 1(a) under agreements providing for the resale by such accounts of those securities within 15 calendar days on terms comparable to those available on such transactions in the market; and (b) for New York Bank account, when appropriate, to undertake with dealers, subject to the conditions imposed on purchases and sales of securities in paragraph 1(c), repurchase agreements in U.S. Government and agency securities, and to arrange corresponding sale and repurchase agreements between its own account and foreign and international accounts maintained at the Bank. Transactions undertaken with such accounts under the provisions of this paragraph may provide for a service fee when appropriate.

Domestic Policy Directive

In Effect January 1, 1992[1]

The information reviewed at this meeting continues to portray a sluggish economy and a depressed state of business and consumer confidence. Total nonfarm payroll employment fell sharply in November; however, the average workweek in the private nonfarm sector edged up and the civilian unemployment rate remained at 6.8 percent. Industrial production fell in November, partly reflecting a sizable drop in motor vehicle assemblies. Consumer spending has been soft on balance in recent months. Real outlays for business equipment appear to be rising slowly, and nonresidential construction has continued to decline. Housing starts were appreciably higher on average in October and November than in the third quarter. The nominal U.S. merchandise trade deficit widened slightly further in September; the deficit in the third quarter was substantially larger than in the second quarter. Wage and price increases have continued to trend downward.

Interest rates have declined appreciably since the Committee meeting on November 5. The Board of Governors approved a reduction in the discount rate from 5 to 4½ percent on November 6. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies declined further over the intermeeting period; the dollar depreciated primarily against the mark and other European currencies.

Expansion in M2 and M3 edged up in November from a slow pace in October; the slightly faster growth reflected a strengthening in the most liquid components of the aggregates. For the year through November, expansion of both M2 and M3 is estimated to have been at the lower ends of the Committee's ranges.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at its meeting in July reaffirmed the ranges it had established in February for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent, respectively, measured from the fourth quarter of 1990 to the fourth quarter of 1991. The monitoring range for growth of total domestic nonfinancial debt also was maintained at 4½ to 8½ percent for the year. For 1992, on a tentative basis, the Committee agreed in July to use the same ranges as in 1991 for growth in each of the monetary aggregates and debt, measured from the fourth quarter of 1991 to the fourth quarter of 1992. With regard to M3, the Committee anticipated that the ongoing restructuring of thrift depository institutions would continue to depress the growth of this aggregate relative to spending and total credit. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might or somewhat lesser reserve restraint would be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from November through March at annual rates of about 3 and 1½ percent, respectively.

1. Adopted by the Committee at its meeting on December 17, 1991.

Authorization for Foreign Currency Operations

In Effect January 1, 1992

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, for System Open Market Account, to the extent necessary to carry out the Committee's foreign currency directive and express authorizations by the Committee pursuant thereto, and in conformity with such procedural instructions as the Committee may issue from time to time:

A. To purchase and sell the following foreign currencies in the form of cable transfers through spot or forward transactions on the open market at home and abroad, including transactions with the U.S. Treasury, with the U.S. Exchange Stabilization Fund established by Section 10 of the Gold Reserve Act of 1934, with foreign monetary authorities, with the Bank for International Settlements, and with other international financial institutions:

Austrian schillings	Italian lire
Belgian francs	Japanese yen
Canadian dollars	Mexican pesos
Danish kroner	Netherlands guilders
Pounds sterling	Norwegian kroner
French francs	Swedish kronor
German marks	Swiss francs

B. To hold balances of, and to have outstanding forward contracts to receive or to deliver, the foreign currencies listed in paragraph A above.

C. To draw foreign currencies and to permit foreign banks to draw dollars under the reciprocal currency arrangements listed in paragraph 2 below, provided that drawings by either party to any such arrangement shall be fully liquidated within 12 months after any amount outstanding at that time was first drawn, unless the Committee, because of exceptional circumstances, specifically authorizes a delay.

D. To maintain an overall open position in all foreign currencies not exceeding $25.0 billion. For this purpose, the overall open position in all foreign currencies is defined as the sum (disregarding signs) of net positions in individual currencies. The net position in a single foreign currency is defined as holdings of balances in that currency, plus outstanding contracts for future receipt, minus outstanding contracts for future delivery of that currency, i.e., as the sum of these elements with due regard to sign.

2. The Federal Open Market Committee directs the Federal Reserve Bank of New York to maintain reciprocal currency arrangements ("swap" arrangements) for the System Open Market Account for periods up to a maximum of 12 months with the following foreign banks, which are among those designated by the Board of Governors of the Federal Reserve System under Section 214.5 of Regulation N, Relations with Foreign Banks and Bankers, and with the approval of the Committee to renew such arrangements on maturity:

Foreign bank	Amount (millions of dollars equivalent)
Austrian National Bank	250
National Bank of Belgium	1,000
Bank of Canada	2,000
National Bank of Denmark	250
Bank of England	3,000
Bank of France	2,000
German Federal Bank	6,000
Bank of Italy	3,000
Bank of Japan	5,000
Bank of Mexico	700
Netherlands Bank	500
Bank of Norway	250
Bank of Sweden	300
Swiss National Bank	4,000
Bank for International Settlements	
Dollars against Swiss francs	600
Dollars against authorized European currencies other than Swiss francs	1,250

Any changes in the terms of existing swap arrangements, and the proposed terms of any new arrangements that may be authorized, shall be referred for review and approval to the Committee.

3. All transactions in foreign currencies undertaken under paragraph 1(A) above shall, unless otherwise expressly authorized by the Committee, be at prevailing market rates. For the purpose of providing an investment return on System holdings of foreign currencies, or for the purpose of adjusting interest rates paid or received in connection with swap drawings, transactions with foreign central banks may be undertaken at non-market exchange rates.

4. It shall be the normal practice to arrange with foreign central banks for the coordination of foreign currency transactions. In making operating arrangements with foreign central banks on System holdings of foreign currencies, the Federal Reserve Bank of New York shall not commit itself to maintain any specific balance, unless authorized by the Federal Open Market Committee. Any agreements or understandings concerning the administration of the accounts maintained by the Federal Reserve Bank of New York with the foreign banks designated by the Board of Governors under Section 214.5 of Regulation N shall be referred for review and approval to the Committee.

5. Foreign currency holdings shall be invested insofar as practicable, considering needs for minimum working balances. Such investments shall be in liquid form, and generally have no more than 12 months

remaining to maturity. When appropriate in connection with arrangements to provide investment facilities for foreign currency holdings, U.S. Government securities may be purchased from foreign central banks under agreements for repurchase of such securities within 30 calendar days.

6. All operations undertaken pursuant to the preceding paragraphs shall be reported promptly to the Foreign Currency Subcommittee and the Committee. The Foreign Currency Subcommittee consists of the Chairman and Vice Chairman of the Committee, the Vice Chairman of the Board of Governors, and such other member of the Board as the Chairman may designate (or in the absence of members of the Board serving on the Subcommittee, other Board Members designated by the Chairman as alternates, and in the absence of the Vice Chairman of the Committee, his alternate). Meetings of the Subcommittee shall be called at the request of any member, or at the request of the Manager for Foreign Operations, for the purposes of reviewing recent or contemplated operations and of consulting with the Manager on other matters relating to his responsibilities. At the request of any member of the Subcommittee, questions arising from such reviews and consultations shall be referred for determination to the Federal Open Market Committee.

7. The Chairman is authorized:

A. With the approval of the Committee, to enter into any needed agreement or understanding with the Secretary of the Treasury about the division of responsibility for foreign currency operations between the System and the Treasury;

B. To keep the Secretary of the Treasury fully advised concerning System foreign currency operations, and to consult with the Secretary on policy matters relating to foreign currency operations;

C. From time to time, to transmit appropriate reports and information to the National Advisory Council on International Monetary and Financial Policies.

8. Staff officers of the Committee are authorized to transmit pertinent information on System foreign currency operations to appropriate officials of the Treasury Department.

9. All Federal Reserve Banks shall participate in the foreign currency operations for System Account in accordance with paragraph 3 G(1) of the Board of Governors' Statement of Procedure with Respect to Foreign Relationships of Federal Reserve Banks dated January 1, 1944.

Foreign Currency Directive

In Effect January 1, 1992

1. System operations in foreign currencies shall generally be directed at countering disorderly market conditions, provided that market exchange rates for the U.S. dollar reflect actions and behavior consistent with the IMF Article IV, Section 1.

2. To achieve this end the System shall:

A. Undertake spot and forward purchases and sales of foreign exchange.

B. Maintain reciprocal currency ("swap") arrangements with selected foreign central banks and with the Bank for International Settlements.

C. Cooperate in other respects with central banks of other countries and with international monetary institutions.

3. Transactions may also be undertaken:

A. To adjust System balances in light of probable future needs for currencies.

B. To provide means for meeting System and Treasury commitments in particular currencies, and to facilitate operations of the Exchange Stabilization Fund.

C. For such other purposes as may be expressly authorized by the Committee.

4. System foreign currency operations shall be conducted:

A. In close and continuous consultation and cooperation with the United States Treasury;

B. In cooperation, as appropriate, with foreign monetary authorities; and

C. In a manner consistent with the obligations of the United States in the International Monetary Fund regarding exchange arrangements under the IMF Article IV.

Procedural Instructions with Respect to Foreign Currency Operations

In Effect January 1, 1992

In conducting operations pursuant to the authorization and direction of the Federal Open Market Committee as set forth in the Authorization for Foreign Currency Operations and the Foreign Currency Directive, the Federal Reserve Bank of New York, through the Manager for Foreign Operations, System Open Market Account, shall be guided by the following procedural understandings with respect to consultations and clearance with the Committee, the Foreign Currency Subcommittee, and the Chairman of the Committee. All operations undertaken pursuant to such clearances shall be reported promptly to the Committee.

1. The Manager for Foreign Operations shall clear with the Subcommittee (or with the Chairman, if the Chairman believes that consultation with the Subcommittee is not feasible in the time available):

A. Any operation that would result in a change in the System's overall open position in foreign currencies exceeding $300 million on any day or $600 million since the most recent regular meeting of the Committee.

B. Any operation that would result in a change on any day in the System's net position in a single foreign currency exceeding $150 million, or $300 million when the operation is associated with repayment of swap drawings.

C. Any operation that might generate a substantial volume of trading in a particular currency by the System, even though the change in the System's net position in that currency might be less than the limits specified in 1.B.

D. Any swap drawing proposed by a foreign bank not exceeding the larger of (i) $200 million or (ii) 15 percent of the size of the swap arrangement.

2. The Manager for Foreign Operations shall clear with the Committee (or with the Subcommittee, if the Subcommittee believes that consultation with the full Committee is not feasible in the time available, or with the Chairman, if the Chairman believes that consultation with the Subcommittee is not feasible in the time available):

A. Any operation that would result in a change in the System's overall open position in foreign currencies exceeding $1.5 billion since the most recent regular meeting of the Committee.

B. Any swap drawing proposed by a foreign bank exceeding the larger of (i) $200 million or (ii) 15 percent of the size of the swap arrangement.

3. The Manager for Foreign Operations shall also consult with the Subcommittee or the Chairman about proposed swap drawings by the System, and about any operations that are not of a routine character.

Meeting Held on February 4–5, 1992

1. Domestic Policy Directive

The information reviewed at this meeting suggested that economic activity remained sluggish. Spending for housing and exports was rising, but retail sales had been weak, and nonresidential construction continued to hold down overall investment expenditures. Nonfarm payroll employment had changed little in December, and industrial production had edged lower in November and December as business firms acted to hold down inventories in the face of slack final demand. Wage and price increases continued to trend downward.

Total nonfarm payroll employment was about unchanged in December after a large decline in November. Manufacturing jobs fell in December for a fourth consecutive month, with nearly all of the losses occurring in durable goods industries. Employment in retail and wholesale trade contracted again, while employment in construction, which had been depressed by unseasonably severe weather in November, registered a small rise. New hires in December were concentrated in health services and local governments. The civilian unemployment rate rose to 7.1 percent in December, its high for the year.

Industrial production declined slightly in December and was unchanged on balance since July; the limited information available suggested that production might have contracted appreciably further in January. Over the November–December period, output was held down in part by reduced production of motor vehicles; in addition, unseasonably warm weather led to lower production of electricity and natural gas. Additional restraints on output included the depressing effects of a strike at a major supplier of industrial equipment and persisting declines in the production of defense and space equipment. By contrast, the output of other types of business equipment had strengthened, particularly in the office and computing component, and the production of construction supplies and a variety of nondurable goods had increased. Total industrial capacity utilization declined further in December but remained somewhat above its low of last March.

Consumer spending had been weak on balance in recent months amid continuing indications of depressed consumer confidence and essentially no growth in disposable income. Nominal retail sales were estimated to have declined appreciably in November and December, and for the fourth quarter decreases in sales were widespread among general merchandise, apparel, and furniture and appliance stores. Against a background of improved consumer attitudes toward homebuying and the strongest quarterly pace of new home sales since the spring of 1990, single-family housing starts rose in December from an upward-revised November level. With high vacancy rates persisting for multifamily units, starts of such units remained near their May 1991 low.

Business fixed investment appeared to have fallen in the fourth quarter as a small rise in equipment spending was offset by further steep reductions in nonresidential construction. After little change in the third quarter, shipments of nondefense capital goods picked up in the fourth quarter, principally because of a surge in outlays for computers. Recent data on orders suggested little growth in business spending for equipment over the near term. Office and other commercial construction activity weakened substantially further in November. The persistently low occupancy rates for commercial structures, and the continuing downtrend in construction contracts and appraisal values of office properties, suggested that nonresidential construction activity would remain depressed for some time.

Business inventories rose noticeably over the months of September through November after substantial liquidation earlier in the year. At the retail level, inventories continued to build, and inventory-to-sales ratios rose for most types of retailers, although the pace of accumulation appeared to have slowed in November. Wholesale inventories expanded sharply in October and November; for most types of distributors, inventory-to-sales ratios had moved up in recent months but had remained well below their highs of a year ago. By contrast, manufacturing stocks in the aggregate continued to decline, despite slowing shipments that led to buildups in stocks of finished goods in some industries. The ratio of stocks to sales in manufacturing remained on a downtrend that began in late 1990.

The nominal U.S. merchandise trade deficit narrowed considerably in November. For the October–November period, a sizable rise in exports that was only partly offset by an increase in imports brought a substantial improvement in the trade balance from the third-quarter rate. The strength in exports, which may have been associated in part with a bunching of shipments, was concentrated in aircraft, machinery, consumer goods, and agricultural products. Among imports, most of the rise was in consumer goods. The available data on economic activity in the major foreign industrial countries suggested that relatively weak growth had continued into the fourth quarter. In most of these countries, with output moving closer to or further below potential, inflationary pressures appeared to have eased somewhat further.

Producer prices of finished goods declined in December; prices of food and energy moved lower, while prices of other finished goods rose at about the reduced pace of earlier months in the year. At the consumer level, prices of nonfood, non-energy items increased in December at the moderate rate evident since the first quarter of 1991 and well below the pace for 1990. Average hourly earnings rose more rapidly in December than in prior months; however, for the year as a whole, this earnings measure increased at a considerably slower pace than in 1990.

At its meeting on December 17, 1991, the Committee adopted a directive that called for initially maintaining the existing degree of pressure on reserve positions but that included a marked bias toward easing during the intermeeting period. Accordingly, the directive indicated that in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or somewhat lesser reserve restraint would be acceptable in the intermeeting period. The reserve conditions contemplated under this directive were expected to be consistent with growth of M2 and M3 at annual rates of around 3 percent and 1½ percent respectively over the period from November through March.

Shortly after the meeting, with incoming information continuing to point to a very sluggish economy, receding inflationary pressures, and slow growth in the broader monetary aggregates, open market operations were directed toward a substantial easing of conditions in reserve markets. This step was taken in conjunction with a reduction in the discount rate from 4½ to 3½ percent that was approved by the Board of Governors effective December 20. Two technical reductions were made to expected levels of adjustment plus seasonal borrowing during the intermeeting period to reflect the downward drift in seasonal borrowing in early winter. Adjustment plus seasonal borrowing averaged a little above expected levels over most of the intermeeting interval, although very large adjustment borrowing occurred on the settlement day of one reserve maintenance period as a result of a reserve shortfall. At the beginning of the intermeeting period, the federal funds rate averaged around 4½ percent; after the easing of reserve conditions, the funds rate dipped to a little below 4¼ percent through the first week of the new year and then dropped further to around 4 percent as relatively mild year-end pressures abated.

In response to the easing in reserve markets, other short-term interest rates declined about the same amount as the federal funds rate, while longer-term rates fell somewhat less. Rates on intermediate- and long-term securities continued to decline through the early part of 1992 as incoming data seemed to indicate further economic weakness. However, these rates began to firm again by mid-January; over the latter part of the intermeeting period, concerns mounted with regard to current and prospective supplies of federal debt offerings, especially in the context of proposals for fiscal stimulus, and market participants reacted to evidence that tended to suggest an improved economic outlook and consequently a reduced prospect of further monetary easing. For the intermeeting period as a whole, interest rates on intermediate-term Treasury issues were up somewhat, while rates on long-term Treasury and private instruments registered mixed changes. Following the 1 percentage point drop in the discount rate, the prime rate was reduced by the same amount, to 6½ percent. Broad stock price indexes rose substantially.

In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies rose slightly on balance over the intermeeting period. The dollar declined early in the period, particularly against the German mark, in response to the easing of monetary policy in the United States and the nearly concurrent rise in official German lending rates. In January, however, the dollar rebounded sharply amid market speculation that interest rates in the United States might not decline further and that interest rates in Germany might have peaked. On balance, the dollar weakened appreciably against the Japanese yen over the intermeeting period in response to concerns about trade imbalances between the two countries and to official intervention during the period in support of the yen.

After accelerating somewhat in the fourth quarter from a very weak performance earlier, growth of M2 and M3 appeared to have slowed in January, partly reflecting temporary distortions in demand deposits and money market funds around year-end. The slower growth also seemed to reflect the attraction of relatively high bond yields and persistently rising prices in the stock market at a time when many banking institutions were aggressively reducing offering rates on deposits. For the year 1991, the expansion of both M2 and M3 was estimated to have been at rates a little above the lower ends of the Committee's ranges, while growth of total domestic nonfinancial debt appeared to have been marginally above the lower end of its monitoring range.

The staff projection prepared for this meeting pointed to a recovery in economic activity. In the near term, a small overhang of inventories and depressed confidence would tend to limit overall increases in spending despite indications of a substantial pickup in residential construction, notably of single-family homes. Subsequently, however, the cumulative effects of earlier declines in interest rates would be expected to lead to a moderate pickup in growth, with the risks to that trajectory for the economy being viewed as about in balance. Stronger consumer spending, a rise in business equipment investment, and a swing from liquidation to accumulation of inventories were projected to provide most of the impetus for faster growth. The retarding effects of depressed nonresidential construction activity and of the ongoing restructuring of household and business balance sheets were expected to lessen gradually as the expansion progressed. The potential nature and size of any stimulative fiscal package remained highly uncertain, and the staff projection did not incorporate major new fiscal initiatives. The substantial though diminishing slack expected in labor and product markets in coming quarters was projected to induce further declines in the underlying rate of inflation.

In their discussion of the economic situation and outlook, Committee members continued to view some strengthening in aggregate demand and overall business activity as the most likely prospect during the months ahead, with the expansion settling into a pattern of moderate growth by the second half of the year. The available information suggested that the sluggish performance of the economy was continuing in early 1992, though there were indications, still very tentative and largely anecdotal, of some improvement. Nonetheless, the decline in interest rates over the second half of 1991 accompanied by the appreciable progress achieved by many financial institutions, business firms, and households in improving their balance sheets appeared to have established a basis for a pickup in final demand. The timing and strength of an upturn remained subject to substantial uncertainties, and the need for further policy stimulus to foster a satisfactory economic expansion could not be ruled out. The uncertainties arose in part from the largely unpredictable course of fiscal policy, the still depressed state of business and consumer confidence, the strength and effects of continuing efforts to shore up balance sheets, and the extent to which economic growth might slow abroad. With regard to the outlook for inflation, the available data and anecdotal information about recent increases in costs and prices reflected quite promising developments, and the members continued to anticipate appreciable progress toward a lower core rate of inflation.

In keeping with the practice at meetings when the Committee establishes its long-run ranges for growth of the money and debt aggregates, the Committee members and Federal Reserve Bank presidents not currently serving as members had prepared projections of economic activity, the rate of unemployment, and inflation for the year 1992. Measured from the fourth quarter of 1991 to the fourth quarter of 1992, the forecasts for growth of real GDP had a central tendency of 1¾ to 2½ percent. Projections of the civilian rate of unemployment in the fourth quarter of 1992 were concentrated in a range of 6¾ to 7 percent. These forecasts pointed to rates of resource utilization that seemed consistent with appreciable progress toward price stability. Projections of the increase in the CPI from the fourth quarter of 1991 to the fourth quarter of 1992 were centered in a range of 3 to 3½ percent; this range compared with a realized increase in the CPI of 3 percent in 1991, but the result for 1991 had been heavily influenced by the sharp decline in oil prices, so the members' forecasts represented a significant decrease in the underlying rate of inflation. Forecasts of growth of nominal GDP had a central tendency of 4½ to 5¾ percent for 1992.

The members acknowledged that there were substantial risks of an outcome outside the central tendency of their forecasts for economic activity. Views differed with regard to the most likely direction of any deviation, but many of the members saw those risks as being in better balance than previously. Among the uncertainties in the outlook was the extent to which financial intermediaries would continue to restrict their extensions of credit to less than prime borrowers. In this connection, a number of members reported on anecdotal indications that banking institutions in various parts of the country appeared to have become somewhat more willing lenders, even though overall survey results and many banker comments did not indicate any easing in credit standards. A second source of uncertainty related to the continuing efforts of business firms and households to strengthen their balance sheets and in the process to divert some of their corporate cash flows or disposable personal incomes from spending to reducing debt and improving equity positions. These efforts together with lower market interest rates already appeared to have induced significant progress toward reducing debt exposures and debt servicing costs, but the financial restructuring process was still under way and the extent to which it would continue to inhibit spending remained unclear. A further source of uncertainty related to the ongoing and widespread adjustments in corporate business structures, including downsizings, that were aimed at improving the competitive efficiency of business firms. While these restructuring activities were serving to strengthen the long-run competitive position of the economy, they tended for the present to inhibit overall spending, both directly and indirectly through the adverse effects of widely publicized job cutbacks on consumer sentiment.

Many of the members observed that fiscal policy developments were adding to the uncertainties in the economic outlook. At the moment, the potential outcome of fiscal initiatives by the Administration and the Congress was unknown. In the view of at least some members, a limited package of short-term fiscal stimulus measures implemented relatively early this year could have a favorable effect on business activity. On the other hand, adoption of fiscal measures involving substantial stimulus, which would further impede the prospects for long-term budgetary balance, would be likely to have strongly adverse repercussions on financial markets and perhaps on business and consumer confidence. Indeed, concerns about the outlook for fiscal policy might well have been an important factor behind the rise in long-term bond yields this year. It also was noted that uncertainty about the exact provisions of the fiscal program that might eventually be adopted was causing some businesses to defer investment decisions.

In their review of business conditions in different parts of the country, members again reported on mixed patterns of activity in recent months, and they described overall conditions in the different regions as ranging from slightly weaker to slightly stronger. Although an expected upturn in general business activity had not materialized thus far, many members sensed some improvement in business attitudes. Notwithstanding the persistence of gloomy consumer sentiment, contacts among retailers indicated that many had experienced somewhat better sales in recent weeks than they had anticipated earlier, though reports from some parts of the country pointed to significant exceptions. Members commented that the pickup in sales of single-family homes together with reduced interest burdens stemming from home mortgage refinancings would tend to stimulate consumer spending in the quarters ahead. Over the near term, production activity was likely to be inhibited to some degree by the moderate buildup that had occurred late in 1991 in wholesale and retail inventories. As the year progressed, however, a pickup in consumer spending probably would encourage some increase in inventory investment. Likewise, cautious business attitudes along with excess capacity in several key industries and the ongoing efforts to improve balance sheets would limit the growth in business spending for plant and equipment for some period of time, probably until an upturn in final demand was well under way. The prospects for commercial construction activity remained severely constrained by high vacancy rates in many parts of the country. On the foreign side, the outlook for relatively sluggish economic growth in several key industrial nations implied more limited growth in U.S. exports; in addition, if sentiment favoring more protectionism were to gather added strength in the context of a weak domestic economy, new trade restrictions might be imposed that would have adverse effects.

With regard to the prospects for inflation, members observed that core inflation was continuing to recede, and in the context of their outlook for relatively limited pressures on production resources, some commented that they would not view an inflation result below the central tendency of the members' projections as a surprising outcome. Developments having favorable implications for inflation included an extended period of subdued monetary growth, highly competitive conditions in domestic and international markets for numerous products, and productivity gains associated with business restructuring activities that were adding to the usual operating efficiencies achieved during the early quarters of cyclical upswings. The members did not rule out the possibility that unanticipated surges in energy or food prices might temporarily arrest or reverse progress toward price stability, but they assumed that such prices would move in line with most other prices in the year ahead.

In keeping with the requirements of the Full Employment and Balanced Growth Act of 1978 (the Humphrey–Hawkins Act), the Committee at this meeting reviewed the ranges for growth of the monetary and debt aggregates in 1992 that it had established on a tentative basis in July 1991. The tentative ranges included expansion of 2½ to 6½ percent for M2 and 1 to 5 percent for M3, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The monitoring range for growth of total domestic nonfinancial debt had been set provisionally at 4½ to 8½ percent for 1992. All of these ranges were unchanged from those for 1991 that the Committee had set in February and reaffirmed in July of last year.

In the Committee's discussion, a majority of the members indicated a preference for affirming the ranges for 1992 that had been established on a tentative basis in July. While those ranges were acceptable to all the members, several expressed a preference for lowering them.

In formulating the Committee's objectives for 1992, members stressed that policy needed to promote sustainable expansion in economic activity while consolidating and extending gains against inflation. Both objectives were attainable, especially in light of the degree of slack in the economy. However, the translation of these objectives into specific money growth ranges was complicated by questions about the relation of the monetary aggregates to spending. Since 1989, the level of M2 had fallen increasingly short of levels that past historical relationships with nominal GDP and market interest rates would have indicated. Insofar as could be judged at this point, retention of a 2½ to 6½ percent range for M2 should provide adequate leeway and operational flexibility to accommodate a satisfactory economic performance. Demand for M2 balances relative to income would continue to be damped if, as appeared likely, banks and thrifts were to reduce further their offering rates on deposits in lagged response to earlier declines in market rates. The reductions in offering rates could be pronounced if banking institutions maintained their cautious lending policies and many prime borrowers continued to channel a larger-than-usual share of their financing needs toward longer-term market sources of funds and away from depository institutions. Under those circumstances, velocity could well rise appreciably and relatively modest M2 growth would not necessarily be inconsistent with a satisfactory economic expansion. On the other hand, the continuing improvement in the balance sheets and capital positions of depository institutions might prompt them as a group to become more willing lenders and thus to bid more aggressively for deposits to fund additional lending. In this case faster growth of M2, perhaps toward the upper end of the tentative range, might be desirable. On balance, the members believed that adoption of the tentative M2 range for 1992 should allow sufficient room for the likely range of developments in the intermediation process. Nonetheless, the substantial uncertainties surrounding the outlook for M2 suggested that the Committee would have to approach monetary developments with a great deal of flexibility over the year ahead.

An unchanged target range for M3 also was seen as likely to provide adequate room for a desirable rate of growth in this aggregate in the context of accommodating the Committee's broad policy objectives. The growth of M3 probably would continue to be affected to a greater extent than that of M2 by the diversion of credit demands to sources outside depository institutions and by the ongoing contraction of the thrift industry in conjunction with the activities of the Resolution Trust Corporation. Accordingly, a lower range for M3 than for M2 appeared to remain appropriate. Retention of an unchanged monitoring range for growth in nonfinancial debt also seemed warranted for 1992, even though the expansion in such debt was likely to accelerate somewhat from a very sluggish pace in 1991, mainly as a result of more rapid growth in the federal debt. Nonfederal debt also might increase a little faster this year, but the pickup was likely to be limited by the still cautious attitudes of households and businesses toward new debt. Thus, the 1991 range for nonfinancial debt should comfortably encompass an expansion of credit to support stronger spending in 1992.

Members who preferred a lower range for M2 believed that a reduction was desirable at this time to underscore the Committee's commitment to its long-run objective of price stability. While the unchanged range supported by the majority might provide the flexibility needed for a desirable anti-inflationary policy in the year ahead, a lower range would be more consistent with the Committee's ultimate objective of price level stability. However, in the view of other members a reduction at this time could be interpreted as an indication that the Committee might not be willing to supply enough liquidity to foster an appreciable strengthening in the economy in 1992, especially if a fairly rapid increase in M2 were needed to compensate for relatively slow money growth in 1991. No member advocated higher monetary growth ranges, but a number suggested that the emergence of more normal patterns of monetary velocity in association with an economic performance in line with the central tendency of the members' projections might appropriately result in M2 growth in the upper half of the Committee's range.

Concerns about the implications of slow money growth in 1991 and the possibility of more normal velocity patterns in 1992 prompted some members to suggest a modification of the current procedure for constructing yearly monetary growth ranges. The modification would involve linking the ranges for the current year to those for the previous year rather than to the actual outcomes for that year. The new approach would place monetary targeting in a multi-year context with the objective of constraining money growth to a desired range over a longer horizon. Such an approach would have advantages over current procedures if the relationship between money growth and spending could be predicted with confidence. In the course of the Committee's discussion, however, a number of members referred to questions that had arisen about that relationship in recent years as thrift institutions were closed and credit flows increasingly bypassed depository institutions. A satisfactory performance of the economy in 1992 might well be accompanied by a rise in velocity, although there was considerable uncertainty about such an outcome. Should velocity in fact rise, the acceleration of the broader aggregates implied by this alternative approach and the associated easing of reserve conditions and short-term interest rates might not be consistent with the Committee's objectives. Given the uncertainties about velocity, a broad array of indicators, in addition to money, would need to continue to be assessed in determining the appropriate stance of the Committee in providing reserves. Members concluded that the proposal should be studied further and reconsidered later in light of changing circumstances.

At the conclusion of the Committee's discussion, all of the members indicated that they favored or could accept the ranges for 1992 that the Committee had established on a tentative basis at its meeting in July 1991. In keeping with the Committee's usual procedures under the Humphrey–Hawkins Act, the ranges would be reviewed at midyear, or sooner if deemed necessary, in light of the behavior of the aggregates and ongoing economic and financial developments. The Committee approved the following paragraph for inclusion in the domestic policy directive:

> The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at this meeting established ranges for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent, respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The monitoring range for growth of total domestic nonfinancial debt was set at 4½ to 8½ percent for the year. With regard to M3, the Committee anticipated that the ongoing restructuring of depository institutions would continue to depress the growth of this aggregate relative to spending and total credit. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

> Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hendricks, Hoenig, Kelley, LaWare, Lindsey, Melzer, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: None.

In the Committee's discussion of policy for the period immediately ahead, all of the members favored or found acceptable a proposal to maintain unchanged conditions in reserve markets and to bias the directive toward possible easing during the intermeeting period. In support of this policy, members observed that reserve conditions had been eased substantially over the past several months, including the easing undertaken in the latter part of December, and that much of the stimulus from recent policy actions had yet to be felt in the economy. The members generally agreed that enough monetary stimulus probably had been implemented to foster the desired upturn in economic activity without further policy moves. Nonetheless, the high degree of uncertainty surrounding the outlook suggested that the Committee needed to remain alert to the possibility of developments that might require additional easing.

In these circumstances, a majority of the members expressed a preference for a directive that was biased toward some easing. The lagged effects of earlier easing actions could prove to be less stimulative than anticipated, in part because of ongoing balance sheet restructuring activities. The persistence of a weak economy might well have especially severe consequences, and, in the view of some members, signs of such an outcome would call for prompt action. However, many members who supported a bias toward ease also stipulated that there should not be an unusually strong presumption that any easing would in fact be implemented during the intermeeting period ahead: The Committee should ease only in response to cumulating evidence that economic activity was not picking up or that monetary growth was falling appreciably short of current expectations. A few members, while not ruling out the possible need for further easing, preferred not to bias the directive in either direction. In this view, more emphasis needed to be put on the inflationary risks of overreacting to the current weakness in the economy, and a symmetrical directive would require more persuasive evidence of the need for some easing before action was taken.

With regard to the outlook for monetary expansion, some members expressed concern about the relatively sluggish growth of the broader aggregates. While the most recent data suggested some pickup in M2 growth, the behavior of that aggregate had been erratic in recent months and it was difficult to discern its underlying trend. According to a staff analysis prepared for this meeting, the growth of M2 and M3 could be expected to accelerate somewhat in the period ahead, given current conditions in reserve markets and some projected strengthening in the economy. However, expansion of M2 probably would continue to be restrained by the aggressive reductions by depository institutions in their offering rates on deposit components of this aggregate and the continuation of related shifts of M2 funds into higher-yielding capital market instruments. In addition, the expected pickup in the pace of RTC resolutions over the balance of the first quarter would tend to moderate the growth of M2 and especially M3. To the extent that subdued growth of the broader aggregates were to reflect such special influences, there would not be significant adverse implications for the overall performance of the economy. Moreover, in the view of some members, the very considerable strength of narrow measures of money and reserves also tended to attenuate concerns about the possibly inadequate expansion of the broader monetary aggregates; indeed, in at least one view, the rapid growth of narrow money would become a worrisome development were it to persist. The members generally concluded, however, that somewhat faster growth in the broader aggregates would be a welcome development.

At the conclusion of the Committee's discussion, all of the members indicated that they were prepared to vote for a directive that called for maintaining the existing degree of pressure on reserve positions. The members also noted their preference for or acceptance of a directive that included some bias toward possible easing during the intermeeting period. Accordingly, in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable during the intermeeting period. The reserve conditions contemplated at this meeting were expected to be consistent with growth of M2 and M3 at annual rates of around 3 percent and 1½ percent respectively over the three-month period from December through March.

At the conclusion of the meeting the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting suggests that economic activity has remained sluggish. Total nonfarm payroll employment was little changed in December, and the civilian unemployment rate rose to 7.1 percent. Industrial production fell slightly in November and December, partly reflecting a sizable drop in motor vehicle assemblies. Consumer spending has been weak on balance in recent months amid continuing indications of depressed consumer confidence and essentially no growth in disposable income. Demand for business equipment has been uneven, while nonresidential construction has remained in a steep decline. Single-family housing starts continued to recover in December. The nominal U.S. merchandise trade deficit narrowed in November, and for October–November combined the trade balance improved substantially from the third-quarter rate. Wage and price increases have continued to trend downward.

Short-term interest rates have declined appreciably since the Committee meeting on December 17, while longer-term rates have registered mixed changes. The Board of Governors approved a reduction in the discount rate from 4½ to 3½ percent on December 20. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies rose slightly on balance over the intermeeting period.

After accelerating somewhat in the fourth quarter, M2 and M3 slowed in January, partly reflecting temporary distortions around year-end. For the year 1991, the expansion of both M2 and M3 is estimated to have been at rates a little above the lower ends of the Committee's ranges. Growth of total domestic nonfinancial debt appears to have been marginally above the lower end of the Committee's monitoring range for the year.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at this meeting established ranges for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent, respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The monitoring range for growth of total domestic nonfinancial debt was set at 4½ to 8½ percent for the year. With regard to M3, the Committee anticipated that the ongoing restructuring of depository institutions would continue to depress the growth of this aggregate relative to spending and total credit. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might or slightly lesser reserve restraint would be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from December through March at annual rates of about 3 and 1½ percent, respectively.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hendricks, Hoenig, Kelley, LaWare, Lindsey, Melzer, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: None.

2. Agreement to "Warehouse" Foreign Currencies

On February 5, 1991, the Committee had approved a reduction from $15 billion to $10 billion in the amount of eligible foreign currencies that the System was prepared to "warehouse" for the Treasury and the Exchange Stabilization Fund (ESF). The purpose of the warehousing facility is to supplement the U.S. dollar resources of the Treasury and the ESF for financing their purchases of foreign currencies and related international operations.

At this meeting, the Committee agreed to reduce the limit further to $5.0 billion, a ceiling that earlier had been in place for many years. System holdings of foreign currencies under the warehousing facility had risen to a peak of $9.0 billion in March 1990, but by the end of August 1991 they had been cut back to their current level of $2.0 billion. Accordingly, the new $5.0 billion ceiling was expected to provide an adequate cushion of unused capacity and, thus, to maintain operational flexibility to respond on short notice to unanticipated developments.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hendricks, Hoenig, Kelley, LaWare, Lindsey, Melzer, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: None.

Meeting Held on March 31, 1992

Domestic Policy Directive

The information reviewed at this meeting suggested that domestic final demand, especially in the consumer sector, had strengthened somewhat in recent months. Production and employment had not picked up commensurately because businesses apparently were meeting much of their increased sales by drawing down inventories. Wage and price increases had continued to trend downward.

Total nonfarm payroll employment rebounded in February from a large drop in January. The February gain was concentrated in retail trade, but employment in services also rose moderately further and manufacturing payrolls, after five months of decline, were lifted somewhat by the return of auto workers from temporary layoffs. The average workweek increased substantially in manufacturing and in some service-producing industries. Although employment picked up in February, appreciable expansion of the labor force brought a rise in the civilian unemployment rate to 7.3 percent, and initial claims for unemployment insurance remained elevated.

Industrial production rose considerably in February but was little changed on balance over the first two months of the year. Part of the increase reflected an upturn in motor vehicle assemblies, with the remainder being spread across a broad range of other goods. Among final products, gains were posted in both business products, notably office and computing equipment, and consumer goods. By contrast, utility output again was held down by unseasonably warm winter weather, and the production of defense and space equipment continued to ebb. Total industrial capacity utilization moved higher in February but remained well below its pre-recession high.

Retail sales registered large gains in January and February after edging down in the fourth quarter of 1991. The stronger sales were associated with sizable increases for most types of durable and nondurable goods. Single-family housing starts rose substantially further in January and February, reaching their highest level since the first quarter of

1990, and sales of both new and existing homes were up considerably on balance over the two months. With vacancy rates persisting at historically high levels, starts in the multifamily sector remained depressed.

Shipments of nondefense capital goods increased sharply in January and February, reflecting strength in office and computing equipment and in business purchases of motor vehicles; in addition, shipments of aircraft rebounded in January from a very low level in the fourth quarter. Recent data on orders pointed to further increases over coming months in outlays for business equipment other than aircraft. Nonresidential construction activity edged up in January but remained below its fourth-quarter average. Further declines were recorded in the construction of office buildings and hotels in January, and persisting weakness in commercial construction was signaled by continued decreases in appraised values of office properties in late 1991.

Business inventories registered steep declines in January after rising substantially in previous months. Stocks at wholesale and retail trade establishments reversed a sizable portion of the accumulation that occurred in the fourth quarter; even so, for many types of businesses in the trade sector, inventory-to-sales ratios remained at elevated levels. In manufacturing, inventories were reduced further in January, with much of the drawdown occurring in defense aircraft and parts, food products, and petroleum. Inventory-to-shipments ratios in most manufacturing industries remained well below the cyclical peaks reached in early 1991.

The nominal U.S. merchandise trade deficit narrowed slightly in January and was essentially unchanged from its average rate in the fourth quarter. A decline in exports was concentrated in aircraft and automotive products. A slightly larger drop in the value of imports reflected weakness in both oil and consumer goods. The available data on fourth-quarter economic activity in the major foreign industrial countries indicated that real output declined in Canada, Germany, Japan, and the United Kingdom, while data for France pointed to little change. For the first quarter of this year, the limited data available showed some signs of recovery in continental Europe but suggested continued sluggishness in the other major industrial countries.

Producer prices of finished goods edged down on balance in January and February, as a reduction in energy prices more than offset an increase in food and other prices. Excluding the food and energy components, producer prices rose over the January–February period at about the 1991 pace. At the consumer level, food prices changed little over the two months while energy prices fell; prices of nonfood, non-energy items increased at about the same rate as last year but significantly below that of 1990. Average hourly earnings of production or nonsupervisory workers in February more than reversed a small decline in January. However, over the twelve-month period ending in February, this measure of worker earnings increased more slowly than in the twelve months ending in February 1991.

At its meeting on February 4–5, 1992, the Committee adopted a directive that called for maintaining the existing degree of pressure on reserve positions but that included a bias toward possible easing during the intermeeting period. Accordingly, the directive indicated that in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable in the intermeeting period. The reserve conditions contemplated under this directive were expected to be consistent with growth of M2 and M3 at annual rates of around 3 percent and 1½ percent respectively over the three-month period from December through March.

Open market operations during the intermeeting period were directed toward maintaining the existing degree of pressure on reserve positions. Expected levels of adjustment plus seasonal borrowing were raised modestly immediately after the Committee meeting in anticipation of a slight rise in seasonal borrowing. In the event, adjustment plus seasonal borrowing remained quite low, averaging a little less than $70 million over most of the intermeeting period; seasonal borrowing, newly subject to a market-based discount rate, increased relatively little and adjustment credit remained at depressed levels. The federal funds rate averaged around 4 percent over most of the intermeeting period, although late in the period the rate averaged a little lower.

Many other market interest rates rose appreciably over the intermeeting period, as market participants interpreted incoming data as indicating that the economic recovery was regaining some momentum. The most pronounced increases occurred at intermediate maturities, perhaps reflecting the improved cyclical outlook for business activity. Although yields on investment-grade corporate debt rose in tandem with rates on U.S. Treasury securities, yields on lesser-rated securities were unchanged to somewhat lower. Most broad indexes of stock prices declined somewhat over the intermeeting period.

In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies increased substantially over the period. The dollar declined initially on market expectations of additional monetary easing in the United States, but it subsequently appreciated in response to indications of a strengthening of the recovery. Late in the intermeeting period, a tightening of money market conditions in Germany, where monetary growth continued to be quite rapid and concerns over wage pressures were mounting, contributed to a retreat in the dollar. The yen weakened on balance in relation to the dollar and other major currencies in response to indications of further declines in economic growth and resultant expectations of another monetary easing action in Japan.

Growth of M2 and M3 accelerated sharply in February, but M2 apparently leveled off or even declined slightly in March and M3 contracted somewhat. Growth of M2 and M3 from December through March appeared to have been, respectively, somewhat above and close to the Committee's expectations. Much of the growth in both aggregates over recent months reflected a surge in transactions balances that, in turn, resulted to an important extent from narrow opportunity costs relative to market interest rates and from a bulge in demand deposits associated with mortgage refinancings and other financial market activity.

The staff projection prepared for this meeting pointed to a continuing recovery in economic activity. In the near term, growth in consumer spending was expected to moderate after the first-quarter spurt, but residential construction was likely to record further substantial gains, and the pace of nonfarm inventory liquidation should slow. Over time, the cumulative effects of earlier declines in interest rates, the progress achieved in strengthening household and business balance sheets, and some diminution of credit supply restraints would provide continuing impetus to economic activity. Moreover, the retarding effects of depressed nonresidential construction activity were expected to lessen as the expansion progressed. The projection did not incorporate any major new fiscal initiatives at the federal level, and it anticipated that spending for goods and services at all levels of government would be restrained somewhat. The substantial, though diminishing, margin of slack in resource utilization was projected to be associated with appreciable further slowing in the underlying rate of inflation.

In the Committee's discussion, the members generally viewed the incoming information, including anecdotal reports from around the country, as providing substantial evidence of some quickening in the pace of overall economic activity. Final demands appeared to be strengthening in the context of improving business and consumer confidence. Nonetheless, key sectors of the economy, such as defense spending and commercial real estate, remained weak and a back-up in long-term interest rates, owing in part to lagging savings and strong demand for credit by the Treasury, threatened to limit gains in housing and business investment. With these cross-currents and sources of uncertainty raising at least some questions about the sustainability of the expansion, careful, ongoing evaluation was warranted. On balance, however, relatively moderate but sustained growth was seen as the most probable outcome. The members generally regarded the prospects for some continuing slack in labor and product markets as consistent with their projections of a downtrend in the core rate of inflation.

With regard to financial developments bearing on the economic outlook, members stressed, as they had at earlier meetings, that considerable progress had been made in strengthening business and consumer balance sheets. While media attention continued to be focused on some large financial and nonfinancial firms that were experiencing difficulties, most businesses now appeared to be much more favorably positioned to weather adverse developments and to finance spending that would support an expanding economy. The improvement stemmed from ongoing efforts to streamline operations and enhance productivity and to reduce balance-sheet leverage and interest costs. For some business firms and many financial institutions, recent reports of a tendency for commercial real estate values to stabilize was a particularly favorable omen. Consumer balance sheets also were benefiting from lower interest rates that tended to lessen debt loads in relation to income and from the appreciated value of stock portfolios. On the negative side, the restructuring of business operations and balance sheets was still exerting considerable constraints on spending and lending activities, and it was unclear how much longer or to what extent those constraints would last. A number of members also expressed concern that the relatively slow growth of the broader monetary aggregates, were it to persist, might prove to be a harbinger of continued restraint in lending and of underlying weakness in the economy.

In their review of business conditions in different regions, members indicated that overall economic activity appeared to be rising in many parts of the nation while some signs of an emerging upturn could be discerned in most other areas. Improving business conditions generally were associated with better retail sales since the start of the year and with the further recovery in housing demand. Indeed, the growing demands for consumer goods stemmed to an extent from the strengthening of housing markets. These developments were accompanied and bolstered by widespread indications of some improvement in business and consumer confidence, and some members commented that pent-up demands for many consumer durables might well materialize in the context of further gains in overall consumer confidence. However, most business executives were still very cautious despite increasing sales and a more favorable outlook for corporate profits, and consumer confidence remained well below earlier levels, apparently reflecting to a major extent the persistence of anxieties about job security and employment opportunities. Retail contacts and available statistical reports suggested that an important part of the spurt in retail sales in January and February was met out of inventories. Further growth in such sales would lead to efforts to rebuild inventories and induce related gains in production and incomes.

Sales of residential real estate and the construction of new homes, principally single-family dwellings, were displaying considerable strength across the country. In a number of areas the increases were appreciably greater than expected, though the gains appeared to be due at least in part to favorable weather conditions and thus might represent some borrowing from the future. Even so, and despite the inhibiting effects of recent increases in mortgage interest rates, the construction of single-family homes and its spillover effects in related industries were believed likely to make an important contribution to the overall expansion of economic activity over the next several quarters.

Construction of nonresidential structures continued to decline in many areas as work on existing buildings was completed and few new projects were started. Vacancy rates for office buildings remained high across the country, but there were indications in at least some major cities that prices and rental rates for commercial real estate might be stabilizing or even tending to firm. However, the better tone in those markets had not translated itself into new building activity. Indeed, commercial construction was likely to remain depressed for an extended period and to hold down the growth in overall business investment at a time when spending for business equipment might be trending appreciably higher.

The outlook for exports to a number of major foreign industrial countries was less encouraging than earlier, given financial and other difficulties that would tend to inhibit economic growth in those countries. On the favorable side, U.S. businesses had significantly enhanced their ability to compete in international markets over the course of recent years, partly through gains in productivity, and they were now in a better position both to sustain the nation's exports and to meet competition from foreign products in domestic markets. Moreover, the improved health of many Latin American economies was being reflected in higher export sales to such countries. Some parts of the country also were benefiting from large increases in the number of foreign visitors. Nevertheless, members suggested that the export sector was vulnerable to weakness from abroad, and reports from some business contacts tended to reinforce those concerns.

Turning to the outlook for fiscal policy, members noted that market concerns about possible legislation that would substantially increase an already massive federal deficit appeared to have subsided. Nonetheless, an important reason for the rise in intermediate- and long-term interest rates since early January had been the apparently worsening outlook for federal deficit financing over the course of the next several years. Such deficits would tend to keep long-term interest rates fairly high, and in association with the nation's relatively low savings, they implied a financial constraint on the ability of the U.S. economy to generate robust increases in investment. Because the volume of savings available for investment was limited, interest rates had tended to react fairly strongly to indications of sizable gains in private spending.

The outlook for moderate economic growth and the associated, if diminishing, slack in labor and product markets were likely to prove consistent in the view of many members with further progress in reducing the core rate of inflation. Competitive price pressures remained strong in many local markets, and efforts to raise prices very often did not succeed. In this competitive environment, business firms seeking to maintain or increase profits were forced to concentrate on measures to curb costs rather than to raise prices. Labor markets were described as generally soft, and most wage settlements continued to have favorable implications for future costs and inflation. The outlook for energy costs, while always subject to unanticipated developments, nonetheless seemed favorable at this point.

In the Committee's discussion of policy, all of the members indicated that they were in favor of maintaining unchanged conditions in reserve markets for the period immediately ahead. A majority also indicated a preference for retaining the current bias in the directive toward possible easing during the intermeeting period, while the remaining members were in favor of moving to a symmetrical directive. A steady policy course, at least for now, was viewed as desirable in the context of encouraging evidence of a strengthening economy and the outlook for continuing expansion at a pace that was deemed likely to be consistent with further progress toward price stability. The members acknowledged that the uncertainties in the economic outlook were considerable, but given the ongoing stimulus stemming from earlier easing actions, they agreed that for now an unchanged policy represented an appropriate balancing of the various risks to a satisfactory economic performance. In this connection, it was suggested that substantial further easing at this time might well fail to provide much added stimulus; indeed, it could prove to be counterproductive because of adverse repercussions in financial markets. Moreover, too much easing at this juncture could establish the basis for unduly rapid growth of money and credit when the economic expansion gathered momentum.

With regard to possible adjustments to the degree of reserve pressure during the intermeeting period, many of the members endorsed the view that it would be premature to move away from a directive that was biased toward ease to a symmetrical directive. While the members generally anticipated that economic and financial developments during the intermeeting period would not call for an adjustment to policy, many remained concerned about the vulnerability of the expansion to a variety of risks. In the circumstances, any policy adjustments in the weeks ahead were more likely to be in the direction of some easing than toward restraint. A number of these members also commented that even though the risks of a deviation from the projected path of the economy now seemed to be in better balance than earlier, the consequences of a substantial shortfall from expectations would be much more severe than the effects of a comparable overshoot. Other members did not rule out the possible need for an easing move in the period ahead, but they believed that the more balanced risks that were now perceived to surround the economic outlook warranted a symmetric directive. Some observed that such a directive did not preclude an easing action that might be triggered by economic or financial developments, including the behavior of the monetary aggregates, in the weeks ahead. Moreover, in the view of some of these members, a directive that remained tilted toward ease under prevailing circumstances could be misread by domestic and international observers as evidence of greater concern about the economic outlook than many members currently felt, or as an indication of a bias on the part of the Committee toward bolstering the real economy rather than securing further progress toward price stability.

In the course of the discussion, members expressed varying degrees of concern about the behavior of the monetary aggregates. According to the most recently available data for March, M2 apparently leveled off or declined slightly and M3 contracted somewhat. Moreover, the weekly pattern toward the end of March suggested the possibility of sluggish growth on average in April. While this development needed to be assessed in the context of emerging information on the economy and financial markets, it was suggested that a persisting shortfall in the growth of M2 and M3 could signal that monetary policy was not positioned to support a satisfactory expansion. For the year through March, growth of M2 had fallen somewhat short of the midpoint of the Committee's range for 1992, and in the view of some members growth near the midpoint or somewhat higher in the range might be more consistent with a desirable economic performance for the year. On the other hand, expansion of narrow money and reserves had been quite robust for some time. In the view of at least one member, the possibility could not be ruled out that this rapid growth could be signaling an overly accommodative monetary policy which, if continued, could boost inflation pressures at some point. Conclusions could not be drawn on the basis of short-term movements in the narrow or broad monetary aggregates, and in any event the implications for the economy of specific monetary growth rates were clouded by a variety of developments that the members had discussed at length at the February meeting. Nonetheless, against the background of relatively sluggish growth in the broader aggregates for an extended period, many members agreed that the ongoing performance of those aggregates should be monitored closely. Indeed, some observed that concerns about the behavior of the broader aggregates, rather than the currently available information on economic activity, persuaded them that a directive that was tilted toward ease was preferable to a symmetrical directive at this time.

At this meeting, the Committee reviewed its practices with regard to the maturity composition of its portfolio of Treasury obligations. The overall approach in recent years had been to meet the long-term need for growth in the System's portfolio through purchases in all maturity sectors of the market for Treasury obligations, with a major emphasis on ensuring substantial liquidity in the System's portfolio. With regard to the Treasury's quarterly financings, the Manager had followed the practice over the past several years of exchanging the bulk of the maturing securities held in the System account into the shortest issue offered by the Treasury, while placing relatively small amounts in the longer-term Treasury offerings. This approach had replaced the earlier practice of rolling over maturing System holdings into the refinancing issues in roughly proportionate amounts to the size of those issues being offered to the public. The System's participation in Treasury financings had contributed importantly to the reduction in the average maturity of the System portfolio in recent years; however, given Treasury techniques with regard to accommodating System rollovers, the System's actions did not have any effect on the amounts or the maturity composition of the securities being acquired by the public. The members generally agreed that current practices for managing the composition of the System's portfolio remained appropriate. Rollovers in Treasury financings would continue to be tilted toward the shorter-maturity offerings, and net additions to System holdings would be made in all maturity areas, taking account of the progress already made in enhancing the liquidity of the System's portfolio.

At the conclusion of the Committee's discussion, all of the members indicated that they favored a directive that called for maintaining the existing degree of pressure on reserve positions. The members also noted their preference for or acceptance of a directive that included some bias toward easing during the intermeeting period. Accordingly, in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable during the intermeeting period. The reserve conditions contemplated at this meeting were expected to be consistent with growth of M2 and M3 at annual rates of around 3½ percent and 1½ percent respectively over the three-month period from March through June.

At the conclusion of the meeting the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting suggests a strengthening in domestic final spending, although industrial production and overall employment do not appear to have picked up correspondingly. Retail sales registered large gains in January and February, with data on inventories, which are available through January, showing some offsetting decline in that month. Single-family housing starts increased substantially further in January and February. Recent data on orders and shipments of nondefense capital goods indicate an increase in outlays for business equipment, but nonresidential construction has remained in a steep decline. The nominal U.S. merchandise trade deficit narrowed slightly in January and was essentially unchanged from its average rate in the fourth quarter. Industrial production rose considerably in February, partly reflecting an upturn in motor vehicle assemblies, but was little changed on balance over the first two months of the year. Total nonfarm payroll employment rebounded in February from a large decline in January. With the labor force growing appreciably in recent months, the civilian unemployment rate has risen to 7.3 percent. Wage and price increases have continued to trend downward.

Most interest rates have risen appreciably since the Committee meeting on February 4–5. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies increased substantially over the intermeeting period.

Growth of M2 and M3 accelerated in February, but M2 appears to have leveled off and M3 to have declined in March. Much of the growth in the broader aggregates over recent months has been accounted for by a surge in transactions balances.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at its meeting in February established ranges for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent, respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The monitoring range for growth of total domestic nonfinancial debt was set at 4½ to 8½ percent for the year. With regard to M3, the Committee anticipated that the ongoing restructuring of depository institutions would continue to depress the growth of this aggregate relative to spending and total credit. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might or slightly lesser reserve restraint would be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from March through June at annual rates of about 3½ and 1½ percent, respectively.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Jordan, Kelley, LaWare, Lindsey, Melzer, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: None.

Meeting Held on May 19, 1992

1. Domestic Policy Directive

The information reviewed at this meeting was mixed, but it suggested on balance that economic activity was expanding at a moderate pace. Retail spending and homebuying apparently had softened after sharp gains early in the year, but recent data on contracts and orders pointed toward some firming in business capital spending. Industrial production and employment had firmed in recent months. Incoming data on prices and labor costs suggested little change from recent trends.

Total nonfarm payroll employment continued to increase in April, with more than half of the job gains occurring in service industries, notably in health and business services. In addition, employment in retail trade establishments registered a relatively strong rise, the number of manufacturing jobs increased for a third straight month, and state and local governments added more workers. By contrast, construction employment was down slightly in April and had changed little on balance since the beginning of the year. The civilian unemployment rate edged down to 7.2 percent in April, and initial claims for unemployment insurance fell somewhat further.

Industrial production rose appreciably further in April, and in the three months ending with that month, industrial output retraced most of the decline that had occurred between October and January. The April advance reflected in part some further recovery in motor vehicle assemblies as well as another solid gain in the production of industrial equipment, especially office and computing equipment. Output of construction supplies also advanced more rapidly, and the production of consumer goods other than automobiles increased slightly further. Total industrial capacity utilization continued to rise in April but was still well below its pre-recession high.

Retail sales rebounded in April after a sizable decline in March; for the two months combined, retail spending was little changed following strong gains in the first two months of the year. Purchases of nondurable goods, particularly general merchandise items, were down on balance for the March–April period, while spending for durable goods rose further. Single-family housing starts fell considerably for a second month in April. The declines followed sizable increases earlier in the year that appeared to have reflected lower mortgage rates, unusually warm winter weather, and the prospect of a tax credit for first-time homebuyers. Starts in the multi-family sector in April reversed the jump in March. Vacancy rates for multi-family units remained at historically high levels.

Business fixed investment apparently firmed in the first quarter after declining moderately over the preceding several quarters. Shipments of nondefense capital goods rose somewhat further in the first quarter, largely as a result of continued growth in outlays for office and computing equipment. Recent data on orders pointed to a pickup in business spending for a broad range of industrial equipment over coming months. Nonresidential construction activity contracted less rapidly in the first quarter. While outlays for office buildings continued to plummet in response to the substantial overhang of unoccupied space, spending for other commercial buildings declined more slowly, and construction of industrial and public utility structures increased. Recent information on building permits and contracts suggested some further slowing of the decline in nonresidential construction.

Business inventories increased considerably in March after changing little in February. At the retail level, about half of the rise in March was in stocks at automobile dealers. For other retailers, the buildup of stocks reversed most of the drawdowns posted in the preceding two months. Inventory-to-sales ratios rose for most categories of retail stores but remained well below the elevated levels at the end of last year. Manufacturing inventories were essentially unchanged in March from the lower levels that prevailed in January and February. For many industries, stock-to-sales ratios in March were at their lowest levels in more than a decade. By contrast, stocks held by wholesalers increased again in March, and inventory-to-sales ratios were little changed from the relatively high level at the end of last year.

The nominal U.S. merchandise trade deficit declined in February, and its average for January–February was somewhat lower than the average rate in the fourth quarter. Exports for the two-month period were about unchanged from the strong fourth-quarter rate but were considerably higher than a year earlier. Imports in January and February were down from the fourth-quarter rate; most of the decline was associated with a fall in prices of oil imports. The available data on first-quarter economic activity in the major foreign industrial countries were mixed; signs of strengthening activity in Europe were offset by indications of continued weakness in Japan and Canada.

Producer prices of finished goods rose at a slightly faster pace in March and April, as energy prices partially retraced earlier declines. Excluding food and energy, producer prices increased over the March–April period at about the subdued average monthly rate seen over the twelve months ending in April. At the consumer level, prices jumped in March and rose more moderately in April. Prices of nonfood, non-energy consumer items increased a little more rapidly on balance in March and April than over the twelve-month period ending in April. Total hourly compensation for private industry workers advanced in the first quarter at a rate close to that recorded during the second half of 1991.

At its meeting on March 31, 1992, the Committee adopted a directive that called for maintaining the existing degree of pressure on reserve positions and that included a bias toward possible easing during the intermeeting period. Accordingly, the directive indicated that in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable in the intermeeting period. The reserve conditions contemplated under this directive were expected to be consistent with growth of M2 and M3 over the period from March through June at annual rates of about 3½ and 1½ percent respectively.

Open market operations during the intermeeting period initially were directed toward maintaining the existing degree of pressure on reserve positions. Prior to mid-April, however, operations were adjusted to implement some easing in the degree of reserve pressure. This action was taken in light of the significant weakness in the broad monetary aggregates and of indications that the economic expansion was not as strong as its pace early in the year and that underlying inflation would continue to trend lower. The management of reserves was complicated to some extent during this period by the uncertainties associated with the mid-April tax date. A reduction in reserve requirements on transactions deposits from 12 percent to 10 percent implemented on April 2 had only minor effects on demands for excess reserves and on volatility in money markets. Expected levels of adjustment plus seasonal borrowing were raised in the intermeeting period in anticipation of a slight rise in seasonal borrowing. Over the three complete reserve maintenance periods during the intermeeting interval, adjustment plus seasonal borrowing averaged a little more than $100 million. The federal funds rate remained around 4 percent early in the intermeeting period but averaged a little below 3¾ percent in the weeks after the easing action.

Most other short-term interest rates fell more than the federal funds rate. Many market participants, interpreting incoming data as suggesting that the economic expansion would remain subdued and that the weakness in the broad monetary aggregates would persist, concluded that some further easing in policy was likely in the near term. Bond yields also fell, but generally by less than short-term rates, and they remained above the lows reached around the turn of the year. Changes in broad indexes of stock prices were mixed over the intermeeting period.

Questions about the prospects for the economic recovery in the United States and the related outlook for interest rates affected the value of the dollar in foreign exchange markets. On a trade-weighted basis in terms of the other G-10 currencies, the dollar remained within a fairly narrow range until late in the period, when growing market expectations of a near-term easing in U.S. monetary policy exerted downward pressure on its value.

M2 and M3 contracted in March and April. The performance of these aggregates was considerably weaker than the Committee's expectations at the time of the March meeting. Expansion in transactions balances, which had accounted for much of the growth in the broader aggregates over previous months, slowed markedly. Some of the slowdown perhaps reflected a reduced need for liquid balances to make personal tax payments, which were unusually weak in April. In addition, some retail time deposit funds evidently were shifted into the capital markets in response to the low offering rates on these deposits relative to market rates. Through April, expansion of M2 was slightly above and that of M3 was slightly below the lower ends of the ranges established by the Committee for the year.

The staff projection prepared for this meeting pointed to a continuing recovery in economic activity. In the near term, expansion in consumer spending was expected to be considerably below the rapid first-quarter pace, and growth in spending on residential construction was likely to moderate in response to the earlier backup in mortgage interest rates. On the other hand, stronger orders for nondefense capital goods portended some pickup in business fixed investment despite the continuing drag exerted by the persisting, though abating, weakness in nonresidential construction; in addition, inventory liquidation was likely to slow from the first-quarter pace. Over time, some easing of restraints on credit supplies and the progress achieved in restructuring business and household balance sheets would help set the stage for sustained, moderate growth in spending. The projection did not incorporate any major new fiscal initiatives at the federal level. The considerable margin of slack in resource utilization, though decreasing, was projected to be associated with appreciable further slowing in the underlying rate of inflation.

In the Committee's discussion, members referred to the indications that the rate of economic growth had slowed since earlier in the year, but they interpreted the recent statistical and anecdotal information as consistent on balance with a continuing and relatively broad-based expansion in overall business activity. Although some sectors of the economy remained troubled, reports from many parts of the country suggested that economic activity was expanding and that business executives were becoming more confident that a sustained recovery was under way. Several members noted, however, that in the absence of strong momentum in any sector of the economy, the advance was proceeding at a pace that was well below the typical rate of growth in the early phases of past cyclical upswings. In such circumstances, a faltering in the recovery, such as had occurred in 1991, could not be ruled out, especially given the financial difficulties still being experienced by many business firms, consumers, and lending institutions that in turn appeared to be reflected in the continued weakness in broad measures of money and credit. A differing view gave more weight to the recently abnormal behavior of the velocities of broad money and debt and the possibility that, once the recovery was more firmly established, some sectors of the economy and thus the economy more generally might generate more strength than was currently projected. With regard to the outlook for inflation, the recent performance of some key indicators of labor compensation and prices was somewhat disappointing. However, members continued to view further progress as likely, given the persisting though diminishing slack that was projected in labor and other production resources.

Many of the members commented that the various financial constraints on the expansion were diminishing and that a sounder financial foundation to support sustained economic recovery was being established. Considerable restructuring of balance sheets by both business firms and households had been accomplished; these developments together with lower interest rates had reduced interest burdens and had increased the capacity to borrow and spend. In the financial sector, banking institutions were continuing to work down problem credits in their loan portfolios and, in the context of growing profits associated with relatively wide interest margins on loans, were rebuilding their capital positions. The access of lending institutions to the capital markets had improved, and there were increasing indications, not yet reflected in the loan data, that banks were seeking lending opportunities more actively in many parts of the country and that loan demand from small and medium-size businesses was tending to revive. Thus, while banking institutions remained cautious lenders and their loan rates were on the high side in relation to market rates, members saw some signs that a more accommodating climate was emerging in loan markets.

In their reports on business conditions in various parts of the country, members noted that at least modest growth seemed to be occurring in most regions, while with some exceptions activity in other areas appeared to be stabilizing after declining earlier. Business confidence seemed to be improving, indeed appreciably so in some areas, and was described as more optimistic even in sections of the country that did not appear to be participating thus far in the economic recovery. Nonetheless, business concerns about the sustainability of the expansion were being reflected in cautious hiring and investment decisions. On balance, current business attitudes pointed to continuing economic expansion, though many business executives did not anticipate a robust recovery and the overall state of confidence appeared to be somewhat fragile.

Turning to individual sectors of the economy, members observed that the strong growth in consumer spending in the early months of the year, apparently outpacing the expansion in income, seemed to have slowed more recently. Nonetheless, improving consumer sentiment against the background of reduced debt burdens and strengthening employment opportunities pointed to further gains in consumer spending. Over time, such spending was likely to be associated more closely with developments in labor markets and the related growth in disposable incomes, though the demand for consumer durables also would respond to changing conditions in the housing markets. In those markets, anecdotal reports from around the country tended to confirm recent data indicating some slowing of activity from the pace at the start of the year, but conditions varied substantially across the nation. Housing activity had tended to display considerable sensitivity to changes in mortgage rates, and the recent declines in the latter along with gains in consumer confidence were seen as likely to encourage some pickup in housing demand and residential construction. Nonresidential construction, especially that of office buildings and hotels, was expected to remain weak for an extended period in many areas as excess capacity was absorbed. On the positive side, rates of occupancy and prices of existing buildings appeared to be approaching bottom or stabilizing in many areas, thereby facilitating sales of repossessed property on the books of financial institutions. Other nonresidential construction activity was mixed; oil and gas drilling was still quite weak, but the construction of manufacturing and wholesale space was displaying some strength in various parts of the country. Gains in final demand, if sustained, were expected to foster appreciable further increases in the production of business equipment.

Government purchases of goods and services continued to be constrained by budgetary problems, including the severe financial difficulties of many state and local governments, and with defense spending projected to decline substantially, the government sector appeared likely to remain a negative influence on economic activity over the next several quarters. With regard to the outlook for exports, members referred to reports of relatively strong sales abroad by firms in some parts of the country. More generally, prospective growth in exports to some key industrial nations could be relatively sluggish if recent economic trends in those nations were to persist, though exports to a number of developing countries appeared to be rising fairly briskly. At the same time, the recovery in the domestic economy was likely to foster relatively rapid growth in imports. On the whole, net exports were expected to make little or no contribution to the expansion in domestic economic activity.

Despite the somewhat disappointing inflation news in recent months, the members generally viewed a slow downtrend in the rate of inflation as a plausible outcome for the year ahead. Reports from various parts of the country emphasized the highly competitive markets for many producer goods and the inability of many sellers to increase profit margins or to pass on rising costs through higher prices. Commodity prices had tended to fluctuate in a narrow range and appeared consistent with progress toward price stability. Consumer resistance to rising prices was described as strong. In the context of the relatively limited pressures on production resources associated with the members' outlook for economic activity and an appropriate monetary policy, the slow process of reducing inflation was believed likely to continue for some time.

In the Committee's discussion of policy for the intermeeting period ahead, all of the members endorsed a proposal to maintain an unchanged degree of pressure in reserve markets. The members agreed that policy seemed to be appropriately positioned at this point to accommodate sustained economic expansion while also encouraging progress toward price stability.

In the course of the Committee's discussion, members devoted considerable attention to the behavior of the monetary aggregates. They expressed varying degrees of concern about the slow growth of M2 and M3 in 1992, including declines in March and April. Some emphasized that the lagging growth of those aggregates this year was occurring after relatively limited expansion over the previous year or so. Although the growth rates and velocities of the broader aggregates were subject to considerable short-run variations and had to be evaluated in the context of surrounding economic and financial circumstances, average growth over longer periods of time had been quite subdued. Plausible explanations, relating importantly to temporary factors such as the unexpectedly weak build-up of balances associated with the April tax date, permitted at least some discounting of the recent weakness of the broader aggregates, and growth of both M2 and M3 according to a staff analysis was likely to resume at a modest pace over the balance of the second quarter. However, in the opinion of a number of members, continuing weakness in these aggregates could be indicative of an increase in the downside risks to the expansion and would thus be a matter of growing concern.

Other members tended to discount to an extent the sluggish behavior of the broader aggregates. In this view, a variety of developments that were reflected in the channeling of credit away from depository institutions seemed to have altered previous relationships between M2 and M3 and measures of spending and income. To an important degree, current spending was being financed internally or, especially in the case of business firms, by raising funds in the capital markets. Moreover, against the background of weak loan demand and relatively low deposit offering rates and an unusually steep yield curve, many depositors were shifting funds from M2 into higher-yielding, longer-term market assets. In these circumstances, satisfactory economic expansion would tend to be consistent with weaker growth and a higher velocity of M2 than would be suggested by historical relationships. Some members viewed the strength of M1 and reserves as indicative of a quite accommodative monetary policy in recent quarters, and they felt that continued rapid expansion in these measures could raise questions about the consistency of current monetary policy with progress toward price stability.

The members expressed differing preferences with regard to possible adjustments to the degree of reserve pressure during the intermeeting period, but all indicated that they could accept a symmetric directive. Some preferred such a directive because it would tend to underscore their view that the risks to the expansion and the possible need to adjust policy were now fairly evenly balanced in either direction. In light of the information on the economy reviewed at this meeting, they felt that current monetary policy was likely to remain properly positioned to accommodate the Committee's objectives for some time and that any adjustment to policy should be approached with considerable caution. In the context of persisting concerns about inflation, an easing in reserve conditions and lower short-term interest rates might well fail at this time to induce lower interest rates in long-term debt markets, though circumstances might change. In any event, the Committee should keep its options open and changing circumstances might warrant a Committee consultation during the weeks ahead.

A number of members expressed a preference for continuing to bias the directive toward possible easing during the intermeeting period. In this view, the risks to the expansion appeared to be tilted at least marginally to the downside, and while a steady policy course might well prove to be appropriate until the next meeting, these members believed it would be desirable for policy to be adjusted fairly promptly should the incoming evidence suggest a faltering expansion, especially if money growth were still lagging. Other members preferred a bias toward possible firming during the intermeeting period. They believed that a relatively stimulative monetary policy was in place and that the next move in policy might well need to be to the tightening side if, in the context of a strengthening economy, the Committee was to continue to pursue its long-run objectives of sustainable economic growth and progress toward price stability.

At the conclusion of the Committee's discussion, all of the members indicated that they favored a directive that called for maintaining the existing degree of pressure on reserve positions. The members also noted that they preferred or could accept a directive that did not include a presumption about the likely direction of any adjustments to policy during the intermeeting period. Accordingly, in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater or slightly lesser reserve restraint might be acceptable during the intermeeting period. The reserve conditions contemplated at this meeting were expected to be consistent with growth of M2 and M3 at annual rates of around 2½ percent and 1½ percent respectively over the two-month period from April through June.

At the conclusion of the meeting the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting suggests on balance that economic activity is expanding at a moderate pace. Total nonfarm payroll employment increased somewhat in April, and the civilian unemployment rate edged down to 7.2 percent. Industrial production rose appreciably further in April partly reflecting some further recovery in motor vehicle assemblies. A rebound in retail sales in April about offset the decline in March. Single-family housing starts fell considerably for a second month in April. Recent data on orders and shipments of nondefense capital goods indicate appreciable increases in outlays for business equipment, and building contracts point to some slowing of the decline in nonresidential construction. The nominal U.S. merchandise trade deficit in January–February was somewhat below its average rate in the fourth quarter. Incoming data on prices and labor costs suggest little change from recent trends.

Most interest rates have fallen since the Committee meeting on March 31. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies declined on balance over the intermeeting period.

M2 and M3 contracted in March and April; and expansion in transactions balances, which had accounted for much of the growth in the broader aggregates over previous months, slowed markedly. Through April, expansion of M2 was slightly above and that of M3 was slightly below the lower ends of the ranges established by the Committee for the year.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at its meeting in February established ranges for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent, respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The monitoring range for growth of total domestic nonfinancial debt was set at 4½ to 8½ percent for the year. With regard to M3, the Committee anticipated that the ongoing restructuring of depository institutions would continue to depress the growth of this aggregate relative to spending and total credit. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint or slightly lesser reserve restraint might be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from April through June at annual rates of about 2½ and 1½ percent, respectively.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Jordan, Melzer, Mullins, Kelley, LaWare, and Lindsey, Ms. Phillips, and Mr. Syron. Votes against this action: None.

2. Authorization for Domestic Open Market Operations

The Committee approved a temporary increase of $2 billion, to a level of $10 billion, in the limit on changes between Committee meetings in System Account holdings of U.S. government and federal agency securities. The increase amended paragraph 1(a) of the Authorization for Domestic Open Market Operations and was effective for the intermeeting period ending with the close of business on July 1, 1992.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Jordan, Melzer, Mullins, Kelley, LaWare, and Lindsey, Ms. Phillips, and Mr. Syron. Votes against this action: None.

The Manager for Domestic Operations advised the Committee that the current leeway of $8 billion for changes in System Account holdings might not suffice to meet the potentially large need to add reserves over the intermeeting period to accommodate a seasonal bulge in currency in circulation, an increase in required reserves, and other factors that might call for substantial reserve additions.

Meeting Held on June 30–July 1, 1992

The information reviewed at this meeting suggested that economic activity was expanding at a moderate pace. Employment and industrial output had continued to rise, but a sizable increase in the labor force had lifted the unemployment rate to a cyclical high. Increased sales and production of motor vehicles were providing a boost to the economy, as was higher spending for capital equipment, especially computers. However, non-auto retail sales and homebuying had slowed since earlier in the year, and the latest data indicated some widening of the merchandise trade deficit. Incoming data on retail prices and labor costs suggested that inflation was slowing.

Total nonfarm payroll employment increased for a fourth straight month in May, and aggregate hours worked by production or nonsupervisory workers exceeded the average for the first quarter. The services industry recorded further sizable job gains in May, while employment in retail trade fell considerably and had changed little on balance thus far this year. Hiring was off slightly in manufacturing, but further increases in overtime hours elevated the factory workweek to a little above its average level for the first half of 1990. The civilian unemployment rate rose sharply in May, to 7.5 percent, reflecting a surge in the number of job seekers. Substantial increases in the labor force since late last year had returned the labor-force participation rate to its average level for the first half of 1990.

Industrial production rose appreciably further in May, partly reflecting continued recovery in motor vehicle assemblies. Also contributing to the rise were large increases in the production of other consumer durables, notably household appliances and furniture, and of business equipment. The recent gains in production had raised the utilization of total industrial capacity considerably, but the average operating rate remained well below its July 1990 peak.

After a surge early in the year, growth in real personal consumption expenditures had slowed despite a strengthening in the demand for motor vehicles. In April and May, spending for goods other than motor vehicles was slightly below the average level for the first quarter, and outlays for services increased only a little. Purchases of new single-family homes declined in May for a fourth straight month. Starts of single-family housing units rebounded in May to a level close to the first-quarter pace, while multifamily housing starts remained depressed in reflection of historically high vacancy rates for such housing.

Shipments of nondefense capital goods other than aircraft over April and May were somewhat above the first-quarter level, boosted mainly by further increases for office and computing equipment. Business purchases of motor vehicles also were stronger. Recent data on orders pointed to a further pickup in business outlays for durable equipment over coming months. Outlays for nonresidential structures continued to trend lower in May, but incoming information on contracts for new construction suggested that nonresidential building activity would decline more slowly in the months ahead. Although construction of office buildings continued to plummet in response to the substantial overhang of vacant office space, spending for other nonresidential structures had firmed since the fourth quarter.

Business inventories rose slightly further in April. Stocks increased relatively sharply at the retail level, but about half the buildup was at automobile dealerships, where the rise in inventories appeared to be about in line with a recent pickup in sales of new vehicles. In manufacturing, inventories continued to decline; with factory shipments rising, the ratio of stocks to shipments was at its lowest level in more than a decade. At wholesale establishments, inventories were trimmed substantially further in April. However, inventory–sales ratios remained near the high end of the range that had prevailed over the past several years.

The nominal U.S. merchandise trade deficit widened in April and was substantially above its average rate for the first quarter. The value of exports declined, largely because of a decline in exports of aircraft. The value of imports increased further in April; a rise in imports of capital goods more than offset a small decline in imports of consumer goods. The available data on economic activity in the major foreign industrial countries in the second quarter were mixed. In Germany and Japan, growth during the first quarter had been boosted by transitory influences that appeared to be unwinding in the second quarter. By contrast, a moderate recovery in economic activity was continuing in Canada, and there were some indications that economic recovery was getting under way in the United Kingdom.

Producer prices of finished goods rose more rapidly in May; sizable increases in the prices of energy and other goods outweighed a further decline in food prices. Apart from anomalous jumps in the prices of a few items, however, increases in prices of nonfood, nonenergy finished goods generally remained modest. Consumer prices posted a small advance in May, despite a relatively large rise in energy costs. Excluding food and energy items, consumer prices increased more slowly in the first five months of this year than in 1991. Average hourly earnings for production or nonsupervisory workers were little changed over April and May and also had risen more slowly thus far this year than in 1991.

At its meeting on May 19, the Committee adopted a directive that called for maintaining the existing degree of pressure on reserve positions and that did not include a presumption about the likely direction of any adjustments to policy during the intermeeting period. Accordingly, the directive indicated that in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater or slightly lesser reserve restraint might be acceptable during the intermeeting period. The reserve conditions contemplated under this directive were expected to be consistent with growth of M2 and M3 at annual rates of about 2½ and 1½ percent respectively over the two-month period from April through June.

Open market operations during the intermeeting period were directed toward maintaining the existing degree of pressure on reserve positions. During the period, several technical increases were made to expected levels of adjustment plus seasonal borrowing to reflect the rising demands for seasonal credit. Actual levels of borrowing averaged about $165 million over the three reserve maintenance periods completed during the intermeeting interval. The federal funds rate remained close to 3¾ percent.

Most other interest rates changed little on balance over the intermeeting period. Rates moved higher in the days following the May meeting as widespread market expectations of a monetary easing action were not realized. Later in the period, however, interest rates fell, especially at intermediate maturities, as markets interpreted incoming data on the economy and the monetary aggregates as indicating a sluggish recovery. Broad indexes of stock prices declined over the period in response to reductions in forecasts of corporate earnings.

In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies declined further over the intermeeting period. The dollar rose initially in response to data pointing to a somewhat stronger economic recovery in the United States but subsequently more than retraced its gains as less positive economic data, including a larger-than-expected trade deficit, were reported.

M2 and M3 changed little in May and appeared to have contracted in June; both retail and large-denomination time deposits continued to run off rapidly. Depository institutions, facing weak loan demand and intent on further bolstering capital positions, had reduced rates on time deposits fairly aggressively earlier in the year, and as a result these components of M2 and M3 had become less attractive relative to alternative investments or debt repayment. In addition, M1 was unusually weak in June. Through June, expansion of the two broad aggregates was somewhat below the lower ends of the ranges established by the Committee for the year. Growth of nonfinancial debt was estimated to be at the lower end of the Committee's monitoring range. Borrowing had been concentrated in the capital markets, with beneficial effects in reducing debt and debt-servicing burdens.

The staff projection prepared for this meeting pointed to a modest pickup in economic growth over the second half of the year and to some further acceleration in 1993. The forecast took into account the lagged effects on aggregate demand of earlier declines in interest rates and the progress that had been made by households and businesses in strengthening their balance sheets. Nonetheless, financial strains were expected to continue to prompt the diversion of some cash flows from business and consumer spending, though the magnitude of such adjustments was projected to lessen over time. Partly as a consequence, moderate growth well below that experienced during typical cyclical upswings in the past was projected in consumer spending and in business investment in durable equipment. Economic expansion also would be restrained by further, though diminishing, declines in business spending on nonresidential structures before a projected upturn in such spending began to materialize in the second half of next year. Moreover, in the government sector, federal purchases of goods and services were forecast to decrease over the projection horizon, largely reflecting cutbacks in defense spending. At the state and local government levels, continuing budget problems were expected to result in a small decline in real purchases during the quarters immediately ahead and in only modest growth later. A persisting though decreasing margin of slack in resource utilization was expected to be associated with further slowing in wage and price inflation.

In the Committee's discussion of economic and financial developments and the outlook for the economy, the members agreed that a sustained expansion at a moderate pace remained the most reasonable expectation and that such an expansion was likely to be associated with further easing of inflation. They noted that considerable progress had been made in correcting major structural imbalances and financial problems in various sectors of the economy and that business and consumer confidence had improved appreciably since the turn of the year. However, the most recent information suggested some weakening in the expansion, and a number of members expressed concern about the apparent absence of cumulating or self-reinforcing improvement in overall economic activity. Sluggish growth of jobs and income, ongoing efforts to strengthen balance sheets, and in the view of a number of members the weakness in broad measures of money and credit suggested that the risks to the economy were more heavily weighted to the downside. Others felt that the expansion was now more firmly entrenched and that the risks were more evenly balanced; some of these members noted, however, that given the likely restrained pace of the expansion, a significant shortfall from their current projections could have more worrisome effects than the limited inflationary pressures that might be fostered by a somewhat stronger-than-projected economy. With regard to the outlook for inflation, the members were encouraged by indications of moderating price and labor cost pressures. Most believed that additional progress toward price stability was likely over the next several quarters in the context of some persisting slack in labor and other production resources and after an extended period of slow growth in key measures of money.

In keeping with the practice at meetings when the Committee sets its long-run ranges for the money and debt aggregates, the members of the Committee and the Federal Reserve Bank presidents not currently serving as members provided specific projections of the growth in nominal and real GDP, the rate of unemployment, and the rate of inflation for the years 1992 and 1993. These projections took account of the monetary growth ranges that the Committee reaffirmed at this meeting for 1992 and established on a tentative basis for 1993; these ranges were expected to be consistent with the Committee's goals of promoting a sustained expansion in the economy and continued progress toward price stability. The projections generally portrayed an economy performing in line with these objectives—that is, with expansion at a moderate pace over the next one and one-half years and inflation slowing gradually further. Forecasts of nominal GDP converged on growth ranges of 5¼ to 6 percent for 1992 as a whole and 5½ to 6¼ percent for 1993. With regard to the rate of expansion in real GDP, the projections had a central tendency of 2¼ to 2¾ percent for 1992 and of 2¾ to 3 percent for 1993, implying a gradual acceleration from the pace currently estimated for the first half of this year. The projected strengthening of the economy was associated with some decline in the rate of civilian unemployment to a consensus range of 6½ to 7 percent by the fourth quarter of 1993. Given the moderate expansion of the economy and the still relatively elevated level of the unemployment rate, the rate of inflation, as measured by the consumer price index, was projected to move somewhat lower; the central tendency of the range expected for 1993 was 2¾ to 3¼ percent.

Members observed that developments relating to the financial condition of households and businesses were likely to continue to have an important influence on economic activity over the quarters ahead. Widespread efforts to strengthen balance sheets along with conservative lending policies at financial intermediaries had exerted a significantly retarding effect on economic activity by diverting cash flows from consumer and investment expenditures or limiting the availability of financing for current spending. However, while the process of adjusting balance sheets was still incomplete and was still restraining business and consumer spending, the combination of greatly reduced interest rates and strengthened balance sheets pointed to subsiding constraints on expenditures from financial factors. At the same time, lending institutions now appeared to be in a better position to accommodate borrowers. Indeed, anecdotal reports from several parts of the country indicated that many banking institutions were intensifying their efforts to make loans, though loan demand remained quite limited. Members also observed that corporate cash flows and profits were much improved.

In their review of economic conditions and business and consumer attitudes in different regions, members reported that gradual expansion characterized most parts of the nation, though they cited some significant exceptions and also noted that on the whole recent indicators pointed to less strength than early in the year. Business and consumer sentiment, while considerably improved since late last year, nonetheless remained quite cautious and seemed vulnerable to adverse developments. Consumers were still very concerned about employment opportunities, while business executives were reluctant to make investment commitments or to build inventories in the absence of firmer indications of a significant pickup in demand.

With regard to developments in major sectors of the economy, members generally viewed some pickup in consumer spending from its recently sluggish pace as a likely development that in turn would provide ongoing support to the expansion. An essential element in sustaining consumer expenditures, and thus the economy more generally, would be the growth in job opportunities and personal incomes. While heavy debt-service burdens and reduced interest incomes, among other factors, continued to curb the ability or willingness of many consumers to increase their spending, some tentative indications of a firming trend in such spending could be drawn from the signs of reviving consumer confidence and anecdotal reports suggesting that consumer spending was growing at least modestly in many areas. In particular, demands for motor vehicles had strengthened, and the related step-up in the production of automotive products had accounted for much of the growth in industrial production over recent months. With regard to the outlook for housing, residential construction had weakened in many parts of the country, though it was holding up well in some areas. The backup in mortgage rates earlier in the year had reinforced the more general cautionary factors that had tended to inhibit overall spending. However, mortgage rates had fallen substantially over the spring, and the members expected housing activity to pick up somewhat over the quarters ahead.

Despite still cautious business attitudes, moderate growth in overall business fixed investment was anticipated over the forecast period. Spending could be buoyed by demands for business equipment, much of which probably would be related to efforts to modernize production facilities for competitive reasons. Rising rates of capacity utilization also could be expected to spur investment demand as time went on. The outlook for nonresidential construction was more negative. Office construction appeared likely to remain severely depressed for an extended period as excess capacity was absorbed in many parts of the country. On the more positive side, anecdotal impressions from several cities suggested that prices and lease terms of office and other commercial structures were tending to stabilize, though the volume of actual transactions remained quite limited.

The government and foreign trade sectors also were not seen as likely to contribute significantly to the expansion. The widespread financial problems of state and local governments pointed to quite limited growth in spending, even though examples of sizable expenditure programs, such as for highway construction in some areas, could be cited. At the federal level, defense spending was on a clear downtrend, and the persistence of large federal deficits argued against sizable new initiatives for nondefense spending. With regard to the external sector, a number of members expressed the view that the outlook for net exports had worsened despite the weakening in the foreign exchange value of the dollar in recent months. The growth in exports appeared to be moderating, and it was uncertain at this point to what extent economic expansion abroad might strengthen and thereby produce increased demand for U.S. goods and services. At the same time, domestic expansion in line with the members' forecasts would add to the demand for imports.

Most members anticipated at least a limited decline in the core rate of inflation over the period through the end of next year. In support of this view, some members emphasized the lagged effects of the very restrained growth in money over a long period while others gave more weight to the outlook for continuing if diminishing slack in labor and other production inputs. In addition, business executives reported that strong competition still was making it very difficult to raise prices and that continuing efforts were being made to improve operating efficiencies and hold down costs. At the same time, surveys of price expectations and conversations with business contacts suggested a view, rooted partly in concerns about the prospects for and implications of further large federal deficits, that inflation ultimately would return to the 4 to 5 percent pace of the 1980s. These attitudes tended to underscore the need for a sound fiscal policy that in conjunction with the continued implementation of an anti-inflationary monetary policy would foster a reduction in inflationary expectations and would facilitate the eventual achievement of price stability.

In keeping with the requirements of the Full Employment and Balanced Growth Act of 1978 (the Humphrey–Hawkins Act), the Committee at this meeting reviewed the ranges for growth in the monetary and debt aggregates that it had established in February for 1992 and decided on tentative ranges for growth in those aggregates in 1993. The current ranges for the period from the fourth quarter of 1991 to the fourth quarter of 1992 included expansion of 2½ to 6½ percent for M2 and 1 to 5 percent for M3. The monitoring range for growth of total domestic nonfinancial debt had been set at 4½ to 8½ percent.

In the course of the Committee's discussion, all of the members supported a proposal to retain the ranges established in February for this year. Although the rates of M2 and M3 growth for the year through June were somewhat below the lower ends of the Committee's ranges for both aggregates, this outcome had not been associated with unexpected weakness in nominal spending; the expansion in nominal GDP over the first half of the year currently was estimated to have been toward the upper end of the central tendency of the members' earlier expectations. Instead, velocity had risen appreciably—a highly unusual occurrence following a period of sharp declines in interest rates. Among the developments helping to explain the weakness in money and the rise in velocity were a variety of business and balance sheet pressures that tended to reduce total borrowing and channel credit flows away from depository institutions, thereby lessening the need of those institutions to increase their monetary liabilities. At the same time, business firms and households, in the course of their restructuring activities and deleveraging of their balance sheets, had found that monetary assets had become less attractive relative to a variety of other financial assets or debt repayment.

It appeared that the balance sheet adjustments by depository institutions and their customers that had contributed to velocity increases were well under way. However, the factors that were tending to depress broad money growth in relation to measures of economic and price performance were likely to persist, and the extent and duration of deviations from historic relationships were highly uncertain. In these circumstances, while an argument could be made that a somewhat lower M2 range might more readily encompass the rate of expansion in money needed for a satisfactory economic performance over the balance of the year, the selection of a different range would imply greater certainty about emerging relationships than was warranted. Instead, the current ranges should be maintained, pending further developments and the possible emergence of a more settled outlook for money demand. Some members also commented that lowering the ranges could be misconstrued as an intention to tighten monetary policy at a time when relatively sluggish growth in the economy and weakness in the monetary aggregates argued for a steady policy course or possibly for some easing.

At the conclusion of this discussion, the Committee voted to reaffirm the 1992 ranges of 2½ to 6½ percent and 1 to 5 percent that it had established in February for growth of M2 and M3 respectively; the Committee also decided to retain the range of 4½ to 8½ percent for growth of nonfinancial debt in 1992. The following statement was approved for inclusion in the Committee's domestic policy directive:

> The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee reaffirmed at this meeting the ranges it had established in February for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent, respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The Committee anticipated that developments contributing to unusual velocity increases could persist in the second half of the year. The monitoring range for growth of total domestic nonfinancial debt also was maintained at 4½ to 8½ percent for the year.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Jordan, Kelley, LaWare, Lindsey, Melzer, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: None.

With regard to the ranges for 1993 to be established on a tentative basis at this meeting, a majority of the members endorsed an extension of the current ranges for another year, but some believed that a somewhat lower range for M2 would be preferable. Members who wanted to retain the current ranges acknowledged that a lower M2 range probably would be desirable at some point to be consistent over time with the Committee's objective of achieving and maintaining reasonable price stability. However, current uncertainties with regard to how soon and to what extent various factors tending to inhibit the growth in M2 would dissipate argued for caution in making any change to the range now. A reduction in the M2 range could be considered next February when the Committee meets to set final ranges for money growth for 1993, or the range could be lowered even sooner if new information on the emerging relationship between the monetary aggregates and nominal spending allowed a determination of the appropriate range to be made with more confidence.

Members who preferred a somewhat lower M2 range for 1993 acknowledged that substantial uncertainties with regard to an appropriate rate of M2 growth were likely to persist for some time, but they felt that relatively subdued monetary expansion was likely to be consistent with an adequate degree of liquidity and a satisfactory economic performance next year. Lowering the M2 range at this point would extend the series of gradual reductions in the ranges that had been implemented over the past five years or so and would have the important advantage of affirming the Committee's commitment to price stability, with favorable implications for inflationary expectations and in turn perhaps also for the strength and sustainability of the expansion. A few members favoring this option were also of the view that more weight ought to be placed on M2 as a guide to policy; this would have possible implications for actions to boost M2 growth in 1992 in addition to reducing the range for 1993 to promote long-run disinflation. All of the members agreed that regardless of the particulars of the decisions to be made at this meeting, it was vital for the Committee to reaffirm its commitment to the goal of achieving price stability. This outcome was the key contribution the Federal Reserve could make toward facilitating the highest possible growth of the economy over time; and maintaining the credibility of the System's anti-inflationary effort was the best means available to the Committee to minimize disruptions to the economy as it was moving toward its potential.

At the conclusion of this discussion, the Committee approved provisional ranges for 1993 that were unchanged from those for 1992. The Committee voted to incorporate the following statement regarding the 1993 ranges in its domestic policy directive:

> For 1993, the Committee on a tentative basis set the same ranges as in 1992 for growth of the monetary aggregates and debt, measured from the fourth quarter of 1992 to the fourth quarter of 1993. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Kelley, LaWare, Lindsey, Melzer, Mullins, and Syron. Votes against this action: Mr. Jordan and Ms. Phillips.

Mr. Jordan and Ms. Phillips dissented because they believed that a somewhat lower M2 range for 1993 would be more consistent with a policy of continuing progress toward price stability. They recognized that the substantial uncertainties surrounding the outlook for M2 growth and its velocity next year made it very difficult to determine an appropriate M2 range, but a lower range would be needed eventually to achieve and sustain stable prices. In the interim, it was important for the System and the credibility of its anti-inflationary policy to continue the practice of gradually reducing the M2 range to be consistent with a noninflationary target. They would have coupled the decrease in the range for 1993 with actions to expand bank reserves immediately with the objective of boosting M2 growth to within its range for 1992. Such a combination would make clear that the decrease in the range for M2 growth in 1993 did not represent a monetary "tightening" in the conventional sense, but rather that it was a step toward lasting reductions in inflation.

Turning to policy for the intermeeting period ahead, the members were divided between those who supported an unchanged policy stance and others who preferred to ease. A majority indicated, however, that they could support an unchanged directive that incorporated a bias toward possible easing.

Members who preferred not to change policy at this point believed that the economy was on a moderate growth path and that in any case the forces restraining the expansion were not the result of inadequate liquidity or a restrictive monetary policy. While the outlook was clouded by unusual forces acting on the economy, the available economic information remained consistent with continuing expansion at a pace that offered favorable prospects for a gradual reduction of unemployment and abatement of inflation. The low level of real and nominal short-term interest rates, the decline in the dollar, and the rapid growth of reserves and narrow money along with the expansion of bond mutual funds—which while not in M2 seemed to provide liquidity at least comparable to that of time deposits—suggested that monetary policy had been quite accommodative. Some members who supported this view expressed concern that in the absence of more definitive indications of a softening economy or much greater weakness in the monetary aggregates, any easing at this point would tend to erode the credibility of the Committee's commitment to an anti-inflationary policy. The result might well be to put substantial and disruptive downward pressure on the dollar in foreign exchange markets and to arrest or reverse the tendency for domestic long-term interest rates to decline.

Most of the members who preferred an immediate easing of policy emphasized the risks of a faltering economy in the period ahead, especially given the recent indications of some slowing in the expansion and the already considerable slack in the economy. Their concerns were heightened by the constraining effects of ongoing structural adjustments in the economy, the weakness in various measures of money, and the limited expansion in total credit. A few of these members focused on the desirability of taking relatively prompt action to foster growth in the broad measures of money within the Committee's ranges for the year. Some members observed that under current circumstances an easing action might have a relatively limited effect in stimulating monetary growth over the months ahead, but such a policy move would nonetheless tend to boost spending by reducing the costs of borrowing.

In their discussion, the members took account of a staff analysis that suggested only modest growth in M2 and virtually none in M3 for the third quarter on the assumption of an unchanged degree of reserve pressure. Relatively weak expansion in these broad measures of money did not appear to have the usual implications for the economy, as evidenced by experience over the first half of the year. The prospects were for continuing balance sheet and other adjustments that would tend to curb the demand for money assets relative to spending and income. Many members nonetheless were concerned about the possible persistence of the recent weakness in reserves and the longer-term sluggish behavior of broad money, especially given the relatively subdued pace of the expansion. While monetary measures might well have lost some of their indicator and predictive properties, continued weakness in money might still be a signal that financial conditions were not yet conducive to fostering a sustained pickup in spending.

The varying policy preferences expressed by the members were reflected in differing views with regard to possible adjustments to the degree of reserve pressure in the intermeeting period ahead. All of the members who favored some immediate easing in policy indicated that they could support an unchanged directive that was tilted toward ease, and at least some of these members anticipated that developments over the near term were likely to trigger an adjustment toward easing. Most of the members who favored an unchanged policy stance at this point also indicated that they could accept a bias toward ease in the directive, especially in light of current uncertainties and the potential problems associated with any significant shortfall in the expansion from current expectations. Other members who preferred a steady policy course believed that it would be premature for the Committee to signal any bias toward easing, given the relatively low probability that they assigned to the potential need for such a move, and they believed that a return to an asymmetric directive after the move to symmetry at the May meeting could have unfavorable repercussions on the Committee's credibility.

At the conclusion of the Committee's discussion, all but two of the members indicated that they favored or could accept a directive that called for maintaining the existing degree of pressure on reserve positions and that included a bias toward possible easing during the intermeeting period. Accordingly, in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable during the intermeeting period. The reserve conditions contemplated at this meeting were expected to be consistent with a resumption of growth in M2 and M3 at annual rates of about 2 percent and ½ percent respectively over the three-month period from June through September.

At the conclusion of the meeting the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting continues to suggest that economic activity is expanding at a moderate pace. Total nonfarm payroll employment increased somewhat further in May, but a surge in job seekers led to a sizable rise in the civilian unemployment rate to 7.5 percent. Industrial production rose appreciably further in May, partly reflecting continued recovery in motor vehicle assemblies. Growth in consumer spending has slackened after a sharp advance earlier this year. Although sales of new homes declined in May, single-family housing starts rebounded to a level close to the first-quarter pace. Recent data on orders and shipments of nondefense capital goods indicate appreciable increases in outlays for business equipment, and the trend of building contracts points to some slowing of the decline in nonresidential construction. The nominal U.S. merchandise trade deficit increased in April and was substantially above its average rate in the first quarter. Incoming data on retail prices and labor costs suggest that inflation is slowing.

Most interest rates have changed little since the Committee meeting on May 19. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies declined further over the intermeeting period.

M2 and M3 changed little in May and appear to have contracted in June; both retail and large-denomination time deposits continued to run off rapidly. Through June, expansion of the two aggregates was somewhat below the lower ends of the ranges established by the Committee for the year.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee reaffirmed at this meeting the ranges it had established in February for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The Committee anticipated that developments contributing to unusual velocity increases could persist in the second half of the year. The monitoring range for growth of total domestic nonfinancial debt also was maintained at 4½ to 8½ percent for the year. For 1993, the Committee on a tentative basis set the same ranges as in 1992 for growth of the monetary aggregates and debt, measured from the fourth quarter of 1992 to the fourth quarter of 1993. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might or slightly lesser reserve restraint would be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from June through September at annual rates of about 2 and ½ percent, respectively.

Votes for short-run policy: Messrs. Greenspan, Corrigan, Angell, Hoenig, Jordan, Kelley, Lindsey, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: Messrs. LaWare and Melzer.

Messrs. LaWare and Melzer dissented because they judged an asymmetric directive, with a bias toward easing, as being inappropriate at this time. In their view, the current stance of monetary policy was not impeding an expansion consistent with the economy's long-run potential. In addition, a bias toward ease, especially in the context of the Committee's decision at the May meeting to adopt a symmetrical directive, suggested an excessive emphasis on short-term economic developments that might undermine the credibility of the System's long-run policies. They were concerned that such a loss of credibility could have adverse effects on the dollar in foreign exchange markets and on long-term interest rates in domestic markets. Mr. Melzer also believed that, if additional easing were undertaken, a greater policy reversal ultimately would be necessary, making the attainment of sustainable economic growth more difficult in the long run.

Meeting Held on August 18, 1992

The information reviewed at this meeting suggested that economic activity was continuing to expand, although at a subdued pace. Consumer spending had firmed recently; business purchases of capital equipment had risen further; and falling mortgage interest rates, which appeared to have triggered a wave of mortgage refinancings, likely were providing some impetus to housing demand. On the other hand, industrial production and employment had increased little on balance, and a sizable expansion in the labor force had raised the unemployment rate to a cyclical high. Recent data on wages and prices indicated that inflation was slowing.

A rebound in total nonfarm payroll employment in July more than offset a decline in June; however, about half the rise over June and July reflected temporary hiring associated with a federally sponsored summer jobs program that recently had been enacted. Apart from the jobs program, moderate gains in employment were recorded in service industries, while payrolls declined in both manufacturing and construction. The average workweek of production or nonsupervisory workers during the June–July period was at its lowest level of the year, and the civilian unemployment rate averaged 7¾ percent.

Industrial production, which had increased noticeably in earlier months, was about unchanged on balance over June and July, as a rise in July retraced a decline that had occurred in June. Much of the July advance stemmed from a higher level of output in mining and utilities, where special factors had held down production in earlier months. Factory output was unchanged in July after a small decline in June; production of computers and other information processing equipment continued to increase at a rapid rate, but output of motor vehicles and parts fell in both months. Production schedules indicated that domestic assemblies of motor vehicles would increase in August. The utilization of total industrial capacity slipped on balance over June and July but remained a little above its December 1991 level.

Retail sales increased moderately in July after registering little growth in the second quarter. General merchandisers reported sharp gains following a period of sluggish sales since April, and sales rose considerably further at apparel outlets and furniture and appliance stores. Sales of motor vehicles dropped back in July from an elevated June pace. With mortgage rates falling, sales of new single-family homes increased in June after leveling off in May, and reports indicated that mortgage applications for home purchases were rising. Permits issued for the construction of new housing units advanced slightly in July, but starts of such units declined further.

Shipments of nondefense capital goods were up sharply in June, partly reflecting continued increases in shipments of office and computing equipment. Data on new orders pointed to a further substantial rise in business purchases of durable equipment in coming months. Nonresidential construction slackened again in June; weakness in industrial construction added to persisting contractions in outlays for commercial office buildings. Recent information on new contracts continued to suggest that nonresidential construction would decline more slowly over the months ahead.

Business inventories surged in June after declining a little in May. At the retail level, inventories increased by a substantial amount, with the accumulation spread about equally among durable and nondurable goods. The jump in inventories lifted retailers' stocks-to-sales ratios to the upper end of the range of the past year. Wholesale trade inventories also expanded sharply in June, with runups reported for a wide range of goods; sales increased by more, however, and the inventory-to-sales ratio in wholesale trade fell slightly. By contrast, manufacturing stocks edged down in June, and the inventory-to-shipments ratio dropped to its lowest level since the middle of 1979.

The nominal U.S. merchandise trade deficit widened again in May. For April and May combined, the deficit was substantially larger than its average rate in the first quarter. The value of exports fell considerably over the two-month period, with reduced shipments of aircraft accounting for the bulk of the decline. The value of imports rose substantially, as imports of oil rebounded from first-quarter lows and imports of a wide range of other goods also increased. Economic activity in the major foreign industrial countries appeared to have slowed on balance in recent months. Canada, France, and Italy seemed to have experienced modest economic growth, but activity apparently had slowed or declined in Germany and Japan, and there was little indication that a recovery had begun in the United Kingdom.

Producer prices of finished goods increased modestly over June and July. Abstracting from the sometimes volatile food and energy components, prices of other finished goods rose at a significantly slower pace in the twelve months ended in July than in the preceding twelve months. At the consumer level, prices advanced only a little in July after a June increase that had been boosted somewhat by a temporary bulge in energy prices. Food prices, which were unchanged on balance over June and July, continued to hold down overall increases in consumer prices. Excluding food and energy items, consumer price inflation over the year ended in July was markedly lower than in the preceding year. Measures of labor costs also evidenced smaller increases. Hourly compensation of private industry workers rose at a substantially slower pace in the second quarter and in the twelve months ended in June. The deceleration in overall compensation reflected slower growth in both its benefits and its wage and salary components. For production or nonsupervisory workers, average hourly earnings were unchanged in July, and the twelve-month change in this measure was substantially reduced.

At its meeting on June 30–July 1, the Committee adopted a directive that called for maintaining the existing degree of pressure on reserve positions and that included a bias toward possible easing during the intermeeting period. Accordingly, the directive indicated that in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable during the intermeeting period. The contemplated reserve conditions were expected to be consistent with a resumption of growth in M2 and M3 at annual rates of about 2 percent and ½ percent respectively over the three-month period from June through September.

The day after the meeting, the Board of Governors approved a reduction in the discount rate from 3½ to 3 percent, and open market operations were directed at allowing the full amount of the reduction to be reflected in money market rates. These actions were taken in the context of a continuing downtrend in inflation and in light of incoming information that suggested flagging momentum in the economic recovery and persisting softness in credit and money. Later in the intermeeting period, a technical increase was made to expected levels of adjustment plus seasonal borrowing to reflect rising demands for seasonal credit. Adjustment plus seasonal borrowing averaged close to expected levels during the two full reserve maintenance periods completed since the meeting. The federal funds rate, which had been around 3¾ percent prior to the monetary easing action, averaged 3¼ percent subsequently.

Other market interest rates declined considerably in early July, reflecting both the sluggishness portrayed by incoming economic data and the monetary policy easing. Commercial banks also lowered their prime rate from 6½ percent to 6 percent. In subsequent weeks, with a steady flow of new information pointing to a hesitant recovery and more favorable trends in wages and prices, yields on intermediate- and long-term Treasury securities dropped further. Over the intermeeting period, yields on most private securities tended to decline by amounts comparable to those on Treasury instruments, but rates on fixed-rate home mortgages fell by somewhat less, apparently owing in large part to heightened mortgage investor concerns about prepayment risk stemming from a surge in refinancing activity. Broad indexes of stock prices changed little over the period.

In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies declined on balance over the intermeeting period. Early in the period, the dollar fell in response to the more uncertain prospects for near-term growth in the United States and the concurrent easing of U.S. monetary policy. Later, the dollar fell further following an increase in the discount rate in Germany and the issuance of unfavorable U.S. trade data for May. Concerted central-bank intervention in foreign exchange markets was undertaken to brake the decline of the dollar, and the latter tended to stabilize over the remainder of the intermeeting period.

M2 and M3 contracted somewhat further in July, despite a resumption of rapid growth in M1. Both broad monetary aggregates were substantially weaker in July than had been anticipated at the time of the June 30–July 1 meeting. The declines in these aggregates apparently reflected in part the continuing redirection of household holdings of time deposits toward bond and stock funds or the repayment of debt, and in part the reduced funding needs of depository institutions owing to the further rechanneling of credit demands outside the depository sector, a development that was encouraged by the declines in interest rates in long-term debt markets. To some extent, the persisting weakness in money also might have been associated with relatively slow expansion in income since the early months of the year. Through July, both M2 and M3 were appreciably below the lower ends of the Committee's ranges for their growth in 1992.

The staff projection prepared for this meeting pointed to a continuation of subdued economic expansion in the near term followed by a gradual pickup in growth through next year. The forecast took account of the further easing of reserve conditions in early July and the substantial rally that had taken place in the bond markets. Housing construction was expected to pick up in response to the declines in mortgage interest rates; and in the business sector, lower interest rates and improved profits and cash flows were projected to enhance access to sources of finance and to provide the basis for an acceleration in plant and equipment spending as the recovery gained momentum. The slow pace of hiring and the modest expansion of incomes currently were tending to restrain consumer spending, but continued progress by households in restructuring balance sheets and reducing debt-servicing burdens, in conjunction with improving job prospects, were expected to foster growth in consumer spending more in line with the expansion of income. In addition, some stimulus to domestic production was projected to emerge over the forecast horizon from improving export demand as a result of the depreciation of the dollar in recent months and some anticipated strengthening of economic activity in the major foreign industrial countries. In the government sector, continuing cutbacks in defense spending were expected to damp federal expenditures, and budget problems at state and local levels of government to constrain spending and result in tax increases. A persisting though decreasing margin of slack in resource utilization was projected to be associated with further progress toward price stability.

In the Committee's discussion of current and prospective economic developments, members referred to statistical and anecdotal indications that the rate of economic expansion had slowed to a relatively subdued pace since the early months of the year. A number of factors seemed to be restraining the expansion, including efforts by business firms and households to restructure balance sheets, some apparent deterioration in business and consumer sentiment, and sluggish economic growth abroad. Nonetheless, the low levels of real and nominal interest rates in short-term debt markets, recent decreases in intermediate- and long-term interest rates and in the foreign exchange value of the dollar, and the fairly ample liquidity suggested by some measures all were consistent with expectations of some strengthening in business activity in coming quarters. Still, in the view of a number of members, the economic expansion was likely to be on a slightly lower track over the next several quarters than they previously had anticipated. At the same time, many commented that they were encouraged by the accumulating signs of diminishing price and wage inflation, and some observed that faster and more convincing progress was being made toward achieving price stability than they had anticipated earlier.

The members recognized that the outlook for the economy was subject to major uncertainties. A number commented that they could not identify any sector of the economy that seemed primed to provide the impetus needed for a vigorous expansion, but they also acknowledged the difficulty of anticipating the pattern and trajectory of an expansion. With regard to domestic economic developments, the ongoing restructuring activities by financial and nonfinancial firms and by households were continuing to exert a restraining effect on economic activity by diverting cash flows from business investment and consumer expenditures. Considerable progress appeared to have been made toward redressing earlier overexpansion and credit excesses. Over time, cash flows would be redirected toward more normal patterns of spending for goods and services, with stimulative implications for the economy. However, the timing and extent of such a development could not be predicted with any degree of confidence, and in any case the positive effects probably would be felt only gradually and there could be substantial restraint on economic activity for a longer period than was anticipated earlier. On the more positive side, banking institutions had made a good deal of progress in improving their capital positions and strengthening their portfolios, and many of these institutions now were reported to be seeking lending opportunities more actively, though the demand for loans remained unusually depressed.

Turning to developments in key sectors of the economy, members noted that, for now, consumers continued to be affected by a high degree of caution that appeared to stem especially from concerns about job security and job opportunities in an environment of continuing business consolidations, cutbacks by state and local governments, and reductions in defense spending. Against the background of quite limited growth in overall demand, which could be met largely through improvements in productivity and lengthening workweeks, business firms were continuing to hold back in their hiring of new workers. Ongoing efforts by many consumers to reduce their debt burdens and lower interest income from declining rates on deposits and market instruments were contributing to the softness in consumer spending. Against this background, some members indicated that they would not rule out a further rise in the personal saving rate.

Overall spending by business firms on fixed investment and inventories was believed likely to remain relatively moderate, at least in the quarters immediately ahead, in light of the negative business sentiment associated in turn with lagging consumer and government expenditures. While spending for equipment was growing at a fairly brisk pace, spurred by efforts to modernize production facilities for competitive reasons, business construction continued to be deterred by an over-supply of space in commercial structures, especially office buildings, in numerous areas around the country. Cautious inventory investment reflected lackluster demand as well as continuing efforts to manage inventories more tightly in relation to sales.

The outlook for housing activity appeared to have improved somewhat after the recent declines in mortgage rates, though the available data and anecdotal reports on housing market developments were mixed. While mortgage refinancing activity had turned sharply upward across the nation, mortgage loan demand for home purchases was still lagging in many areas.

Given serious budgetary problems at all levels of government, the public sector of the economy was not viewed as likely to provide stimulus to the expansion over the next several quarters. At the federal level, continuing declines in defense spending were expected to be offset only in part by fairly slow growth in other expenditures for goods and services, and some of the most depressed areas of the country were strongly affected by trends in the defense industry. At the state and local government levels, the well-publicized budget problems of California were shared to one degree or another by many other parts of the country; spending curbs seemed likely to hold down any impetus to demand from this sector of the economy, while increases in state and local taxes would tend to restrain business and household demand.

The outlook for the nation's foreign trade balance was difficult to evaluate. The decline in the foreign exchange value of the dollar had favorable implications for net exports over time, but the outlook for relatively restrained expansion in key industrial countries pointed to limited growth in the demand for U.S. exports. At the same time, even moderate economic growth in the U.S. economy could be expected to foster some further increases in imports over coming quarters despite the lower dollar.

With regard to the outlook for inflation, many of the members commented on what they viewed as increasingly persuasive evidence of slower rates of increase in wages and prices. Against the background of relatively restrained growth in economic activity and the related outlook for limited pressures on labor and other productive resources, a number of members indicated that they had lowered their inflation forecasts for the next several quarters. There were widespread reports of strong competitive pressures in most industries and of successful efforts to hold down costs through improvements in productivity. On the negative side, the considerable depreciation of the dollar in recent months and lingering concerns about future price pressures, apparently associated especially with worries about the outlook for the federal budget, could tend to impair progress toward price stability. On balance, however, members saw the prospects for significantly less inflation over the projection horizon as quite promising.

Turning to policy for the intermeeting period, a majority of the members indicated that they favored an unchanged policy, while some expressed a preference for further easing either at this meeting or in the near future. The members who supported a steady policy course recognized that in a period characterized by relatively sluggish economic expansion and a wide variety of risks to the economy, conditions might emerge that would warrant consideration of some further easing. For the time being, however, they preferred a wait-and-see approach in view of the recent easing of reserve conditions and the considerable declines in longer-term interest rates and in the foreign exchange value of the dollar. The Committee should continue to evaluate a variety of indicators for signs that the expansion might be falling short of an acceptable growth path.

Some members commented that an easing of monetary policy under current conditions would incur too great a risk of adversely affecting domestic bond markets. One aspect of that risk was the possibility of a destabilizing decline of the dollar in foreign exchange markets; the potential for such a decline had prompted the recent exchange market intervention in support of the dollar by the United States and several other nations. Any further easing in this view should be implemented only under conditions or circumstances in which the System's commitment to its price stability objective was not likely to be brought into question. An unchanged policy also would give the Committee more room to respond vigorously, if necessary, to a weaker-than-expected economy or to disruptive conditions in financial markets, should they develop at some point.

Members who leaned toward some near-term easing of reserve conditions commented that such a policy move was not likely to foster inflationary pressures under current or prospective economic conditions, given the appreciable margin of unused resources in the economy. At the same time, an easier monetary policy would accelerate balance-sheet restructuring activities and tend to compensate for the adverse effects of such activities on spending. A greater degree of monetary policy easing than had been needed in the past seemed to be required to overcome the depressing effects of the restructuring activities and to cushion an already sluggish expansion against the possibility of some further loss in momentum.

One factor weighing in favor of careful consideration of a more accommodative posture in reserve markets was the behavior of the broad monetary aggregates. The staff analysis prepared for this meeting suggested that some pickup in the growth of M2 and M3, though to a still quite sluggish pace, was likely over the months ahead on the assumption of unchanged conditions in reserve markets. Members observed that the indications of some renewed M2 growth since late July tended to support that conclusion; some also drew encouragement from the sharp upturn in the growth of reserves and M1 in July. The members noted that growth of the broader aggregates in line with current expectations implied expansion for the year at rates somewhat below the lower ends of the Committee's ranges. Such a development would be consistent with the Committee's policy objectives if, as expected, unusual strength in the velocity of M2 and M3 were to persist over the balance of the year. In the circumstances, monetary growth and indicators of velocity behavior would need to be monitored carefully over coming months.

In the Committee's discussion of possible intermeeting adjustments to the degree of reserve pressure, a majority of the members indicated their preference or acceptance of a directive that was biased toward possible easing during the weeks ahead. Members who preferred some easing over the near term indicated that they could support a directive that gave particular weight to developments that might call for an easing move. Some others noted that while they might have preferred a symmetric directive in current circumstances, the proposed bias in the directive was acceptable because an easing of reserve conditions was more likely than a tightening in the intermeeting period. Moreover, a return to a symmetric directive might well be misread as a change in policy that the Committee did not intend at this point. Two members expressed a strong preference for a symmetric directive because they were persuaded that monetary policy should not be eased except in response to compelling new evidence that current policy was impeding an expansion of the economy in line with its long-run potential. They noted that a symmetric directive would not rule out a policy change, in either direction, during the intermeeting period if such a change appeared to be warranted by the incoming economic or financial information.

At the conclusion of the Committee's discussion, all but two of the members indicated that they favored or could accept a directive that called for maintaining the existing degree of pressure on reserve positions and that included a bias toward possible easing during the intermeeting period. Accordingly, in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable during the intermeeting period. The reserve conditions contemplated at this meeting were expected to be consistent with growth in M2 and M3 at annual rates of about 2 percent and ½ percent respectively over the six-month period from June through December.

At the conclusion of the meeting, the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting suggests that economic activity is continuing to expand at a subdued pace. Total nonfarm payroll employment rebounded in July after declining in June, and the civilian unemployment rate edged down to 7.7 percent. Manufacturing output was unchanged in July, but overall industrial production was boosted by a higher level of mining and utility output. Retail sales increased moderately in July. Permits issued for the construction of new housing units rose slightly in July, but housing starts fell. Recent data on orders and shipments of nondefense capital goods indicate further increases in outlays for business equipment, while nonresidential construction has remained soft. The nominal U.S. merchandise trade deficit in April–May was substantially above its average rate in the first quarter. Incoming data on wages and prices suggest that inflation is slowing.

Interest rates have declined considerably since the Committee meeting on June 30–July 1. The Board of Governors approved a reduction in the discount rate from 3½ to 3 percent on July 2. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies declined further over the first several weeks of the intermeeting period, but it has stabilized more recently.

M2 and M3 contracted somewhat further in July. Through July, both aggregates were appreciably below the lower ends of the ranges established by the Committee for the year.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at its meeting on June 30–July 1 reaffirmed the ranges it had established in February for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The Committee anticipated that developments contributing to unusual velocity increases could persist in the second half of the year. The monitoring range for growth of total domestic nonfinancial debt also was maintained at 4½ to 8½ percent for the year. For 1993, the Committee on a tentative basis set the same ranges as in 1992 for growth of the monetary aggregates and debt measured from the fourth quarter of 1992 to the fourth quarter of 1993. The behavior of the mone tary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might or slightly lesser reserve restraint would be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from June through December at annual rates of about 2 and ½ percent, respectively.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Jordan, Kelley, Lindsey, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: Messrs. LaWare and Melzer.

Messrs. LaWare and Melzer dissented because they did not favor a directive that was biased toward possible easing during the intermeeting period. In their view, monetary policy already was appropriately stimulative, as evidenced in part by the low level of short-term interest rates and by the rapid growth in reserves since early this year, and was consistent with the promotion of economic growth in line with the economy's long-run potential. Business and consumer confidence were in fact at low levels, but they reflected a variety of problems facing the economy that were unrelated to the stance of monetary policy. Accordingly, what was needed at this point was a more patient monetary policy—one that was less predisposed to react to near-term weakness in economic data and that allowed more time for the effects of earlier easing actions to be reflected in the economy. Indeed, an easing move in present circumstances might well stimulate inflationary concerns by reducing confidence in the System's willingness to pursue an anti-inflationary policy and thus could have adverse repercussions on domestic bond markets and further damaging effects on the dollar in foreign exchange markets.

Meeting Held on October 6, 1992

The information reviewed at this meeting suggested that economic activity was expanding at a subdued pace. Domestic final sales appeared to have picked up in the third quarter, led by an increase in consumer spending and another sharp gain in business purchases of office and computing equipment, but demand had remained sluggish in most other sectors of the economy. The limited growth in overall demand was being met in part through higher imports, and as a consequence, industrial production and employment had been weak. Recent data on wages and prices continued to suggest that inflation was slowing.

Total nonfarm payroll employment fell somewhat further in September, reflecting a drop in government jobs associated with the end of a federally funded summer jobs program. Employment in the private sector was up in September, as new hiring in the services industry more than offset job losses in manufacturing and construction; employment in other industries was little changed after a sizable decline in August. The civilian unemployment rate edged down to 7.5 percent in September when the labor force registered another decrease.

After a considerable gain in July, industrial production declined appreciably in August, and available information suggested further weakness in September. The decline in industrial output since July partly reflected the disruptive effects of Hurricane Andrew on oil and gas production and of a labor strike on the manufacture of automobiles and parts. However, output of a broad range of other goods also was down. One area of continuing strength was the production of business equipment, notably office and computing equipment. The utilization of total industrial capacity fell on balance over July and August, retracing a portion of the increase that occurred over the first half of the year.

Real personal consumption expenditures were little changed in August after increasing appreciably in the two previous months; for July and August combined, spending was moderately higher than in the second quarter. In August, outlays for services continued to rise, while expenditures for most major categories of goods declined. Housing starts climbed in August, with starts of single-family homes reaching their highest level since March. By contrast, permit issuance and sales of new and existing homes edged lower in August.

Shipments of nondefense capital goods slowed considerably in July and August, retracing much of the sharp gain recorded in June. Shipments of office and computing equipment slackened on balance over the two months; however, after adjusting for ongoing rapid declines in prices, the underlying upward trend in demand for such equipment remained robust. Recent data on orders and shipments of nondefense capital goods suggested that business outlays for durable equipment, particularly for items other than computers, would grow more slowly in coming months. Outlays for nonresidential construction contracted again in August, with steep decreases occurring for commercial and industrial structures. Data on contracts continued to indicate that spending for new construction would remain sluggish over the months ahead.

Total business inventories rose somewhat further in July following a large increase in June. In manufacturing, inventory stocks were little changed over June and July but were up sharply in August as factory shipments of goods slowed; as a result, the ratio of inventories to shipments for all manufacturing rebounded to the middle of the range that had prevailed over the previous year. At the wholesale level, inventories were trimmed a little in July after a sizable rise in June, and the stocks-to-shipments ratio remained relatively high. Retail trade inventories expanded at a considerable pace in July, but a rebound in sales lowered the inventory-to-sales ratio somewhat at most types of stores.

The nominal U.S. merchandise trade deficit widened somewhat in July from its average rate in the second quarter. Imports, particularly of capital goods and consumer goods, remained on the fairly strong upward path evident during the first half of the year. Exports increased by a smaller amount in July; exports of agricultural products rose noticeably, but exports of nonagricultural goods were about unchanged from the pace of the previous three quarters. Recent indicators of economic activity in the major foreign industrial countries suggested a continuation of sluggish growth on average in those countries.

Producer prices of finished goods edged up in August in association with a rebound in prices of fresh fruits and vegetables. Abstracting from the volatile food and energy components, the increase in prices of other finished goods over the twelve months ended in August was considerably smaller than the rise over the previous twelve-month period. At the consumer level, prices of non-food, non-energy items registered another modest increase, and the twelve-month change in this measure also was down substantially from a year earlier. In September, a drop in the average hourly earnings of production or non-supervisory workers retraced part of a sizable rise in August. Over the twelve months ended in September, these earnings grew at a significantly slower rate than in the preceding twelve-month period.

At its meeting on August 18, the Committee adopted a directive that called for maintaining the existing degree of pressure on reserve positions and that included a bias toward possible easing during the intermeeting period. Accordingly, the directive indicated that in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable during the intermeeting period. The contemplated reserve conditions were expected to be consistent with growth in M2 and M3 at annual rates of about 2 percent and ½ percent respectively over the six-month period from June through December.

Open market operations during the intermeeting period were directed initially toward maintaining the existing degree of pressure on reserve positions. In early September, operations were adjusted to implement some easing in reserve pressures. This action was taken in response to incoming information that suggested unexpected sluggishness in economic activity and a smaller-than-anticipated pickup in the growth of the broad monetary aggregates. Adjustment plus seasonal borrowing tended to run a little above expected levels during the intermeeting interval, reflecting in part reserve shortfalls that produced sharp increases in borrowing at the end of two reserve maintenance periods. The reserve shortfalls along with quarter-end pressures contributed to a somewhat higher federal funds rate than had been expected following the monetary easing action.

Other short-term interest rates also declined somewhat, while longer-term rates were about unchanged since the Committee meeting on August 18. Short-term debt markets reacted to the Committee's easing action in early September and subsequently to growing expectations of further System easing in the context of continued indications of a sluggish economic expansion. Yields on intermediate-term securities also fell. However, rates on long-term obligations were little changed on balance; the System's policy easing and generally weak economic data tended to reduce bond yields, but long-term debt markets also appeared to reflect growing concerns about the fiscal outlook and increased uncertainty stemming in part from volatility in the foreign exchange markets and policy developments abroad.

In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies fluctuated widely over the intermeeting period but ended somewhat higher on balance. The dollar weakened considerably early in the period on disappointing reports about the U.S. economy and related expectations of Federal Reserve easing. In mid-September, the dollar moved sharply higher as turmoil in European currency markets prompted some safe-haven buying of dollars and resulted in interest rate reductions in Germany. More recently, reduced tensions within the European Monetary System and heightened expectations of further easing by the Federal Reserve induced renewed declines in the dollar.

Expansion of M2 and M3 resumed in August, though at fairly slow rates, and limited growth appeared to have continued in September. Through September, both aggregates were estimated to have grown at rates somewhat below the lower ends of the ranges established by the Committee for the year. The pickup in the broad aggregates seemed to reflect the cumulative effects on demand deposits and liquid retail deposits of declines in market interest rates since midyear and a related drop in opportunity costs. Currency growth strengthened further in August and September, evidently owing in part to further foreign demand. Bank credit growth also picked up in both months in conjunction with an upturn in bank loans.

The staff projection prepared for this meeting indicated that economic activity would expand at a slow pace in the current quarter and that growth would pick up gradually in 1993 to a rate that would remain quite moderate by past cyclical standards. The declines that had occurred in interest rates were expected to boost housing activity to some extent, particularly in the single-family sector. Gains in expenditures for equipment were projected to be large enough to raise business fixed investment despite sluggish spending for nonresidential construction. As employment growth was restored and further improvements in household balance sheets were achieved, consumer spending would strengthen. The projection pointed to some decline in federal government purchases, reflecting further cutbacks in defense expenditures, and weak spending by state and local governments. The persisting slack in resource utilization in this forecast was projected to be associated with additional progress in reducing inflation.

In the Committee discussion of current and prospective economic developments, many of the members expressed disappointment and concern about the sluggish pace of the expansion, and a number commented that the softening in several recent business indicators could portend quite slow economic growth over the months immediately ahead. Business and consumer sentiment was relatively depressed and seemed to have worsened a bit further recently in some parts of the country. While further deterioration in business activity culminating in an economic downturn could not be ruled out, some of the very latest data had a slightly more positive tone, and the members generally continued to view somewhat stronger economic growth as a reasonable prospect for the year ahead. However, no important sector of the economy seemed poised to provide much impetus to business activity, and the timing of the acceleration from the presently sluggish advance remained uncertain. Nonetheless, declines over the third quarter in the foreign exchange value of the dollar and in domestic interest rates—the latter along the entire maturity spectrum—suggested improved conditions for greater expansion. Recently, these more favorable conditions had been reflected in an upturn in money growth and bank lending activity. With regard to the outlook for inflation, the available statistics and anecdotal information continued to indicate appreciable progress toward the goal of price stability.

In the course of the Committee's discussion, the members gave a great deal of emphasis to the uncertainties that surrounded the economic outlook, including potential developments abroad. Several members commented that against the background of a relatively weak expansion, the recent volatility in some domestic financial markets and in the foreign exchange market tended to underscore the risks of developments that could have adverse effects on the economy. Another key uncertainty related to the ongoing restructuring of business firms and of business and consumer balance sheets. Those activities were continuing to divert financial flows from spending to savings or debt reduction, and prior experience provided little basis for determining when such restructuring might come closer to being completed and flows of funds redirected on balance into more normal spending channels. Nonetheless, the members drew considerable encouragement from the substantial progress that already had been made by business firms in improving their balance sheets and by many lenders, notably banking institutions. While some banks clearly were continuing to experience financial difficulties, many had pared their problem assets and strengthened their capital positions. Moreover, a growing number of reports suggested that banks were intensifying their efforts to find creditworthy borrowers, though when such efforts might become more general was another source of uncertainty.

Consumer spending seemed to have been reasonably well maintained in most parts of the country, including indications of some growth in a number of areas where overall business activity appeared to be moving sideways or even edging lower. At least in some parts of the country, retailers were expressing moderate optimism with regard to their prospective sales during the upcoming holiday season. Even so, very cautious consumer attitudes, associated especially with concerns about employment prospects, seemed likely to restrain overall growth in consumer spending over the next several months. Indeed, barring unanticipated economic developments leading to a major strengthening in employment opportunities, continuing efforts by many households to improve their financial positions could be expected in the context of an already low saving rate to limit the contribution of the consumer sector to faster economic growth for some considerable period.

In their comments about developments in other key sectors of the economy, members also cited single-family housing construction as a source of some stimulus in many regions. The manufacturing of related building materials had exhibited a corresponding pickup recently. Other construction activity, notably that of office structures, remained weak, but there were reports of some improvement or continuing growth in the construction of industrial facilities and public works projects in some parts of the country. In the energy sector, a firming of gas prices was encouraging somewhat greater production. On balance, there was little current evidence that construction, other than in the single-family sector, would provide significant impetus to the overall expansion in the year ahead. Likewise, flagging demand was curtailing the production of aircraft and inducing at least temporary cutbacks in auto assemblies. In addition, the foreign trade sector was not expected to add significantly to demands on the U.S. economy despite the decline in the foreign exchange value of the dollar. While the latter had fostered large increases in tourism from abroad in a number of areas and some domestic producers reportedly were gaining market share, recessions or weak expansion in major foreign trading nations were likely to limit the growth in foreign demand for U.S. goods.

The fiscal outlook remained uncertain. The large federal deficit was still tending to preclude the adoption of spending or tax reduction programs that would increase fiscal stimulus, but some members suggested that continued sluggishness in the economy might well overcome current inhibitions against new initiatives. In any event, defense spending was on a clear downtrend and was exerting an adverse effect on overall economic activity in many parts of the country. At the state and local government levels, severe fiscal problems probably would continue to curb spending and force many jurisdictions to raise taxes so long as a relatively weak economy continued to hold down revenues.

With regard to the outlook for inflation, the members were encouraged by the further indications of a disinflationary trend in prices and wages, and they saw little likelihood that upward pressures on prices would emerge over the next year or two, even in the context of some pickup in the expansion of economic activity. While medical, tuition, and some other costs were rising at relatively rapid rates, members cited widespread examples of very strong competitive pressures in markets for goods, including key agricultural products, and ongoing efforts by firms to cut costs in the face of steady or even declining prices in the markets for their products. Nonetheless, business contacts still seemed to anticipate rising inflation at some point for the economy generally if not in their own industries, and long-term interest rates still appeared to embody higher rates of inflation.

In the Committee's discussion of policy for the intermeeting period ahead, the members generally agreed that current uncertainties made an assessment of the economic outlook and the determination of an appropriate course for monetary policy particularly difficult. While the members' preferences for policy implementation ranged from the maintenance of unchanged reserve conditions to an immediate easing move, a majority indicated that they could support a policy prescription of maintaining unchanged reserve conditions for the present while biasing the directive strongly toward possible easing during the intermeeting period.

Members who favored an unchanged policy stance argued that despite the softness in a number of recent economic indicators they could see no currently persuasive evidence of a cumulative deterioration in the economy. Moreover, earlier monetary policy easing actions had provided a substantial amount of stimulus to the economy that would continue to exert its effects over time. Real short-term interest rates were at very low levels, and intermediate-term rates had declined considerably since midyear. The reductions in interest rates had greatly facilitated the progress already achieved by business firms and households in restructuring their debts and reducing their debt service burdens, thereby strengthening the financial underpinnings of the economy. The dollar recently had been subject to considerable volatility in the foreign exchange markets, and there was some risk that an easing of monetary policy at this time might tend to destabilize it. These members concluded that the present stance of monetary policy continued to reflect an appropriate balancing of the need to sustain progress toward price stability while encouraging an acceptable rate of economic growth.

Members who favored an immediate easing of policy believed that the outlook for the economy and prices argued for a policy move at this time. These members acknowledged that a good deal of uncertainty surrounded the economic outlook. However, there were some risks that an already sluggish economy might weaken further. In the circumstances, a prompt easing move would be a desirable and prudent course, particularly in a situation in which they saw a minimal risk that inflation would be deflected from its downward trend. In the view of some of these members, continued expansion in the broad monetary aggregates at rates below the Committee's ranges suggested that financial conditions were not yet conducive to a pickup in business activity that was sufficiently robust to reduce margins of underutilized resources. An easing in monetary policy seemed to be widely anticipated in financial markets, and a failure to take action at this time might well result in an undesirable backup in market interest rates, thus further weakening the outlook.

A majority of the members noted that they could support an unchanged directive that included a decided presumption of some easing if indications of stronger economic activity failed to emerge or the recent firming in money and credit flows showed signs of ebbing materially. It was anticipated that any decision to ease reserve conditions during this period would be coordinated with the consideration of a reduction in the discount rate by the Board of Governors. Two members felt strongly that a directive calling for unchanged reserve conditions should also provide for an unbiased intermeeting instruction. While such a directive would not rule out an intermeeting adjustment—in either direction—it would require more substantial evidence of changing or unexpected economic or financial information before a policy action was implemented. Several members, including some who favored an immediate easing of policy, expressed some discomfort about the extent to which the Committee might be seen as reacting to individual pieces of incoming data rather than to an accumulation of information and analysis regarding the course of the economy and prices.

In the course of the discussion, members commented that the pickup in the growth of the broad monetary aggregates in August and September was a reassuring development, even though the rates of expansion were still quite sluggish. According to a staff analysis prepared for this meeting, the growth of both aggregates was likely to remain quite limited over the balance of the year and to fall somewhat short of the lower bounds of the Committee's ranges for 1992 as a whole. Despite the lingering effects of earlier declines in short-term interest rates, the projected expansion of M2 and especially that of M3 would be expected to remain below the growth of nominal GDP, and the velocity of these monetary aggregates would continue to display unusual strength in comparison with past patterns. The persistence of slow growth in the broader aggregates probably would involve further decreases in deposit offering rates and shifts of funds to higher-yielding alternatives such as bond and stock mutual funds, with little effect on consumer spending or overall economic activity. The members nonetheless recognized the need to assure adequate monetary expansion for a growing economy and noted that money growth appreciably below current expectations would be a matter of increasing concern. A differing view focused on the growth of M1 and reserves, which had been very rapid since the latter months of 1991. In this view, the outsized growth in narrow measures of money was indicative of a quite stimulative monetary policy, but given the long lags that were involved, the inflationary consequences of such growth, if allowed to continue, might not become evident until much later, perhaps not until well into 1994.

At the conclusion of the Committee's discussion, a majority of the members indicated their acceptance of a directive that called for maintaining the existing degree of pressure on reserve positions and an understanding that there would be a marked bias toward possible easing during the intermeeting period. Two of the members expressed a strong preference for a symmetric directive with regard to possible intermeeting policy adjustments, while two others were firmly persuaded of the desirability of an immediate increase in reserve availability to strengthen the growth of M2. Accordingly, in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, it was decided that slightly greater monetary restraint might be acceptable or slightly lesser monetary restraint would be acceptable during the intermeeting period. The reserve conditions contemplated at this meeting were expected to be consistent with growth in M2 and M3 at annual rates of about 2 and 1 percent respectively over the three-month period from September through December.

At the conclusion of the meeting, the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting suggests that economic activity is expanding at a subdued pace. Total nonfarm payroll employment declined somewhat further in September, but the civilian unemployment rate edged down to 7.5 percent. Industrial production is estimated to have declined appreciably since July. Real personal consumption expenditures appear to have risen moderately in the third quarter. Data on housing have been mixed, but on balance they continue to suggest a gradual uptrend in housing expenditures. Recent data on orders and shipments of nondefense capital goods indicate slower growth in outlays for business equipment, while expenditures for nonresidential construction have been weak. The nominal U.S. merchandise trade deficit widened somewhat in July from its average rate in the second quarter. Incoming data on wages and prices suggest that inflation is slowing.

Short-term interest rates have declined somewhat, while longer-term rates are about unchanged since the Committee meeting on August 18. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies fluctuated widely over the intermeeting period but ended the period higher on balance.

Expansion of M2 and M3 resumed in August, though at fairly slow rates, and limited growth appears to have continued in September. Through September both aggregates were estimated to have grown at rates somewhat below the lower ends of the ranges established by the Committee for the year.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at its meeting on June 30–July 1 reaffirmed the ranges it had established in February for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The Committee anticipated that developments contributing to unusual velocity increases could persist in the second half of the year. The monitoring range for growth of total domestic nonfinancial debt also was maintained at 4½ to 8½ percent for the year. For 1993, the Committee on a tentative basis set the same ranges as in 1992 for growth of the monetary aggregates and debt measured from the fourth quarter of 1992 to the fourth quarter of 1993. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might or slightly lesser reserve restraint would be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from September through December at annual rates of about 2 and 1 percent, respectively.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Kelley, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: Messrs. Jordan, LaWare, Lindsey, and Melzer.

Messrs. Jordan and Lindsey preferred immediate action by the Committee to increase the availability of bank reserves sufficiently to achieve the Committee's pre-announced target growth for M2 in 1992. Such reserve provision would likely be associated with further declines in short-term market interest rates. They believed that this policy action by the Committee should be accompanied by an announcement of reductions of the upper and lower limits of the range for M2 growth in 1993. They felt that it was important to make clear that near-term action to increase M2 expansion was not an abandonment of the long-term objective of non-inflationary monetary growth.

Messrs. LaWare and Melzer dissented because they did not want to bias the directive toward possible easing during the intermeeting period. In their view, a variety of indicators, including the level of short-term interest rates and the growth of reserves, suggested that monetary policy already was positioned to foster an expansion in economic activity consistent with the economy's long-run potential. Moreover, further easing at this time would incur a substantial risk of destabilizing the dollar in the foreign exchange markets. In these circumstances, they favored a steady monetary policy that was not disposed to react to near-term weakness in economic data and that allowed more time for the effects of earlier easing actions to be felt in the economy. Mr. Melzer also expressed concern that the progress already made toward achieving price stability might be jeopardized if very rapid growth in M1 were to continue.

Meeting Held on November 17, 1992

1. Domestic Policy Directive

The information reviewed at this meeting suggested that economic activity had been expanding at a moderate pace. Consumer spending had picked up somewhat, business purchases of capital equipment continued to rise at a brisk pace, and housing demand had increased moderately since midyear. At the same time, part of these demands were being met through higher imports, and recent gains in industrial production and employment had been limited. Incoming data on wages and prices had been mixed but suggested on balance a continuing trend toward lower inflation.

Total nonfarm payroll employment rose slightly in October after declining in August and September. Substantial job gains were recorded in the services industries, especially in health services and the cyclically sensitive business services, and employment in construction rebounded from a September decline. In manufacturing, the number of jobs declined further in October, although total hours worked were unchanged as the drop in employment was offset by an increase in overtime. Government employment continued to contract, reflecting the end of a federally funded summer jobs program and early retirements by postal workers. Initial claims fell somewhat during October, and the civilian unemployment rate edged down to 7.4 percent.

Industrial production rose somewhat further in October following a modest increase in the third quarter. Much of the October gain reflected a sharp rise in light truck assemblies, but there was another sizable advance in the manufacture of office and computing equipment. Elsewhere, the production of consumer goods other than motor vehicles and parts had changed little in recent months, and the output of defense and space equipment remained on a downward trend in October. Utilization of industrial capacity edged higher in October but was still near its 1991 low.

Retail sales increased appreciably in September and October, led by a substantial rise in sales at automotive dealers. Sales at general merchandisers, apparel outlets, furniture and appliance stores, and building materials and supplies centers also were up noticeably over the two months. Housing starts rose significantly in August and then edged up further in September to their highest level since March. Sales of new homes had increased on balance over recent months, and the inventory of new homes for sale in September had reached its lowest level since 1983.

Real outlays for producers' durable equipment posted another strong increase in the third quarter. A sharp advance in outlays for computing equipment outweighed a dropoff in aircraft purchases from an unsustainably high level in the second quarter. Purchases of items other than aircraft and computing equipment rose at a rapid rate in the third quarter, and recent data on orders for such goods pointed to additional growth in the near term. Expenditures for nonresidential construction, which had fluctuated within a narrow range earlier in the year, dropped sharply in the third quarter. Office construction registered the largest decline, but other commercial and industrial building also fell considerably.

Business inventories rose only slightly in September, but over the third quarter as a whole stocks grew at the same rate as in the second quarter. In manufacturing, stocks were drawn down in September, retracing a sizable portion of the runup that had occurred in August. In most manufacturing industries, inventory-to-shipments ratios in September were at or near the bottom of their recent ranges. Wholesale inventories rose modestly in the third quarter, and the stocks-to-sales ratio in September was at the low end of the range posted over the past year. At the retail level, inventories rebounded in September from an August decline, leaving the inventory-to-sales ratio for the retail sector unchanged from the second quarter.

The nominal U.S. merchandise trade deficit widened sharply in August; for July and August combined, the deficit was somewhat larger than its average rate in the second quarter. The value of exports was little changed from the second quarter, but the value of imports increased appreciably. Most of the increase in imports was in capital goods, especially computers, and consumer goods. Recent indicators suggested that economic activity in the major foreign industrial countries had remained sluggish in the third quarter. A recovery seemed to have gotten under way in Canada, but the economies of most European countries and Japan evidenced little if any forward impetus, and the downturn that began in western Germany in the second quarter appeared to have persisted into the third quarter.

Producer prices of finished goods edged up in October, reflecting a slight increase in food prices and a further sharp advance in prices of energy products. Excluding the finished food and energy components, producer prices declined slightly, and for the twelve-month period ended in October, this measure of prices increased considerably less than it had in the comparable year-earlier period. At the consumer level, prices of nonfood, non-energy goods and services advanced more rapidly in October than in other any month since March. Over the twelve months ended in October, however, the rise in this index of consumer prices was considerably smaller than that recorded in the year-earlier period. Increases in labor costs, measured by the total hourly compensation of private industry workers, slowed further in the third quarter, and both the wage and benefits components of this index had increased substantially less over the four quarters that ended in September than in the preceding four quarters.

At its meeting on October 6, the Committee adopted a directive that called for maintaining the existing degree of pressure on reserve positions and that included a marked bias toward possible easing during the intermeeting period. Accordingly, the directive indicated that in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable during the intermeeting period. The contemplated reserve conditions were expected to be consistent with growth in M2 and M3 at annual rates of about 2 percent and 1 percent respectively over the three-month period from September through December.

Open market operations during the intermeeting period were directed toward maintaining the existing degree of pressure on reserve positions. The emergence of more favorable indications regarding the performance of the economy and the continued more rapid expansion of money and credit were seen as obviating the need to implement an easing in reserve conditions that had been contemplated as a strong possibility under the directive issued at the October 6 meeting. Several small technical decreases were made during the intermeeting period to expected levels of adjustment plus seasonal borrowing to reflect the usual pattern of diminishing needs for seasonal credit. Actual borrowing averaged close to expected levels over the three reserve maintenance periods completed since the October meeting. Early in the intermeeting period, the federal funds rate exhibited some of the firmness that had prevailed over most of the previous period, but subsequently it averaged close to expected levels.

Most other interest rates increased appreciably over the intermeeting period. At the beginning of the period, rates generally incorporated an expected near-term easing of monetary policy. Subsequently, when an easing move was not forthcoming and when concerns about fiscal stimulus increased amid some signs of firmer economic activity and increasing money and credit demands, market interest rates rose for all maturities. The largest increases were in intermediate maturities, which were especially affected by expectations of additional federal borrowing and of a stronger economy that would stimulate rising private credit demands over the next few years. Expectations of firmer economic growth also boosted stock prices appreciably over the period.

With interest rates rising in the United States and falling abroad, the trade-weighted value of the dollar in terms of the other G-10 currencies rose very substantially over the intermeeting period. Declines in interest rates in foreign countries were widespread, reflecting signs of greater economic weakness as well as actual or prospective easing in monetary policies abroad. The dollar was particularly robust against European currencies but advanced only moderately against the yen.

M2 growth strengthened somewhat in October from its pace in the two previous months. The acceleration of M2 growth reflected more rapid expansion of its transaction components that appeared to be associated in part with the lagged effect of earlier declines in market interest rates and opportunity costs and the heavy pace of mortgage refinancing activity. M3 grew more slowly in October partly owing to reduced needs for managed liabilities in conjunction with somewhat weaker expansion in bank credit. Through October, both broad aggregates were estimated to have grown at rates a little below the lower ends of the ranges established for the year by the Committee.

The staff projection prepared for this meeting suggested a continuing expansion in economic activity. Growth was expected to pick up gradually over 1993 to a rate that, although quite moderate by past cyclical standards, would be sufficient to reduce the margins of unemployed labor and capital resources. The recent backup in long-term interest rates and the appreciation of the dollar in foreign exchange markets would exert some restraining influence over the next several quarters. Continuing cautiousness on the part of consumers facing uncertain job and income prospects would tend to hold down gains in consumption for some period ahead. But, as further progress was made in improving household balance sheets and employment growth gradually resumed, consumer spending would strengthen. Additional gains in outlays for business equipment were expected over coming quarters as firms sought to meet increasing demand for goods and to respond to competitive pressures by modernizing product lines and achieving labor-cost savings. The projection pointed to sluggish export demand in light of sustained economic weakness abroad. While recognizing the possibility of a stimulative fiscal initiative in 1993, the staff retained for this forecast the assumption employed in several previous forecasts that fiscal policy would remain mildly restrictive owing in large part to a substantial decline in defense spending. The persisting slack in resource utilization over the forecast horizon was expected to be associated with additional progress in reducing inflation.

In the Committee's discussion of current and prospective economic developments, the members indicated that they were encouraged by the somewhat more positive tone in the latest economic reports and by the signs of improving business and consumer confidence. The expansion appeared to have gathered somewhat more upward momentum than many had anticipated earlier, though a number of members commented that relatively slow economic growth was likely to persist over the nearer term. The outlook beyond the next quarter or two was subject to considerable uncertainty and indeed to both upside and downside risks. The advent of a new Administration and a new Congress early next year made fiscal policy especially hard to predict. Members observed that indications of some improvement in overall domestic demands, should they persist, might well generate considerable strengthening in production activity as businesses attempted to maintain or build up their currently lean inventories. On the other hand, the recent appreciation of the dollar and the signs of growing weakness in major foreign economies could have adverse implications for demands for goods produced in the United States. On balance, moderate but sustained growth in overall economic activity was seen as a likely prospect, though the gains probably would be uneven both in terms of their timing and the sectors of the economy that would be affected. Against this background, the members generally continued to view further progress toward price stability as a reasonable expectation and an important element in enabling the expansion to be sustained.

In their review of developments in key sectors of the economy, the members generally agreed that while the evidence of a strengthening business expansion was still quite limited and much of it was still anecdotal, there were growing indications of improving business and consumer confidence. Some members cautioned that changing attitudes alone could not be relied on as harbingers of a more satisfactory economic performance, as experience in recent years made clear, but the improved financial condition of many business firms, households, and lending institutions provided a further basis for optimism. A good deal of progress already had been made toward reducing debt burdens, and the retarding effects of balance sheet adjustments on current spending seemed likely to lessen over the forecast horizon. Moreover, despite many lingering problems, the general health of the banking industry had improved markedly and there were spreading reports of greater efforts by banks to find creditworthy borrowers. At the same time, the members saw signs that demands for bank loans might be picking up a bit from very depressed levels.

The latest data on retail sales and anecdotal reports from many parts of the country suggested some improvement in consumer spending. There were widespread reports of increasing optimism among retailers regarding the outlook for sales during the holiday season. Sales of automobiles and trucks appeared to be rising. The members nonetheless generally continued to view the outlook for consumer spending with considerable caution. Consumers remained concerned about job prospects against the background of continuing downsizing and restructuring activities by many business firms. Ongoing efforts to reduce debt burdens also seemed to be exerting a retarding effect on consumer spending. Against this background, the upturn in consumer confidence indicated by a recent survey could prove to be relatively fragile and short-lived. On balance, a strengthening trend in consumer spending, though to a relatively moderate pace by past business recovery standards, was still expected to provide major support for a sustained economic expansion.

Since the stimulus from the consumer sector coincided with relatively lean inventories, its effects might well be reinforced for a time by business efforts to build their inventories. Business spending for equipment also appeared likely to remain fairly robust, given a moderate expansion in sales and the improving financial condition of many businesses. The housing sector was viewed as another potential, though limited, source of stimulus over the forecast horizon. There were reports of improving home sales and home construction activity in many parts of the country, including some otherwise depressed areas, and many business contacts also were seeing better demand for construction materials and home furnishings. On the negative side, nonresidential construction remained weak across much of the nation, and further reductions in construction activity were likely as major projects were completed. However, nonresidential construction was being maintained or even trending higher in a few areas and appeared to have bottomed out in others. The rise in natural gas prices had spurred drilling activity in recent months, but some members commented that the outlook for significant further gains in that industry was not promising.

Many of the members stressed that the external sector constituted a major source of downside risk for the economy. The economic prospects for major foreign economies appeared to have deteriorated recently, and given the appreciation of the dollar, net exports might well worsen further over the next several quarters. The possible failure of ongoing trade negotiations would further dampen the outlook for U.S. trade. For the present, anecdotal reports from around the country on export sales were mixed, with such sales still well maintained in some industries and areas but slowing in others.

The outlook for fiscal policy constituted a major source of uncertainty; while the enactment of some fiscal policy measures now appeared to be increasingly likely, there was no reliable way to predict their overall size, specific provisions, or the timing of their effects. For now, the downtrend in federal government purchases of goods and services constituted a sizable negative in the forecast of aggregate demands. In particular, the cutbacks in defense expenditures were having a major effect on local economies in several parts of the country. Any new fiscal initiatives might well contain some stimulative elements designed to provide a boost to a relatively slow economic expansion. However, the delays usually encountered in enacting such legislation together with the subsequent lags before much of the effects were felt in the economy implied continued fiscal drag during the quarters immediately ahead; moreover, the propensity for financial markets to raise interest rates in anticipation of fiscal policy stimulus might also damp spending for some period. Some members saw a risk that much of the fiscal stimulus would be felt at a time when economic activity might already be gaining considerable momentum.

Turning to the outlook for inflation, members commented that despite a disappointing report on consumer prices for October, the disinflationary trend still appeared to be well established. In the view of most members, the outlook for relatively subdued pressures on resources over the forecast horizon together with the slow growth over an extended period in broad measures of money augured well for further progress toward price stability. Members were continuing to observe strong competitive pressures in local markets, and business contacts were still emphasizing the stout resistance that they encountered when they tried to raise prices to widen profit margins or to pass along rising costs. Most businessmen currently saw and anticipated little or no inflation in their own industries. Consumers also remained highly price conscious. At the same time, however, there seemed to be a widespread view in the business community and among consumers that at some point the rate of inflation was likely to rise appreciably from its recent level, and such expectations tended to have adverse repercussions in long-term debt markets and to create tensions in wage negotiations and other price-setting activities. Members noted that current inflationary expectations had been built up over a period of many years and an extended period of reduced inflation probably would be required before they disappeared.

At this meeting, the Committee had a preliminary discussion of the ranges for monetary growth in 1993 that it had established on a tentative basis at the meeting on June 30–July 1, 1992. The ranges in question had been set at 2½ to 6½ percent for M2 and 1 to 5 percent for M3 and were unchanged from those adopted for 1992. While there had been considerable sentiment at midyear in favor of lowering the ranges, a majority of the members had concluded then that uncertainties about the prospective relationship between the monetary aggregates and nominal spending argued for caution in making any changes. The information since midyear had confirmed the persistence of sizable increases in the velocity of M2 and M3. A recent staff study had provided some reasons for this unusual behavior, and staff analysis pointed to a strong probability that velocity would rise again next year.

During the discussion, the members generally agreed that developments since mid-1992 had reinforced the case for some reduction in the 1993 range for M2, and they indicated that they probably would support proposals for a lower range. Such a reduction would be a technical adjustment intended to take account of the atypical strength in velocity. Some noted that a lower range also would be seen as underscoring the desire of the Committee to avoid any pickup in inflation should the expansion gain momentum and indeed as promoting further progress toward price stability, thereby establishing a sounder basis for sustained growth in the economy at its highest potential. The ranges would be voted on in February before their scheduled announcement to the Congress, and by that time more information would be available to gauge the prospective behavior of M2 during 1993.

In the Committee's discussion of policy for the intermeeting period ahead, a majority of the members indicated a preference for maintaining unchanged conditions in reserve markets, but several others believed that some easing would be a more appropriate policy. Members who supported a steady policy course emphasized the growing if still tentative indications of a strengthening economy—including the pickup in money and credit growth—and the apparent upturn in business and consumer confidence. Some also cited the increased prospects of fiscal policy measures that were likely to provide some net stimulus to the economy over the intermediate term. Members who preferred to ease monetary policy at this time referred to what they viewed as an unsatisfactory outlook for economic activity, and some stressed the desirability of taking prompt action to promote sustained growth in the broader monetary aggregates within the Committee's ranges. Members who favored an immediate easing also endorsed coupling such a policy move with a reduction at this time in the tentative M2 range for 1993 in order to emphasize the Committee's commitment to noninflationary economic growth.

In the course of the discussion, the members took account of a staff analysis that suggested some moderation in the growth of M2 over the remainder of the year, assuming unchanged conditions in reserve markets. While M2 growth on a quarterly average basis was expected to be stronger in the current quarter than in the previous two quarters, expansion for the year as a whole was still projected to fall a little below the Committee's annual range. Some members commented that an important policy objective would be to prevent M2 growth from faltering—such a development might parallel a similar pause in the economy—as it had earlier in the current expansion. On the other hand, some members noted the persisting increases in M2 velocity. They remarked that the level of short-term interest rates together with the very rapid expansion in M1 and reserves pointed to an adequate availability of liquidity in the economy and thus suggested that current monetary policy already was appropriately stimulative and properly positioned to support the projected strengthening in economic activity. Indeed, in one view, continued rapid expansion in the narrrow measures of money and reserves, if allowed to continue, would be a matter of increasing concern with respect to the longer-run implications for inflation.

In the Committee's discussion of possible adjustments to policy during the intermeeting period, many of the members expressed a preference for a directive that did not bias potential adjustments in either direction. In this view, the expansion was on a reasonably solid footing, the risks to the expansion were now fairly evenly balanced, and a steady policy course should be maintained in the absence of unanticipated developments with significant implications for the economic outlook. Other members, while encouraged by recent economic developments, wanted to bias the directive toward ease, though without the strong presumption of some potential easing that had been associated with the previous directive. They observed that the economy was still expanding at a relatively subdued pace, inflation was on a downward track, and given the earlier tendency for the recovery to weaken, they believed that the Committee should react relatively promptly to indications, including any downturn in money growth, that the economy might again be falling short of a moderate growth path. Most of the members who preferred to ease immediately indicated that they could accept an unchanged directive that was biased toward ease, and such a directive also was acceptable to many members who favored a symmetrical directive.

At the conclusion of the Committee's discussion, all but three of the members indicated their acceptance of a directive that called for maintaining the existing degree of pressure on reserve positions and that would include some bias toward possible easing during the intermeeting period. Two of the members expressed a strong preference for a symmetric directive with regard to possible intermeeting policy adjustments, while another was firmly persuaded of the desirability of an immediate increase in reserve availability to strengthen the growth of M2. Accordingly, in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, the Committee decided that slightly greater monetary restraint might be acceptable or slightly lesser monetary restraint would be acceptable during the intermeeting period. The reserve conditions contemplated at this meeting were expected to be consistent with growth in M2 and M3 at annual rates of about 3½ and 1 percent respectively over the three-month period from September through December.

At the conclusion of the meeting, the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting suggests that economic activity has been expanding at a moderate pace. Total nonfarm payroll employment was up slightly in October after declining in the previous two months, and the civilian unemployment rate edged down to 7.4 percent. Industrial production rose somewhat in October. Retail sales increased considerably in September and October. There was some strengthening in residential construction activity over the summer months. Outlays for business equipment have continued to increase, and recent data on orders for nondefense capital goods point to further growth in the near term; expenditures for nonresidential construction have remained weak. The nominal U.S. merchandise trade deficit widened somewhat in July–August from its average rate in the second quarter. Recent data on wages and prices have been mixed but suggest on balance a continuing trend toward lower inflation.

Most interest rates have increased appreciably since the Committee meeting on October 6. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies rose very substantially over the intermeeting period.

M2 has expanded at a moderate pace since midsummer, with all of its growth stemming from its M1 component, while M3 grew slowly. Through October, both aggregates were estimated to have grown at rates a little below the lower ends of the ranges established by the Committee for the year.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at its meeting on June 30–July 1 reaffirmed the ranges it had established in February for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The Committee anticipated that developments contributing to unusual velocity increases could persist in the second half of the year. The monitoring range for growth of total domestic nonfinancial debt also was maintained at 4½ to 8½ percent for the year. For 1993, the Committee on a tentative basis set the same ranges as in 1992 for growth of the monetary aggregates and debt, measured from the fourth quarter of 1992 to the fourth quarter of 1993. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might or slightly lesser reserve restraint would be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from September through December at annual rates of about 3½ and 1 percent, respectively.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Kelley, Lindsey, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: Messrs. Jordan, LaWare, and Melzer.

Mr. Jordan dissented because he preferred taking immediate action to increase the availability of bank reserves sufficiently to raise M2 growth to a pace more consistent with the Committee's annual range. Because desirable M2 expansion in line with the Committee's objectives would be likely to fall within a lower range next year, he would announce concurrently a reduction in the 1993 range to make clear that near-term action to increase M2 expansion was not an abandonment of the long-term objective of noninflationary monetary growth.

Messrs. LaWare and Melzer dissented because they did not want to bias the directive toward possible easing during the intermeeting period. In their view, recent developments pointed to a strengthening economy, and they favored a steady policy that was not predisposed to react to near-term weakness in economic or monetary data. More time was needed to evaluate the effects of prior monetary policy actions, and they were concerned that the adoption of a more stimulative policy over the near term might well establish a basis for greater inflation later. Mr. Melzer was concerned that rapid growth in total bank reserves, the monetary base, and M1 over the past two years might already have laid a foundation for accelerating nominal GDP growth and a reversal of the disinflationary trend. In addition, he noted that policy errors can easily be made at this stage of the business cycle. In an economic expansion, efforts to resist increases in the federal funds rate through large reserve injections eventually lead to higher inflation and higher nominal interest rates.

2. Authorization for Domestic Open Market Operations

The Committee approved a temporary increase of $3 billion, to a level of $11 billion, in the limit on changes between Committee meetings in System Account holdings of U.S. government and federal agency securities. The increase amended paragraph 1(a) of the Authorization for Domestic Open Market Operations and was effective for the intermeeting period ending with the close of business on December 22, 1992.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Jordan, Kelley, LaWare, Lindsey, Melzer, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: None.

The Manager of the System Open Market Account advised the Committee that the current leeway of $8 billion for changes in System Account holdings might not be sufficient to accommodate the potentially large need to add reserves over the intermeeting period ahead to meet an anticipated seasonal bulge in the demand for currency and required reserves.

Meeting Held on December 22, 1992

The information reviewed at this meeting suggested that economic activity was rising appreciably in the fourth quarter. Consumer spending, in association with an apparent upturn in wage income and a surge in confidence, had improved considerably; sizable gains were being registered in the sales and starts of single-family homes; and business spending for capital equipment remained strong. There also had been solid advances in industrial output, and private payroll employment had turned up. Data on wages and prices had been slightly less favorable recently, and on balance they raised the possibility that the trend toward lower inflation might be slowing a little.

Total nonfarm payroll employment expanded for the third consecutive month in November, and the average workweek increased further. A sizable rise in government employment largely reflected temporary hiring to staff polling places during the general election. Private employment also picked up somewhat, despite a decline in construction jobs and weaker-than-usual seasonal hiring in the retail trade sector. A range of service industries recorded further gains in employment, and the number of jobs in manufacturing increased after three months of sizable declines. The civilian unemployment rate fell further in November, to 7.2 percent.

Industrial production recorded another advance in November. Motor vehicle assemblies were about unchanged, but significant gains were evident elsewhere, notably in the production of business equipment, construction supplies, and industrial materials. The output of consumer goods rose slightly further in November; all of the increase was in the production of nondurable goods. Reflecting the higher level of output, total utilization of industrial capacity edged higher in November to a level slightly above that at the end of 1991.

Retail sales, buoyed by strong gains in disposable income and a marked improvement in consumer attitudes, rose sharply in October and posted a further increase in November. Sales of light trucks were up substantially in the October–November period, and sales of a wide variety of other goods, both durable and nondurable, also advanced considerably. Single-family starts rose over October and November to their highest level since February, but starts of multifamily units remained at depressed levels. Sales of new and existing homes continued on an upward trend, although the preliminary estimate for new home sales was down in October.

The limited data available suggested that real business fixed investment was continuing to expand at a brisk pace. Shipments of nondefense capital goods were up on balance over September and October. A decline in shipments of office and computing equipment, which had accounted for most of the gains in shipments since early 1991, was more than offset by a considerable rise in shipments of other items. Among other indicators of spending for durable equipment over the September–October period, sales of heavy trucks rose sharply, and business purchases likely accounted for some of the recent sizable increase in sales of light trucks; on the other hand, shipments of complete aircraft were weak. Nonresidential construction activity turned up on balance in September and October, partly reflecting a steadying of expenditures for office buildings, which had plunged during the summer. At the same time, construction of other commercial structures recovered from a sharp decline in August, while outlays for industrial structures remained weak. A sharp increase in drilling activity occurred in October, apparently in response to higher natural gas prices and the expiration at year-end of a drilling subsidy.

Business inventories were drawn down appreciably further in October. In manufacturing, reductions in stocks were smaller in October than in September. The ratios of stocks to shipments in most industries were at or near the bottom of their recent ranges. In the trade sector, a sharp drop in stocks held by auto dealers more than accounted for an overall decline in retail inventories in October. Aside from auto dealers, a slight increase in retail stocks coupled with a strong increase in sales produced a small decline in inventory-to-sales ratios. Wholesale inventories fell again in October, and the inventory-to-sales ratio for this sector was near the low end of the range observed over the past two years.

The nominal U.S. merchandise trade deficit narrowed somewhat in October from its average rate in the third quarter, reflecting both a considerable increase in the value of exports and a decline in the value of imports. Most of the expansion in exports was in capital goods, notably aircraft and industrial machinery, and consumer goods. The reduction in imports was primarily in consumer goods and in passenger cars imported from Canada. Recent indicators generally pointed to continued weakness in the economies of the major foreign industrial countries. During the third quarter, economic activity contracted further in Japan and western Germany and expanded slowly in France and Canada. In the United Kingdom, activity appeared to have changed little.

Producer prices of finished goods fell slightly in November, reflecting sharp declines in the prices of food, gasoline, and fuel oil. Excluding the finished food and energy components, producer prices edged higher and, for the twelve months ended in November, rose at a considerably slower pace than in the comparable year-earlier period. By contrast, at the consumer level, prices of nonfood, nonenergy goods increased over October and November at a faster rate than in the previous several months. Consumer prices of apparel, tobacco, and used cars rose sharply in October, and airfares surged in October and November as domestic airlines sought to restore profit margins that had been squeezed by promotions over the summer. Even with these upticks, however, the index of consumer prices excluding food and energy increased considerably more slowly in the twelve months ended in November than in the year-earlier period. Average hourly earnings of private production or nonsupervisory workers also rose more rapidly in November; the strongest gains were in the finance, insurance, and real estate category, but sizable increases were recorded in several other sectors as well. Nevertheless, average hourly earnings rose more slowly over the twelve months ended in November than over the year-earlier period.

At its meeting on November 17, the Committee adopted a directive that called for maintaining the existing degree of pressure on reserve positions and that included some bias toward possible easing during the intermeeting period. Accordingly, the directive indicated that in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable during the intermeeting period. The contemplated reserve conditions were expected to be consistent with growth of M2 and M3 at annual rates of about 3½ and 1 percent respectively over the three-month period from September through December.

Open market operations during the intermeeting period were directed toward maintaining the existing degree of pressure on reserve positions. One small technical decrease was made during the period to expected levels of adjustment plus seasonal borrowing to reflect the usual pattern of diminishing needs for seasonal credit. Because of settlement-day pressures, actual borrowing along with the federal funds rate tended to average a little above expected levels.

Changes in other short-term interest rates were mixed over the intermeeting period. In the market for Treasury securities, bill rates were essentially unchanged while bond yields fell despite the emergence of a more robust economic picture. Tending to offset the effects of the latter on long-term rates was the tenor of statements emanating from the incoming Administration, which were viewed by market participants as reducing the likelihood of a large fiscal stimulus package. The recent step-up in the size of bill auctions and the potential for some shortening of the maturity of Treasury debt issues under the new Administration also might have contributed to the flattening of the Treasury yield curve. Market expectations of year-end pressures sharply boosted interest rates on very short-term private paper for a time; however, concerns about year-end pressures subsequently abated, and much of the rise in rates was retraced. Most three- to six-month private rates fell on balance over the period; the lower rates likely were associated with lessened expectations of year-end pressures but also might have reflected perceptions of reduced credit risks in a strengthening economy. Buoyed by the prospects for a stronger economy and the declines that had occurred in bond yields, most major indexes of stock prices reached record highs.

In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies was essentially unchanged on balance over the intermeeting period. The dollar moved moderately higher over the first half of the period in response to incoming data suggesting that the prospects for sustained economic growth in the United States were improving while the economic outlook for Japan and Germany was deteriorating somewhat. Later in the period, the dollar gave up its gains, partly as a result of strong anti-inflationary statements from Bundesbank officials that damped market expectations of near-term monetary easing in Germany. The relative stability of the dollar contrasted sharply with the rekindling of exchange rate pressures among a number of European currencies.

The growth of M2 slowed in November, and on average it had expanded at a moderate pace in recent months; the limited available data indicated a further reduction in growth of this aggregate in December. The recent behavior of M2 largely reflected a sharp falloff in the expansion of demand deposits associated with a backup in money market rates in previous months and a likely slowing in the rate of increase in mortgage refinancing activity. M3 expanded at a relatively slow rate in November and appeared to be declining in December. For the year, both M2 and M3 apparently grew at rates a little below the lower ends of the annual ranges established by the Committee.

The staff projection prepared for this meeting suggested a continuing expansion in economic activity that would be associated with gradual reductions in the margins of unemployed or underutilized labor and capital resources. The pickup in economic activity in recent months, through its positive effects on confidence and incomes, was expected to provide greater momentum to the economy in the near term. However, this impetus would in part be offset by weaker export demand as a result of slower growth abroad and the higher level of the dollar; the earlier backup in long-term interest rates, only part of which was retraced in recent weeks, also would have a restraining effect. Consumer spending, which had outpaced income growth in the second half of 1992, was projected to expand more in line with incomes in coming quarters. Residential construction was expected to strengthen gradually as concerns about employment security receded and incomes improved. Spending increases on business equipment were expected to be sustained in part by continuing efforts to improve productivity, and investment in industrial building and in commercial structures other than office buildings would begin to pick up in 1993. While recognizing the possibility of a stimulative fiscal initiative in 1993, the staff retained for this forecast the assumption in several recent forecasts that fiscal policy would be mildly restrictive. The persisting, though diminishing, slack in resource utilization over the forecast period was expected to be associated with additional progress in reducing inflation.

In the Committee's discussion of current and prospective economic developments, the members cited growing indications of a somewhat stronger expansion than had seemed to be under way earlier and a marked improvement in business and consumer confidence, especially over the past month or two. Although substantial uncertainties still surrounded the outlook, these developments provided encouraging support for forecasts of continued economic growth at a pace sufficient to reduce gradually margins of unutilized resources. The expansion now seemed to have gathered fairly broad-based momentum that might be reinforced over the quarters ahead by business efforts to build up inventories in the context of generally low inventory-to-sales ratios. Moreover, the improving financial condition of many households and business firms, notably banking institutions, was a promising development that should reduce constraints on economic growth over coming quarters. The possibility of expansionary fiscal measures was another source of potential short-term stimulus to the economy, though one surrounded by substantial uncertainty with respect to the nature, size, and timing of any fiscal initiatives and the longer-run consequences. On the negative side, many of the members stressed what they regarded as a worsening outlook for U.S. exports; they also noted the continuing weakness in commercial construction, defense spending, and the retarding effects on employment of ongoing downsizing and restructuring by many business and financial firms. With regard to the outlook for inflation, some of the recent reports on prices and wages had been less favorable than earlier. However, against the background of continuing though diminishing slack in production resources, favorable trends in productivity, and restrained growth in the broad measures of money, the members generally continued to anticipate further progress toward price stability over the forecast horizon.

The statistical evidence of a stronger expansion was bolstered by anecdotal reports of improving business conditions across much of the nation. Confidence appeared to be rising in most areas and indeed seemed to be leading the statistics. Some members observed, however, that representatives of many larger business firms did not seem to share the ebullient mood of their smaller business counterparts, possibly reflecting the still active retrenchment efforts of many large firms and growing indications for some of weakening markets abroad. There also were significant geographic exceptions to the improving business climate, notably in areas that were substantially affected by cutbacks in defense spending, business consolidation and cost-cutting activities, and underlying weakness in the energy industry. On balance, regional weakness in parts of the country such as southern California tended to be masked in the overall economic statistics by what were increasingly robust business conditions in the rest of the nation.

Personal consumption expenditures had posted relatively good gains over the past several months, and retail sales were displaying considerable strength in the ongoing holiday season according to anecdotal reports from around the country. Further growth in consumer expenditures was expected to provide a key underpinning for continuing economic expansion. A development that might well be buttressing consumer spending was the improvement in existing home sales and the related capital gains that were tending to supplement the recent strengthening in disposable incomes. Nonetheless, the contribution of the consumer sector was likely to be constrained by a number of factors despite the recent surge in consumer confidence. In particular, an already low saving rate and still substantial household debt burdens would tend to restrain the growth in consumption expenditures. Moreover, it seemed likely that gains in employment would continue to be relatively limited, owing to further business restructuring activities and related improvements in productivity that would tend to hold down the demand for new workers. Even so, the pace of business hiring could be expected to quicken as existing workers were utilized more fully and the practical limits to increasing output through overtime work were reached.

Continuing efforts to improve productivity were seen as likely to stimulate appreciable further expansion in business fixed investment. Much of that expansion was expected to take the form of substantial further growth in outlays for business equipment, especially if an investment tax credit were to be enacted. At the same time, investment in nonresidential structures was projected to stabilize for the nation as a whole next year after declining in recent years. In this connection, members drew some encouragement from anecdotal reports that prices, rental rates, and other terms relating to the value of commercial real estate seemed to be bottoming out in several depressed markets, though a turnaround involving significant new construction was unlikely for an extended period in many of those markets. The outlook for housing construction was more promising, especially for the single-family sector. Housing activity had strengthened at least marginally in recent months in many parts of the country, and the conjunction of reduced mortgage rates and some projected increase in incomes was expected to support at least a gradual uptrend in housing construction.

With regard to fiscal policy, members noted that the bond markets had responded favorably in recent weeks to indications that the incoming Administration would give emphasis to reducing the federal budget deficit over time. Indeed, the prompt enactment of legislation to achieve that objective undoubtedly would bolster business and consumer confidence as well as bond markets, with favorable effects on the economy. Some members cautioned, however, that those effects would tend to be negated to the extent that lower federal spending was offset by legislated increases in required spending by business firms to finance worker benefits and other programs; such spending would reduce profits and incentives to expand and ultimately would boost costs and prices. In any event, the course of fiscal legislation remained highly uncertain in terms of its size, structure, and timing and thus its near- and longer-term effects on the economy.

Many of the members saw a substantial risk that lagging exports could exert a significant constraint on the domestic expansion. There were increasing indications of a weaker economic performance in many foreign countries, which were reinforced by recent anecdotal reports from contacts at domestic firms engaged in international business activities. However, while the risks for prospective economic activity abroad seemed to be tilted to the downside, stimulative policy responses by foreign authorities—some of which had already been initiated—might well alter developing trends. For now, though, diverging business trends in the United States and foreign nations in association with the rise that had occurred in the dollar over the course of recent months pointed to a worsening trade balance for the United States.

The members generally anticipated further progress toward price stability, although some now expected somewhat less improvement than they had earlier. In the view of many members, key factors underlying a favorable inflation outlook included the persisting, though decreasing, slack in the utilization of production resources associated with the moderate expansion expected in overall economic activity and the slow growth that had occurred for an extended period in the broad measures of money. While recent data on consumer prices and wages had a somewhat less favorable tenor, price competition remained vigorous in markets for many goods and developments in long-term debt markets suggested some shift in expectations toward lower inflation. It also was noted that ongoing cutbacks in work forces by many employers, including widely publicized reductions by some major corporations, were tending to limit demands for higher wages. Another important influence was the strong competition from foreign suppliers in the context of sluggish demands in their own markets and the rise in the foreign exchange value of the dollar. Rapid increases in the narrow measures of money and reserves also were cited as possibly signifying a risk on the other side if such increases persisted—that is, that monetary policy might soon be accommodating renewed inflationary pressures.

In the Committee's discussion of short-run policy for the period until the next meeting, all of the members expressed a preference for maintaining an unchanged degree of pressure on reserve positions; all also indicated that they could support a shift from the tilt toward ease incorporated in recent directives to a symmetrical directive that would not include any bias with regard to possible adjustments to the degree of reserve restraint during the intermeeting period. Improved prospects for moderate economic growth argued for maintaining the Committee's current stance in reserve markets, and they also warranted a shift toward a more balanced approach to possible intermeeting changes in policy. At the same time, the still considerable uncertainties surrounding the economic outlook, including some lingering questions about the sustainability of the expansion, indicated the desirability of a cautious approach to any policy changes. In this connection, several members referred to the swings in the outlook that had characterized the current expansion, including the recent reversal of sentiment regarding the strength of the expansion, and the associated risks of premature or misdirected policy moves.

The members observed that the next policy move might be in either direction. For example, the need for some easing could not be ruled out should the expansion again appear to be faltering. Substantial weakness in the monetary aggregates over coming months would be one factor to be weighed in assessing the economic outlook, though velocity developments also would have to be taken into account. On the other hand, a stronger economic performance might raise questions as to the need for a tightening move at some point during the year ahead as a means of maintaining progress toward price stability while continuing to encourage maximum sustainable economic expansion. If a tightening move were to be needed, it would be desirable to implement such a move before inflation pressures showed through in the actual price statistics in order to avoid sharp and potentially disruptive tightening actions later. One member expressed concern about the risk of maintaining an overly stimulative monetary policy for too long, with adverse consequences for inflation; while not prepared to tighten policy at this point, he indicated a preference for biasing the directive toward restraint.

In the course of this discussion, the members took account of a staff analysis that pointed to quite sluggish growth in M2 and M3 over the months ahead and to a marked slowing in the expansion of M1. The broader monetary aggregates were expected to continue to be affected by the various factors that had inhibited their growth over the past two years and that had induced a substantial diversion of credit flows from banking institutions into capital market instruments. Moreover, some special factors that had boosted the growth of the broader aggregates in recent months, such as the enlarged volume of mortgage refinancing activity, would tend to dissipate in the months immediately ahead, assuming no significant change in mortgage interest rates. While the atypically slow growth of the broader aggregates during the current economic recovery did not under prevailing circumstances have the usual implications for the performance of the economy, given the concomitant and unusual rise in their velocities, several members nonetheless expressed concern about the persistence of the lagging growth. A few were more concerned about the behavior of the narrower measures of money such as M1 or the monetary base whose growth had been unsustainably rapid over much of 1992, though these now gave some indications of moderating. There was general agreement that the performance of the various monetary aggregates should continue to be monitored with special care.

At the conclusion of the Committee's discussion, all of the members indicated their support of a directive that called for maintaining the existing degree of pressure on reserve positions and that did not include a presumption about the likely direction of any adjustments to policy during the intermeeting period. Accordingly, in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, the Committee decided that slightly greater or slightly lesser monetary restraint would be acceptable during the intermeeting period. The reserve conditions contemplated at this meeting were expected to be consistent with M2 growth at an annual rate of about 1½ percent and with M3 about unchanged over the four-month period from November through March.

At the conclusion of the meeting, the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting suggests that economic activity has been rising appreciably in the current quarter. Total nonfarm payroll employment has increased slightly since September, and the average workweek has moved higher. The civilian unemployment rate fell further in November to 7.2 percent. Industrial production posted solid gains in October and November. Retail sales increased sharply in October and rose further in November. Residential construction activity appears to have increased from the third-quarter pace. Indicators of business fixed investment have been mixed recently, but on balance they suggest further growth. The nominal U.S. merchandise trade deficit narrowed somewhat in October from its average rate in the third quarter. Recent data on wages and prices suggest on balance a possible slowing in the trend toward lower inflation.

Changes in short-term interest rates have been mixed since the Committee meeting on November 17 while bond yields have edged lower. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies was essentially unchanged on balance over the intermeeting period.

Over the course of recent months, M2 has expanded at a moderate pace, while M3 has continued to expand at a very slow rate. More recently, both aggregates have weakened somewhat. Both appear to have grown at rates a little below the lower ends of the ranges established by the Committee for the year.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at its meeting on June 30–July 1 reaffirmed the ranges it had established in February for growth of M2 and M3 of 2½ to 6½ percent and 1 to 5 percent respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The Committee anticipated that developments contributing to unusual velocity increases could persist in the second half of the year. The monitoring range for growth of total domestic nonfinancial debt also was maintained at 4½ to 8½ percent for the year. For 1993, the Committee on a tentative basis set the same ranges as in 1992 for growth of the monetary aggregates and debt measured from the fourth quarter of 1992 to the fourth quarter of 1993. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint or slightly lesser reserve restraint would be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with M2 growing at a rate of around 1½ percent and M3 about unchanged in the period from November through March.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Jordan, Kelley, LaWare, Lindsey, Melzer, and Mullins, Ms. Phillips, and Mr. Syron. Votes against this action: None. ■

Consumer and Community Affairs

Concerns about possible discrimination in mortgage lending and access to credit by minorities and low-income households continued to receive special attention from the Division of Consumer and Community Affairs in 1992. This chapter presents the efforts of the Board to address these concerns and to promote fair lending. It summarizes the Board's actions to enforce existing federal consumer protection laws and to implement new statutory protections. It also discusses the community affairs program of the Board and Reserve Banks; reports on the examination of institutions for compliance with consumer laws—by the Federal Reserve and other regulatory agencies—and on the System's handling of consumer complaints; details the activities of the Board's Consumer Advisory Council; and reports on congressional testimony on consumer affairs issues.

Regulatory Matters

The Board took these actions with regard to consumer affairs regulations:

- Proposed an amendment to Regulation B (Equal Credit Opportunity) giving credit applicants the right to receive copies of appraisal reports
- Amended Regulation C (Home Mortgage Disclosure) to expand the coverage of the act and to implement a small-institution exemption standard for nondepository mortgage companies
- Revised Regulation Z (Truth in Lending) to provide a limited exception that allows banks to include a demand provision in home equity lines to executive officers and proposed comparable language for closed-end loans in the staff commentary to Regulation Z. Other proposed amendments applicable to home equity lines were not adopted
- Provided an exception, pursuant to temporary authority granted by the Depository Institutions Disaster Relief Act of 1992, with regard to the right of rescission—the three-day waiting period normally applicable to the disbursement of funds in credit transactions secured by a consumer's home. The exception allows borrowers in certain disaster areas to waive their right of rescission and permits creditors to use preprinted waiver forms in these limited instances
- Amended Regulation CC (Expedited Funds Availability) to permit institutions, on an exception basis, to extend holds on checks that usually require next-day and second-day availability. The Board also finalized the hold schedule for deposits made at nonproprietary automated teller machines
- Adopted Regulation DD, implementing the Truth in Savings Act (TISA), to require depository institutions to provide consumers with account disclosures. At year-end the Board published proposed changes after the Congress amended TISA by extending the mandatory compliance date, changing a part of the advertising rules, and modifying a notice provision
- Issued guidance through updates to the official staff commentaries to Regulations B and Z.

Regulation B (Equal Credit Opportunity)

In December the Board issued proposed revisions to Regulation B (Equal Credit

Opportunity) to provide credit applicants the right, upon written request, to receive copies of appraisal reports. The revisions to Regulation B implement statutory amendments contained in the Federal Deposit Insurance Corporation Improvement Act. The proposed amendments specify that the appraisal provision covers applications to be secured by a lien on a residential structure containing one- to four-family units. They also provide the time frames in which applicants must request, and creditors must give, a copy of an appraisal report. The proposal would require most creditors to notify applicants in writing of the right to receive a copy of an appraisal report unless a copy is provided automatically.

Regulation C (Home Mortgage Disclosure)

Regulation C generally applies to mortgage lenders that have assets of more than $10 million and are located in metropolitan areas. It requires disclosure of data concerning home purchase and home improvement loans. Lenders submit data—about loans they originate, about the disposition of other applications they receive, and about loans that they purchase—to their supervisory agencies, and the Federal Financial Institutions Examination Council (FFIEC) uses the data to prepare HMDA disclosure statements for individual institutions.[1] During 1992, the Board, the other banking agencies, and the Department of Housing and Urban Development processed data covering the 1991 lending activity of more than 9,300 institutions; and the FFIEC produced more than 25,900 individual disclosure statements.

The information now available under HMDA has expanded the opportunities for analysis of home lending activity. Before 1989, HMDA data revealed information only about the geographic distribution of residential lending by covered institutions. Statutory amendments to HMDA, enacted in 1989, expanded disclosures to include the disposition of applications—approved, denied, withdrawn, or files closed for incompleteness—and the race or national origin, income, and sex of applicants and borrowers. The amendments also expanded coverage to include independent mortgage companies.

The regulatory agencies use the HMDA data in assessing lender compliance with the Community Reinvestment Act and the fair lending laws. These data are also used by community organizations, financial institutions, and the public to obtain a greater awareness and understanding of residential lending activities in local communities.

Lenders make their HMDA disclosure statements available to the public. The FFIEC also prepares reports showing the overall lending activity among all reporting lenders in each of the nation's 341 metropolitan areas. These reports and copies of the individual reports are available at central depositories. Data from the loan application register will be available on magnetic tape and personal computer diskettes from the FFIEC.

Like the HMDA data for 1990, the data for 1991 indicate that rates of credit denial are higher for black and Hispanic loan applicants than for Asian and white applicants, even when applicants are in

1. The FFIEC consists of representatives from the five financial regulatory agencies: the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS).

the same income bracket. Also, analysis of the data shows that the rate of loan denial generally increases with an increase in the proportion of minority residents in a neighborhood. Income levels account for some of the variation in loan-disposition rates among racial groups. However, even after controlling for income, white applicants for conventional home loans in all income groups had lower rates of denial than black and Hispanic applicants.

The HMDA data alone are not sufficient to determine whether a lender is discriminating unlawfully. Specifically, the data do not reflect the wide range of financial and property-related factors that lenders consider in evaluating loan applications. The data do provide a means for targeting specific application files to review and for generating questions to ask of the institution's management. Examiners evaluate targeted files by applying the lender's underwriting standards to the application data to determine whether the applicant received fair treatment.

In November the Board adopted an amendment to Regulation C that will expand HMDA coverage of nondepository mortgage companies in metropolitan areas. Previously such lenders, like depository institutions, were covered only if their assets exceeded $10 million in the preceding calendar year. A statutory provision contained in the Federal Deposit Insurance Corporation Improvement Act (FDICIA) directed the Board to set a new exemption standard for mortgage companies comparable to the asset test for depository institutions. Under the revised regulation, nondepository mortgage lenders continue to be covered by HMDA if their assets exceed $10 million; they are also covered if they originated 100 or more home-purchase loans in the preceding calendar year.

In December the Board solicited comments on a proposal requiring earlier public access to the HMDA data to implement an amendment to the act made by the Housing and Community Development Act of 1992. Under the proposal, covered lenders will make disclosure statements available to the public within three business days, instead of thirty days, after receiving the statements from supervisory agencies. Also, they will make a copy of their loan application register available to the public beginning March 31, 1993; to protect the privacy of mortgage applicants and borrowers, they will delete certain items—the loan or application number, the date of application, and the date action was taken.

The FFIEC issued a revised version of *A Guide to HMDA Reporting, Getting it Right,* to assist institutions. The comprehensive guide discusses the law's requirements, coverage, and management responsibilities; it also sets forth detailed directions for gathering data, plus step-by-step instructions for completing the reporting form.

Regulation Z (Truth in Lending)

In July the Board adopted a final rule regarding home equity disclosures and laws dealing with lines of credit to executive officers. The revision of Regulation Z resolved a conflict between the home equity disclosure rules and regulations on loans to bank executive officers. A demand provision in loans to executive officers is required by the Federal Reserve Act and Regulation O (Loans to Executive Officers, Directors, and Principal Shareholders of Member Banks), but a demand provision is generally prohibited by the home equity rules in Regulation Z. To resolve the conflict, the final rule provides a limited exception in Regulation Z for transactions involving bank officers.

Pursuant to the decision by the U.S. Court of Appeals for the District of Columbia Circuit in *Consumers Union of U.S., Inc. v. Board of Governors* (938 F.2d 266), the Board reconsidered whether to require disclosure of the discounted initial rate and certain payment examples for each payment option in home equity lines offered to consumers.[2] After further analysis and a review of comment letters, the Board left the existing rules unchanged. The Board concluded that the current requirements provide the most useful information to consumers and fulfill congressional intent.

In November, the Board acted under authority granted by the Depository Institutions Disaster Relief Act of 1992 (DIDRA), and created an exception to the three-day delay period normally applicable to disbursement of funds in credit transactions (other than purchase money) secured by a consumer's home. The exception provides easier access to funds in emergency situations for transactions that take place (or for creditors that are located) in areas of Florida, Hawaii, Louisiana, and Los Angeles declared to be disaster areas by the President. Lenders have the option to routinely accept a consumer's waiver of the right to rescind and are permitted to use preprinted waiver forms. The exception expires one year from the enactment of DIDRA (October 23, 1992) or from the date the area was declared a disaster, whichever is earlier.

2. Consumers Union challenged certain provisions of the Home Equity Loan Consumer Protection Act. The U.S. District Court for the District of Columbia rendered a decision in favor of the Board on several aspects of the lawsuit (*Consumers Union of U.S., Inc. v. Board of Governors*, 736 F. Supp. 337). On appeal by Consumers Union, the D.C. Circuit decided in favor of the Board on four issues and remanded two other issues for reconsideration by the Board. The Board proposed amendments in response to the decision but did not adopt them.

Regulation CC (Expedited Funds Availability)

In August the Board issued final amendments to Regulation CC pursuant to provisions in FDICIA. The amendments permit banks to extend, on an exception basis, holds on checks that usually require next-day and second-day availability, and permit one-time notices of exception holds in certain cases. The Board also made permanent the availability schedules for deposits at nonproprietary automated teller machines and reaffirmed administrative enforcement authority of federal regulatory agencies over U.S. offices and branches of foreign banks.

In December the Board published a pamphlet entitled *Guide to Regulation CC Compliance*. It identifies five areas that pose problems for institutions and are frequently cited as violations: providing a specific availability-policy disclosure, training employees to ensure compliance, posting the availability policy where employees accept deposits, providing the deposit availability notice on preprinted deposit slips, and providing next-day availability when required. The pamphlet discusses these problems in detail to increase understanding of Regulation CC and to minimize compliance problems.

Regulation DD (Truth in Savings)

In September the Board adopted Regulation DD to implement the Truth in Savings Act (TISA). The act's effective date was originally set for March 21, 1993, but in late 1992 was extended three months by the Congress. The final regulation closely reflected the statutory provisions and addressed many of the concerns raised by more than 1,400 comment letters. The Board exercised its regulatory authority judiciously by creating exceptions when necessary to further the purposes of the act.

Regulation DD requires depository institutions to disclose to consumers before they open an account the costs and other features related to the account, the interest rate, and the annual percentage yield. Institutions must calculate interest on the full amount of principal on deposit in the account for each day and are prohibited from using a "low-balance method" or "investable-balance method" to calculate interest. Account disclosures are to state an annual percentage yield (APY), an interest rate, and the period of time that the interest rate will be in effect. Other disclosures apply to the minimum balance required to open the account, to avoid fees, or to obtain the APY; the balance computation method; the name and description of any fees for maintaining the account; any limitations on the number or amount of withdrawals and deposits or on checks that may be written on an account for any period; any early withdrawal penalties; and details regarding renewal policies.

For variable-rate accounts, disclosures will alert the consumer to potential rate changes and the frequency of such changes. Special maturity notices will be given for time deposit accounts and will differ for rollover and nonrollover accounts. When a change in one of the disclosed terms may reduce the APY or adversely affect the consumer, the institution is required to give advance notice. Although periodic statements are not required, if institutions provide statements they must include information regarding fees imposed, the total number of days in the period, the interest earned, and the annual percentage yield earned.

Because the new regulation governs advertising of deposit accounts, overlapping rules in Regulation Q (Interest on Deposits) will be eliminated on June 21, 1993—the mandatory compliance date for Regulation DD. Any rate advertised must be stated as an annual percentage yield, and no other rate except an interest rate may be shown. Other disclosures apply when the APY or a bonus is stated in the advertisement. Limited exceptions from certain advertising disclosures apply to broadcast or electronic media, outdoor media, telephone response machines, or lobby boards.

Besides delaying the compliance date, the Housing and Development Act amendments make a minor change to the advertising rules and modify a notice provision. In December the Board issued proposed amendments to the regulation to implement the changes, and proposed interpretations to provide guidance on other issues raised by institutions since the Board released the final rule in September 1992.

The Board is conducting a two-phase cost study of the law's effect. In November 1992 the Board sent out more than 4,000 surveys to financial institutions covering, for the first phase, pre-implementation account practices and, for the second phase, start-up compliance costs and any changes in account practices attributable to the regulation. Replies for the second phase are anticipated in July 1993. The study will provide an assessment of the effect of TISA on the financial industry and, in general, the extent of regulatory costs.

In conjunction with the cost study, the Board has arranged for the University of Michigan to conduct a telephone survey among consumers in 1993. It will assess consumer knowledge of deposit accounts and bank practices before

Regulation DD goes into effect. Some time after the effective date, another survey will be taken. The two surveys will be used to provide data on the benefits of the TISA to consumers.

Interpretations

In 1992 the Board continued to offer legal interpretations and guidance through official staff commentaries. These commentaries, intended to help financial institutions and others apply the regulations to specific situations, are updated periodically to address significant questions that arise.

In April the Board issued revisions to the staff commentary to Regulation B to clarify the relationship with Regulation C in regard to data collection. Both regulations require lenders to collect data on home loan applications about the race or national origin of applicants or borrowers. Loan brokers, correspondents, or others who are prohibited from collecting monitoring information under Regulation B will not be in violation when they collect the data for a creditor that is subject to Regulation C.

In December the Board proposed revisions to the commentary to Regulation Z. Disclosures about collateral securing a transaction need not specify whether the security interest is newly acquired or existing. The proposed revision also states that the model form for rescission, when refinancing with an original creditor, adequately discloses the existence of a security interest when a new one is acquired. Consistent with the rule applicable to home equity lines, the proposed commentary would provide that if an institution retains the ability to demand payment of a loan in its closed-end credit agreement with its executive officers to the extent required by federal law, the institution need not provide demand disclosures.

The Board published a proposed policy statement on branch closings to help depository institutions comply with a FDICIA requirement. Covered institutions must adopt a written branch closing policy and provide ninety days' notice of any proposed branch closing to customers and to their federal regulator. The notice to the regulator must detail the reasons behind the decision and give supporting statistical information. A notice of the decision must be posted at the branch thirty days before its closing.

Community Affairs

Through its community affairs program, the Federal Reserve System conducts outreach, education, and technical assistance activities to help financial institutions and the public understand and address community development and reinvestment issues. During 1992, the Reserve Banks increased the resources devoted to community affairs activities so that they could respond to an increase in the number of requests from banks and others for assistance and information on the Community Reinvestment Act (CRA), fair lending, and community development. The Reserve Banks also increased their efforts to work with financial institutions, banking associations, governmental entities, businesses, and community groups to develop community development lending programs that help finance affordable housing, small and minority businesses, and other community revitalization projects. The Federal Reserve's community affairs program responded to several federal and state legislative inquiries and initiatives involving the CRA and bank involvement in community development.

Various community affairs initiatives addressed growing concerns related to the availability of credit to minority borrowers and communities. The Federal

Reserve Bank of Kansas City sponsored a conference for bankers on "Credit and the Economically Disadvantaged," focusing on barriers faced by minority borrowers and steps banks can institute to ensure that credit is offered on an equitable basis. The Boston and New York Reserve Banks cosponsored a conference on credit issues affecting Native Americans, especially those living on reservations, in pursuing economic development programs.

Also, as part of the community affairs program, the Board updated its publication, *Directory: Bank Holding Company Community Development Investments*, which presents profiles of community development corporations (CDCs), limited partnerships, and other community development projects in which bank holding companies have been allowed to invest. Community affairs staff members responded to inquiries from banks and bank holding companies concerning investments in CDCs and in limited partnerships or equity pools for low-income housing. Legislation authorizing state member banks to make community development investments, enacted in late 1992, is expected to stimulate additional interest.

Two Reserve Banks supported collaborative multibank approaches to lending and investment to promote community development. The Atlanta Reserve Bank provided technical assistance to help create consortium CDCs or loan funds in Florida and Mississippi. The San Francisco Reserve Bank assisted financial institutions in San Diego to help create a multibank CDC that focuses on small business financing and also worked with institutions in Nevada and the State of Washington to form statewide reinvestment corporations.

Several Reserve Banks developed new educational programs for bankers. The Boston Reserve Bank created a new community development curriculum for bankers, and the Kansas City Reserve Bank conducted a series of seminars on community development lending, primarily for bankers in smaller communities. The Chicago and Minneapolis Reserve Banks cosponsored two seminars on rural community development. The San Francisco, Atlanta, and Philadelphia Reserve Banks sponsored CRA seminars targeted specifically to members of boards of directors and senior management of commercial banks.

Overall, the Reserve Banks' Community Affairs programs sponsored or cosponsored more than 110 conferences and seminars on fair lending, community development, and reinvestment topics. Often in these programs, the Reserve Banks worked with state bankers associations. Also, Community Affairs staff members of the Board and the Reserve Banks made more than 300 presentations at conferences, seminars, and meetings that were sponsored by banking, governmental, business, and community organizations.

In conjunction with outreach efforts, the Philadelphia, St. Louis, and San Francisco Reserve Banks developed and published community profiles that identify key community and economic development needs and describe resource organizations in major communities in their Districts. These profiles are available to banks and to community and business organizations to help stimulate collaborative approaches. The Philadelphia Reserve Bank's profile covered community needs and opportunities in the Vineland, New Jersey, area. Discussions with financial institutions serving that area led to the creation of a lenders council that addresses community development and reinvestment issues.

Staff members of the Reserve Banks in community affairs continued to support the Federal Reserve's supervisory responsibilities. Reserve Bank staff members were increasingly called on for direct technical assistance to help individual institutions with less-than-satisfactory CRA ratings strengthen their CRA programs. Several Reserve Banks also assisted in conducting HMDA analyses to help target institutions and areas for educational and technical assistance activities related to the CRA and fair lending. The Board's community affairs staff, working with Reserve Bank examiners, revamped and conducted a one-week seminar on advanced CRA examination techniques for consumer affairs examiners. The Board's staff also presented a special course segment for senior commercial examiners on community development lending and investment by banks.

FFIEC and Other Interagency Activities

The Board and the other banking agencies undertake certain initiatives to ensure compliance with the CRA and fair lending laws through the FFIEC, an interagency body that prescribes uniform principles, standards, and report forms for the examination of financial institutions at the federal level.[3] Through the FFIEC, the agencies acted to refine and strengthen enforcement of fair lending laws, provide education and training in CRA responsibilities, and identify and promote successful techniques that ensure equal treatment of loan applicants.

Regarding CRA responsibilities, the FFIEC took the following actions. In March 1992, the banking agencies amended the CRA guidelines to clarify that examiners should view favorably an institution's working through minority financial institutions to help serve the credit needs of low-income and minority households. In April, the FFIEC updated the series of interagency questions and answers that provides financial institutions with guidance on how to meet their CRA responsibilities. In June, the FFIEC offered clarification on the level of recordkeeping and documentation financial institutions need to maintain, along with the issuance of new examination procedures for the CRA.

In the area of fair lending, the FFIEC took several actions. In March, the agencies distributed to the institutions they supervise a brochure, prepared jointly through the FFIEC, entitled *Home Mortgage Lending and Equal Treatment.* The brochure identifies and cautions lenders about lending standards and practices that may produce unintended discriminatory effects. It focuses on discrimination based on race and includes examples of subtle forms of discrimination, such as unduly conservative appraisal practices that may lead to rejection or reduced loan amounts for property in minority areas; property standards, such as size and age, which may exclude homes in minority and low-income areas; and unrealistically high minimum-loan amounts. The Federal Reserve published a brochure in 1991, entitled *Home Mortgages: Understanding the Process and Your Right to Fair Lending,* to inform consumers about the mortgage application process and about their rights under fair lending and consumer protection laws. In December, the FFIEC contracted with an outside consultant for a review of the agencies' examination procedures to enforce civil rights laws. The contractor will examine the existing training and other procedures and recommend improvements. In the meantime, the FFIEC's task force on consumer compliance is revising an

3. For the member-agencies of the FFIEC, see p. 186, note 1.

interagency policy statement on the enforcement of the ECOA and the Fair Housing Act and is working on the supervisory enforcement policy for the two statutes.

Federal financial regulators continue to pursue discussions with the Department of Justice, HUD, and the Federal Trade Commission to strengthen enforcement of civil rights laws with regard to lending. Amendments to the Fair Housing Act in 1990 strengthened HUD's enforcement authority, and HUD and the banking regulators have entered into a memorandum of understanding to refer to each other, and to coordinate their investigation of, complaints alleging fair housing violations. The banking agencies are also exploring ways to work with the Department of Justice in detecting possible patterns of discrimination against minority applicants. Coordination among the regulatory agencies will generally enhance enforcement of fair lending laws and detection of possible discrimination and may produce new techniques to uncover unlawful discrimination.

The agencies took further actions to improve enforcement of fair lending laws—through HMDA-based targeting of institutions with questionable lending patterns, revision of examination strategies to identify possible discrimination, and preparation of education programs on fair lending practices for industry. The agencies also encouraged financial institutions and their trade associations to strengthen their fair lending education for management, lending personnel, and consumers.

Mortgage Lending Discrimination

The data released under HMDA in October 1991 documented sharp contrasts in the credit experience of various racial and ethnic groups and raised concerns about possible discrimination in the mortgage lending process. The HMDA data for 1992 continued to show these disparate lending patterns.[4] Suggestions of possible discrimination were intensified by a major investigation of an Atlanta thrift institution completed in 1992 by the Department of Justice and a research study by the Federal Reserve Bank of Boston, both reporting evidence of disparate treatment of minorities by lenders.

Findings from the Boston Study

During 1992 the Federal Reserve Bank of Boston undertook a detailed study of lending in the Boston metropolitan area, in cooperation with the other federal banking agencies and HUD. The study was initiated in response to the large differences in rates of denial of home loan applications among whites, blacks, and Hispanics in Boston that were revealed by the 1990 HMDA data: a ratio of nearly three rejections for black and Hispanic applicants to one for white applicants. The study sought to analyze whether racial disparities in denial rates for mortgages among surveyed lenders reflected the equal application of legitimate credit standards.

Because the only financial data collected under HMDA are for income, the Boston Reserve Bank collected thirty-eight additional items of information pertaining to financial characteristics, employment experience, and credit history—information that lenders voluntarily provided from their files. The study revealed substantial differences based on financial and other economic

4. See Glenn B. Canner and Dolores S. Smith, "Expanded HMDA Data on Residential Lending: One Year Later," *Federal Reserve Bulletin*, vol. 78 (November 1992), pp. 801–27.

circumstances of typical white applicants and those of minority applicants. Statistical analysis also revealed, however, that after controlling for significant economic factors, unexplained differences remained in loan approval rates for black, Hispanic, and white applicants. Specifically, the model showed that minority applicants with the same economic and property characteristics as white applicants would be expected to experience a denial rate of 17 percent, as compared with an 11 percent rate for white applicants.

Racial or ethnic background was generally not found to be a factor in the case of clearly qualified or clearly unqualified applicants. Disparities were evident, however, among applicants with some negative characteristics (such as high debt or income ratios) or weaknesses in credit history. For such applicants, national origin or ethnic background appeared to be a consideration. The authors of the study suggest that differences in treatment may arise from differences in the level of assistance received from loan officers. The degree to which the findings reflect outright discrimination by individual loan officers and financial institutions in the market is unclear. The findings do confirm, however, that greater attention is needed to ensure the fairness of the mortgage lending process.

After the October release of the results of the Boston study, member agencies of the FFIEC issued a joint statement that addressed the issue of disparate treatment. In this statement, the agencies attempted to shift the focus from a debate about whether unequal treatment is occurring to an emphasis on initiatives that will ensure fair lending practices. The interagency statement reiterated concerns about fair treatment of applicants for mortgage loans. The statement pointed to the increase in the amount of empirical data suggesting that economic factors might not explain differences in denial rates.

Use of the Expanded HMDA Data

The HMDA data enable regulatory agencies to select specific loan files to review during on-site examinations and also to target specific lenders for more extensive fair lending and CRA investigations. Several of the supervisory agencies, as well as the Department of Justice, are using the new HMDA data to identify institutions to review, based either on the large disparities in denial rates among different racial groups or on the low number of applications from minority households in relation to the racial composition of the community. Acting in concert, the agencies are developing techniques using automated access to the data to detect evidence of differential treatment. Through these combined efforts, the agencies also seek to identify the factors that underlie disparate lending patterns.

A data analysis system recently implemented by several of the agencies seeks to maximize the usefulness of the HMDA data by allowing examiners to formulate and test specific hypotheses regarding lenders' treatment of different groups. The data available about loan applicants' race or ethnic origin, sex, and income—together with information on the disposition of loan applications—provides an opportunity to focus on the accessibility of home purchase and home improvement loans to certain groups of consumers. The analysis system enables examiners to determine whether disposition patterns (for example, rates of loan denial) differ significantly for one group of applicants compared with another. Examiners can also use this evaluation technique to select specific loan application files for on-site review.

The Federal Reserve routinely uses the expanded HMDA data to evaluate a lender's geographic delineation of its local CRA service area. Although many factors affect the selection of the primary area a lender seeks to serve, the HMDA data help determine whether the geographic distribution both of home loans extended and of applications received are consistent with the boundaries of the delineated community. If an institution's home lending activity is substantially outside its delineated community, examiners will require the institution to substantiate the low number of applications from the local community. In some instances, the lender may need to consider revising the boundaries of their local service area, for example, by expanding the area to be more in line with the geographic pattern of the home loans they provide. (The Board and the FDIC have initiatives under way to develop a computer-based mapping technology that will assist examiners in matching a bank's lending activity with the boundaries of its delineated community.)

Historically, examiners have used the HMDA data to assess lenders' compliance with the twelve assessment criteria established by the regulations that implement the CRA. Among these criteria, the HMDA data are used in evaluating the following factors:

- The geographic distribution of the institution's credit applications, extensions, and denials
- The institution's record of originating or purchasing residential mortgage loans, housing rehabilitation credit, home improvement loans, and loans to small businesses and farms within its community
- Evidence of prohibited, discriminatory, or other illegal credit practices.

The expanded data provide opportunities for a more comprehensive assessment of lending patterns. Over the past two years, the Federal Reserve, in consultation with the other banking agencies, has developed and implemented a computer-based system for analysis of HMDA data. The system uses both HMDA data and information from the U.S. Census of Population and Housing. For example, one of the analysis reports in the new system shows examiners how the residential lending performance of an institution compares with the performance of other lenders serving the same local community. If other institutions report significantly larger numbers of applications and home loans per housing unit, the institution being examined may be asked to focus on determining how to meet the credit needs of its community, perhaps by reassessing its marketing activities.

The HMDA data are being used by financial institutions themselves to develop strategies and programs (including a different mix of products) that will help them address the credit needs of the various segments of their communities. The data are one source of information for assessing the geographic distribution of their lending, as encouraged by the agencies' policy statement on geographic analysis. For community organizations and other members of the public, the HMDA data provide a basis for discussing the record of the lending institutions in their local communities, and for documenting protests of applications by banks for mergers and expansions.

Other Uses of HMDA Data

Considerable information about the home loan purchase and securitization activities of secondary market institutions, particularly government-sponsored enterprises, the Federal

National Mortgage Association (FNMA), the Federal Home Loan Mortgage Corporation (FHLMC), and the Government National Mortgage Association (GNMA), has long been publicly available. Before 1989, however, secondary market data were produced mostly in aggregate form. With the 1989 amendments to HMDA, covered lenders are required to identify secondary market purchasers by type of entity. As a consequence, the expanded HMDA data provide new opportunities to profile the characteristics of both the borrowers whose loans are purchased by secondary market entities and the neighborhoods in which those borrowers reside.

A paper delivered at FNMA's annual housing conference in May 1992 presented the first assessment of the HMDA data as it pertains to secondary market activity. That study, which focused on the 1990 HMDA data, revealed that the secondary market's loan purchase distributions, arranged by borrower and neighborhood characteristics, generally reflect those of loan origination patterns in the primary market. The borrower and locational characteristics of loans supported by GNMA guarantees accurately reflect that agency's specialization in government-backed loans, whereas the borrower and locational attributes of loans purchased or securitized by FNMA and FHLMC more closely align with the characteristics of borrowers relying on conventional home loans. The HMDA data also indicate that in the primary market, a somewhat larger share of conventional home loans is granted to borrowers whose incomes are below the median family income for the metropolitan area where they reside than is true for the loans purchased or securitized by FNMA and FHLMC

The expanded HMDA data provide an important database for HUD's Office of Federal Housing Enterprise Oversight, the new secondary market regulatory agency established by statute. The information can be used to help assess the success of efforts made by FNMA and FHLMC in reaching certain statutory mandates for supporting loans to moderate-income homebuyers and properties located in central-city neighborhoods.

Compliance with Consumer Regulations

Data received from the five federal agencies that supervise financial institutions and from other federal supervisory agencies indicate that compliance with the Expedited Funds Availability Act decreased from 1991 levels, whereas compliance with the Truth in Lending Act, the Equal Credit Opportunity Act, and the Electronic Fund Transfer Act remained essentially unchanged. This section summarizes these compliance data for the reporting period July 1, 1991, to June 30, 1992.[5]

Equal Credit Opportunity Act (Regulation B)

The financial regulatory agencies reported that compliance with Regulation B remained about the same as in 1991. In the 1992 reporting period, 57 percent of examined institutions were in compliance with the Equal Credit Opportunity Act (ECOA) compared with 58 percent for 1991. Four agencies that were able to provide the frequency of violations (the Board, the NCUA, the OCC, and the OTS) reported that of the institutions examined that were not in full compliance, 77 percent had between one and

5. Not all the federal agencies that regulate financial institutions use the same method to compile compliance data. However, the data support the general conclusions presented here.

five violations—an improvement over the 73 percent reported for 1991. The most frequent violations involved the failure to take the following actions:

- Notify the applicant of the action taken within thirty days of the date that the creditor receives a completed application
- Provide a written notice of adverse action that contains a statement of the action taken, the name and address of the creditor, the ECOA notice, and the name and address of the federal agency that enforces compliance
- Provide the specific reasons for adverse action
- Follow the prescribed form of the ECOA notice
- Request information for monitoring purposes about race or national origin, sex, marital status, and age on credit applications primarily for the purchase or refinancing of a primary dwelling.

The Board issued two written agreements, one cease-and-desist order, and one civil money penalty involving violations of Regulation B. The OTS issued one cease-and-desist order and imposed eighteen civil money penalties. The FDIC issued three cease-and-desist orders involving Regulation B.

The Federal Trade Commission (FTC) obtained a consent judgment against a large mortgage company for the failure to retain records of rejected applications as required under Regulation B. The FTC also obtained consent judgments against related lenders in cases alleging age, sex, and marital status discrimination.

The Farm Credit Administration (FCA) reported a satisfactory level of compliance with ECOA. As a result of examinations and enforcement activities, the FCA took formal actions against three institutions for violations of Regulation Z or Regulation B or both. These institutions are now in substantial compliance. The total number of violations decreased 8 percent from 1991 levels.

The other agencies that enforce ECOA—the Department of Transportation, the Interstate Commerce Commission, the Small Business Administration, the Packers and Stockyards Administration of the Department of Agriculture, and the Securities and Exchange Commission—reported substantial compliance by the institutions they supervise.

Electronic Fund Transfer Act (Regulation E)

The financial regulatory agencies found that, at 85 percent, the level of compliance with Regulation E remained similar to that in 1991. The following five rules were the most frequently violated provisions of Regulation E:

- Provide, in a timely manner, a written statement outlining the terms and conditions of the electronic fund transfer (EFT) service.
- Provide a summary of a consumer's liability for unauthorized EFTs.
- Provide a statement for each monthly cycle in which an EFT occurred, or at least quarterly if no transfer occurred.
- Provide a notice of the procedures for resolving alleged errors at least once each calendar year.
- Investigate and resolve alleged errors promptly.

The Board issued one written agreement and one cease-and-desist order involving violations of Regulation E. The OTS issued one cease-and-desist order and imposed one civil money penalty. The FTC reported ongoing litigation involving one telemarketing company that allegedly failed to obtain written authorization from consumers for preauthorized transfers.

Consumer Leasing (Regulation M)

The financial regulatory agencies reported substantial compliance with Regulation M, which implements the consumer leasing provisions of the Truth in Lending Act. More than 99 percent of examined institutions were in full compliance with the regulation. The violations the agencies noted involved the failure to provide disclosures that were clearly written, conspicuously displayed, and presented in logical sequence.

Truth in Lending Act (Regulation Z)

The data from the financial regulatory agencies show that, on average, 44 percent of examined institutions were in full compliance with Regulation Z, up slightly from 42 percent in 1991.[6] The Board, the NCUA, and the OCC showed increases in compliance, while the FDIC and the OTS reported declines. Four agencies were able to provide the frequency of violations (the Board, the NCUA, the OCC, and the OTS); they indicated that of the financial institutions examined that were not in full compliance, 57 percent had between one and five violations (the lowest frequency category), an improvement over the 53 percent reported for 1991.

The most frequent violations of Regulation Z observed by the five agencies were the failure to accurately disclose the finance charge, the annual percentage rate (APR), the amount financed, and the number, amounts, and timing of payments scheduled to repay the obligation; and the general failure to provide Truth in Lending disclosures that accurately reflected the terms of the legal obligation.

The Board issued two written agreements, one cease-and-desist order, and one civil money penalty involving violations of Regulation Z. The OTS issued four cease-and-desist orders and imposed eighteen civil money penalties. Under the Truth in Lending Policy Guide and interagency enforcement policy on Regulation Z, a total of 368 institutions supervised by the Board, the FDIC, the OCC, and the OTS refunded \$4.1 million on 23,967 accounts in 1992, compared with roughly \$5.7 million on 26,796 accounts in 1991.

The FTC continued its Truth in Lending enforcement program and issued final consent orders in three cases involving the understatement of credit costs, including the APR and finance charge, in violation of Regulation Z. In its enforcement efforts against telemarketing and other frauds on consumers regarding credit card overcharges, the FTC entered a consent judgment against an individual in the marketing of travel certificates. The agency is litigating another case regarding distribution of redress funds to consumers who purchased vacation packages from defendants.

Educating consumers and businesses about their rights and responsibilities is an integral part of the FTC's enforcement activities. In this effort, the FTC released a publication on reverse mortgages and updated publications on refinancing home mortgages and on exercising the right of rescission under Regulation Z.

Other agencies found that the institutions they supervise were generally in compliance with Regulation Z. The Department of Transportation reported a satisfactory level of compliance with

6. The percentage of institutions in full compliance with the regulations given in this report is calculated using a straight average of the percentage of institutions in compliance as reported by the five financial regulatory agencies.

Regulation Z by foreign and domestic carriers. Consumer inquiries that were investigated resulted in no formal enforcement proceedings for violations. The FCA reported that violations had decreased more than 16 percent from the 1991 reporting period. As a result of examinations and enforcement activities, the FCA took formal actions against three institutions for violations of Regulation Z or Regulation B or both. These institutions are now in substantial compliance with the regulations. The Packers and Stockyards Administration of the Department of Agriculture received no complaints and initiated no enforcement actions. It believes that individuals and firms it regulates are in substantial compliance.

Community Reinvestment Act (Regulation BB)

The Community Reinvestment Act (CRA) requires the Board to encourage financial institutions under its jurisdiction to help meet the credit needs of their entire communities, including low- and moderate-income neighborhoods, in a manner consistent with safe and sound banking practices. The Board, the OCC, the FDIC, and the OTS assess the CRA performance of the institutions they supervise during regular compliance examinations and take the CRA record into account, along with other factors, when acting on certain applications.

The Federal Reserve System maintains a three-faceted program for enforcing and fostering better bank performance under the CRA:

- Examination of institutions to assess compliance
- Dissemination of information on community development techniques to bankers and the public through community affairs offices at Reserve Banks
- Analyses of CRA compliance when processing applications from bank and bank holding companies.

Federal Reserve examiners review performance in fair lending, community revitalization, and other relevant areas to assess CRA compliance. During the 1991 reporting period (July 1, 1991, through June 30, 1992), they conducted 711 examinations for compliance with the consumer laws, including those that address fair lending, and 674 for compliance with the CRA. During the reporting period, 93 banks received outstanding ratings for meeting community credit needs, 523 received satisfactory ratings, 52 received "needs to improve" ratings, and 6 received "substantial noncompliance" ratings. When appropriate, examiners suggested ways to improve CRA performance.

In March the Board issued a policy statement to reiterate the need for institutions to analyze the geographic distribution of their lending patterns as part of the CRA planning process. The Board encouraged institutions to document these analyses and to make them accessible to examiners. Such analyses represent one of the twelve factors considered by the agencies in assessing CRA performance.

In June, the FFIEC adopted revised CRA examination procedures. Although the agencies expect a reasonable level of documentation of an institution's CRA record, the new procedures emphasize that the predominant concern under the CRA is the degree to which an institution is helping to meet the credit needs in all areas of its community. The FFIEC also released *A Citizen's Guide to the CRA* to increase awareness and understanding of the act. The guide reviews the background of the CRA, the policies and procedures of the enforcement agencies, and the 1990 changes to the CRA. As a part of the Financial Institutions

Reform, Recovery and Enforcement Act of 1989 (FIRREA), effective July 1990, regulatory agencies were required to make institutions' CRA ratings available to the public and to include public discussion and involvement in the CRA process. It describes the public role in the CRA process and how public opinion is regarded in evaluating certain types of applications.

The examination procedures also implement a provision contained in FDICIA relating to notice of branch closings and to giving favorable consideration in CRA evaluations to an institution that donates, sells on favorable terms, or makes available on a rent-free basis branch facilities in minority neighborhoods to minority- or women-owned depository institutions. The Housing and Community Development Act of 1992, enacted in October, adds another provision, directing the agencies to give favorable consideration to certain institutions. These institutions are those that have engaged in capital investments, loan participations, or other ventures in cooperation with minority- and women-owned institutions and low-income credit unions to help meet the credit needs of the communities in which such institutions and credit unions are chartered.

During calendar year 1992, adverse CRA ratings were at issue in forty-five applications from banks and bank holding companies received by the Federal Reserve System, an increase over the number in previous years. Thirty-one such applications posed CRA ratings issues in 1991, and forty-two in 1990. The number of applications that were protested because of CRA performance also increased: twenty-nine applications were protested in 1992, compared with twenty-four in 1991 and twenty-seven in 1990. Of the thirty, nine also contained ratings issues and are included in the total count of forty-four for calendar year 1992. At year-end, twenty-three of the protested applications had been approved and six were still pending.

In March 1992, the Board approved an application by BankAmerica Corporation to merge with Security Pacific Corporation. The Board received almost 350 comments on that application and held four public meetings—in California, Washington, and Arizona—at which approximately 175 commenters provided testimony.

The Board denied an application by Gore-Bronson Bancorp, Incorporated, an Illinois corporation, to acquire indirectly 96.3 percent of the voting shares of Water Tower Trust and Savings Bank. The Board denied the application based on the CRA performance records of Gore-Bronson's two bank subsidiaries and of Water Tower Trust and Savings Bank, as well as on considerations of financial and future prospects.

Expedited Funds Availability Act (Regulation CC)

The financial regulatory agencies reported that the level of compliance with Regulation CC declined from 73 percent in the 1991 reporting period to 69 percent in 1992. The four agencies that were able to provide the frequency of violations (the Board, the NCUA, the OCC, and the OTS) reported that of the institutions examined that were not in full compliance, 85 percent had between one and five violations. The most frequent violations of Regulation CC were the failure to take the following actions:

- Provide next-day availability as required for certain items
- Provide a written notice when the time is extended for the availability of funds
- Provide two-day availability for local checks

• Adequately train employees and provide procedures to ensure compliance

• Follow certain procedures for exceptions for large deposits.

The Board issued one written agreement and one cease-and-desist order involving violations of Regulation CC. The OTS issued one cease-and-desist order and imposed seven civil money penalties.

Economic Effects of the Electronic Fund Transfer Act

In keeping with statutory requirements, the Board monitors the effect of the Electronic Fund Transfer Act on the compliance costs and consumer benefits from EFT services. In 1992, there were no new requirements or changes in the regulation that altered the economic effect of the act.

A large number of consumer accounts and financial institutions are covered by the act. In 1992, about three-fourths of all households in the United States had one or more EFT features on accounts at financial institutions. About two-thirds of all banks and thrift institutions offered EFT services and were covered by the act. Because of continued growth in the availability and use of EFT services, the economic effect of the act increased in 1992.

Automated teller machines (ATMs) are the most widely used EFT service in the United States. Most of the nation's depository institutions offer consumers access to ATMs, and more than half of all households currently have ATM access cards. ATM services have become more widely available with the continuing expansion of shared networks. Almost all ATM terminals in operation today participate in one or more shared networks. The monthly average number of ATM transactions increased about 13 percent, from 535 million in 1991 to 605 million in 1992. During the same period, the number of installed ATMs rose about 5 percent.

Direct deposit is another widely used EFT service. More than 40 percent of all U.S. households receive direct deposit of funds into their accounts. Direct deposit is particularly widespread in the public sector, with 54 percent of social security payments and about two-thirds of federal salary and retirement payments made by direct deposit. Although direct deposit is less common in the private sector, there too it has grown substantially in recent years.

Point-of-sale (POS) systems account for a small share of all EFT transactions, but their use grew rapidly in 1992. The volume of transactions on POS systems rose 31 percent, to 25.5 million a month; and the number of POS terminals rose 50 percent, to 117,000.

The benefits of the law are difficult to measure because they cannot be isolated from consumer protections that are provided even in the absence of regulation. The available evidence provides no indication of serious consumer problems with electronic transactions. In 1992, about 85 percent of depository institutions examined by federal agencies were in full compliance with Regulation E. Statistics indicate that institutions that are not in full compliance generally had fewer than five violations. The violations primarily involved the failure of institutions to provide one or more disclosures to consumers.

The Board's Consumer Complaint Control System provides another source of information on potential problems. In 1992, fifty-two of the complaints processed involved electronic transactions. The Federal Reserve System forwarded twenty-five complaints that did not involve state member banks to other agencies for resolution. Of the remaining twenty-seven complaints, one involved a violation of the act or regulation.

The Board also obtains information about potential problems from consumer surveys carried out by the University of Michigan. A December 1990 survey of consumer attitudes contained several Board-sponsored questions about consumer experience with EFT. The survey results suggest that EFT problems are relatively infrequent and that the vast majority of problems that do occur are resolved satisfactorily. Of the households that had accounts with EFT features, 7.5 percent reported having experienced EFT errors in the previous twelve months. This percentage is about the same as that reported in surveys from 1981 and 1983. In 1990, 88.0 percent of those experiencing problems had complained to the institution about the error, and 87.8 percent of the complainants reported that the error was resolved to their satisfaction.

The incremental costs associated with the EFTA are also difficult to quantify, again because the industry practices that would have evolved in the absence of the statutory requirements are unknown.

Complaints about State Member Banks

The Board and the Federal Reserve Banks investigate complaints against state member banks and forward to appropriate enforcement agencies complaints that involve other creditors or businesses. In 1992 the System received 2,586 complaints: 2,145 by mail, 427 by telephone, and 14 in person. The Federal Reserve investigated the 1,002 complaints that were against state member banks (see accompanying table). The System also received 1,778 oral and written inquiries about consumer credit and banking policies and practices. In responding to these complaints and inquiries, staff of the Board and the Reserve Banks gave specific explanations of laws, regulations, and banking practices and provided printed materials on the general issues.

A second table summarizes the nature and resolution of the 1,002 complaints against state member banks, eighty-one of which were pending at year-end. About 63 percent involved loan functions: 11 percent alleged discrimination on a prohibited basis, and 52 percent

Consumer Complaints to the Federal Reserve System Regarding Financial Institutions, by Subject and Institution, 1992

Subject	State member banks	Other institutions [1]	Total
Regulation B (Equal Credit Opportunity)	91	57	148
Regulation E (Electronic Fund Transfers)	27	25	52
Regulation Q (Interest on Deposits)	18	31	49
Regulation Z (Truth in Lending)	114	215	329
Regulation BB (Community Reinvestment)	1	4	5
Regulation CC (Expedited Funds Availability)	18	38	56
Fair Credit Reporting Act	21	72	93
Fair Debt Collection Practices Act	6	10	16
Fair Housing Act	7	4	11
Real Estate Settlement Procedures Act	0	4	4
Unregulated practices	699	1,124	1,823
Total	**1,002**	**1,584**	**2,586**

1. Complaints against these institutions were referred to the appropriate regulatory agencies.

concerned credit denial on nonprohibited bases (such as length of residency) and other unregulated lending practices (such as release or use of credit information). Approximately 25 percent involved disputes about interest on deposits and general deposit account practices. The remaining 12 percent concerned disputes regarding electronic fund transfers, trust services, and other miscellaneous bank practices.

In May 1992 the member-agencies of the FFIEC signed a memorandum of understanding with HUD regarding cooperation in the investigation of complaints alleging violations of the Fair Housing Act. In early June 1992 the Board sent the Reserve Banks procedures for investigating complaints alleging violations of the act by state member banks. As of December 1992 the Federal Reserve had referred nine such complaints to HUD under the memorandum; investigations completed by the Federal Reserve in six of the complaints revealed no evidence of discrimination. Three of the investigations were pending at year-end.

Consumer Complaints Received by the Federal Reserve System, by Function, Institution, and Resolution, 1992

Type of institution and resolution	Total	Function					
		Loans		Deposits	Electronic fund transfers	Trust services	Other
		Discrimination	Other				
Complaints about state member banks, by type							
Insufficient information[1]	25	1	13	8	0	0	3
Information furnished to complainant[2]	115	18	62	20	2	0	13
Bank legally correct							
No reimbursement or accommodation	447	59	232	107	17	4	28
Reimbursement or accommodation—goodwill[3]	170	10	113	33	1	1	12
Bank error							
No reimbursement	31	6	12	10	1	0	2
Reimbursement	62	1	29	19	2	0	11
Factual dispute[4]	34	2	11	16	0	3	2
Possible bank violation[5]	9	1	5	0	1	0	2
Matter in litigation[6]	13	0	5	4	3	0	1
Customer error	15	0	10	5	0	0	0
Pending, December 31	81	13	29	28	0	1	10
Total, state member banks	1,002	111	521	250	27	9	84
Percent	100	11	52	25	3	1	8
Complaints referred to other agencies	1,584	69	957	323	25	26	184
Total	**2,586**	**180**	**1,478**	**573**	**52**	**35**	**268**

1. The staff has been unable, after follow-up correspondence with the consumer, to obtain sufficient information to process the complaint.
2. When it appears that the complainant does not understand the law and that there has been no violation on the part of the bank, the Federal Reserve System explains the law in question and provides the complainant with other pertinent information.
3. The bank appears to be legally correct but has chosen to make an accommodation.
4. Involves a factual dispute not resolvable by the Federal Reserve System or a contractual dispute that can be resolved only by the courts. Consumers wishing to pursue the matter may be advised to seek legal counsel or legal aid or to use small claims court.
5. The Federal Reserve determined that a state member bank violated a law or regulation, and the bank took corrective measures voluntarily or as indicated by the Federal Reserve.
6. Parties are seeking resolution through the courts.

Unregulated Practices

In 1992 the Board continued to monitor, under section 18(f) of the Federal Trade Commission Act, complaints about banking practices not subject to existing regulations in order to focus on those that may be unfair or deceptive. Three categories each accounted for 10 percent or less of the 1,823 complaints: refinancings of real estate loans (182); denial of credit applications based on credit history (84); and debt collection tactics (55). Each of these categories account for a small number (7 percent or less) of all consumer complaints received by the System.

The mortgage refinancing complaints covered a wide variety of practices, including alleged delays by lenders in processing applications; lenders not refunding application fees in instances where refinancing applications were denied; and alleged failure by lenders to honor their lock-in commitments. Many of the complaints about credit denials based on credit history indicated that the applicant underestimated the importance lenders give to a poor credit history or a lack of borrowing experience when assessing the applicant's creditworthiness. The complaints about debt collection tactics were usually about the methods lenders employed to collect late payments or outstanding debts.

Consumer Advisory Council

The Consumer Advisory Council met in March, June, and October to advise the Board on its responsibilities under the consumer credit protection laws and on other issues dealing with financial services to consumers. The council's thirty members come from consumer and community-based organizations, financial institutions, academia, and state and local government. Council meetings are open to the public.

During 1992 the council considered a variety of topics including the Boston Reserve Bank's survey of mortgage lending practices in Boston, implementation of the Truth in Savings Act, the possible application of Regulation E to electronic benefit transfer programs, a review of CRA performance evaluations, lending patterns reflected by Home Mortgage Disclosure Act data, and other matters.

In March the council discussed amendments to the Equal Credit Opportunity Act giving mortgage loan applicants the right to receive copies of appraisal reports on properties associated with their loans.

In June, the council adopted a resolution that urged the lending industry and the regulatory community to conclude the debate about whether discrimination exists in mortgage lending and to begin focusing on how best to detect and remedy the problem. The committee also introduced a list of suggestions for how regulators, HUD, and mortgage lenders might strive to combat discrimination in lending.

A roundtable discussion, known as the Members Forum, gives council members the opportunity to offer their views on a variety of topics. During 1992 the council discussed matters such as whether there were any visible signs of an economic recovery within their industries or local economies and whether there was any evidence that obtaining a loan was becoming easier.

During the year, the council also considered the following issues:

- The burdens and benefits of consumer protection rules and the merits of possible actions that could be taken to reduce the regulatory burden associated with them
- Concerns about the consistency and quality of the publicly available CRA performance evaluations for individual

institutions within and among the banking agencies, and the type of information contained in the reports, including a statutory directive that examiners discuss the data they use to reach a conclusion about an institution's CRA efforts.

Testimony and Legislative Recommendations

The Board testified on matters relating to the 1990 HMDA data and to disclosures and substantive requirements for lease–purchase transactions.

Matters Relating to the 1990 HMDA Data

In May the Board testified in a joint hearing before the Subcommittee on Housing and Community Development and the Subcommittee on Consumer Affairs and Coinage, addressing concerns raised by the release of the 1990 HMDA data. The Board joined other agencies in discussing how best to address the disturbing statistics reflected in the rejection rates for Hispanic and black mortgage applicants compared with white applicants applying for mortgage loans. The Board provided information on how HMDA data would be used to strengthen fair lending enforcement and CRA activities.

Disclosures and Substantive Requirements for Lease–Purchase Transactions

The Board testified in June before a House banking subcommittee about the proposed Lease–Purchase Agreement Act, which would impose disclosure and substantive requirements on "lease–purchase" transactions, also known as rental–purchase or rent-to-own arrangements. Lease–purchase transactions are distinguishable from transactions covered by the Consumer Leasing or Truth in Lending laws. The lessee's ability to terminate the lease removes the lease–purchase transaction from coverage under Truth in Lending, and the month-to-month feature distinguishes it from the leases covered by the Consumer Lease Act, which covers leases of more than four months.

In its testimony, the Board noted that, with the high level of state legislation, it is not clear whether federal legislation is warranted. In 1983, the Board offered a legislative recommendation for amending the Consumer Leasing Act to expand its coverage of lease–purchase transactions, but the Congress did not enact the amendments. Since then, more than thirty states have enacted lease–purchase laws containing provisions similar to the bill introduced in 1983.

The Board made substantive and technical recommendations for revising the bill in the event federal legislation was deemed appropriate. The Board also suggested that, inasmuch as it has no supervisory role with the parties engaged in lease–purchase transactions, the Congress may find it more appropriate to designate another agency to issue the implementing rules.

Recommendations of Other Agencies

Each year the Board asks those agencies that have enforcement responsibilities under Regulations B, E, M, Z, and CC for recommendations of changes to the regulations or the underlying statutes. In 1992 the Department of Transportation (DOT) offered a recommendation regarding Truth in Lending. In its recommendation, the DOT noted that U.S. travel agents and carriers participating in the Airline Reporting Corporation (ARC) maintain a weekly sales and refund system. The short time frame of this system ensures compliance with a section of Regulation Z that requires a creditor to submit a credit card refund within seven business days. Because of documented financial losses by carriers resulting from the short processing requirement, however, ARC instituted new procedures for reporting, processing, and settling credit card refunds. The processing time for credit card refunds under the new procedures may exceed seven business days. If the Board determines that the new procedures fail to comply with Regulation Z, the DOT recommends that the Board amend the section or grant a waiver or exemption to allow the airline industry to retain the ARC procedures. ■

Litigation

During 1992, the Board of Governors was named in seventeen lawsuits, compared with twenty-seven in 1991. Seven new lawsuits were filed in 1992, one of which raised questions under the Bank Holding Company Act. As of December 31, 1992, nine cases were pending.

Bank Holding Companies—Antitrust Action

In *United States v. Society Corp.*, No. 92-CV0525 (N.D. Ohio, filed March 13, 1992), the Department of Justice challenged the acquisition by Society Corporation, a bank holding company, of Ameritrust Corporation under the antitrust laws. The Board had approved the transaction on February 13, 1992 (78 *Federal Reserve Bulletin* 302). The case was settled.

Bank Holding Company Act—Review of Board Actions

In *Synovus Financial Corporation v. Board of Governors*, No. 89–1394 (D.C. Circuit, filed June 21, 1989), petitioner sought review of a Board order dated May 22, 1989, approving the application of SouthTrust Corporation to acquire a national bank in Georgia by relocating an Alabama national bank subsidiary across state lines pursuant to 12 U.S.C. §30 (75 *Federal Reserve Bulletin* 516). On December 20, 1991, the Court of Appeals held that the Board has no authority over interstate relocations and vacated the Board's order (952 F.2d 426). Synovus's petition for a rehearing was denied on March 27, 1992.

In *Citicorp v. Board of Governors*, No. 90–4124 (2d Circuit, filed October 4, 1990), petitioner sought review of a Board order requiring Citicorp to terminate certain insurance activities by a nonbank subsidiary of Citicorp's subsidiary bank in Delaware (76 *Federal Reserve Bulletin* 977). On June 10, 1991, the Court of Appeals vacated the Board's order (936 F.2d 66). A petition for certiorari filed by the Independent Insurance Agents of America was denied on January 13, 1992 (112 S.Ct. 869).

In *First Interstate BancSystem of Montana, Inc. v. Board of Governors*, No. 91–1525 (D.C. Circuit, filed November 1, 1991), petitioner sought review of a Board order dated October 7, 1991, denying on Community Reinvestment Act grounds petitioner's application under section 3 of the Bank Holding Company Act to merge with Commerce Bancshares of Wyoming, (77 *Federal Reserve Bulletin* 1007). On December 14, 1992, the court dismissed the action on the parties' joint motion.

In *State of Idaho, Department of Finance v. Board of Governors*, No. 92–70107 (9th Circuit, filed February 24, 1992), petitioner sought review of a Board order determining, in accordance with *Synovus v. Board of Governors*, 952 F.2d 426 (D.C. Circuit 1991), that no application is required for a bank holding company to relocate its subsidiary bank across state lines. The case is pending.

Litigation Under the Financial Institutions Supervisory Act

In *Board of Governors v. Pharaon*, No. 91–CIV–6250 (S.D. New York, filed

September 17, 1991), the Board sought to freeze the assets of an individual pending administrative adjudication of a civil money penalty assessment by the Board. On September 17, 1991, the court issued an order temporarily restraining the transfer or disposition of the individual's assets. The order has been extended by agreement.

In *Board of Governors v. Shoaib*, No. CV 91–5152 (C.D. California, filed September 24, 1991), the Board sought to freeze the assets of an individual pending administrative adjudication of a civil money penalty assessment by the Board. On October 15, 1991, the court issued a preliminary injunction restraining the transfer or disposition of the individual's assets. The case is pending.

In *Greenberg v. Board of Governors*, No. 91–4200 (2nd Circuit, filed November 22, 1991), petitioners sought review of a Board order dated October 28, 1991, prohibiting former national bank officials from banking. The Board's orders were affirmed on June 19, 1992 (968 F.2d 164).

In *Davis v. Board of Governors*, No. 91–6972 (U.S. Supreme Court, filed December 4, 1991), petitioner sought review of *Burke v. Board of Governors*, 940 F.2d 1360 (10th Circuit 1991), in which the court of appeals upheld Board orders assessing civil money penalties and issuing orders of prohibition. The Supreme Court denied the petition for certiorari on May 18, 1992 (112 S.Ct. 1957).

In *Board of Governors v. bin Mahfouz*, No. 92–CIV–5096 (S.D. New York, filed July 8, 1992), the Board sought to freeze an individual's assets pending the administrative adjudication of civil money penalty assessment by the Board. On July 8, 1992, the court issued a temporary order restraining the transfer or disposition of the individual's assets. On October 30, 1992, the parties filed a stipulation of dismissal without prejudice.

In *CBC, Inc. v. Board of Governors*, No. 92–9572 (10th Circuit, filed December 2, 1992), petitioners seek review of a civil money penalty assessment against a bank holding company and three of its officers and directors for failure to comply with reporting requirements. The case is pending.

Other Actions

In *Fields v. Board of Governors*, No. 3:91CV7069 (N.D. Ohio, filed February 5, 1991), the plaintiff appeals the denial of a request for information under the Freedom of Information Act. The Board's motion for summary judgment was granted in part and its motion to dismiss was denied on June 23, 1992. The case is pending.

In *In Re Subpoena Served Upon the Board of Governors of the Federal Reserve System*, Nos. 91–5427 and 91–5428 (D.C. Circuit, filed December 27, 1991), the Board appealed from an order of the U.S. District Court requiring the Board and the Office of the Comptroller of the Currency to comply with a subpoena issued in a shareholder derivative suit against the Fleet/Norstar Financial Group seeking bank examination and deliberative information. On June 26, 1992, the Court of Appeals affirmed the District Court order in part, and remanded for further consideration of issues related to the privilege issue (967 F.2d 630). On August 6, 1992, the District Court ordered the matter held in abeyance pending settlement of the underlying action.

In *Zemel v. Board of Governors*, No. 92–1057 (D. District of Columbia, filed May 4, 1992), the plaintiff alleges discriminatory practices under the Age Discrimination in Employment Act. The case is pending.

In *Castro v. Board of Governors*, No. 92–1764 (D. District of Columbia, filed July 29, 1992), plaintiff appealed the denial of his request under the Freedom of Information Act. The action was dismissed on plaintiff's motion on November 30, 1992.

In *Fields v. Board of Governors*, No. 92–3920 (6th Circuit, filed September 14, 1992), plaintiff brought a Federal Tort Claims Act complaint alleging misrepresentation during the application process. The District Court for the Northern District of Ohio granted the Board's motion to dismiss on August 10, 1992. Plaintiff's appeal to the Sixth Circuit was voluntarily dismissed on December 18, 1992.

In *DLG Financial Corporation v. Board of Governors*, No. 392 Civ. 2086–G (N.D. Texas, filed October 9, 1992), plaintiffs seek to enjoin the Board and the Federal Reserve Bank of Dallas from taking certain enforcement actions, and seek money damages on a variety of tort and contract theories. On October 9, 1992, the court denied plaintiffs' motion for a temporary restraining order. The case is pending.

In *U.S. Check v. Board of Governors*, No. 92–2892 (D. District of Columbia, filed December 30, 1992), plaintiff seeks review of the denial of its request for information under the Freedom of Information Act. The case is pending. ■

Legislation Enacted

In 1992 the Congress enacted four pieces of legislation directly affecting the Federal Reserve or the institutions it regulates: the Depository Institutions Disaster Relief Act of 1992, the Federal Reserve Bank Branch Modernization Act, the Futures Trading Practices Act of 1992, and the Housing and Community Development Act of 1992.

Depository Institutions Disaster Relief Act of 1992

The Depository Institutions Disaster Relief Act of 1992, Public Law 102–485, was enacted on October 23, 1992. The major provisions of the act are as follows:

- When the President designates a major disaster area, any of the federal agencies that regulate financial institutions may exempt such institutions, for up to three years, from the real estate appraisal requirements of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 with respect to property in the disaster area if the agency determines that the exemption would facilitate recovery from the disaster and would be consistent with safety and soundness.
- For 180 days after enactment, the Board may make exceptions to the Truth in Lending Act and the Expedited Funds Availability Act with respect to transactions or depository institutions in a disaster area, with the exceptions expiring no later than the earlier of October 23, 1994, or one year following the President's determination of a disaster area.
- For eighteen months after enactment, the federal agencies that regulate financial institutions may permit, under specified conditions, certain insured depository institutions located in a major disaster area to subtract qualified assets attributable to the deposit of insurance proceeds from total assets in determining the institutions' leverage ratios.
- For 180 days after enactment, the appropriate regulatory agencies may take actions with respect to depository institutions, other regulated entities, or transactions in a major disaster area without complying with certain requirements of the Administrative Procedures Act; the agencies may also exempt such institutions from publication requirements relating to the establishment of branches or for other purposes.

The act also authorizes state member banks to make community development investments to promote the public welfare to the extent permissible under state law and subject to regulation by the Board. The Board generally may permit a state member bank to invest up to 5 percent of its capital in community development projects and may permit an adequately capitalized state member bank to invest up to 10 percent of its capital in such projects if the Board determines that the higher investment will not pose a significant risk to the insurance fund.

Federal Reserve Bank Branch Modernization Act

The Federal Reserve Bank Branch Modernization Act, Public Law 491, was enacted on October 24, 1992. The act removes a statutory $140 million cumulative ceiling on expenditures for all

Branch buildings of Federal Reserve Banks and substitutes a requirement of Board approval for the acquisition or construction of Branch buildings.

Futures Trading Practices Act of 1992

The Futures Trading Practices Act of 1992, Public Law 102–546, was enacted on October 28, 1992. The act reauthorizes the Commodity Futures Trading Commission (CFTC) for two years and contains a variety of measures relating to the regulation of the trading of futures and options contracts.

Title V of the act directs any contract market in stock index futures or options on stock index futures to submit to the Board any rule establishing or changing levels of either initial or maintenance margin on such contracts. The Board may request an exchange to set margins on stock index contracts at levels that the Board believes are appropriate to preserve the financial integrity of the exchange and its clearing system or to prevent systemic risk. The Board also may direct an exchange to amend its rules to effect the requested margin levels. The act permits the Board to delegate to the CFTC its authority over margin levels for stock index contracts.

Housing and Community Development Act of 1992

The Housing and Community Development Act of 1992, Public Law 102–550, was enacted on October 28, 1992. The act addresses housing, community development, crime, and other issues.

Title IX

Title IX, Subtitle A, of the act clarifies or amends a variety of regulatory and other programs as follows:

- The provisions of the Real Estate Settlement Procedures Act (RESPA) that prohibit the payment of "kickbacks" or other fees with respect to the provision of settlement services are to be understood as also applying to services relating to the origination and processing of mortgage loan applications.
- The coverage of RESPA is extended to refinancings and second mortgages.
- By amendment of the Community Reinvestment Act, federal bank regulatory agencies may consider certain ventures undertaken by a depository institution in cooperation with financial institutions owned by minorities or women and low-income credit unions as a factor in determining whether the depository institution is meeting the credit needs of local communities.
- The Board must, in consultation with the other federal regulators of depository institutions, submit within one year of the law's enactment a report to the Congress comparing residential, small business, and commercial lending by insured depository institutions in low-income, minority, and distressed areas to such lending in other areas.
- For any precomputed consumer credit transaction with a term of more than sixty-one months that is consummated after September 30, 1993, lenders must refund in full any unearned interest charged to a consumer that has prepaid the obligation, and it prohibits the use of the "rule of 78s" and other methods that are unfavorable to the consumer when calculating unearned interest.

Subtitle A also amends the Home Mortgage Disclosure Act of 1975 (HMDA) as follows:

- Depository institutions must make the information in loan application registers available upon request, subject to regulations of the Board concerning format and appropriate deletions.

• Depository institutions must maintain and disclose the information in loan application registers according to timetables in the act, and depository institutions may charge a reasonable fee for providing copies of the information.

• Depository institutions must make HMDA disclosure statements available to the public no later than three business days after receipt of the statements from the Federal Financial Institutions Examination Council.

• A timetable in the act shortens the period before initial public disclosure of loan application information statements and HMDA disclosure statements.

Subtitle B of Title IX contains the following provisions:

• By amendment of RESPA, lenders need not provide a loan applicant with a good faith estimate of real estate settlement costs and consumer information concerning settlement costs when the application is denied within three days of its receipt;

• Existing requirements for the establishment of a maximum interest rate on any adjustable rate mortgage are to be understood as applying only to consumer loans.

• Federal regulators of financial institutions may establish a limit below which an appraisal by a state-licensed or state-certified appraiser would not be required for real estate lending transactions by insured depository institutions, but the regulator must certify that establishment of the threshold does not represent a threat to the safety and soundness of the financial institutions it regulates.

• By amendment of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), the Board may exclude transactions from the limits on extensions of credit to insiders, if the Board determines such transactions pose a minimal risk, and it may exclude a depository institution's bank holding company from insider lending limits placed on shareholders of a depository institution.

• By amendment of FDICIA, regulations concerning safety and soundness required by FDICIA may not set specific levels or ranges on compensation of directors, officers, or employees of insured depository institutions.

• By amendment of the Truth in Savings Act, the effective date for compliance with regulations implementing that act are delayed and on-premises displays that include interest rate information are excluded from disclosure requirements if the displays include the annual percentage yield and indicate that further information can be obtained concerning terms of the account.

Title XV

Title XV of the act contains the Annunzio–Wylie Anti–Money Laundering Act. Portions of Subtitle A relate to insured depository institutions, as follows:

• The Federal Deposit Insurance Corporation (FDIC) may appoint itself as conservator or receiver for any insured state depository institution that has been convicted of money laundering.

• The FDIC must consider revoking the insurance of an insured state depository institution convicted of money laundering, and it may consider revocation of insurance for an insured state depository institution convicted of offenses related to the reporting of cash transactions.

• The Office of the Comptroller of the Currency (OCC) must consider revoking the franchise of any national bank or federal branch or agency of a foreign bank convicted of money laundering, and the OCC may consider revocation for any national bank or federal branch or agency of a foreign bank convicted of offenses related to the reporting of cash transactions.

• The Board must consider terminating a state agency, uninsured state branch, or state commercial lending company subsidiary of a foreign bank if any of these entities, or the foreign bank itself, is convicted of money laundering or offenses related to the reporting of cash transactions.

• A federal regulator of financial institutions may consider removing an institution-affiliated party who has violated requirements related to the reporting of cash transactions or had knowledge of certain violations concerning money laundering.

• A federal regulator of financial institutions may suspend or prohibit an institution-affiliated party charged with money laundering if continued service or participation by such party poses a threat to the depository institution, and the regulator must remove or prohibit any institution-affiliated party convicted of money laundering.

• A person convicted of money laundering cannot participate in the affairs of an insured depository institution except with the permission of the FDIC.

Portions of Subtitle B of Title XV relate to insured depository institutions and other financial institutions, as follows:

• The Department of the Treasury must prescribe regulations requiring depository institutions to identify customers that are defined as financial institutions under the rules for reporting cash transactions.

• A depository institution must not disclose the existence of Treasury orders subjecting the institution to special rules for recording and reporting cash transactions.

• When the Board and Treasury determine that records of payment orders transferring funds through wholesale funds transfer systems have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings, the agencies may jointly prescribe regulations concerning the maintenance of such records by insured depository institutions

• The Board and Treasury—after considering the degree of usefulness of records of payment orders that are related to international transactions in criminal, tax, or regulatory investigations or proceedings and the effect that such recordkeeping will have on the cost and efficiency of the payment system—must jointly prescribe regulations concerning the maintenance of records of such transfers made through wholesale transfer systems or on the books of an insured depository institution or a business that provides check cashing services, money transmittal services, or issuance or redemption of money orders, travelers' checks, or similar instruments.

• Treasury may require a financial institution to report any suspicious transaction; the financial institution must not disclose the existence of such reports to the parties involved in the transaction; and the institution is immune from potential liability under any law for reporting the transaction without notifying the parties to the transaction.

• Treasury may require financial institutions to carry out programs to deter and detect money laundering.

Subtitle F of Title XV authorizes Treasury to require insured depository institutions to request copies of cash transaction reports from any financial institution, other than another depository institution, that engages in any reportable transactions with the depository institution with respect to any earlier transactions involving the same coin, currency, or monetary instruments. ■

Banking Supervision and Regulation

The past year was in many respects a transitional period for the U.S. banking system and for the Federal Reserve's banking supervision and regulation activities. After having experienced weak profitability and a rise in problem assets for several years, the commercial banking industry in 1992 reported its highest profitability in more than a decade, and problem assets decreased. These achievements were possible in large part because of declining market interest rates. The industry's capital ratios also improved significantly from 1991, with the equity capital ratio reaching its highest point since 1966. Banking organizations drove up their capital ratios mainly by retaining a greater share of their profits and by issuing record amounts of new equity; these actions were taken in anticipation of the full phase-in of the international capital standards and in preparation for domestic banking legislation that went into effect at the end of 1992.

One consequence of this overall improvement was that the number of bank failures during 1992 was lower than had been anticipated. Nonetheless, the number of troubled and failed institutions remained high, and problem commercial real estate loans continued to stress much of the industry. Earlier efforts by banking organizations and the regulatory agencies to address the industry's problems and to strengthen lending standards had led to concerns about the availability of bank loans to creditworthy borrowers; those concerns persisted throughout 1992. Surveys of senior lending officers indicated that banks had generally taken measures to adopt more conservative lending policies and practices, in part in response to the losses associated with some laxities in the 1980s. Anecdotal evidence indicated that the move to tighten standards was caused, in part, by concerns that examiners were being overly critical in evaluating loans. Building on earlier policy statements, the Federal Reserve during the year further addressed possible disincentives to prudent bank lending. These efforts included continuing clarification of Federal Reserve policies to examiners and other supervisory staff members to promote realistic loan evaluation procedures.

The industry's recent problems gave rise in late 1991 to major legislation designed to improve banking and bank supervisory practices, generally with the purpose of reducing potential costs to the public. The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) contained numerous provisions covering broad aspects of bank lending and operating standards. Developing regulations to implement this statute was a major activity of the division during 1992 and will remain one throughout much of 1993. FDICIA specifies supervisory policies and actions for all banks, especially for those that are undercapitalized. The statute also directs the banking and thrift regulatory agencies to more formally address noncredit risks in bank capital standards and gives the Federal Reserve broader supervisory authority over foreign banks operating in the United States. Many provisions of FDICIA require the issuance of uniform rules by the banking and thrift regulatory agencies; as a consequence, the amount of interagency coordination on supervisory issues increased significantly during 1992.

The Congress enacted as part of FDICIA the Foreign Bank Supervision Enhancement Act of 1991 (FBSEA). This legislation expanded the authority of the Federal Reserve to regulate and supervise foreign banks conducting business in the United States. To implement the act, the Board issued interim amendments to Regulation K relating to the international banking operations of foreign banking organizations in the United States. In November 1992 the Board approved the final regulations. The Department of the Treasury and the Board also completed two joint studies required by FBSEA. The first study found that the Basle risk-based capital framework provides an appropriate basis for evaluating the capital equivalency of U.S. and foreign banks. The second study concluded that foreign banks should continue to operate branches in the United States pursuant to the International Banking Act of 1978, as amended, and FBSEA, as opposed to operating only through subsidiaries.

To meet its additional responsibilities, the Division of Banking Supervision and Regulation was reorganized in July, and the Division's authorized staff level was increased. Several new sections of the division were created to coordinate issues dealing with Federal Reserve Bank supervisory procedures, industry accounting practices, computerized information, enforcement activities, and foreign bank supervision.

Scope of Responsibilities for Supervision and Regulation

The Federal Reserve is the primary federal supervisor and regulator of all U.S. bank holding companies and of state-chartered commercial banks that are members of the Federal Reserve System. In its supervision of the general operations of these organizations, the Federal Reserve primarily seeks to promote their safety and soundness and their compliance with laws and regulations, including the Bank Secrecy Act and consumer and civil rights laws.[1] The Federal Reserve also reviews the following specialized activities of these institutions: electronic data processing, fiduciary activities, government securities dealing and brokering, municipal securities dealing and clearing, and securities underwriting and dealing through section 20 subsidiaries.

The Federal Reserve is responsible for the supervision of (1) all Edge Act corporations and agreement corporations, (2) the international operations of state member banks and U.S. bank holding companies, and (3) the operations of foreign banking companies in the United States.[2] In addition, the FBSEA increased the Federal Reserve's authority over branches, agencies, commercial lending subsidiaries, and representative offices of foreign banks in the United States with respect to the establishment, examination, and termination of such offices.

1. The Board's Division of Consumer and Community Affairs is responsibile for coordinating the Federal Reserve's supervisory activities with regard to the compliance of banking organizations with consumer and civil rights laws. To carry out this responsibility, institutions are examined by specially trained Reserve Bank examiners. The chapter of this REPORT covering consumer and community affairs describes these regulatory responsibilities. Compliance with other statutes and regulations, which is treated in this chapter, is the responsibility of the Board's Division of Banking Supervision and Regulation and the Reserve Banks, whose examiners check for safety and soundness.

2. Edge Act corporations are chartered by the Federal Reserve, and agreement corporations are chartered by the states, to provide all segments of the U.S. economy with a means of financing international trade, especially exporting.

The Federal Reserve also exercises important regulatory influence over the entry into, and the structure of, the U.S. banking system through its administration of the Bank Holding Company Act, the Bank Merger Act, and the Change in Bank Control Act for bank holding companies and state member banks. Also, the Federal Reserve is responsible for regulatory margin requirements on securities transactions. The Federal Reserve coordinates its supervisory activities with other federal and state regulatory agencies and with the bank regulatory agencies of other nations.

Supervision for Safety and Soundness

To ensure the safety and soundness of banking organizations, the Federal Reserve conducts on-site examinations, visitations, and inspections and off-site surveillance and monitoring, and it undertakes enforcement and other supervisory actions.

Examinations and Inspections

The on-site review of operations is an integral part of ensuring the safety and soundness of financial institutions. Examinations of state member banks, of branches and agencies of foreign banks, and of Edge Act and agreement corporations, as well as inspections of bank holding companies and their subsidiaries, entail (1) an appraisal of the quality of the institution's assets, (2) an evaluation of management, including internal policies, operations, and procedures, (3) an assessment of the key financial factors of capital, earnings, asset and liability management, and liquidity, and (4) a review for compliance with applicable laws and regulations.

State Member Banks

At the end of 1992, 957 state-chartered banks belonged to the Federal Reserve System, 25 fewer than at year-end 1991. These banks represented about 8 percent of all insured commercial banks and held about 17 percent of all insured commercial bank assets.

Federal Reserve guidelines call for all state member banks to be examined at least annually by either a Reserve Bank or state banking agency. Large or troubled banks must be examined at least annually by a Reserve Bank. Since December 19, 1992, FDICIA has required an on-site, full scope examination during each twelve-month period for all depository institutions; however, well-capitalized and well-managed institutions with assets of less than $100 million may be examined every eighteen months.

In conformance with Federal Reserve guidelines, all state member banks were examined at least once in 1992 except for five healthy, well-managed banks whose examinations were deferred into the first quarter of 1993. Altogether, the Reserve Banks conducted 815 examinations (some of them jointly with state agencies), and state banking departments conducted 368 independent examinations. Also in conformance with Federal Reserve guidelines, Reserve Bank officials held 261 meetings with directors of large state member banks as well as with directors of state member banks that displayed significant weaknesses.

Bank Holding Companies

At year-end 1992 the number of bank holding companies totaled 6,348, 93 fewer than at year-end 1991. These organizations controlled about 8,500 insured commercial banks and held approximately 93 percent of the assets of all insured commercial banks in the United States.

Federal Reserve guidelines call for annual inspections of large bank holding companies and smaller companies with significant nonbank assets. Small companies (those with assets of less than $150 million) that do not appear to have problems are inspected on a sample basis, and medium-sized companies that do not appear to have problems are inspected on a three-year cycle.

The inspection focuses on the operations of the parent holding company and its nonbank subsidiaries. In judging the condition of subsidiary banks, Federal Reserve examiners consult the examination reports of the federal and state banking authorities that have primary responsibility for the supervision of these banks. In 1992, 2,119 bank holding companies were inspected, 2,006 by Federal Reserve examiners and 113 by state examiners. The assignment of some examiners to work on other industry problems and major mergers and acquisitions in 1992 required the deferment to 1993 of 38 bank holding company inspections. During 1992, Reserve Bank officials held 575 meetings with the boards of directors of bank holding companies to discuss supervisory concerns.

Enforcement Actions, Civil Money Penalties, and Significant Criminal Referrals

In 1992 the Federal Reserve Banks recommended, and members of the Board's staff initiated and worked on, 255 formal enforcement cases involving 634 separate actions dealing with unsafe or unsound practices and violations of law. The actions included written agreements, cease-and-desist orders, removal and prohibition orders, and civil money penalties. Of these, 96 cases involving 176 actions were completed by year-end, including the assessment and collection of more than $230 million in civil money penalties. In addition to these enforcement actions, the staffs of the Board of Governors and several Reserve Banks during 1992 continued their investigation, the most extensive ever conducted by the Federal Reserve, regarding activities of the Bank of Credit and Commerce International (BCCI) in the United States and other countries. As a result of the investigation, which was continuing at year-end, the Board in 1992 initiated 43 actions. By year-end 1992, several of the BCCI actions had been completed, with the Board assessing more than $230 million in fines.

All final enforcement actions issued by the Board of Governors and all written agreements executed by the Federal Reserve Banks in 1992 are available to the public. In addition to formal enforcement actions, the Federal Reserve Banks initiated and worked on 356 informal enforcement actions and completed 336 of them through instruments such as memoranda of understanding with state member banks, bank holding companies, and foreign financial institutions subject to the jurisdiction of the Federal Reserve. The staff of the Board of Governors also obtained approximately $475 thousand in restitution to, and more than $9.4 million in capital infusions into, state member banks and bank holding companies through informal actions that were taken in lieu of the issuance of formal enforcement orders or agreements.

In 1992 the Division of Banking Supervision and Regulation forwarded 393 criminal referrals to the Fraud Section of the Criminal Division of the Department of Justice for inclusion in its significant referral tracking system.

Specialized Examinations

The Federal Reserve conducts specialized examinations in the following areas of bank activity: electronic data processing, fiduciary activities, dealing and brokering in government and municipal securities, and underwriting and dealing in securities through section 20 securities subsidiaries. The Federal Reserve also reviews state member banks and bank holding companies that act as transfer agents.

Electronic Data Processing

Under the Interagency EDP Examination Program, the Federal Reserve examines the electronic data processing activities of state member banks, Edge Act and agreement corporations, and independent data centers that provide EDP services to these institutions. In 1992 the Federal Reserve System also assumed supervisory responsibility for examining data centers associated with U.S. branches and agencies of foreign banks. The Federal Reserve conducted 364 on-site EDP reviews for the year. The Federal Reserve also was the agency-in-charge on 4 examinations of 13 large, independent data service providers conducted jointly with the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS).

Fiduciary Activities

The Federal Reserve has supervisory responsibility for institutions that hold more than $3.6 trillion of discretionary and nondiscretionary assets in various fiduciary capacities. This group of institutions includes 317 state-chartered member banks and trust companies and 53 nonmember trust companies that are subsidiaries of bank holding companies.

On-site examinations are essential to ensure the safety and soundness of financial institutions that have fiduciary operations. The scope of these examinations includes (1) an evaluation of management, policies, audit procedures, and risk management, (2) an appraisal of the quality of trust assets, (3) an assessment of earnings, (4) a review for conflicts of interest, and (5) a review for compliance with laws, regulations, and general fiduciary principles.

During 1992, Federal Reserve examiners conducted 200 on-site trust examinations of state member banks and trust companies engaged in fiduciary activities. The institutions examined in 1992 held more that $2.2 trillion in fiduciary assets.

Government Securities Dealers and Brokers

The Federal Reserve is responsible for examining state member banks and some foreign banks that are government securities dealers and brokers for their compliance with the Government Securities Act of 1986 and with regulations of the Department of the Treasury. Forty-four state member banks, three state branches of foreign banks, and one state agency of a foreign bank have notified the Board that that they are government securities dealers or brokers that are not otherwise exempt from Treasury regulations. During 1992 the Federal Reserve conducted twenty-six examinations of broker–dealer activities in government securities at state member banks and foreign banks.

Municipal Securities Dealers and Clearing Agencies

The Securities Act Amendments of 1975 made the Board responsible for supervising state member banks and bank holding companies that act as municipal securities dealers or as clearing agencies. Registered with the Board are forty-three banks that act as municipal securities dealers and three clearing agencies that act as custodians of securities involved in transactions settled by bookkeeping entries. In 1992 the Federal Reserve examined all three of the clearing agencies and twenty-two of the banks that deal in municipal securities.

Securities Subsidiaries of Bank Holding Companies

Section 20 of the Banking Act of 1933, commonly known as the Glass–Steagall Act, prohibits the affiliation of a member bank with a company that is "engaged principally" in underwriting or dealing in securities. The Board in 1987 approved proposals by banking organizations to underwrite and deal on a limited basis in specified classes of bank "ineligible" securities (that is, commercial paper, municipal revenue bonds, conventional residential mortgage-related securities, and securitized consumer loans) in a manner consistent with the Glass–Steagall Act and the Bank Holding Company Act. At that time the Board limited revenues from these newly approved activities to no more than 5 percent of total revenues for each securities subsidiary. This limit was subsequently increased in September 1989 to 10 percent.

In January 1989 the Board approved applications by five U.S. bank holding companies to underwrite and deal in corporate and sovereign debt and equity securities, subject in each case to reviews of managerial and operational infrastructure and other conditions and requirements specified by the Board. Four of these organizations subsequently received authorization to commence underwriting and dealing in corporate and sovereign debt securities, and two received authorization to commence equity underwriting and dealing in equity securities.

At year-end 1992, thirty foreign and domestic banking organizations had so-called section 20 subsidiaries authorized to underwrite and deal in ineligible securities. Of these subsidiaries, eight could underwrite all debt or equity securities; three could underwrite all debt securities; and eighteen could underwrite only the types of debt securities approved by the Board in 1987. The Federal Reserve uses specialized inspection procedures in reviewing operations of these securities subsidiaries. During 1992 the Federal Reserve conducted twenty-four inspections of section 20 subsidiaries.

Transfer Agents

Federal Reserve examiners conduct separate reviews of state member banks and bank holding companies that act as transfer agents. Transfer agents countersign and monitor the issuance of securities, register their transfer, and exchange or convert them. During 1992, System examiners reviewed 82 of the 177 banks and bank holding companies registered with the Board as transfer agents.

Surveillance and Monitoring

The Federal Reserve monitors the financial condition and performance of individual banking organizations and the banking system as a whole to identify areas of supervisory concern. Automated screening systems are used to identify organizations with poor or deteriorating financial profiles and to identify adverse trends affecting the banking system. Information from these systems are then used in decisions to allocate examination resources or take other appropriate supervisory actions. Among the automated systems used by the Federal Reserve to monitor banking organizations is the System to Estimate Examination Ratings (SEER), which is used to track the overall financial condition of individual organizations. SEER statistically estimates an institution's supervisory rating based on its quarterly Reports of Condition and Income. A number of supplementary screening systems are used to monitor specific areas of supervisory interest. Another automated system tracks examinations and inspections and summarizes the results and supervisory actions.

To assist supervisory staff in evaluating individual bank holding companies, the Federal Reserve produces and distributes the quarterly Bank Holding Company Performance Report, which provides detailed financial information on the condition and performance of each bank holding company. The Federal Reserve also produces several aggregate reports on the national and regional performance and condition of the banking industry.

Automated monitoring systems rely heavily on the information in regulatory reports filed by banking organizations. To ensure the timeliness and accuracy of the reports, the Federal Reserve maintains the Regulatory Reports Monitoring System to track domestic and foreign banking organizations that file late or inaccurately.

International Activities

The Federal Reserve is responsible for supervising international activities through various vehicles.

Edge Act and Agreement Corporations

Edge Act corporations are international banking organizations chartered by the Board to provide all segments of the U.S. economy with a means of financing international trade, especially exports. An agreement corporation is a company that enters into an agreement with the Board not to exercise any power that is impermissible for an Edge Act corporation. In 1992 the Federal Reserve examined all ninety-four Edge Act and agreement corporations, which held about $30 billion in total assets at year-end.

Foreign-Office Operations of U.S. Banking Organizations

The Federal Reserve examines the international operations of state member banks, Edge Act corporations, and bank holding companies, principally at the U.S. head offices of these organizations, where the ultimate responsibility for their foreign offices lies. In 1992 the Federal Reserve conducted full-scope and targeted-scope examinations of ten foreign branches of state member banks and forty-nine foreign subsidiaries of Edge Act corporations and bank holding companies. All of the examinations abroad were conducted with the cooperation of the supervisory authorities of the countries in which they took place; when applicable, the examinations were coordinated with the Office of the Comptroller of the Currency. Also, examiners made eighty-five visits to the overseas offices to obtain current financial and operating information and, in some instances, to evaluate their compliance with corrective measures or test-check their adherence to safe and sound practice.

U.S. Activities of Foreign Banks

Foreign banks continue to be significant participants in the U.S. banking system. As of year-end 1992, 288 foreign banks from 57 countries operated 502 state-licensed branches and agencies, of which 33 are insured by the FDIC. These foreign banks also operated 76 branches and agencies licensed by the OCC, of which 7 have FDIC insurance. Foreign banks also operated approximately 240 representative offices and directly owned 14 Edge Act corporations and 13 commercial lending companies. In addition, foreign banks held an interest of at least 25 percent in 117 U.S. commercial banks. Altogether, these foreign banks control approximately 21 percent of banking assets in the United States.

The Federal Reserve has broad authority to supervise and regulate foreign banks that engage in banking and related activities in the United States through branches, agencies, commercial lending companies, representative offices, Edge Act corporations, banks, and certain nonbanking companies. In 1992, 314 such offices were examined by the Federal Reserve together, in some cases, with state or other federal regulatory authorities.

Before the December 1991 passage of FBSEA, the Federal Reserve had residual authority to examine all branches, agencies, and commercial lending subsidiaries of foreign banks in the United States. The International Banking Act of 1978 instructed the Federal Reserve to use, to the extent possible, the examination reports of other state and federal regulators. The FBSEA amended the International Banking Act and increased the Federal Reserve's authority with respect to these foreign bank operations, including representative offices. The Federal Reserve has acted to ensure that all branches and agencies licensed by the state or federal government are examined on-site at least once during each twelve-month period. These examinations are usually coordinated with other state and federal regulators. The FBSEA also authorizes the Federal Reserve to terminate the operations of foreign banks in the United States under certain conditions. In addition, the legislation requires Federal Reserve approval to establish foreign bank branches, agencies, commercial lending subsidiaries, and representative offices in the United States. Applications by two Taiwanese banks to establish a branch and agency respectively were approved in December 1992.

Supervisory Policy

During 1992 the Federal Reserve undertook several major supervisory and regulatory policy initiatives. Most of these initiatives involved the implementation of actions required under FDICIA. Other initiatives included several amendments to the Board's risk-based capital guidelines and other rules and policies, as well as the continuation of a review of internal supervisory policies related to the availability of credit.

Federal Deposit Insurance Corporation Improvement Act of 1991

In 1992 the Board issued final rules to implement various sections of FDICIA, as required by the Congress. In addition, the Board initiated proposals in 1992 to implement sections of FDICIA that had statutory deadlines during 1993. The major Board actions of 1992 to implement FDICIA as it relates to supervisory policy covered the following sections of the law:

• Section 122: On November 17 the banking and thrift regulatory agencies, working under the auspices of the Federal Financial Institutions Examination Council (FFIEC), approved regulatory reporting changes to gather information on lending to small businesses and small farms; the changes will become effective as of the June 30, 1993 report date.

• Section 131: On September 18 the Board issued a final rule implementing the provisions pertaining to prompt corrective action, which became effective on December 19, 1992.

• Section 132: On September 14, the Board issued an advance notice of proposed rulemaking requesting public comment on safety and soundness standards with regard to operations, management, credit underwriting, asset quality, earnings, stock valuations, and employee compensation. Final regulations are to be issued by August 1, 1993, and are to become effective by December 1, 1993.

• Section 304: On December 2 the Board adopted a rule with regard to real estate standards that matched rules issued separately by the other banking and thrift regulatory agencies. The rules will become effective on March 19, 1993.

• Section 305: On August 8 the banking regulatory agencies issued an interagency advance notice of a proposed rulemaking, requesting comment on the incorporation of interest rate risk and the risks of portfolio concentrations and nontraditional activities into the risk-based capital framework. A proposed rulemaking is expected to be issued in early 1993, and final rules are required to be issued by mid-June 1993.

• Section 306: On April 22 the Board adopted amendments to Regulations O and Y to provide safeguards against insider abuse; the amendments apply a new aggregate lending limit applicable to all of a bank's insiders and expand the application of existing lending limits under Regulation O to loans to directors and their related interests. These changes became effective on May 18.

• Section 308: On November 20 the Board approved an amendment to Regulation F to limit the exposure of insured depository institutions to the exposure of any other depository institution. This rule will be phased in and will become fully effective on June 19, 1995.

The more significant of these FDICIA provisions and the Board actions taken in connection with them are discussed in more detail below along with other significant policy initiatives on which the Board acted in 1992.

Risk-Based Capital Standards at Year-End 1992

On December 31, 1992, the two-year phase-in period for the risk-based capital standards ended. At that time, the minimum standard of total capital to risk-adjusted assets that banking organizations were expected to maintain was raised from 7.25 percent to 8 percent. The risk-based capital standards were developed in conjunction with the FDIC and OCC to implement the Basle Accord, which is a risk-based capital framework proposed by the Basle Committee on Banking Regulations and Supervisory Practices and endorsed by the central bank governors of the Group of Ten countries in July 1988.

During 1992 the Board adopted the following amendments to its risk-based capital guidelines:

• On January 17 the Board amended the guidelines to remove the limit on the amount of noncumulative perpetual preferred stock a bank holding company may include in its tier 1 capital. The guidelines for bank holding companies continue to limit cumulative perpetual preferred stock to 25 percent of tier 1 capital.

• The Congress, as part of the Resolution Trust Corporation Refinancing, Restructuring, and Improvement Act of 1991, required that the federal banking agencies lower the risk weight from

100 percent to 50 percent on two types of loans: (1) those for multifamily housing and (2) those to finance the construction of presold one- to four-family residential properties. On April 10 the Board issued a proposal to lower the risk weight for multifamily housing loans meeting certain criteria. On December 29 the Board adopted an interim rule, effective immediately, to lower the risk weight for presold one- to four-family residential construction loans. Final rules covering these changes were to be adopted in 1993.

• In early 1992 the Board and the other banking and thrift regulatory agencies, as part of an interagency effort to achieve uniformity in their risk-based capital guidelines, proposed revisions to the guidelines to provide explicit guidance on the types and amounts of intangible assets that may be included in capital. The Board approved a final rule on December 9, which became effective in February 1993.

• The Board lowered the risk weight from 20 percent to zero for certain collateralized transactions such as certain indemnified securities lending arrangements. This change, which became effective on December 30, 1992, recognizes the minimal risk in such transactions and is consistent with the Basle Accord.

Interest Rate Risk

With regard to interest rate risk, the proposal set forth in the notice of proposed rulemaking issued in accordance with section 305 would require some additional reporting by all banks but would impose additional capital requirements on only those institutions having exceptionally high measures of risk. This approach seeks to balance the regulatory burden associated with more precise measures of interest rate risk with the commercial banking industry's favorable experience in adapting to changing rate environments.

Prompt Corrective Action

Section 131 of FDICIA established a regime of "prompt corrective action" that provides for successively more stringent regulatory actions as an insured depository institution's capital deteriorates through five capital categories: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized. The final rule, which was developed in conjunction with the three other banking and thrift regulatory agencies, specifies minimum levels of capital for those categories.

The relevant capital measures established for the four highest categories consist of the total, the tier 1 risk-based capital measures, and the tier 1 leverage ratio. After an opportunity for a hearing, an institution may be downgraded to the next lower category (but not into the critically undercapitalized category) if the appropriate regulatory agency has determined that the institution is in an unsafe or unsound condition or if it has received a less-than-satisfactory rating for asset quality, management, earnings, or liquidity in its most recent report of examination. An institution is deemed to be critically undercapitalized if its ratio of tangible equity to total assets is 2 percent or less.

Real Estate Lending Standards

In accordance with section 304, a regulation issued jointly by the four agencies prescribes real estate lending standards that require each insured depository institution to adopt and maintain a comprehensive written real estate lending policy. These policies must be consistent with safe and sound banking practices and must be appropriate to the size of the institution and the nature and scope of the institution's operations. They also must address certain lending considerations, including loan-to-value limits; loan administration procedures; portfolio diversification standards; and documentation, approval, and reporting requirements. The agencies also issued the Interagency Guidelines for Real Estate Lending Policies to be used in conjunction with the regulation, which was scheduled to become effective on March 19, 1993.

Credit Availability

The Federal Reserve continued to work in a number of policy and supervisory areas to ease problems related to the availability of bank credit. The policy changes that were implemented phased out the reporting of highly leveraged transactions and made adjustments to risk-based capital definitions, to treatment of intangible assets, and to examination and reporting procedures. In addition, the Federal Reserve continued to work with other supervisors of depository institutions to ensure that supervisory policies and practices are not encouraging overly cautious lending policies at depository institutions that could deter lenders from meeting the financial needs of creditworthy borrowers. In an effort to gauge the effect of these and other changes, the Federal Reserve initiated or participated in a number of surveys and held several meetings across the country to further determine the causes of credit availability problems and work toward appropriate solutions. In this regard, System officials also testified before the Congress on a number of occasions on the actions undertaken to alleviate these problems.

Small Business and Farm Information

The reporting requirements approved by the FFIEC pursuant to section 122 of FDICIA generally require insured banks, thrift institutions, and U.S. branches of foreign banks to report annually on the number and amount of currently outstanding nonfarm nonresidential real estate loans, commercial loans, and agricultural real estate and agricultural loans in various size categories. These reporting requirements will become effective with the filings of Reports of Condition and Income beginning on June 30, 1993.

Real Estate Appraisals

The 1987 interagency guidelines for real estate appraisals were revised to incorporate the requirements of the Board's real estate appraisal regulation, which was issued in 1990. The revised guidelines were developed by an interagency working group, and each of the banking and thrift regulatory agencies have issued separate, but similar, guidelines. The Board's guidelines, which were issued in September 1992, provide information on evaluations for real estate related financial transactions that do not require the services of a state certified or licensed appraiser and on requirements for administering an institution's appraisal and evaluation programs.

In November 1992 the Board in conjunction with the other banking and thrift regulatory agencies issued an order granting relief from certain real estate appraisal requirements for several major disaster areas, in particular, those affected by Hurricanes Andrew and Iniki, and for the Los Angeles civil unrest. The Board acted under provisions of the Depository Institutions Disaster Relief Act of 1992 (DIDRA). DIDRA gives the regulatory agencies the authority to waive the appraisal requirements of title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) for transactions involving property located in major disaster areas. The Board and the other agencies also adopted uniform policies pursuant to DIDRA that will be followed in granting similar relief in future major disaster areas.

Highly Leveraged Transactions

The Federal Reserve, together with the other banking and thrift regulatory agencies, decided to phase out the supervisory definition of highly-leveraged transactions and to discontinue regulatory reporting requirements for such transactions by banking organizations after the June 30, 1992, reporting date. Nonetheless, the agencies will continue to closely review all highly leveraged credits during the examination process, and examiners will continue to use guidance previously issued by the agencies in the assessment of individual credits to finance corporate restructurings and the evaluation of internal processes for initiating and reviewing such credits.

Staff Training

The training of System staff members emphasizes analytical and supervisory themes common to the four areas of supervision and regulation—examinations, inspections, applications,

Training Programs for Banking Supervision and Regulation, 1992

Program	Number of sessions	
	Total	Regional
Schools or seminars conducted by the Federal Reserve		
Banking I (after March, examiner training school I)	12	5
Banking II	12	7
Banking III	5	1
Credit analysis	12	10
Abbreviated cash flow seminar	3	3
Real estate lending seminar	6	3
Senior lending seminar	2	...
Senior forum for current banking and regulatory issues	2	...
Bank operations school	4	3
Effective writing for banking supervision staff	16	16
Management skills school	5	3
Conducting meetings with management	18	18
Bank holding company applications	1	...
Bank holding company inspection	7	6
Advanced EDP examinations	1	...
Basic entry-level trust	1	...
Advanced trust school	1	...
Consumer compliance examination I	2	...
Consumer compliance examination II	2	...
Advanced CRE examination techniques	1	...
Seminar for senior supervisors of foreign central banks [1]	3	...
Other agencies conducting courses [2]		
Federal Financial Institutions Examination Council	88	22
Federal Deposit Insurance Corporation and Office of the Comptroller of the Currency	9	...
Federal Bureau of Investigation [3]	4	4

1. Conducted jointly with the World Bank.
2. Open to Federal Reserve employees.
3. Cosponsored by the Federal Reserve, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, Office of Thrift Supervision, and the Resolution Trust Corporation.

and surveillance—and stresses the interdependence of these areas. During 1992 the Federal Reserve conducted a variety of schools and seminars, and Federal Reserve staff members participated in several courses offered by, or cosponsored with, other agencies, as shown in the accompanying table. In 1992 the Federal Reserve trained 2,167 students in System schools, 881 in FFIEC schools, and 108 in other schools, for a total of 3,156 students, including 154 representatives from foreign central banks.

The Federal Reserve System also provided scholarship assistance to the states for training their examiners in Federal Reserve and FFIEC schools. Through this program, 570 state examiners were trained; 304 in Federal Reserve courses, 246 in FFIEC programs, and 20 in other courses.

Five new schools were added to the training program during the year: Real Estate Lending Seminar, Senior Lending Seminar, Bank Operations School, Management Skills, and Advanced EDP Examinations.

During 1992 the Federal Reserve began integrating its core supervision schools with those of the FDIC. In March the introductory school was merged, and six sessions of the joint school were offered during the year. In November and December, the pilot sessions of the joint second school were held.

Federal Financial Institutions Examination Council

The Board and the three other banking and thrift regulatory agencies, pursuant to the recommendation of the FFIEC, issued on January 10, 1992, a revised "Supervisory Policy Statement on Securities Activities."[3] The statement, which became effective on February 10, 1992, supersedes the "Supervisory Policy Concerning Selection of Securities Dealers and Unsuitable Investment Practices," issued in 1988. The new policy statement addresses the selection of securities dealers and requires depository institutions to establish prudent policies and strategies for securities transactions. The statement also defines securities trading or sales practices that are viewed by the agencies as being unsuitable when conducted in an investment portfolio, indicates characteristics of loans held for sale or trading, and establishes a framework for identifying when certain mortgage-derivative products are high-risk mortgage securities, which must be reported as securities held for sale or for trading.

Under the auspices of the FFIEC, the Board and the three other agencies during 1992 continued their study of appropriate regulatory reporting and capital treatments to be applied to recourse arrangements for depository institutions and bank holding companies; they also continued their review of guidance on the allowance for loan and lease losses. An interagency policy statement on the allowance is expected to be published in early 1993.

The Federal Reserve continued its participation in the work of the FFIEC's Appraisal Subcommittee. The subcommittee was established in November 1989, pursuant to title XI of FIRREA, to monitor the overall implementation of real estate appraisal reform. The sub-

3. The FFIEC consists of representatives from the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision.

committee is working with the state appraisal regulatory agencies to implement programs to license and certify appraisers. During 1992 the staff members of the subcommittee completed 20 state field reviews. Pursuant to title XI, the subcommittee has developed a national registry of appraisers licensed and certified by the states. As of the end of the year, the database included 35,000 appraisers from 36 states.

Pursuant to section 221 of FDICIA, the FFIEC on December 8 approved for submission to the Congress its *Study on Regulatory Burden*. Done in consultation with insured depository institutions and consumer and community groups, the study reviewed policies, procedures, and requirements of the banking and thrift regulatory agencies. It identified rule changes that could reduce unnecessary regulatory burden without diminishing compliance with, or enforcement of, consumer laws and without endangering the safety and soundness of insured institutions.

During 1992 the FFIEC took several actions with regard to regulatory reporting requirements. On May 22 the FFIEC issued a policy statement concerning the frequency and timing of changes in regulatory reporting requirements. Under this advance notification policy, the agencies, subject to certain exceptions, will announce before the end of each year all reporting changes that will take effect in the following year. The policy should ensure that depository institutions have at least ninety days' notice of changes in their regulatory reporting requirements and, accordingly, should lessen the regulatory burden associated with reporting changes.

In response to a new accounting standard regarding income taxes, issued in February 1992 by the Financial Accounting Standards Board (FASB Statement No. 109), the FFIEC on July 28 issued a request for public comment on possible regulatory treatments for deferred tax assets. After it evaluated these comments and held further interagency discussions, the FFIEC announced on December 23, that, for regulatory purposes, federally supervised banks and thrift associations should report deferred tax assets in accordance with generally accepted accounting principles. At the same time, the FFIEC recommended that the banking and thrift regulatory agencies amend their regulatory capital standards to limit the amount of deferred tax assets that can be included in capital.

The FFIEC also approved a number of revisions to the Reports of Condition and Income (Call Report), which are filed quarterly by all insured commercial banks. These revisions will become effective as of the March 31, 1993, reporting date. Some of these revisions—including those pertaining to the collection of data on loans to small businesses and small farms, off-balance sheet items, deposits in lifeline accounts, preferred deposits, and insured and uninsured deposits—implement certain reporting-related requirements of FDICIA. Other revisions adopted in 1992 relate to intangible assets that are grandfathered for regulatory capital purposes and to past-due and nonaccrual loans and leases that are wholly or partially guaranteed by the U.S. government.

In November 1992 the FFIEC adopted a supplement to the Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks to obtain improved data for supervisory purposes and for the analysis of U.S. credit and deposit flows in connection with international indebtedness. The supplement was proposed for public comment at the end of 1991, and the final version was scheduled to be implemented on March 31, 1993.

Regulation of the U.S. Banking Structure

The Board administers the Bank Holding Company Act, the Bank Merger Act, and the Change in Bank Control Act for bank holding companies and state member banks. In doing so, the Federal Reserve acts on a variety of proposals that directly or indirectly affect the structure of U.S. banking at the local, regional, and national levels. The Board also has primary responsibility for regulating the international operations of domestic banking organizations and the overall U.S. banking operations of foreign banks, whether conducted directly through a branch or agency or indirectly through a subsidiary commercial lending company. In addition, the Board has established regulations for the interstate banking activities of these foreign banks and for foreign banks that control a U.S. subsidiary commercial bank.

Bank Holding Company Act

By law, a company must obtain the Federal Reserve's approval if it is to form a bank holding company by acquiring control of one or more banks. Moreover, once formed, a bank holding company must receive the Federal Reserve's approval before acquiring additional banks or nonbanking companies.

In reviewing an application filed by a bank holding company, the Federal Reserve considers the financial and managerial resources of the applicant, the future prospects of both the applicant and the firm to be acquired, the convenience and needs of the community to be served, the potential public benefits, and the competitive effects of the proposal.

In 1992 the Federal Reserve acted on 1,119 bank holding company and related applications. The Federal Reserve approved 194 proposals to organize bank holding companies and denied 2; approved 85 proposals to merge existing bank holding companies; approved 217 bank acquisitions by existing bank holding companies and denied 1; approved 594 requests by existing companies to acquire nonbank firms engaged in activities closely related to banking and denied 3; and approved 23 other applications. Data on these applications are shown in the accompanying table. Included in the totals are applications related to the sale of failed thrift institutions by the Resolution Trust Corporation.

Bank Merger Act

The Bank Merger Act requires that all proposed mergers of insured depository institutions be acted upon by the appropriate federal banking agency. If the institution surviving the merger is a state member bank, the Federal Reserve has primary jurisdiction. Before acting on a proposed merger, the Federal Reserve considers the financial and managerial resources of the applicant, the future prospects of the existing and combined institutions, the convenience and needs of the community to be served, and the competitive effects of the proposal. The Federal Reserve must also consider the views of certain other agencies on the competitive factors involved in the transaction.

During 1992 the Federal Reserve approved 120 merger applications. As required by law, each merger is described in this REPORT (in table 16 of the Statistical Tables chapter).

When the OCC, the FDIC, or the OTS has jurisdiction over a merger, the Federal Reserve is asked to comment on the competitive factors to assure comparable enforcement of the antitrust provisions of the act. The agencies have adopted standard terminology for assessing competitive factors in merger cases to assure consistency in administering the act. The Federal Reserve submitted 763 reports on competitive factors to the other federal banking agencies in 1992.

Change in Bank Control Act

The Change in Bank Control Act requires that persons seeking control of a bank or bank holding company obtain approval from the appropriate federal banking agency before the transaction occurs. Under the act, the Federal Reserve is responsible for reviewing changes in the control of state member banks and of bank holding companies. In so doing, the Federal Reserve must review the financial condition, competence, experience, and integrity of the acquiring person; consider the effect on the financial condition of the bank or bank holding company to be acquired; and determine the effect on competition in any relevant market.

The appropriate federal banking agencies are required to publish notice of each proposed change in control and to invite public comment, particularly from persons located in the markets served by the institution to be acquired. The federal banking agencies are also required to assess the qualifications of each person seeking control; the Federal Reserve routinely makes such a determination and verifies information contained in the proposal.

In 1992 the Federal Reserve acted on 145 proposed changes in control of state member banks and bank holding companies.

Public Notice of Federal Reserve Decisions

Each decision by the Federal Reserve that involves a bank holding company, bank merger, change in control, or international banking proposal is effected by an order or announcement. Orders state the decision along with the essential facts of the application and the basis for

Bank Holding Company Decisions by the Federal Reserve, Domestic Applications, 1992

Proposal	Direct action by the Board of Governors		Action under authority delegated by the Board of Governors					Total
			Director of the Division of Banking Supervision and Regulation		Office of the Secretary	Federal Reserve Banks		
	Approved	Denied	Approved	Denied	Approved	Approved	Permitted	
Formation of holding company	7	2	0	0	3	184	0	196
Merger of holding company	17	0	0	0	7	61	0	85
Retention of bank	0	0	0	0	0	0	0	0
Acquisition								
Bank	34	1	0	0	17	166	0	218
Nonbank	132	3	7[1]	0	36	327	92	597
Bank service corporation	0	0	0	0	1	0	4	5
Other	0	0	18	0	0	0	0	18
Total	**190**	**6**	**25**	**0**	**64**	**738**	**96**	**1,119**

1. Each of these actions represents the acquisition of a savings association that was subsequently merged into an existing subsidiary of a bank holding company, as permitted by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989.

the decision; announcements state only the decision. All orders and announcements are released immediately to the public; they are subsequently reported in the Board's weekly H.2 statistical release and in the monthly *Federal Reserve Bulletin*. The H.2 release also lists applications and notices received by the Federal Reserve during the preceding week.

Timely Processing of Applications

The Federal Reserve maintains target dates and procedures for the processing of applications. These target dates promote efficiency at the Board and the Reserve Banks and reduce the burden on applicants. The time allowed for a decision is sixty days; during 1992, 93 percent of the decisions met this standard.

Delegation of Applications

Historically, the Board has delegated certain regulatory functions—including the authority to approve, but not to deny, certain types of applications—to the Reserve Banks, to the Director of the Board's Division of Banking Supervision and Regulation, and to the Secretary of the Board. The delegation of responsibility for applications permits staff members at both the Board and the Reserve Banks to work more efficiently by removing routine cases from the Board's agenda.

In the fall of 1992, in an effort to increase efficiency and reduce regulatory burden in the applications process, the Board greatly expanded the number of applications that may be acted upon by the Reserve Banks under delegated authority. In addition, the Board approved procedural changes to streamline the review of certain proposals by both Board staff members and the Reserve Banks and to expedite the preacceptance review of applications. In 1992, 80 percent of applications were acted on under delegated authority.

Board Policy Decisions and Developments in Bank Related Activities

In July 1992 the Board requested public comment on alternative methods to adjust the 10 percent revenue test that limits underwriting and dealing in ineligible securities by section 20 subsidiaries of bank holding companies. The matter was still under consideration at year-end.

Proposals to Engage in New Nonbanking Activities

In 1992 the Board expanded the list of generally permissible nonbanking activities for bank holding companies to include (1) combined investment advisory and securities brokerage activities, (2) additional financial advisory activities, and (3) higher-residual-value leasing activities. The Board also approved certain modifications to its investment advisory policy statement to permit bank holding companies to recommend and broker shares of mutual funds when the mutual fund is advised by the bank holding company or one of its subsidiaries.

At year-end, the Board was considering a proposal by a foreign bank to engage in a new activity that will involve the clearing of futures transactions that generally have been executed by other pre-approved execution groups.

Other Pending Rulemakings

Three other rulemakings were under consideration at year-end. The first proposal would ease the restrictions on the underwriting and dealing activities of bank holding companies to permit certain joint marketing activities and the employment of management officials working in both the holding company and in the securities subsidiary. The second proposal would rescind an existing rule that permits bank holding companies to establish or acquire indirectly, through their state-chartered bank subsidiaries, nonbank operations subsidiaries engaged in activities that may be conducted by the parent bank. The third proposal would permit bank holding companies to engage in real estate investment activities within certain limitations.

Applications by State Member Banks

State member banks must obtain the permission of the Federal Reserve to open new domestic branches, to make investments in bank premises that exceed 100 percent of capital stock, and to add to their capital bases from sales of subordinated debt. During the year, the Board substantially reduced the filing requirements for creating new domestic branches and approved modification of the regulation governing the establishment of bank premises. In addition, the Board reduced the prior review requirements for new debt instruments of state member banks that are intended to qualify as capital. State member banks must still give six months' notice of their intention to withdraw from membership in the Federal Reserve, although the notice period may be shortened or eliminated in specific cases.

Stock Repurchases by Bank Holding Companies

A bank holding company sometimes purchases its own shares from its shareholders. If the company borrows the money to buy the shares, the transaction increases the debt of the bank holding company and simultaneously decreases its equity. Relatively larger purchases may undermine the financial condition of a bank holding company and its bank subsidiaries. The Federal Reserve may object to stock repurchases by holding companies that fail to meet certain standards, including the Board's capital guidelines.

In the past, the Board's regulations have required all bank holding companies to give advance notice of repurchases that retire 10 percent or more of the company's consolidated equity capital. During the second half of 1992 the Board approved modification of the regulation that would exempt "well-capitalized" banking holding companies from having to give advance notice. In 1992 the Federal Reserve reviewed eighty-eight proposed stock repurchases by bank holding companies, eighty-six of which were acted on by the Reserve Banks on behalf of the Board.

International Activities of U.S. Banking Organizations

The Board has several statutory responsibilities in supervising the international operations of U.S. banking organizations. The Board must provide authorization and regulation of foreign branches of member banks; of overseas investments by member banks, Edge Act corporations, and bank holding companies; and of investments by bank holding companies in export trading companies. In addition, the Board is required to charter and regulate Edge Act corporations and their investments.

Foreign Branches of Member Banks

Under provisions of the Federal Reserve Act and of Regulation K (International

Banking Operations), member banks in most cases must seek Board approval to establish branches in foreign countries. In reviewing proposed foreign branches, the Board considers the requirements of the law, the condition of the bank, and the bank's experience in international business. In 1992 the Board approved the opening of three foreign branches.

By the end of 1992, 120 member banks were operating 774 branches in foreign countries and overseas areas of the United States; 88 national banks were operating 660 of these branches, and 32 state member banks were operating the remaining 114 branches.

Edge Act and Agreement Corporations

Under sections 25 and 25(a) of the Federal Reserve Act, Edge Act corporations and agreement corporations may engage in international banking and foreign financial transactions. These corporations, which are usually subsidiaries of member banks, may (1) conduct a deposit and loan business in states other than that of the parent, provided that the business is strictly related to international transactions and (2) make foreign investments that are broader than those of member banks because they can invest in foreign financial organizations, such as finance companies and leasing companies, as well as in foreign banks.

In 1992 the Federal Reserve approved one new agreement corporation. At year-end, there were ninety-four Edge Act and agreement corporations, which together had forty-four branches. The Board requires each Edge Act corporation that is engaged in banking to maintain a ratio of equity to risk assets of at least 7 percent. In line with the 1991 revision of Regulation K, this ratio of equity to risk assets was replaced with a minimum ratio of qualifying total capital to weighted risk assets of 10 percent effective January 1, 1993.

Foreign Investments

Under authority of the Federal Reserve Act and the Bank Holding Company Act, U.S. banking organizations may engage in activities overseas with the authorization of the Board. Significant investments require prior review by the Board, although pursuant to Regulation K, most foreign investments may be made under general-consent procedures that involve only after-the-fact notification to the Board.

Export Trading Companies

In 1982 the Bank Export Services Act amended Section 4 of the Bank Holding Company Act to permit bank holding companies, their subsidiary Edge Act or agreement corporations, and bankers' banks to invest in export trading companies, subject to certain limitations and after Board review. The purpose of this amendment was to allow effective participation by bank holding companies in the financing and development of export trading companies. The Export Trading Company Act Amendments of 1988 provide additional flexibility for bank holding companies engaging in export trading company activities. In 1992, one new export trading company was approved; since 1982 the Federal Reserve has acted affirmatively on notifications by forty-eight bank holding companies to establish export trading companies.

Enforcement of Other Laws and Regulations

The Board is also responsible for the enforcement of various laws, rules, and regulations other than those specifically related to bank safety and soundness and the integrity of the banking structure.

Bank Secrecy Act

The Currency and Foreign Transactions Reporting Act of 1970 (the Bank Secrecy Act) was originally aimed at identifying and tracking proceeds of illegal activity by creating records of various financial transactions that otherwise would not be identifiable. These records are also useful for determining the safety and soundness of financial institutions. Through regular examinations, the Federal Reserve monitors compliance with the Bank Secrecy Act by the institutions it supervises.

During 1992 the Federal Reserve significantly increased the number of targeted examinations of financial institutions to determine compliance with the Bank Secrecy Act. In addition the Federal Reserve enhanced its enforcement actions related to the act, which included the issuance of civil money penalties and cease-and-desist orders. Over the last year, the Federal Reserve has on numerous occasions assisted law enforcement agencies conducting criminal investigations of financial institutions suspected of Bank Secrecy Act violations and related violations.

In the area of training, the Federal Reserve trains all new examiners in the provisions of the Bank Secrecy Act and in the detection of money laundering and gives refresher courses in these areas to more seasoned examiners. The Federal Reserve has also participated in numerous programs to inform the financial community about the Federal Reserve's belief in strict compliance with the Bank Secrecy Act.

Securities Regulation

Under the Securities Exchange Act of 1934, the Board is responsible for regulating credit in certain transactions involving the purchase or carrying of securities. The Board limits the amount of credit that may be provided by securities brokers and dealers (Regulation T), by banks (Regulation U), and by other lenders (Regulation G). Regulation X extends these credit limitations, or margin requirements, to certain borrowers and to certain credit extensions, such as credit obtained from foreign lenders by U.S. citizens.

Several regulatory agencies enforce compliance with the securities credit regulations. The Securities and Exchange Commission, the National Association of Securities Dealers, and the national securities exchanges examine brokers and dealers for compliance with Regulation T. The federal banking agencies examine banks under their respective jurisdictions for compliance with Regulation U. The compliance of other lenders with Regulation G is examined by the Board, the Farm Credit Administration, the National Credit Union Administration, and the Office of Thrift Supervision, according to the jurisdiction involved. At the end of 1992, 605 lenders were registered under Regulation G, and 363 came under the Board's supervision. Of these 363, the Federal Reserve regularly inspects 231 every second or third year according to the type of credit they extend. The others are exempted from periodic on-site inspections by the Federal Reserve, which instead monitors them through the periodic regulatory reports they file. During 1992, Federal Reserve examiners inspected 64 lenders for compliance with Regulation G.

The Federal Reserve monitors the market activity of all OTC stocks to determine which of them are subject to the Board's margin regulations. The Board publishes the resulting *List of Marginable OTC Stocks* quarterly. In 1992 the OTC list was revised in February, May, August, and November. The November OTC list contained 3,110 stocks.

Pursuant to a 1990 amendment to Regulation T, the Board publishes a list of foreign stocks that are eligible for margin treatment at broker–dealers on the same basis as domestic margin securities. In 1992 the foreign list was revised in February, May, August, and November. The November foreign list contained 301 foreign stocks.

In April 1992 the Board announced that it is conducting a review of Regulation T to consider whether any provisions of the regulation need updating. In August 1992 the Board requested comment in connection with an advance notice of proposed rulemaking that identified areas scheduled for review and invited comment on all areas of Regulation T.

Under section 8 of the Securities Exchange Act, a nonmember domestic or foreign bank may lend to brokers or dealers posting registered securities as collateral only if the bank has filed an agreement with the Board that it will comply with all the statutes, rules, and regulations applicable to member banks regarding credit on securities. The Board processed no new agreements in 1992.

In 1992 the Securities Regulation Section of the Board's Division of Banking Supervision and Regulation issued forty-seven interpretations of the margin regulations. Those interpretations that presented sufficiently important or novel issues were published in the *Securities Credit Transactions Handbook,* which is part of the Federal Reserve Regulatory Service. These interpretations serve as a guide to the margin regulations.

Financial Disclosure by State Member Banks

State member banks must disclose certain information of interest to investors, including financial reports and proxy statements, if they issue securities registered under the Securities Exchange Act of 1934. By statute, the Board's financial disclosure rules must be substantially similar to those issued by the Securities and Exchange Commission. At the end of 1991, thirty-seven state member banks, most of which are small or medium-sized, were registered with the Board under the Securities Exchange Act.

Loans to Executive Officers

Under Section 22(g) of the Federal Reserve Act, state member banks must include in each quarterly Report of Condition all extensions of credit made by the bank to its executive officers since

Loans by State Member Banks to their Executive Officers, 1991–92

Period	Number	Amount (dollars)	Range of interest rates charged (percent)
October 1–December 31, 1991	744	15,293,000	5.5–21.0
January 1–March 31, 1992	796	22,589,000	5.0–21.0
April 1–June 30, 1992	838	21,485,000	5.0–21.0
July 1–September 30, 1992	758	17,543,000	4.5–21.0

SOURCE. Report of Condition.

the date of the bank's previous report of condition. The accompanying table summarizes this information.

Federal Reserve Membership

At the end of 1992, 4,619 banks were members of the Federal Reserve System, a decrease of 219 from the previous year-end. Member banks operated 35,469 branches on December 31, 1992, a net increase of 659 for the year.

Member banks accounted for 39 percent of all commercial banks in the United States and for 66 percent of all commercial banking offices, the same percentages as at year-end 1991. ■

Regulatory Simplification

In 1978 the Board of Governors established the Regulatory Improvement Project in the Office of the Secretary to help minimize the burdens imposed by regulation. In 1986 the Board reaffirmed its commitment to regulatory improvement, renaming the project the Regulatory Review Section and creating a subcommittee of the Board called the Regulatory Policy and Planning Committee. The purpose of the regulatory simplification function is to ensure that the economic effect of regulation on small business is considered, to afford interested parties the opportunity to participate in designing regulations and to comment on them, and to ensure that regulations are written in simple and clear language. Board staff members continually review regulations for their adherence to these objectives.

During 1992 the Board took several actions to reduce the regulatory burden on supervised institutions. Some of these actions were responses to legislation; others were internal initiatives.

Reviews of Regulatory Burden

During 1992 the Board participated in two reviews of Federal Reserve regulations. Early in the year, the Board completed an internal review of all regulations and recommended changes to them that would reduce unnecessary regulatory burden. Initiatives were established, including simplified application procedures, and these initiatives were implemented over the course of the year.

The Federal Reserve also participated in the *Study on Regulatory Burden*, required of the Federal Financial Institutions Examination Council (FFIEC) under section 221 of the Federal Deposit Insurance Corporation Improvement Act of 1991. Section 221 requires the FFIEC to complete four tasks: (1) review the policies, procedures, recordkeeping practices, and documentation requirements used to monitor and enforce compliance with all laws under the jurisdiction of the banking agencies and laws affecting depository institutions under the jurisdiction of the Secretary of the Treasury; (2) determine whether such policies, procedures, and requirements impose unnecessary burdens on insured depository institutions; (3) identify any opportunities to reduce unnecessary burdens without diminishing the effectiveness of consumer laws or endangering the safety and soundness of insured institutions; (4) report these opportunities to the Congress within one year.

The Regulatory Planning and Review Section was responsible for organizing and drafting the study for the FFIEC. The section drafted the final report after it coordinated the work of an interagency task force, which held public hearings in Kansas City, San Francisco, and Washington. The FFIEC submitted the 281-page report to the Congress on December 17, 1992. Congressional hearings on the report's findings were expected to be held in early 1993.

Reserve Requirements

In August the Board adopted amendments to Regulation D, Reserve Requirements of Depository Institutions, to simplify the procedure used by depository institutions to calculate reserve requirements. One amendment shortened the lag in counting vault cash for required reserves by two weeks. This action synchronizes movements in required reserves and vault cash, which improves the ability of depository institutions to manage their required reserve balances. A second amendment gave institutions more flexibility to manage reserves from one maintenance period to another by doubling the carryover allowance for reserve balances to the larger of $50,000 or 4 percent of the sum of required reserves and required clearing balances.

Bank Holding Companies

During 1992 the Board announced a series of changes in its Regulation Y, Bank Holding Companies and Change in Bank Control, to expand permissible activities of bank holding companies and their subsidiaries.

In April the Board approved an amendment to add non-full-payout leasing to the leasing activities that are generally permissible for bank holding companies. The amendment raises the maximum estimated residual value of leased personal property to up to 100 percent of the acquisition cost of the leased property, subject to certain conditions.

In April the Board also approved an amendment to Regulation Y to permit the provision of financial advisory services to financial and nonfinancial institutions and to individuals with high net worth under certain conditions, and the offering of investment advisory services and securities brokerage services on a combined basis under certain conditions. This amendment enables Federal Reserve Banks to expedite the applications process for bank holding companies to engage in these activities.

In July the Board announced an amendment to an interpretive rule regarding investment advisory activities of bank holding companies. The amendment provides that a bank holding company and its nonbank subsidiaries may broker shares in an investment company that is also advised by the bank holding company or any of its subsidiaries. The amended rule also provides that a bank holding company and its nonbank subsidiaries may give investment advice to customers regarding the purchase and sale of shares of an investment company that is also advised by an affiliate of the bank holding company. In either case, the bank holding company engaging in these activities must disclose the potential for conflict of interest or adverse effects.

Application Procedures

In June the Board adopted amendments to Regulation Y to streamline certain procedural requirements in the applications process that would make filing of applications for mergers and acquisitions less burdensome. The amendments increased the size of nonbank companies that bank holding companies may acquire under the expedited fifteen-day notice procedures; they increased the relative size of nonbank assets that bank holding companies may acquire in the ordinary course of business without prior approval; and they described the criteria for determining the waiver of an application with certain bank mergers.

Policy on Disaster Relief

In November the federal agencies that regulate financial institutions announced several regulatory changes to facilitate recovery in major disaster areas such as those areas affected by hurricanes and civil unrest. The agencies developed the policies in response to the regulatory flexibility permitted by the Depository Institutions Disaster Relief Act of 1992. The agencies' changes covered the following points:

- A waiver, by all of the agencies, of real estate appraisal requirements of Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989
- A Federal Reserve order to permit an exception to the rules in Regulation Z regarding consumer waiver of the right to cancel certain home-secured loans
- An extension of an interagency statement concerning reduced examiner criticism of restructured debts and extended repayment terms—so long as the efforts are consistent with safe and sound banking practices
- An indication that the agencies will give positive consideration, under the Community Reinvestment Act, to financial institutions that actively participate in programs to meet the needs of communities that are devastated by disasters—even if the low- and moderate-income neighborhoods aided are outside an institution's delineated community. ■

Federal Reserve Banks

During 1992 the Federal Reserve Banks made significant progress in preparing for consolidation of their mainframe data processing operations. Currently, each of the twelve Banks maintains a general purpose data processing center. Eventually, the twelve centers, together with four backup facilities, will be consolidated at three "consolidation centers"—the Reserve Bank head offices in Richmond and Dallas and the New York Bank's East Rutherford Operations Center in New Jersey. The objectives of automation consolidation include greater reliability, increased control of payment system risk in a national banking environment, improved security of the total automation environment, enhanced responsiveness to changing business requirements, and greater efficiency.

The Federal Reserve Automation Services (FRAS) organization, which was established to plan and manage the automation consolidation effort and to operate the consolidated data centers, is headquartered at the Federal Reserve Bank of Richmond. FRAS reports to the Richmond Bank's board of directors through an oversight committee composed of senior Reserve Bank officials. Major FRAS accomplishments during 1992 include preparing facilities, hiring staff, installing the computer equipment needed to support the Reserve Banks that will be moving their mainframe processing to FRAS during 1993, acquiring software, and planning interoffice communication connections. Also during 1992 the Federal Reserve Banks developed plans for moving mainframe workloads to FRAS.

By December 1992 the Federal Reserve Banks of Richmond and Dallas had moved their data processing operations to FRAS computing equipment. Of the remaining Banks, all but New York plan to move their electronic payment applications to FRAS by 1994 and all other mainframe workloads to FRAS by 1995. The New York Bank plans to move its electronic payment applications to FRAS during the first half of 1996.

Developments in Federal Reserve Services

The Monetary Control Act of 1980 requires the Federal Reserve System to recover all the costs it incurs in providing services to depository institutions. In 1992, income from priced services totaled $938.6 million and costs totaled $892.7 million, resulting in net income of $44.8 million and a recovery rate of 105.1 percent. In 1991 the System recovered 102.9 percent of its priced services costs.[1]

Check Collection

The Federal Reserve's operating expenses and imputed costs for commercial check collection in 1992 totaled

1. For a detailed breakdown of revenue, cost, and net revenue, see the first pro forma income statement at the end of this chapter. *Revenue* is the sum of income from services and investment income. *Cost* is the sum of operating expenses, imputed costs, earnings credits, imputed income taxes, and the targeted return on equity. *Net revenue* is net income less the targeted return on equity.

$545.7 million (see the second pro forma income statement for priced services, at the end of this chapter). Check operations for the year generated $576.0 million in revenue and a net of $2.4 million in other income and expenses. Income from operations after imputed costs was $30.3 million. The Federal Reserve Banks handled 19.1 billion checks, an increase of 1.7 percent over 1991 volume.

In October the Board approved several modifications to the Reserve Banks' check collection service. After a thorough evaluation of service levels, the Board approved new minimum service standards, effective January 1, 1993. The new standards are designed to speed interdistrict check collection, to improve deadlines and availability, and to provide more uniform service nationwide. The Board also approved a service option that allows depository institutions to mix returned checks with forward-collection checks, effective January 1, 1993. The latter action was based on the results of a pilot project in which three Federal Reserve Districts accepted intermingled deposits of returned and forward-collection checks and in turn presented intermingled cash letters to participating depository institutions. (Normally, the items are deposited separately.) The pilot project indicated that intermingling contributes to cost savings and improves quality for both the Reserve Banks and participating institutions.

During 1992 the Federal Reserve continued to explore technological improvements that would enhance check processing. Pilot projects were begun to test interdistrict truncation, in which depositing financial institutions in one district can truncate physical checks and forward the items electronically to the district where the paying bank is located, and intra- and interdistrict transmission of adjustment requests via Fedline. Significant progress was made in developing medium- and high-speed digital image applications for check collection. A high-speed image archival system for Treasury checks is scheduled for testing in 1993.

Automated Clearinghouse

In 1992 the operating expenses and imputed costs of providing commercial automated clearinghouse (ACH) services totaled $60.5 million; income from the service was $60.1 million. The Federal Reserve Banks processed 1,327 million commercial transactions during the year, an increase of 18.5 percent over 1991 volume.

By the end of 1992, 92 percent of all depository institutions that originate or receive commercial ACH transactions through the Federal Reserve Banks had established electronic connections. By July 1, 1993, all institutions using this service must convert to electronic connections. The use of electronic connections will enable the Banks to improve the ACH service significantly by speeding delivery of ACH payments and reducing the associated risk. In August 1992 the Treasury Department requested public comment on a proposal that would require all government-only ACH receivers to establish electronic connections to the Reserve Banks by July 1, 1994. Final action on the proposal is expected in early 1993.

Funds Transfer

The operating expenses and imputed costs of providing funds transfer services in 1992 totaled $69.2 million, and income was $85.6 million. The number of Fedwire funds transfers originated increased 4.3 percent over the 1991 volume, to 69.8 million transfers.

In October the Board requested public comment on a proposal to change the opening time for the Fedwire funds transfer service from 8:30 a.m. to 6:30 a.m. eastern time (ET). Comment was also invited on changing the opening time of the book-entry securities transfer service to 6:30 a.m. ET, should the funds transfer service start to open earlier. The earlier openings are believed likely to facilitate efforts to strengthen settlements of futures and options transactions among banks and bank customers. The Board also requested comment on a longer-term objective of further lengthening Fedwire operating hours and possibly moving to round-the-clock operations. The Board indicated that expanding Fedwire operating hours has the potential to reduce risks and to support payments and settlements related to international financial activity.

Net Settlement

The Federal Reserve provides net settlement services to four national and numerous local netting arrangements. These arrangements settle their participants' net positions either via Fedwire funds transfers using special settlement accounts at the Federal Reserve or via accounting entries to their settling participants' reserve or clearing accounts at the Federal Reserve.

Two of the national arrangements, the Clearing House Interbank Payments System and the Participants Trust Company, process and net large-dollar transactions associated with interbank funds transfers and payments related to the settlement of mortgage-backed securities transactions, respectively. The other two national arrangements, Visa and Chexs, process and net small-dollar transactions associated with automated clearing house and check payments, respectively. The Chexs settlement arrangement was approved by the Board in April 1992. The majority of local arrangements are check clearinghouses.

In 1992, about 650,000 net settlement entries were processed by the Reserve Banks for local netting arrangements; the value of these entries was about $640 billion. An estimated $2.3 trillion in net settlements were processed through special Fedwire settlement accounts for national arrangements in 1992. Cost and revenue data for the net settlement activity are combined with data for the funds transfer service.

Securities and Fiscal Agency Services

The Federal Reserve provides book-entry securities services for debt issues of the U.S. Treasury and for certain federally sponsored agencies, such as the Federal Home Loan Mortgage Corporation and the Student Loan Marketing Association. Only the services related to federal agency securities are priced by the Federal Reserve. In 1992, operating expenses and imputed costs totaled $11.6 million and earned income was $13.1 million. The Federal Reserve processed 3.3 million government agency securities transfers during the year, a 16.6 percent increase over 1991 volume.

The Federal Reserve continues to operate Treasury Direct, the book-entry securities safekeeping system for individuals who invest in Treasury securities and use the Treasury Department as custodian. Treasury Direct has grown to more than 1.1 million accounts with a total par value of $62.5 billion. During 1992, the Reserve Banks processed 2.1 million applications to purchase securities, issued 6.4 million payments related to Treasury Direct, and handled more than 1.2 million telephone and written inquiries from Treasury Direct account holders.

Also during 1992 the Federal Reserve Bank of New York developed the Treasury Automated Auction Processing System (TAAPS) for the Treasury Department. When TAAPS becomes available in the second quarter of 1993, it will enable bidders for new issues of Treasury securities, after having established electronic connections with a Federal Reserve Bank, to submit their bids electronically instead of on paper and will facilitate the Federal Reserve's review of bids.

All Federal Reserve Banks have fully implemented the Regional Delivery System (RDS) for issuance of over-the-counter savings bonds. In 1992 the System printed more than 67 million savings bonds, including over-the-counter and other types of savings bonds. The System is now preparing to consolidate savings bonds operations at five sites, down from the current twelve sites; consolidation should be completed within three years.

Definitive Securities Safekeeping and Noncash Collection

The operating expenses and imputed costs of providing priced definitive securities safekeeping and noncash collection services in 1992 totaled $12.8 million, and income was $10.6 million. The average number of definitive securities issues and receipts maintained in priced safekeeping accounts at the Federal Reserve Banks decreased 28.1 percent during 1992, to 41,472. The number of noncash collection items processed decreased 27.1 percent, to 1.6 million.

The Board has announced that because of declining volumes in both services, the System will, by the end of 1993, discontinue its priced definitive safekeeping service and consolidate most of its noncash collection operations at the Cleveland Bank and the Jacksonville Branch of the Atlanta Bank.

Currency and Coin

In its currency and coin operations, the Federal Reserve continued to focus on effectiveness of controls, efficiency of processing, and maintenance of quality in circulating currency.

In 1992, income from priced cash services was $12.9 million, and the cost was $12.3 million. Three Federal Reserve Districts provided transportation of cash by armored carrier; the San Francisco District discontinued this service during the year. Three Districts provided wrapped coin to depository institutions, and two Districts provided nonstandard packaging of currency orders and deposits and nonstandard frequency of access to cash services.

In March the Federal Reserve began distributing a new series of $50 note with two new features—a security thread and microprinting—to discourage photocopied counterfeits. The new series of $10 and $20 notes—also incorporating the new features—were distributed during the fourth quarter, and distribution of a new series of $5 note is scheduled for 1993. A new series of $1 note incorporating the new security features is not planned. In June the Bureau of Engraving and Printing began producing $1 notes using the web-fed intaglio currency press, which prints both sides of the note in a single pass through the press.

The first production machine for the System's new currency-processing equipment (ISS-3000) was delivered to the New York Bank's new processing center in October, and training for use of the equipment was conducted throughout the year. The new equipment will be installed throughout the System by 1997.

The Federal Reserve System continued to work with the Treasury Department and other agencies to deter counterfeiting and laundering of U.S. currency.

Float

Federal Reserve float increased to a daily average of $417 million in 1992, from $348 million in 1991. The costs of Federal Reserve float associated with priced services are recovered each year.

Examinations

The Federal Reserve Act, section 21, requires the Board of Governors to "order an examination of each Federal Reserve Bank" at least once a year. The responsibility is assigned to the Board's Division of Reserve Bank Operations and Payment Systems. In 1992 the Board also engaged a certified public accounting (CPA) firm to examine one of the twelve Federal Reserve Banks; in 1993, two Banks will be examined by a CPA firm. The findings of all examinations are reported to the management and directors of the respective Banks and to the Board of Governors.

To assess conformance with policies established by the Federal Open Market Committee (FOMC), the Division of Reserve Bank Operations and Payment Systems also annually audits the accounts and holdings of the System Open Market Account at the Federal Reserve Bank of New York and the foreign currency operations conducted by that Bank. The Division furnishes copies of these reports to the FOMC. All examination procedures used by the Division are reviewed each year by a public accounting firm.

Income and Expenses

The accompanying table summarizes the income, expenses, and distribution of net earnings of the Federal Reserve Banks for 1992 and 1991.

Income was $20,235 million in 1992, compared with $22,553 million in 1991. Expenses totaled $1,604 million ($1,298 million in operating expenses, $177 million in earnings credits granted to depository institutions, and

Income, Expenses, and Distribution of Net Earnings of Federal Reserve Banks, 1992 and 1991[1]

Millions of dollars

Item	1992	1991
Current income	20,235	22,553
Current expenses	1,475	1,429
Operating expenses[2]	1,298	1,265
Earnings credits granted	177	164
Current net income	18,760	21,124
Net addition to (deduction from) current net income	−959	496
Cost of unreimbursed services to Treasury	29	90
Assessments by the Board of Governors	424	371
For expenditures of Board	129	110
For cost of currency	295	261
Net income before payments to Treasury	17,348	21,158
Dividends paid	172	153
Payments to Treasury (interest on Federal Reserve notes)	16,774	20,778
Transferred to surplus	402	228

1. Details may not sum to totals because of rounding.
2. Operating expenses include a net periodic credit for pension costs of $141 million in 1992 and $83 million in 1991.

$129 million in assessments for expenditures by the Board of Governors). The cost of currency was $295 million. Income from financial services was $758 million.

The profit and loss account showed a net deduction of $959 million, primarily a result of realized and unrealized losses on assets denominated in foreign currencies. Dividends paid to member banks, as required by law, totaled $172 million, $19 million more than in 1991. The rise reflects an increase in the capital and surplus of member banks and a consequent increase in the paid-in capital stock of the Federal Reserve Banks.

Payments to the U.S. Treasury in the form of interest on Federal Reserve notes totaled $16,774 million, compared with $20,778 million in 1991. The payments consist of all net income after deduction of dividends and deduction of the amount necessary to bring the surplus of the Banks to the level of capital paid in.

In the Statistical Tables chapter of this report, table 6 details income and expenses of each Federal Reserve Bank for 1992, and table 7 shows a condensed statement for each Bank for 1914–92. A detailed account of the assessments and expenditures of the Board of Governors appears in the next chapter—Board of Governors Financial Statements.

Holdings of Securities and Loans

Average daily holdings of securities and loans during 1992 were $283,104 million, an increase of $26,175 million over 1991 (see accompanying table). Average daily holdings of U.S. government securities increased $26,368 million over 1991, and average daily holdings of loans decreased $193 million. The average rate of interest on holdings of U.S. government securities decreased from 7.51 percent in 1991 to 6.13 percent in 1992, and the average rate of interest on loans decreased from 5.73 percent to 3.43 percent.

Volume of Operations

Table 9, in the Statistical Tables chapter, shows the volume of operations in the principal departments of the Federal Reserve Banks for the years 1988–92.

Securities and Loans of Federal Reserve Banks, 1990–92

Millions of dollars, except as noted

Item and year	Total	U.S. government securities [1]	Loans [2]
Average daily holdings [3]			
1990	237,444	236,523	921
1991	256,929	256,559	370
1992	283,104	282,927	177
Earnings			
1990	20,067	19,995	73
1991	19,283	19,262	21
1992	17,342	17,336	6
Average interest rate (percent)			
1990	8.45	8.45	7.88
1991	7.51	7.51	5.73
1992	6.13	6.13	3.43

1. Includes federal agency obligations.
2. Does not include indebtedness assumed by FDIC.
3. Based on holdings at opening of business.

Federal Reserve Bank Premises

Construction of the new East Rutherford, New Jersey Operations Center for the Federal Reserve Bank of New York and the new headquarters building for the Federal Reserve Bank of Dallas was essentially completed by June, and the Banks began moving staff and operations into the buildings at that time. Operations are now underway at both facilities, and complete conversion of all operations is planned for early 1993.

In June the Board authorized the Federal Reserve Banks of Richmond and Dallas to renovate their head offices and the Federal Reserve Bank of New York to construct an addition to and to renovate its East Rutherford Operations Center—all to accommodate the new Federal Reserve Automation Services. The modifications at all three facilities had progressed sufficiently by October to allow installation of the first phase of the automation equipment. Construction at all three sites is planned to be completed during 1993.

Design work for the new head offices of the Federal Reserve Banks of Cleveland and Minneapolis continued during 1992. In November the Board approved the site selection for the new head office for the Minneapolis Bank.

Other facility projects approved by the Board during 1992 include renovation of the check processing facility at the Federal Reserve Bank of Richmond and a multiyear renovation program for the Federal Reserve Bank of San Francisco's Salt Lake City Branch.

In the Federal Reserve Bank Branch Modernization Act (enacted on October 24, 1992), the Congress eliminated the funding ceiling on Branch facilties. The action will enable the Banks to address deficiencies at several Branch buildings and to improve the effectiveness and efficiency of the Branch facilities.

Table 8, in the Statistical Tables chapter, shows the cost and book values of premises owned or occupied by the Federal Reserve Banks and the cost of other real estate owned by the Reserve Banks.

Pro Forma Balance Sheet for Priced Services, December 31, 1992 and 1991[1]
Millions of dollars

Item	1992		1991	
Short-term assets[2]				
Imputed reserve requirement on clearing balances	699.2		453.8	
Investment in marketable securities	5,127.8		3,328.2	
Receivables	66.6		63.4	
Materials and supplies	6.5		5.7	
Prepaid expenses	12.3		13.1	
Items in process of collection	4,062.4		4,167.4	
Total short-term assets		9,974.7		8,031.7
Long-term assets[3]				
Premises	378.5		360.1	
Furniture and equipment	176.2		163.5	
Leases and leasehold improvements	51.3		22.0	
Prepaid pension costs	141.7		97.3	
Total long-term assets		747.6		642.9
Total assets		**10,722.4**		**8,674.5**
Short-term liabilities				
Clearing balances and balances arising from early credit of uncollected items	8,820.7		4,576.0	
Deferred-availability items	1,068.8		3,373.4	
Short-term debt	85.3		82.3	
Total short-term liabilities		9,974.7		8,031.7
Long-term liabilities				
Obligations under capital leases	1.2		1.2	
Long-term debt	192.3		173.1	
Total long-term liabilities		193.5		174.3
Total liabilities		**10,168.3**		**8,206.0**
Equity		554.1		468.6
Total liabilities and equity[4]		**10,722.4**		**8,674.5**

1. Details may not sum to totals because of rounding.

2. The imputed reserve requirement on clearing balances held at Reserve Banks by depository institutions reflects a treatment comparable to that of compensating balances held at correspondent banks by respondent institutions. The reserve requirement imposed on respondent balances must be held as vault cash or as nonearning balances maintained at a Reserve Bank; thus, a portion of priced services clearing balances held with the Federal Reserve is shown as required reserves on the asset side of the balance sheet. The remainder of clearing balances is assumed to be invested in three-month Treasury bills, shown as investment in marketable securities. Receivables are (1) amounts due the Reserve Banks for priced services and (2) the share of suspense-account and difference-account balances related to priced services. Materials and supplies are the inventory value of short-term assets. Prepaid expenses include salary advances and travel advances for priced-service personnel. Items in process of collection (CIPC) is gross Federal Reserve CIPC stated on a basis comparable to that of a commercial bank. It reflects adjustments for intra-System items that would otherwise be double-counted on a consolidated Federal Reserve balance sheet; adjustments for items associated with nonpriced items, such as those collected for government agencies; and adjustments for items associated with providing fixed availability or credit before items are received and processed. Among the costs to be recovered under the Monetary Control Act is the cost of float, or net CIPC during the period (the difference between gross CIPC and deferred-availability items, which is the portion of gross CIPC that involves a financing cost), valued at the federal funds rate.

3. Long-term assets used solely in priced services, the priced-services portion of long-term assets shared with nonpriced services, and an estimate of the assets of the Board of Governors used in the development of priced services. Effective Jan. 1, 1987, the Reserve Banks implemented Financial Accounting Standards Board Statement No. 87, Employers' Accounting for Pensions. Accordingly, in 1992 the Reserve Banks recognized a credit to expenses of $53.5 million and a corresponding increase in this asset account.

4. Under the matched-book capital structure for assets that are not "self-financing," short-term assets are financed with short-term debt. Long-term assets are financed with long-term debt and equity in a proportion equal to the ratio of long-term debt to equity for the fifty largest bank holding companies, which are used in the model for the private sector adjustment factor (PSAF). The PSAF consists of the taxes that would have been paid and the return on capital that would have been provided had priced services been furnished by a private-sector firm. Other short-term liabilities include clearing balances maintained at Reserve Banks and deposit balances arising from float. Other long-term liabilities consist of obligations on capital leases.

Pro Forma Income Statement for Federal Reserve Priced Services, Calendar Years 1992 and 1991 [1]

Millions of dollars

Item	1992		1991	
Income from services provided to depository institutions [2]		758.4		737.5
Operating expenses [3]		606.1		611.9
Income from operations		152.3		125.6
Imputed costs [4]				
Interest on float	14.5		19.0	
Interest on debt	19.8		19.4	
Sales taxes	11.2		9.9	
FDIC insurance	8.9	54.4	6.3	54.6
Income from operations after imputed costs		97.9		71.0
Other income and expenses [5]				
Investment income	180.2		175.0	
Earnings credits	177.8	2.4	162.3	12.7
Income before income taxes		100.3		83.7
Imputed income taxes [6]		29.5		25.5
Net income		**70.8**		**58.1**
MEMO				
Targeted return on equity [7]		24.9		32.5

1. Details may not sum to totals because of rounding.

2. Income for priced services is realized from direct charges to an institution's account or from charges against accumulated earnings credits.

3. Operating expenses include direct, indirect, and other general administrative expenses of the Reserve Banks for priced services and the expenses of staff members of the Board of Governors working directly on the development of priced services, which were $1.9 million in 1992 and $2.0 million in 1991. The credit to expenses under FASB 87 is reflected in operating expenses (see the pro forma balance sheet, note 3).

4. Interest on float is derived from the value of float to be recovered, either explicitly or through per-item fees, during the period. Float costs include costs for checks, book-entry securities, noncash collection, ACH, and funds transfers.

Interest is imputed on debt assumed necessary to finance priced-service assets. The sales taxes and FDIC insurance assessment that the Federal Reserve would have paid had it been a private-sector firm are among the components of the PSAF (see the pro forma balance sheet, note 4).

The following list shows the daily average recovery of float by the Reserve Banks for 1992 in millions of dollars:

Total float	521.1
Unrecovered float	–42.5
Float subject to recovery	563.6
Sources of recovery of float	
Income on clearing balances	61.0
As-of adjustments	209.3
Direct charges	128.8
Per-item fees	164.5

Unrecovered float includes float generated by services to government agencies and by other central bank services. Float recovered through income on clearing balances is the result of the increase in investable clearing balances; the increase is produced by a deduction for float for cash items in process of collection, which reduces imputed reserve requirements. The income on clearing balances reduces the float to be recovered through other means. As-of adjustments and direct charges are midweek closing float and interterritory check float, which may be recovered from depositing institutions through adjustments to the institution's reserve or clearing balance or by valuing the float at the federal funds rate and billing the institution directly. Float recovered through per-item fees is valued at the federal funds rate and has been added to the cost base subject to recovery in 1992.

5. Investment income is on clearing balances and represents the average coupon-equivalent yield on three-month Treasury bills applied to the *total* clearing balance maintained, adjusted for the effect of reserve requirements on clearing balances. Expenses for earnings credits granted to depository institutions on their clearing balances are derived by applying the average federal funds rate to the *required* portion of the clearing balances, adjusted for the net effect of reserve requirements on clearing balances.

6. Calculated at the effective tax rate derived from the PSAF model.

7. The after-tax rate of return on equity that the Federal Reserve would have earned had it been a private business firm, as derived from the PSAF model. This amount is adjusted to reflect the deferral of $1.1 million for 1992 automation consolidation, an amount that the Reserve Banks plan to recover, along with a finance charge, by the end of 1999.

Pro Forma Income Statement for Federal Reserve Priced Services, by Service, 1992[1]
Millions of dollars

Item	Total	Commercial check collection	Funds transfer and net settlement	Commercial ACH	Definitive safekeeping and noncash collection	Book-entry securities	Cash services
Income from services	758.4	576.0	85.6	60.1	10.6	13.1	12.9
Operating expenses	606.1	501.9	64.4	56.6	11.9	10.7	12.3
Income from operations	152.3	74.1	21.3	3.5	−1.3	2.5	.6
Imputed costs[2]	54.4	43.8	4.8	3.9	.9	.9	.0
Income from operations after imputed costs	97.9	30.3	16.5	−.4	−2.2	1.6	.6
Other income and expenses, net[3]	2.4	2.4	.0	.0	.0	.0	.0
Income before income taxes	100.3	32.7	16.4	−.4	−2.2	1.6	.6

1. Details may not sum to totals because of rounding. The effect of implementing FASB 87 (see the pro forma balance sheet, note 3) is reported only in the "total" column in this table and has not been allocated to individual priced services. Taxes and the aftertax targeted rate of return on equity, as shown on the overall pro forma income statement, have not been allocated among services because these elements relate to the organization as a whole.

2. Includes interest on float, interest on debt, sales taxes, and the FDIC assessment. Float costs are based on the actual float incurred for each priced service. Other imputed costs are allocated among priced services according to the ratio of operating expenses less shipping expenses for each service to the total expenses for all services less the total shipping expenses for all services.

3. Income on clearing balances and the cost of earnings credits. Because clearing balances relate directly to the Federal Reserve's offering of priced services, the income and cost associated with these balances are allocated to each service based on the ratio of income from each service to total income.

Activity in Federal Reserve Priced Services, Calendar Years 1992, 1991, and 1990[1]
Thousands of items, except as noted

Service	1992	1991	1990	Percent change 1992–91	Percent change 1991–90
Funds transfers	69,803	66,921	62,559	4.3	7.0
Commercial ACH	1,326,632	1,119,073	915,257	18.5	22.3
Commercial checks	19,052,928	18,742,950	18,594,652	1.7	.8
Securities transfers	3,266	2,800	2,555	16.6	9.6
Definitive safekeeping	41	57	82	−28.1	−30.5
Noncash collection	1,636	2,243	2,854	−27.1	−21.4
Cash transportation	282	338	330	16.6	2.4

1. Activity is defined as follows: for wire transfer of funds, the number of basic transactions originated; for ACH, total number of commercial items processed; for commercial checks, total number of commercial checks collected, including both processed and fine-sort items; for securities, number of basic transfers originated on line; for definitive safekeeping, average number of issues or receipts maintained; for noncash collection, number of items on which fees are assessed; and for cash transportation, number of armored-carrier stops.

Income and Expenses for Locally Priced Federal Reserve Services, by District, 1992[1]
Millions of dollars

District	Total revenue	Operating expense	Float expense	Total expense	Net revenue
	Commercial check collection				
Boston	35.3	33.8	.7	34.5	.8
New York	69.6	65.0	1.6	66.6	3.0
Philadelphia	31.2	27.5	1.1	28.6	2.6
Cleveland	32.0	28.4	1.1	29.5	2.5
Richmond	54.9	48.5	1.6	50.1	4.8
Atlanta	76.4	64.0	1.7	65.7	10.7
Chicago	76.6	62.6	1.9	64.5	12.1
St. Louis	24.0	19.9	1.0	20.9	3.1
Minneapolis	31.3	26.7	.4	27.1	4.2
Kansas City	36.8	30.7	.8	31.5	5.3
Dallas	41.9	35.5	1.4	36.9	5.0
San Francisco	66.2	59.5	.8	60.3	5.9
System total	**576.0**	**502.1**	**14.1**	**516.2**	**60.0**
	Definitive safekeeping and noncash collection				
Boston	.5	.8	*	.8	−.3
New York	2.3	2.2	*	2.2	.1
Philadelphia	.8	.8	*	.8	.0
Cleveland	1.3	1.2	*	1.2	.1
Richmond	.5	.8	*	.8	−.3
Atlanta	1.9	2.0	*	2.0	−.1
Chicago	1.6	1.7	*	1.7	−.1
St. Louis	.6	.5	*	.5	.1
Minneapolis	.1	.1	*	.1	.0
Kansas City	.4	.8	*	.8	−.4
Dallas	.7	1.0	*	1.0	−.3
San Francisco	*	*	*	*	*
System total	**10.6**	**11.9**	**.0**	**11.9**	**−1.2**
	Cash services				
Boston	*	...	...	*	*
New York	*	...	...	*	*
Philadelphia	1.7	...	...	1.7	.0
Cleveland	1.9	...	...	1.8	.1
Richmond	*	...	...	*	*
Atlanta	*	...	...	*	*
Chicago	.5	...	...	.5	.0
St. Louis	.1	...	...	.1	.0
Minneapolis	2.9	...	...	2.6	.3
Kansas City	.6	...	...	.5	.1
Dallas	*	...	...	*	*
San Francisco	5.1	...	...	5.1	.0
System total	**12.9**	...	...	**12.3**	**.5**

1. Details may not sum to totals because of rounding; also, expenses related to research and development projects are reported at the System level, and therefore the sum of expenses for the twelve Districts may not equal the System total. The financial results for each Reserve Bank shown here do not include the dollars to be recovered through the PSAF and the net income on clearing balances. To reconcile net revenue by priced service shown in this table with that shown in the income statement by service, adjustments must be made for imputed interest on debt, sales taxes, FDIC assessment, Board expenses for priced services, and net income on clearing balances.

*In absolute value, greater than zero and less than $50,000.

Board of Governors Financial Statements

The financial statements of the Board were audited by Coopers & Lybrand, independent public accountants, for 1992 and 1991.

Report of Independent Accountants

To the Board of Governors of the
Federal Reserve System

We have audited the accompanying balance sheets of the Board of Governors of the Federal Reserve System (the Board), as of December 31, 1992 and 1991, and the related statements of revenues and expenses and fund balance and cash flows for the years then ended. These financial statements are the responsibility of the Board's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Board of Governors of the Federal Reserve System as of December 31, 1992 and 1991, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

Coopers & Lybrand

Washington, D.C.
February 12, 1993

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

BALANCE SHEET

	As of December 31,	
	1992	1991
ASSETS		
CURRENT ASSETS		
Cash	$ 9,853,172	$ 4,498,138
Accounts receivable	2,543,876	1,227,367
Prepaid expenses and other assets	1,462,101	778,485
Total current assets	13,859,149	6,503,990
PROPERTY, BUILDINGS AND EQUIPMENT, NET (Note 3)	48,968,026	50,338,953
Total assets	$62,827,175	$56,842,943
LIABILITIES AND FUND BALANCE		
CURRENT LIABILITIES		
Accounts payable	$ 5,311,460	$ 3,609,392
Accrued payroll and related taxes	1,978,051	1,120,332
Accrued annual leave	5,612,406	5,057,365
Unearned revenues and other liabilities	1,366,877	1,257,442
Total current liabilities	14,268,794	11,044,531
COMMITMENTS (Note 5)	—	—
FUND BALANCE	48,558,381	45,798,412
Total liabilities and fund balance	$62,827,175	$56,842,943

The accompanying notes are an integral part of these statements.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

STATEMENT OF REVENUES AND EXPENSES AND FUND BALANCE

	For the years ended December 31, 1992	1991
BOARD OPERATING REVENUES		
Assessments levied on Federal Reserve Banks for Board operating expenses and capital expenditures	$128,955,300	$109,631,000
Other revenues (Note 4)	6,795,747	4,855,384
Total operating revenues	135,751,047	114,486,384
BOARD OPERATING EXPENSES		
Salaries	81,981,637	75,391,334
Retirement and insurance contributions	13,106,634	11,590,355
Contractual services and professional fees	7,527,562	3,113,853
Depreciation and net losses on disposals	6,079,387	5,682,355
Travel	3,953,838	3,542,401
Repairs and maintenance	3,757,815	2,877,050
Postage and supplies	3,687,785	3,344,444
Utilities	3,607,431	3,286,946
Software	2,751,537	2,478,238
Printing and binding	2,089,901	2,059,165
Other expenses (Note 4)	4,447,551	3,709,310
Total operating expenses	132,991,078	117,075,451
BOARD OPERATING REVENUES OVER (UNDER) EXPENSES	2,759,969	(2,589,067)
ISSUANCE AND REDEMPTION OF FEDERAL RESERVE NOTES		
Assessments levied on Federal Reserve Banks for currency costs	295,400,650	261,316,379
Expenses for currency printing, issuance, retirement, and shipping	295,400,650	261,316,379
CURRENCY ASSESSMENTS OVER (UNDER) EXPENSES	—	—
TOTAL REVENUES OVER (UNDER) EXPENSES	2,759,969	(2,589,067)
FUND BALANCE, Beginning of year	45,798,412	48,387,479
FUND BALANCE, End of year	$ 48,558,381	$ 45,798,412

The accompanying notes are an integral part of these statements.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

STATEMENT OF CASH FLOWS

Increase (Decrease) in Cash

	For the years ended December 31, 1992	1991
Cash Flows from Operating Activities		
Board operating revenues over (under) expenses	$ 2,759,969	$(2,589,067)
Adjustments to reconcile operating revenues over (under) expenses to net cash provided by operating activities:		
Depreciation and net losses on disposals	6,079,387	5,682,355
Increase in accounts receivable, and prepaid expenses and other assets	(2,000,125)	(31,932)
Increase in accrued annual leave	555,041	296,852
Increase (Decrease) in accounts payable	1,702,068	(599,325)
Increase (Decrease) in payroll payable	857,719	(2,552,920)
Increase in unearned revenue and other liabilities	109,435	215,275
Net cash provided by operating activities	10,063,494	421,238
Cash Flows from Investing Activities		
Proceeds from disposals of furniture and equipment	15,104	36,156
Capital expenditures	(4,723,564)	(5,215,541)
Net cash used in investing activities	(4,708,460)	(5,179,385)
Net Increase (Decrease) in Cash	5,355,034	(4,758,147)
Cash Balance, Beginning of year	4,498,138	9,256,285
Cash Balance, End of year	$ 9,853,172	$ 4,498,138

The accompanying notes are an integral part of these statements.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

NOTES TO FINANCIAL STATEMENTS

(1) Significant Accounting Policies

Board Operating Revenues and Expenses—Assessments made on the Federal Reserve Banks for Board operating expenses and capital expenditures are calculated based on expected cash needs. These assessments, other operating revenues, and operating expenses are recorded on the accrual basis of accounting.

Issuance and Redemption of Federal Reserve Notes—The Board incurs expenses and assesses the Federal Reserve Banks for the costs of printing, issuing, shipping, and retiring Federal Reserve Notes. These assessments and expenses are separately reported in the statements of revenues and expenses because they are not Board operating transactions.

Property, Buildings, and Equipment—The Board's property, buildings, and equipment are stated at cost less accumulated depreciation. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets, which range from four to ten years for furniture and equipment and from ten to fifty years for building equipment and structures. Upon the sale or other disposition of a depreciable asset, the cost and related accumulated depreciation are removed from the accounts and any gain or loss is recognized.

Reclassification—Certain amounts from prior years have been reclassified to conform with current year presentation.

(2) Retirement Benefits

Substantially all of the Board's employees participate in either the Retirement Plan for Employees of the Federal Reserve System or the Civil Service Plan. The System's Plan is a multiemployer plan which covers employees of the Federal Reserve Banks, the Board, and the Plan Administrative Office. Employees of the Board who entered on duty before 1984 are covered by a contributory defined benefits program under the Plan. Employees of the Board who entered on duty after 1983 are covered by a non-contributory defined benefits program under the Plan. The Civil Service Plan is a defined contribution plan.

Contributions to the System's Plan are actuarially determined and funded by participating employers at amounts prescribed by the Plan's administrator. No separate accounting is maintained of assets contributed by the participating employers and net pension cost for the period is the required contribution for the period. As of December 31, 1992, actuarial calculations showed that the fair value of the assets of the System's Plan exceeded the projected benefit obligations. Based on these calculations and similar calculations performed for 1991, it was determined that employer funding contributions were not required for the years 1992 and 1991 and the Board was not assessed a contribution for these years. Excess Plan assets will continue to fund future years' contributions.

Board contributions to the Civil Service Plan directly match employee contributions. The Board's contributions to the Civil Service Plan totaled $708,030 in 1992 and $674,700 in 1991.

Employees of the Board may also participate in the Federal Reserve System's Thrift Plan. Under the Thrift Plan, members may contribute up to a fixed percentage of their salary. Board contributions are based upon a fixed percentage of each member's basic contribution and were $3,419,000 in 1992 and $2,696,800 in 1991.

The Board also provides certain health benefits for retired employees. The cost of providing the benefits is recognized by expensing the insurance premiums which were $554,195 in 1992 and $479,476 in 1991.

(3) Property, Buildings, and Equipment

The following is a summary of the components of the Board's fixed assets, at cost, net of accumulated depreciation.

	As of December 31, 1992	1991
Land and improvements	$ 1,301,314	$ 1,301,314
Buildings	63,856,738	63,726,137
Furniture and equipment	38,550,995	35,146,359
	103,709,047	100,173,810
Less accumulated depreciation	54,741,021	49,834,857
Total property, buildings, and equipment	$ 48,968,026	$ 50,338,953

(4) Other Revenues and Other Expenses

The following are summaries of the components of Other Revenues and Other Expenses.

	For the years ended December 31, 1992	1991
Other Revenues		
Data processing revenue	$2,737,073	$2,364,284
Subscription revenue	1,537,013	1,744,775
Reimbursement of regulatory investigation costs	1,500,000	—
Reimbursable services to other agencies	471,590	334,922
Miscellaneous	550,071	411,403
Total other revenues	$6,795,747	$4,855,384

(4) OTHER REVENUES AND OTHER EXPENSES—Cont.

Other Expenses		
Cafeteria operations, net	$ 765,478	$ 783,362
Tuition, registration, and membership fees	866,965	692,131
Equipment and facility rentals	873,672	682,962
Subsidies and contributions	735,835	638,975
Miscellaneous	1,205,601	911,880
Total other expenses	$4,447,551	$3,709,310

(5) COMMITMENTS

The Board has entered into several operating leases to secure office, classroom, and warehouse space for periods ranging from two to ten years. Minimum future rental commitments under those operating leases having an initial or remaining noncancelable lease term in excess of one year at December 31, 1992, are as follows:

1993	$ 1,915,444
1994	2,225,724
1995	1,946,477
1996	1,854,642
1997	1,837,538
after 1997	569,226
	$10,349,051

Rental expenses under these operating leases were $644,609 and $635,100 in 1992 and 1991, respectively.

(6) FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL

The Board is one of the five member agencies of the Federal Financial Institutions Examination Council (the "Council"). During 1992 and 1991, the Board paid $324,300 and $241,040, respectively, in assessments for operating expenses of the Council. These amounts are included in subsidies and contributions for 1992 and 1991. ■

Statistical Tables

1. Detailed Statement of Condition of All Federal Reserve Banks Combined, December 31, 1992[1]

Thousands of dollars

ASSETS				
Gold certificate account				**11,055,613**
Special drawing rights certificate account				**8,018,000**
Coin				**446,078**
Loans and securities				
Loans to depository institutions			**674,690**	
Federal agency obligations				
Bought outright			**5,412,625**	
Held under repurchase agreement			**631,000**	
U.S. Treasury securities				
Bought outright				
Bills	**141,794,280**			
Notes	**118,179,154**			
Bonds	**35,037,172**			
Total bought outright		**295,010,606**		
Held under repurchase agreement		**7,463,000**		
Total securities			**302,473,606**	
Total loans and securities				**309,191,921**
Items in process of collection				
Transit items			7,770,112	
Other items in process of collection			1,141,236	
Total items in process of collection				**8,911,348**
Bank premises				
Land			157,201	
Buildings (including vaults)	758,056			
Building machinery and equipment	208,635			
Construction account	156,148			
Total bank premises		1,122,839		
Less depreciation allowance		254,306	868,533	
Bank premises, net				**1,025,734**
Other assets				
Furniture and equipment		922,125		
Less depreciation		534,813		
Total furniture and equipment, net			387,312	
Denominated in foreign currencies[2]			21,513,571	
Interest accrued			3,259,086	
Premium on securities			2,918,509	
Overdrafts			239,164	
Prepaid expenses			492,823	
Suspense account			103,377	
Real estate acquired for banking-house purposes			28,363	
Other			309,792	
Total other assets				**29,251,996**
Total assets				**367,900,690**

1.—Continued

Liabilities		
Federal Reserve Notes		
Outstanding (issued to Federal Reserve Banks)	363,479,179	
Less held by Federal Reserve Banks	49,271,395	
Total Federal Reserve notes, net		**314,207,783**
Deposits		
Depository institutions		**32,078,917**
U.S. Treasury, general account		**7,491,659**
Foreign, official accounts		**205,745**
Other deposits		
Officers' and certified checks	24,214	
International organizations	124,960	
Other[3]	222,461	
Total other deposits		**371,635**
Deferred credit items		**5,561,352**
Other liabilities		
Discount on securities	1,766,442	
Sundry items payable	69,775	
Suspense account	14,312	
All other	25,826	
Total other liabilities		**1,876,354**
Total liabilities		**361,793,445**
Capital Accounts		
Capital paid in		**3,053,622**
Surplus		**3,053,622**
Other capital accounts[4]		**0**
Total liabilities and capital accounts		**367,900,690**

1. Amounts in boldface type indicate items in the Board's weekly statement of condition of the Federal Reserve Banks.
2. Of this amount $7,889.5 million was invested in securities issued by foreign governments, and the balance was invested with foreign central banks and the Bank for International Settlements.
3. In closing out the other capital accounts at year-end, the Reserve Bank earnings that are payable to the Treasury are included in this account pending payment.
4. During the year, includes undistributed net income, which is closed out on December 31.

2. Statement of Condition of Each Federal Reserve Bank, December 31, 1992 and 1991

Millions of dollars[1]

Item	Total 1992	Total 1991	Boston 1992	Boston 1991
ASSETS				
Gold certificate account	11,056	11,059	705	747
Special drawing rights certificate account	8,018	10,018	511	711
Coin	446	528	19	34
Loans				
To depository institutions	675	218	0	0
Other	0	0	0	0
Acceptances held under repurchase agreements	0	0	0	0
Federal agency obligations				
Bought outright	5,413	6,045	346	409
Held under repurchase agreements	631	553	0	0
U.S. Treasury securities				
Bought outright[2]	295,011	266,486	18,843	18,041
Held under repurchase agreements	7,463	15,345	0	0
Total loans and securities	309,192	288,647	19,189	18,450
Items in process of collection	8,911	8,286	634	464
Bank premises	1,026	987	90	89
Other assets				
Denominated in foreign currencies[3]	21,514	27,626	794	1,111
All other	7,738	5,911	376	303
Interdistrict Settlement Account	0	0	−1,634	−1,287
Total assets	**367,901**	**353,061**	**20,683**	**20,623**
LIABILITIES				
Federal Reserve notes	314,208	287,906	18,572	18,350
Deposits				
Depository institutions	32,079	29,413	1,442	1,391
U.S. Treasury, general account	7,492	17,697	0	0
Foreign, official accounts	206	968	5	6
Other	372	1,706	21	81
Total deposits	40,148	49,783	1,468	1,478
Deferred credit items	5,561	7,259	311	443
Other liabilities and accrued dividends[4]	1,876	2,810	115	156
Total liabilities	**361,793**	**347,758**	**20,466**	**20,428**
CAPITAL ACCOUNTS				
Capital paid in	3,054	2,652	108	99
Surplus	3,054	2,652	108	98
Other capital accounts	0	0	0	0
Total liabilities and capital accounts	**367,901**	**353,061**	**20,683**	**20,623**
FEDERAL RESERVE NOTE STATEMENT				
Federal Reserve notes outstanding (issued to Bank)	363,479	366,468	21,432	23,044
Less: Held by Bank	49,271	78,562	2,860	4,693
Federal Reserve notes, net	**314,208**	**287,906**	**18,572**	**18,350**
Collateral for Federal Reserve notes				
Gold certificate account	11,056	11,059	...	...
Special drawing rights certificate account	8,018	10,018	...	...
Other eligible assets	0	0	...	...
U.S. Treasury and federal agency securities	295,134	266,829	...	...
Total collateral	**314,208**	**287,906**	...	...

For notes see end of table.

2.—Continued

New York		Philadelphia		Cleveland		Richmond	
1992	1991	1992	1991	1992	1991	1992	1991
4,042	3,914	347	318	658	692	941	948
2,808	3,395	303	319	556	645	652	961
13	16	24	40	26	30	95	99
0	7	592	45	0	0	0	105
0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0
2,106	2,382	165	160	341	378	423	478
631	553	0	0	0	0	0	0
114,769	105,022	8,979	7,041	18,569	16,674	23,068	21,079
7,463	15,345	0	0	0	0	0	0
124,969	123,309	2,736	7,246	18,909	17,052	23,492	21,662
1,352	969	538	592	442	354	760	608
137	127	45	44	36	34	128	123
6,258	7,606	852	1,312	1,308	1,428	1,383	1,688
3,421	2,918	199	146	375	350	876	374
−19,514	−12,000	2,183	3,172	1,420	1,766	−220	321
123,485	**130,253**	**14,227**	**13,189**	**23,731**	**22,352**	**28,106**	**26,784**
105,028	100,834	11,341	10,872	21,680	19,950	25,083	23,426
7,531	6,461	2,207	1,470	1,341	1,572	2,025	2,210
7,492	17,697	0	0	0	0	0	0
107	859	6	7	9	8	9	9
195	642	8	74	15	88	32	66
15,324	25,658	2,221	1,551	1,364	1,667	2,068	2,285
629	866	368	490	220	270	392	541
733	1,353	62	66	114	143	144	191
121,715	**128,710**	**13,992**	**12,979**	**23,378**	**22,029**	**27,686**	**26,443**
885	771	117	105	176	161	210	171
885	771	117	105	176	161	210	171
0	0	0	0	0	0	0	0
125,485	**130,253**	**14,227**	**13,189**	**23,731**	**22,352**	**28,106**	**26,784**
119,266	128,066	13,058	13,068	23,683	23,151	29,944	31,583
14,238	27,231	1,717	2,196	2,003	3,201	4,861	8,158
105,028	**100,834**	**11,341**	**10,872**	**21,680**	**19,950**	**25,083**	**23,426**
...	...	...	...	...	...	...	...
...	...	...	...	...	...	...	...
...	...	...	...	...	...	...	...

2. Statement of Condition of Each Federal Reserve Bank, December 31, 1992 and 1991—Continued

Millions of dollars[1]

Item	Atlanta		Chicago	
	1992	1991	1992	1991
ASSETS				
Gold certificate account	503	479	1,270	1,370
Special drawing rights certificate account	318	303	1,036	1,336
Coin	38	46	30	53
Loans				
To depository institutions	1	1	2	13
Other	0	0	0	0
Acceptances held under repurchase agreements	0	0	0	0
Federal agency obligations				
Bought outright	184	202	670	760
Held under repurchase agreements	0	0	0	0
U.S. Treasury securities				
Bought outright[2]	10,043	8,912	36,537	33,486
Held under repurchase agreements	0	0	0	0
Total loans and securities	10,229	9,115	37,210	34,259
Items in process of collection	1,305	895	923	799
Bank premises	57	57	112	112
Other assets				
Denominated in foreign currencies[3]	1,971	2,799	2,603	3,420
All other	326	205	777	599
Interdistrict Settlement Account	3,833	1,987	−3,444	237
Total assets	**18,579**	**15,887**	**40,517**	**42,183**
LIABILITIES				
Federal Reserve notes	13,232	11,426	35,485	37,207
Deposits				
Depository institutions	4,083	2,970	3,422	3,102
U.S. Treasury, general account	0	0	0	0
Foreign, official accounts	13	15	17	19
Other	5	117	49	211
Total deposits	4,101	3,102	3,489	3,332
Deferred credit items	600	792	621	702
Other liabilities and accrued dividends[4]	67	81	231	301
Total liabilities	**18,000**	**15,401**	**39,825**	**41,542**
CAPITAL ACCOUNTS				
Capital paid in	290	243	346	321
Surplus	290	243	346	321
Other capital accounts	0	0	0	0
Total liabilities and capital accounts	**18,579**	**15,887**	**40,517**	**42,183**
FEDERAL RESERVE NOTE STATEMENT				
Federal Reserve notes outstanding (issued to Bank)	17,318	17,196	38,700	41,660
Less: Held by Bank	4,086	5,771	3,215	4,452
Federal Reserve notes, net	**13,232**	**11,426**	**35,485**	**37,207**

1. Components may not sum to totals because of rounding.
2. Includes securities loaned—fully guaranteed by U.S. Treasury securities pledged with Federal Reserve Banks—and excludes securities sold and scheduled to be bought back under matched sale-purchase transactions.
3. Valued monthly at market exchange rates.
4. Includes exchange-translation account reflecting the monthly revaluation at market exchange rates of foreign-exchange commitments.

2.—Continued

St. Louis		Minneapolis		Kansas City		Dallas		San Francisco	
1992	1991	1992	1991	1992	1991	1992	1991	1992	1991
304	328	195	171	329	370	463	515	1,299	1,207
168	307	186	172	199	334	377	463	904	1,072
25	29	16	14	36	31	27	43	98	94
5	25	1	0	5	9	0	3	69	11
0	0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0	0
132	160	84	78	146	168	199	237	616	633
0	0	0	0	0	0	0	0	0	0
7,218	7,058	4,598	3,445	7,981	7,386	10,823	10,456	33,583	27,886
0	0	0	0	0	0	0	0	0	0
7,356	7,243	4,683	3,523	8,131	7,563	11,021	10,695	34,268	28,528
294	275	415	544	482	515	418	773	1,349	1,498
30	29	33	32	51	53	161	141	146	147
531	724	566	782	807	1,055	1,717	2,105	2,724	3,597
152	128	120	77	169	136	282	192	667	482
5,311	−1,609	2,555	2,640	5,062	−810	2,314	1,600	2,134	3,983
14,171	**7,453**	**8,768**	**7,955**	**15,266**	**9,247**	**16,781**	**16,526**	**43,589**	**40,608**
12,824	6,035	7,458	6,691	13,544	7,145	14,082	13,530	35,878	32,440
952	914	721	653	1,079	1,313	1,808	1,646	5,466	5,713
0	0	0	0	0	0	0	0	0	0
3	4	4	4	5	6	11	11	18	20
3	42	5	38	6	60	27	97	6	192
958	960	730	695	1,090	1,379	1,846	1,754	5,490	5,924
204	255	390	399	362	458	356	722	1,108	1,321
44	73	29	31	53	68	73	96	212	251
14,031	**7,322**	**8,608**	**7,816**	**15,049**	**9,049**	**16,357**	**16,103**	**42,688**	**39,936**
70	66	80	70	109	99	212	211	450	336
70	66	80	70	109	99	212	211	450	336
0	0	0	0	0	0	0	0	0	0
14,171	**7,453**	**8,768**	**7,955**	**15,266**	**9,247**	**16,781**	**16,526**	**43,589**	**40,608**
14,440	8,883	8,191	8,117	15,086	9,618	16,914	17,683	45,448	44,400
1,617	2,848	733	1,427	1,542	2,473	2,831	4,152	9,570	11,961
12,824	**6,035**	**7,458**	**6,691**	**13,544**	**7,145**	**14,082**	**13,530**	**35,878**	**32,440**

3. Federal Reserve Open Market Transactions, 1992[1]

Millions of dollars

Type of transaction	Jan.	Feb.	Mar.	Apr.
U.S. TREASURY SECURITIES				
Outright transactions (excluding matched transactions)				
Treasury bills				
Gross purchases	0	123	505	0
Gross sales	1,628	0	0	0
Exchanges	26,750	24,435	21,674	27,526
Redemptions	1,600	0	0	0
Others within 1 year				
Gross purchases	0	0	0	0
Gross sales	0	0	0	0
Maturity shift	1,174	6,020	2,552	877
Exchanges	−989	−2,742	−2,512	−1,863
Redemptions	0	0	0	0
1 to 5 years				
Gross purchases	0	1,027	1,425	0
Gross sales	0	0	0	0
Maturity shift	−1,050	−6,020	−2,552	−654
Exchanges	539	2,292	2,512	1,484
5 to 10 years				
Gross purchases	0	0	0	0
Gross sales	0	0	0	0
Maturity shift	−124	96	0	−223
Exchanges	451	300	0	379
More than 10 years				
Gross purchases	0	0	0	0
Gross sales	0	0	0	0
Maturity shift	0	−96	0	0
Exchanges	0	150	0	0
All maturities				
Gross purchases	0	1,150	1,930	0
Gross sales	1,628	0	0	0
Redemptions	1,600	0	0	0
Matched transactions				
Gross sales	136,922	123,000	128,230	125,999
Gross purchases	136,282	124,654	126,673	128,149
Repurchase agreements[2]				
Gross purchases	21,412	9,824	48,758	18,432
Gross sales	33,228	13,353	46,953	20,237
Net change in U.S. Treasury securities	−15,684	−725	2,178	345
FEDERAL AGENCY OBLIGATIONS				
Outright transactions				
Gross purchases	0	0	0	0
Gross sales	0	0	0	0
Redemptions	85	0	0	49
Repurchase agreements[2]				
Gross purchases	390	571	1,640	224
Gross sales	808	706	1,640	224
Net change in agency obligations	−503	−135	0	−49
Total net change in System Open Market Account	**−16,186**	**−860**	**2,178**	**295**

1. Sales, redemptions, and negative figures reduce holdings of the System Open Market Account; all other figures increase such holdings. Details may not sum to totals because of rounding.

2. In July 1984 the Open Market Trading Desk discontinued accepting bankers acceptances in repurchase agreements.

3.—Continued

May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.	Total
4,110	306	0	271	595	4,072	1,064	3,669	14,714
0	0	0	0	0	0	0	0	1,628
24,275	22,028	30,755	25,041	22,277	28,907	25,468	29,562	308,699
0	0	0	0	0	0	0	0	1,600
0	285	0	0	350	0	461	0	1,096
0	0	0	0	0	0	0	0	0
2,459	3,447	985	4,448	2,753	2,010	7,160	2,777	36,662
−5,225	−1,854	−1,669	−4,617	−1,905	−982	−4,615	−1,570	−30,543
0	0	0	0	0	0	0	0	0
200	1,993	0	400	3,500	200	4,172	200	13,118
0	0	0	0	0	0	0	0	0
−2,113	−3,447	−514	−4,036	−2,753	−1,762	−6,800	−2,777	−34,478
4,311	1,854	1,478	3,567	1,905	884	3,415	1,570	25,811
0	597	0	195	750	0	1,176	100	2,818
0	0	0	0	0	0	0	0	0
−346	0	−471	−412	0	−248	−187	0	−1,915
614	0	191	700	0	97	800	0	3,532
0	655	0	0	731	0	947	0	2,333
0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	−173	0	−269
300	0	0	350	0	0	400	0	1,200
4,310	3,836	0	866	5,927	4,272	7,820	3,969	34,079
0	0	0	0	0	0	0	0	1,628
0	0	0	0	0	0	0	0	1,600
118,972	126,977	127,051	103,708	116,331	116,024	115,020	144,232	1,482,467
117,524	129,216	126,137	101,410	115,579	114,917	117,020	142,578	1,480,140
38,777	10,792	12,224	39,484	68,697	18,698	42,373	48,904	378,374
38,533	11,036	12,224	31,868	59,628	35,383	39,117	44,697	386,257
3,107	5,831	−914	6,184	14,244	−13,520	13,075	6,521	20,642
0	0	0	0	0	0	0	0	0
0	0	0	0	0	0	0	0	0
160	40	85	54	37	0	0	121	632
1,281	402	94	601	3,222	1,778	2,760	1,601	14,565
1,281	402	94	548	1,800	3,253	2,506	1,224	14,486
−160	−40	−85	−1	1,385	−1,475	254	256	−554
2,946	**5,791**	**−1,000**	**6,183**	**15,629**	**−14,995**	**13,329**	**6,777**	**20,089**

4. Federal Reserve Bank Holdings of U.S. Treasury and Federal Agency Securities, December 31, 1990–92[1]

Millions of dollars

Description	December 31			Increase or decrease (–)	
	1992	1991	1990	1992	1991
U.S. Treasury securities, total	**302,474**	**281,831**	**252,103**	**20,643**	**29,728**
By term					
1–15 days[2]	12,824	21,109	22,530	–8,285	–1,421
16–90 days	70,610	66,759	57,538	3,851	9,221
91 days to 1 year	103,582	90,655	75,428	12,927	15,227
1–5 years	68,750	64,299	58,749	4,451	5,550
5–10 years	18,903	14,469	13,121	4,434	1,348
More than 10 years	27,805	24,540	24,736	3,265	–196
By type of holding					
Held outright					
Treasury bills[3]	141,794	132,635	112,520	9,159	20,115
Treasury notes	118,179	101,520	91,407	16,659	10,113
Treasury bonds	35,037	32,331	31,163	2,706	1,168
Held under repurchase agreements	7,463	15,345	17,013	–7,882	–1,668
Federal agency obligations, total	**5,413**	**6,045**	**6,342**	**–632**	**–297**
By term					
1–15 days	190	200	200	–10	0
16–90 days	810	811	737	–1	74
91 days to 1 year	1,064	1,329	1,639	–265	–310
1–5 years	2,511	2,508	2,555	3	–47
5–10 years	696	1,008	1,022	–312	–14
More than 10 years	142	188	188	–46	0
By type of holding					
Held outright					
Federal Farm Credit Banks	1,296	1,440	1,560	–144	–120
Federal Home Loan Banks	1,766	2,029	2,161	–263	–132
Federal Land Banks	66	66	108	0	–42
Federal National Mortgage Association	2,167	2,342	2,346	–175	–4
U.S. Postal Service	0	37	37	–37	0
Washington Metropolitan Area Transit Authority	117	117	117	0	0
General Services Administration	0	12	12	–12	0
Held under repurchase agreements	631	553	1,341	78	–788

1. Details may not sum to totals because of rounding.
2. Includes the effects of temporary transactions (repurchase agreements and matched sale–purchase agreements).
3. Includes the effects of matched sale–purchase agreements.

5. Number and Salaries of Officers and Employees of Federal Reserve Banks, December 31, 1992

Federal Reserve Bank (including) branches	President	Other officers		Employees			Total	
	Annual salary (dollars)	Number	Annual salaries (dollars)	Number: Full-time	Number: Part-time	Annual salaries (dollars)	Number	Annual salaries (dollars)
Boston	172,400	55	5,125,500	1,232	252	47,400,373	1,540	52,698,273
New York	257,700	175	18,147,325	3,994	68	149,316,167	4,238	167,721,192
Philadelphia	180,000	63	5,759,350	1,326	130	41,693,141	1,520	47,632,491
Cleveland	160,000	62	5,438,350	1,229	74	36,357,531	1,366	41,955,881
Richmond	199,200	81	6,763,500	1,941	124	55,810,045	2,147	62,772,745
Atlanta	206,800	75	6,236,200	2,288	60	67,044,427	2,424	73,487,427
Chicago	216,300	97	8,401,650	2,405	45	78,809,730	2,548	87,427,680
St. Louis	186,200	52	3,975,400	1,074	110	31,256,076	1,237	35,417,676
Minneapolis	170,100	48	4,082,300	1,046	110	33,047,797	1,205	37,300,197
Kansas City	153,000	57	4,815,000	1,568	41	47,019,381	1,667	51,987,381
Dallas	155,600	57	4,745,650	1,562	51	47,340,298	1,671	52,241,548
San Francisco	224,000	95	9,338,625	2,364	74	83,027,160	2,534	92,589,785
Federal Reserve Automation Service		23	2,205,775	203	0	9,461,880	226	11,667,655
Total	**2,281,300**	**940**	**85,034,625**	**22,232**	**1,139**	**727,584,006**	**24,323**	**814,899,931**

6. Income and Expenses of Federal Reserve Banks, 1992

Dollars

Item [1]	Total	Boston	New York	Philadelphia	Cleveland
CURRENT INCOME					
Loans	6,067,617	151,445	992,253	343,370	51,177
U.S. Treasury and federal agency securities	17,336,350,446	1,121,372,762	6,824,747,348	504,283,274	1,083,681,615
Foreign currencies	2,122,018,858	78,725,876	615,293,854	85,045,492	127,851,245
Priced services	758,392,481	44,676,475	106,480,551	41,061,467	43,856,163
Other	12,198,537	361,601	7,104,890	263,036	284,196
Total	**20,235,027,938**	**1,245,288,159**	**7,554,618,896**	**630,996,639**	**1,255,724,397**
CURRENT EXPENSES					
Salaries and other personnel expenses	845,649,640	53,598,166	174,461,911	47,560,571	46,745,596
Retirement and other benefits [2]	65,803,906	12,733,411	41,466,468	12,025,524	11,616,831
Fees	25,490,088	4,784,742	2,248,141	728,888	2,075,464
Travel	37,213,324	1,986,917	5,458,686	1,905,612	2,347,623
Software expenses	35,874,992	1,921,494	8,016,353	1,656,512	1,645,050
Postage and other shipping costs	85,468,987	4,718,052	11,032,923	4,633,677	6,201,564
Communications	10,016,433	511,418	2,125,978	473,529	728,499
Materials and supplies	55,069,920	3,225,555	9,536,278	3,261,890	2,903,058
Building expenses					
Taxes on real estate	23,289,904	3,147,448	4,662,387	1,870,149	1,366,691
Property depreciation	38,762,965	3,142,836	5,401,142	1,841,677	1,874,174
Utilities	29,299,069	2,304,715	4,974,857	3,155,158	1,776,957
Rent	28,103,045	626,580	18,716,964	232,748	351,764
Other	22,049,349	712,127	3,285,944	1,150,650	775,648
Equipment					
Purchases	6,635,049	369,833	173,868	347,233	165,912
Rentals	21,507,097	798,771	5,165,035	800,371	761,219
Depreciation	96,803,422	5,135,673	18,590,193	3,892,074	6,410,854
Repairs and maintenance	54,879,234	3,202,914	9,124,858	2,763,498	3,777,792
Earnings-credit costs	177,076,512	10,285,795	36,530,922	19,217,932	7,166,749
Other	38,436,737	2,540,311	6,128,698	1,668,530	2,374,800
Shared costs, net [3]	0	(715,064)	(2,589,340)	3,214,578	2,097,431
Recoveries	(39,890,532)	(9,285,111)	(3,885,810)	(2,976,430)	(3,505,458)
Expenses capitalized [4]	(2,555,498)	(316,949)	(5,760)	(71,472)	(383,494)
Total	**1,654,983,643**	**105,429,634**	**360,620,696**	**109,352,899**	**99,274,725**
Reimbursements	(180,453,120)	(9,155,026)	(37,712,388)	(19,326,840)	(16,428,504)
Net expenses	1,474,530,523	96,274,608	322,908,308	90,026,059	82,846,221

For notes see end of table.

6.—Continued

Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
336,934	231,213	403,053	840,557	1,300,667	554,580	180,646	681,722
1,353,341,163	584,086,217	2,145,434,724	432,402,201	255,108,267	470,007,424	645,882,649	1,916,002,802
136,035,263	195,621,407	257,123,513	52,606,311	56,065,690	79,665,515	168,875,236	269,109,456
65,425,789	92,977,699	99,463,226	30,872,707	40,733,402	48,337,755	53,344,955	91,162,291
312,604	692,820	952,994	253,027	449,419	107,338	290,689	1,125,923
1,555,451,752	**873,609,356**	**2,503,377,510**	**516,974,803**	**353,657,445**	**598,672,612**	**868,574,175**	**2,278,082,194**
72,117,094	77,324,778	90,838,796	37,067,307	37,950,193	54,919,567	55,690,342	97,375,319
17,770,550	20,375,430	22,449,851	9,195,081	8,560,144	14,616,290	12,944,810	22,857,247
8,038,001	1,636,053	955,689	817,399	1,424,007	689,009	932,340	1,160,355
4,011,529	3,735,201	4,222,085	1,948,207	2,266,213	2,591,317	2,387,032	4,352,902
5,198,745	2,325,782	4,334,676	1,556,991	2,073,586	1,502,577	2,171,104	3,472,122
7,519,064	10,509,949	9,594,569	4,053,560	5,738,104	5,983,218	4,869,062	10,615,245
698,383	1,112,598	989,319	589,922	457,643	750,176	911,293	667,675
5,888,751	5,754,751	6,140,565	3,262,950	2,161,529	3,345,383	3,920,803	5,668,407
2,167,950	1,768,180	1,276,525	467,756	923,326	842,022	2,377,097	2,420,373
4,312,079	3,104,326	4,649,505	1,845,743	1,244,003	3,210,652	2,471,471	5,665,357
2,620,658	2,327,123	2,518,235	1,583,692	939,176	1,518,966	2,053,148	3,526,384
1,801,945	1,229,812	2,016,872	414,712	517,921	307,044	1,633,386	253,296
2,547,807	2,458,119	5,067,774	826,055	648,959	912,063	1,538,706	2,125,497
775,373	820,731	1,071,816	210,073	651,398	280,921	668,144	1,099,748
1,517,480	2,057,272	3,285,886	454,140	687,087	2,341,675	1,280,452	2,357,709
15,749,986	7,408,769	13,106,225	3,133,021	4,456,801	2,674,234	5,887,544	10,358,048
5,624,074	5,962,848	8,825,071	1,911,667	2,672,577	1,952,564	2,853,256	6,208,115
11,456,445	13,536,275	28,964,791	4,140,554	4,131,376	9,186,372	11,216,676	21,242,624
4,386,618	4,416,321	4,843,183	1,507,238	1,566,178	2,109,684	2,658,805	4,236,371
(8,550,309)	1,128,205	(5,715,685)	2,763,260	428,788	3,226,170	2,730,578	1,981,387
(5,202,261)	(2,693,365)	(3,369,408)	(1,295,976)	(996,350)	(917,480)	(1,756,557)	(4,006,326)
(274,157)	(308,927)	(102,070)	(77,447)	(241,946)	(355,804)	(343,938)	(73,534)
160,175,805	**165,990,231**	**205,964,270**	**76,375,905**	**78,260,713**	**111,686,620**	**119,095,555**	**203,564,321**
(11,519,875)	(14,092,111)	(19,557,478)	(10,000,764)	(6,856,866)	(11,819,229)	(8,862,605)	(15,121,434)
148,655,930	151,898,120	186,406,792	66,375,141	71,403,847	99,867,391	110,232,950	188,442,887

6. Income and Expenses of Federal Reserve Banks, 1992—Continued

Dollars

Item[1]	Total	Boston	New York	Philadelphia	Cleveland
PROFIT AND LOSS					
Current net income	18,760,497,416	1,149,013,550	7,372,518,318	540,970,580	1,172,878,177
Additions to and deductions from current net income[5]					
Profits on sales of U.S. Treasury and federal agency securities	131,447,796	8,828,460	49,980,606	3,632,617	8,018,932
Profit on foreign exchange transactions	366,450,220	11,931,153	97,121,050	15,218,772	21,833,127
Other additions	(298,078,707)	(12,504,152)	(99,700,683)	(15,346,861)	(22,242,170)
Total additions	199,819,309	8,255,461	47,400,973	3,504,528	7,609,888
Total deductions	(1,158,895,231)	(39,878,680)	(314,525,769)	(42,771,873)	(65,595,821)
Net additions to or deductions (–) from current net income	(959,075,922)	(31,623,219)	(267,124,796)	(39,267,344)	(57,985,932)
Cost of unreimbursed Treasury services	28,711,766	1,256,859	2,522,156	1,413,181	1,751,905
Assessments by Board					
Board expenditures[6]	128,955,300	4,699,200	37,396,200	5,135,700	7,795,200
Cost of currency	295,400,650	18,350,965	101,456,057	10,548,662	18,485,886
Net income before payment to U.S. Treasury	17,348,353,778	1,093,083,307	6,964,019,109	484,605,693	1,086,859,253
Dividends paid	171,762,927	6,096,633	49,868,773	6,856,094	10,100,417
Payments to U.S. Treasury (interest on Federal Reserve notes)	16,774,476,501	1,076,527,924	6,800,550,135	465,532,198	1,061,696,036
Transferred to surplus	402,114,350	10,458,750	113,600,200	12,217,400	15,062,800
Surplus, January 1	2,651,507,750	97,852,000	771,420,400	105,100,500	161,155,750
Surplus, December 31	3,053,622,100	108,310,750	885,020,600	117,317,900	176,218,550

1. Details may not sum to totals because of rounding.
2. The effect of the 1987 implementation of Financial Accounting Standards Board Statement No. 87—Employers' Accounting for Pensions—is recorded in the Total column only and has not been distributed to each District. Accordingly, the sum of the Districts will not equal the Total column for this category or for Total net expenses, and New York will not sum to Current net income. The effect of FASB 87 on the Reserve Banks was a reduction in expenses of $140,870,731.
3. Includes distribution of costs for projects performed by one Bank for the benefit of one or more other Banks.
4. Includes expenses for labor and materials temporarily capitalized and charged to activities when the products are consumed.
5. Includes reimbursement from the U.S. Treasury for uncut sheets of Federal Reserve notes, gains-losses on the sale of Reserve Bank buildings, counterfeit currency that is not charged back to the depositing institution, and stale Reseve Bank checks that are written off.
6. For additional details, see the last four pages of the preceding section: Board of Governors, Financial Statements.

6.—Continued

Richmond	Atlanta	Chicago	St. Louis	Minneapolis	Kansas City	Dallas	San Francisco
1,406,795,823	721,711,236	2,316,970,718	450,599,662	282,253,598	498,805,221	758,341,226	2,089,639,308
11,254,137	4,472,899	16,210,524	4,176,758	1,888,462	3,944,925	4,907,714	14,131,763
23,177,649	34,233,757	46,416,592	10,301,032	11,858,119	14,698,435	27,748,498	51,912,037
(24,906,389)	(34,608,612)	(47,538,468)	66,769,209	(11,894,065)	(15,328,997)	(28,086,690)	(52,690,830)
9,525,397	4,098,044	15,088,647	81,246,999	1,852,516	3,314,363	4,569,522	13,352,971
(69,481,045)	(98,902,259)	(130,557,878)	(104,836,552)	(28,487,784)	(40,892,351)	(86,117,364)	(136,847,856)
(59,955,648)	(94,804,215)	(115,469,230)	(23,589,553)	(26,635,268)	(37,577,988)	(81,547,843)	(123,494,885)
2,891,351	3,010,027	3,240,033	1,669,383	1,957,630	2,582,431	2,317,745	4,099,064
8,474,000	11,888,400	15,443,600	3,183,400	3,431,000	4,810,500	10,274,600	16,423,500
25,527,479	15,152,205	33,248,750	7,170,003	6,643,480	7,858,863	14,354,345	36,603,955
1,309,947,345	596,856,389	2,149,569,105	414,987,323	243,586,220	445,975,439	649,846,693	1,909,017,904
11,464,752	16,384,793	19,888,622	4,091,876	4,681,827	6,210,600	13,076,651	23,041,886
1,258,927,693	533,630,395	2,104,451,832	406,545,547	228,761,942	430,257,039	636,266,342	1,771,329,417
39,554,900	46,841,200	25,228,650	4,349,900	10,142,450	9,507,800	503,700	114,646,600
170,507,100	242,799,000	320,864,550	65,582,350	69,826,350	99,312,100	211,439,600	335,648,050
210,062,000	289,640,200	346,093,200	69,932,250	79,968,800	108,819,900	211,943,300	450,294,650

7. Income and Expenses of Federal Reserve Banks, 1914–92[1]

Dollars

Federal Reserve Bank and period	Current income	Net expenses	Net additions or deductions (–)	Assessments by Board of Governors	
				Board expenditures	Costs of currency
All Banks					
1914–15	2,173,252	2,018,282	5,875	302,304	...
1916	5,217,998	2,081,722	–193,001	192,277	...
1917	16,128,339	4,921,932	–1,386,545	237,795	...
1918	67,584,417	10,576,892	–3,908,574	382,641	...
1919	102,380,583	18,744,815	–4,673,446	594,818	...
1920	181,296,711	27,548,505	–3,743,907	709,525	...
1921	122,865,866	33,722,409	–6,314,796	741,436	...
1922	50,498,699	28,836,504	–4,441,914	722,545	...
1923	50,708,566	29,061,539	–8,233,107	702,634	...
1924	38,340,449	27,767,886	–6,191,143	663,240	...
1925	41,800,706	26,818,664	–4,823,477	709,499	...
1926	47,599,595	24,914,037	–3,637,668	721,724	1,714,421
1927	43,024,484	24,894,487	–2,456,792	779,116	1,844,840
1928	64,052,860	25,401,233	–5,026,029	697,677	805,900
1929	70,955,496	25,810,067	–4,861,642	781,644	3,099,402
1930	36,424,044	25,357,611	–93,136	809,585	2,175,530
1931	29,701,279	24,842,964	311,451	718,554	1,479,146
1932	50,018,817	24,456,755	–1,413,192	728,810	1,105,816
1933	49,487,318	25,917,847	–12,307,074	800,160	2,504,830
1934	48,902,813	26,843,653	–4,430,008	1,372,022	1,025,721
1935	42,751,959	28,694,965	–1,736,758	1,405,898	1,476,580
1936	37,900,639	26,016,338	485,817	1,679,566	2,178,119
1937	41,233,135	25,294,835	–1,631,274	1,748,380	1,757,399
1938	36,261,428	25,556,949	2,232,134	1,724,924	1,629,735
1939	38,500,665	25,668,907	2,389,555	1,621,464	1,356,484
1940	43,537,805	25,950,946	11,487,697	1,704,011	1,510,520
1941	41,380,095	28,535,547	720,636	1,839,541	2,588,062
1942	52,662,704	32,051,226	–1,568,208	1,746,326	4,826,492
1943	69,305,715	35,793,816	23,768,282	2,415,630	5,336,118
1944	104,391,829	39,659,496	3,221,880	2,296,357	7,220,068
1945	142,209,546	41,666,453	–830,007	2,340,509	4,710,309
1946	150,385,033	50,493,246	–625,991	2,259,784	4,482,077
1947	158,655,566	58,191,428	1,973,001	2,639,667	4,561,880
1948	304,160,818	64,280,271	–34,317,947	3,243,670	5,186,247
1949	316,536,930	67,930,860	–12,122,274	3,242,500	6,304,316
1950	275,838,994	69,822,227	36,294,117	3,433,700	7,315,844
1951	394,656,072	83,792,676	–2,127,889	4,095,497	7,580,913
1952	456,060,260	92,051,063	1,583,988	4,121,602	8,521,426
1953	513,037,237	98,493,153	–1,058,993	4,099,800	10,922,067
1954	438,486,040	99,068,436	–133,641	4,174,600	6,489,895
1955	412,487,931	101,158,921	–265,456	4,194,100	4,707,002
1956	595,649,092	110,239,520	–23,436	5,339,800	5,603,176
1957	763,347,530	117,931,908	–7,140,914	7,507,900	6,374,195
1958	742,068,150	125,831,215	124,175	5,917,200	5,973,240
1959	886,226,116	131,848,023	98,247,253	6,470,600	6,384,083
1960	1,103,385,257	139,893,564	13,874,702	6,533,700	7,455,011
1961	941,648,170	148,253,719	3,481,628	6,265,100	6,755,756
1962	1,048,508,335	161,451,206	–55,779	6,654,900	8,030,028
1963	1,151,120,060	169,637,656	614,835	7,572,800	10,062,901
1964	1,343,747,303	171,511,018	725,948	8,655,200	17,229,671
1965	1,559,484,027	172,110,934	1,021,614	8,576,396	23,602,856
1966	1,908,499,896	178,212,045	996,230	9,021,600	20,167,481
1967	2,190,403,752	190,561,166	2,093,876	10,769,596	18,790,084
1968	2,764,445,943	207,677,768	8,519,996	14,198,198	20,474,404
1969	3,373,360,559	237,827,579	–557,553	15,020,084	22,125,657

For notes see end of table.

7.—Continued

Dividends paid	Payments to U.S. Treasury			Transferred to surplus (section 13b)	Transferred to surplus (section 7)
	Franchise tax	Under section 13b	Interest on Federal Reserve notes		
217,463	. . .	. . .	. . .	. . .	. . .
1,742,775	. . .	. . .	. . .	. . .	. . .
6,804,186	1,134,234	. . .	. . .	. . .	1,134,234
5,540,684	. . .	. . .	. . .	. . .	48,334,341
5,011,832	2,703,894	. . .	. . .	. . .	70,651,778
5.654,018	60,724,742	. . .	. . .	. . .	82,916,014
6,119,673	59,974,466	. . .	. . .	. . .	15,993,086
6,307,035	10,850,605	. . .	. . .	. . .	-659,904
6.552.717	3.613.056	. . .	. . .	. . .	2,545,513
6,682,496	113,646	. . .	. . .	. . .	-3,077,962
6,915,958	59,300	. . .	. . .	. . .	2,473,808
7,329,169	818,150	. . .	. . .	. . .	8,464,426
7,754,539	249,591	. . .	. . .	. . .	5,044,119
8,458,463	2,584,659	. . .	. . .	. . .	21,078,899
9,583,911	4,283,231	. . .	. . .	. . .	22,535,597
10,268,598	17,308	. . .	. . .	. . .	-2,297,724
10,029,760	. . .	. . .	. . .	. . .	-7,057,694
9,282,244	2,011,418	. . .	. . .	. . .	11,020,582
8,874,262	. . .	. . .	. . .	. . .	-916,855
8,781,661	. . .	. . .	. . .	-60,323	6,510,071
8,504,974	. . .	297,667	. . .	27,695	607,422
7,829,581	. . .	227,448	. . .	102,880	352,524
7,940,966	. . .	176,625	. . .	67,304	2,616,352
8,019,137	. . .	119,524	. . .	-419,140	1,862,433
8,110,462	. . .	24,579	. . .	-425,653	4,533,977
8,214,971	. . .	82,152	. . .	-54,456	17,617,358
8,429,936	. . .	141,465	. . .	-4,333	570,513
8,669,076	. . .	197,672	. . .	49,602	3,554,101
8,911,342	. . .	244,726	. . .	135,003	40,327,237
9,500,126	. . .	326,717	. . .	201,150	48,409,795
10,182,851	. . .	247,659	. . .	262,133	81,969,625
10,962,160	. . .	67,054	. . .	27,708	81,467,013
11,523,047	. . .	35,605	75,283,818	86,772	8,366,350
11,919,809	. . .	. . .	166,690,356	. . .	18,522,518
12,329,373	. . .	. . .	193,145,837	. . .	21,461,770
13,082,992	. . .	. . .	196,628,858	. . .	21,849,490
13,864,750	. . .	. . .	254,873,588	. . .	28,320,759
14,681,788	. . .	. . .	291,934,634	. . .	46,333,735
15,558,377	. . .	. . .	342,567,985	. . .	40,336,862
16,442,236	. . .	. . .	276,289,457	. . .	35,887,775
17,711,937	. . .	. . .	251,740,721	. . .	32,709,794
18,904,897	. . .	. . .	401,555,581	. . .	53,982,682
20,080,527	. . .	. . .	542,708,405	. . .	61,603,682
21,197,452	. . .	. . .	524,058,650	. . .	59,214,569
22,721,687	. . .	. . .	910,649,768	. . .	-93,600,791
23,948,225	. . .	. . .	896,816,359	. . .	42,613,100
25.569,541	. . .	. . .	687,393,382	. . .	70,892,300
27,412,241	. . .	. . .	799,365,981	. . .	45,538,200
28,912,019	. . .	. . .	879,685,219	. . .	55,864,300
30,781,548	. . .	. . .	1,582,118,614	. . .	-465,822,800
32,351,602	. . .	. . .	1,296,810,053	. . .	27,053,800
33,696,336	. . .	. . .	1,649,455,164	. . .	18,943,500
35,027,312	. . .	. . .	1,907,498,270	. . .	29,851,200
36,959,336	. . .	. . .	2,463,628,983	. . .	30,027,250
39,236,599	. . .	. . .	3,019,160,638	. . .	39,432,450

7. Income and Expenses of Federal Reserve Banks, 1914–92—Continued

Dollars

Federal Reserve Bank and period	Current income	Net expenses	Net additions or deductions (–)	Assessments by Board of Governors	
				Board expenditures	Costs of currency
1970	3,877,218,444	276,571,876	11,441,829	21,227,800	23,573,710
1971	3,723,369,921	319,608,270	94,266,075	32,634,002	24,942,528
1972	3,792,334,523	347,917,112	(49,615,790)	35,234,499	31,454,740
1973	5,016,769,328	416,879,377	(80,653,488)	44,411,700	33,826,299
1974	6,280,090,965	476,234,586	(78,487,237)	41,116,600	30,190,288
1975	6,257,936,784	514,358,633	(202,369,615)	33,577,201	37,130,081
1976	6,623,220,383	558,128,811	7,310,500	41,827,700	48,819,453
1977	6,891,317,498	568,851,419	(177,033,463)	47,366,100	55,008,163
1978	8,455,309,401	592,557,841	(633,123,486)	53,321,700	60,059,365
1979	10,310,148,406	625,168,261	(151,148,220)	50,529,700	68,391,270
1980	12,802,319,335	718,032,836	(115,385,855)	62,230,800	73,124,423
1981	15,508,349,653	814,190,392	(372,879,185)	63,162,700	82,924,013
1982	16,517,385,129	926,033,957	(68,833,150)	61,813,400	98,441,027
1983	16,068,362,117	1,023,678,474	(400,365,922)	71,551,000	152,135,488
1984	18,068,820,742	1,102,444,454	(412,943,156)	82,115,700	162,606,410
1985	18,131,982,786	1,127,744,490	1,301,624,294	77,377,700	173,738,745
1986	17,464,528,361	1,156,867,714	1,975,893,356	97,337,500	180,779,673
1987	17,633,011,623	1,146,910,699	1,796,593,917[2]	81,869,800	170,674,979
1988	19,526,431,297	1,205,960,134	(516,910,320)	84,410,500	164,244,653
1989	22,249,275,725	1,332,160,712	1,295,622,583	89,579,700	175,043,736
1990	23,476,603,651	1,349,725,812	2,201,470,397	103,752,200	193,006,998
1991	22,553,001,815	1,429,322,157	496,200,596	109,631,000	261,316,379
1992	20,235,027,938	1,474,530,523	(959,075,921)	128,955,300	295,400,650
Total, 1914–92	**327,024,393,711**	**23,327,575,426**	**5,033,440,856**	**1,702,932,908**	**2,892,278,773**
Aggregate for each Bank, 1914–92					
Boston	17,510,241,589	1,536,760,720	176,817,307	62,076,686	176,277,091
New York	100,942,121,779	4,654,600,297	1,362,089,342	449,498,786	819,473,971
Philadelphia	12,539,376,489	1,258,714,306	266,817,425	80,985,118	119,237,918
Cleveland	21,509,043,278	1,524,890,436	229,623,399	122,500,690	182,276,473
Richmond	25,954,044,920	1,883,930,090	287,133,942	93,295,676	262,910,197
Atlanta	13,965,150,283	2,089,230,229	459,027,806	135,671,160	160,222,932
Chicago	45,637,643,168	3,043,175,507	614,195,126	233,842,672	391,886,858
St. Louis	10,694,638,342	1,205,707,159	131,115,614	51,026,272	101,612,154
Minneapolis	5,895,288,860	1,097,323,678	160,304,365	50,138,415	51,246,620
Kansas City	13,370,608,835	1,505,093,970	205,601,031	71,027,509	124,278,758
Dallas	17,884,398,161	1,401,811,145	417,928,983	115,730,973	159,995,511
San Francisco	41,121,838,008	2,506,681,750	762,807,515	237,138,951	342,860,290
Total	**327,024,393,711**	**23,327,575,426**[4]	**5,033,440,856**	**1,702,932,908**	**2,892,278,773**

1. Details may not sum to totals because of rounding.
2. For 1987 and subsequent years, includes the cost of services provided to the Treasury by Federal Reserve Banks for which reimbursement was not received.
3. The $3,182,294,299 transferred to surplus was reduced by direct changes of $500,000 for charge-off on Bank premises (1927), $139,299,557 for contributions to capital of the Federal Deposit Insurance Corporation (1934) and $3,657 net upon elimination of sec. 13b surplus (1958); and was increased by transfer of $11,131,013 from reserves for contingencies (1945), leaving a balance of $3,053,622,100 on December 31, 1992.
4. See note 2, table 6.

7.—Continued

Dividends paid	Payments to U.S. Treasury			Transferred to surplus (section 13b)	Transferred to surplus (section 7)
	Franchise tax	Under section 13b	Interest on Federal Reserve notes		
41,136,551	...	...	3,493,570,636	...	32,579,700
43,488,074	...	...	3,356,559,873	...	40,403,250
46,183,719	...	...	3,231,267,663	...	50,661,000
49,139,682	...	...	4,340,680,482	...	51,178,300
52,579,643	...	...	5,549,999,411	...	51,483,200
54,609,555	...	...	5,382,064,098	...	33,827,600
57,351,487	...	...	5,870,463,382	...	53,940,050
60,182,278	...	...	5,937,148,425	...	45,727,650
63,280,312	...	...	7,005,779,497	...	47,268,200
67,193,615	...	...	9,278,576,140	...	69,141,200
70,354,516	...	...	11,706,369,955	...	56,820,950
74,573,806	...	...	14,023,722,907	...	76,896,650
79,352,304	...	...	15,204,590,947	...	78,320,350
85,151,835	...	...	14,228,816,297	...	106,663,100
92,620,451	...	...	16,054,094,674	...	161,995,900
103,028,905	...	...	17,796,464,292	...	155,252,950
109,587,968	...	...	17,803,894,710	...	91,954,150
117,499,115	...	...	17,738,879,542	...	173,771,400
125,616,018	...	...	17,364,318,571	...	64,971,100
129,885,339	...	...	21,646,417,306	...	130,802,300
140,757,879	...	...	23,608,397,730	...	180,291,500
152,553,160	...	...	20,777,552,290	...	228,356,150
171,762,924	...	...	16,774,476,500	...	402,114,350
2,754,989,793	**149,138,300**	**2,188,893**	**297,784,105,648**	**(3,657)**	**3,182,294,299**[3]
111,081,103	7,111,395	280,843	15,662,542,654	135,411	118,405,575
752,463,230	68,006,262	369,116	94,981,347,191	(433,412)	922,277,171
142,267,053	5,558,901	722,406	10,994,765,084	290,661	131,648,122
209,452,772	4,842,447	82,930	19,478,514,975	(9,906)	189,452,343
146,788,151	6,200,189	172,493	23,613,223,232	(71,517)	215,941,808
205,293,997	8,950,561	79,264	11,509,424,416	5,491	294,906,740
370,919,941	25,313,526	151,045	41,798,035,964	11,682	361,421,954
84,089,294	2,755,629	7,464	9,292,522,213	(26,515)	75,072,878
77,740,274	5,202,900	55,615	4,678,449,297	64,874	83,846,013
112,663,153	6,939,100	64,213	11,624,491,429	(8,674)	112,959,850
176,895,747	560,049	102,083	16,217,311,054	55,337	216,220,778
365,335,077	7,697,341	101,421	37,933,478,137	(17,089)	460,162,067
2,754,989,793	**149,138,300**	**2,188,893**	**297,784,105,648**	**(3,657)**	**3,182,294,299**

8. Acquisition Costs and Net Book Value of Premises of Federal Reserve Banks and Branches, December 31, 1992[1]

Dollars

Federal Reserve Bank or Branch	Acquisition costs				Net book value	Other real estate[4]
	Land	Buildings (including vaults)[2]	Building machinery and equipment	Total[3]		
BOSTON	22,073,501	83,813,108	5,675,602	111,562,211	89,589,840	...
NEW YORK	20,354,440	93,625,754	42,251,939	156,232,132	132,903,040	...
Buffalo	887,844	3,303,946	2,749,659	6,941,449	4,183,960	...
PHILADELPHIA	2,251,556	55,005,678	5,903,704	63,160,938	45,093,745	...
CLEVELAND	1,074,281	10,045,664	6,858,976	17,978,922	12,775,360	1,224,363
Cincinnati	2,246,599	14,413,715	7,623,142	24,283,455	11,936,230	...
Pittsburgh	1,658,376	8,905,759	4,341,196	14,905,331	11,228,347	...
RICHMOND	5,812,396	69,596,875	18,390,034	93,799,305	65,404,897	...
Baltimore	6,476,335	26,826,903	3,842,189	37,145,427	29,676,789	...
Charlotte	3,129,645	27,402,251	4,737,485	35,269,381	32,659,481	...
ATLANTA	1,209,360	12,167,223	4,319,451	17,696,034	13,209,887	13,086,575
Birmingham	3,197,830	1,905,770	1,074,511	6,178,112	4,148,312	...
Jacksonville	1,665,439	16,589,720	2,363,391	20,618,549	18,345,872	944,483
Miami	3,717,791	12,783,499	2,223,399	18,724,690	14,457,087	...
Nashville	592,342	1,474,678	1,645,209	3,712,230	1,594,679	...
New Orleans	3,087,693	3,505,766	1,581,930	8,175,389	5,259,297	292,710
CHICAGO	4,565,008	109,377,091	19,008,997	132,951,095	103,770,536	...
Detroit	797,734	4,702,524	5,087,151	10,587,408	8,263,699	...
ST. LOUIS	700,378	15,270,459	5,298,206	21,269,043	18,226,743	...
Little Rock	1,148,492	2,148,507	1,003,022	4,300,021	2,509,188	...
Louisville	700,075	2,859,819	1,131,238	4,691,132	3,839,645	...
Memphis	1,135,623	4,274,152	2,280,473	7,690,248	5,220,981	...
MINNEAPOLIS	1,394,384	27,701,819	7,851,532	38,947,735	21,540,113	...
Helena	1,954,514	9,036,528	486,396	11,477,438	11,051,196	...
KANSAS CITY	1,829,420	15,376,497	11,593,946	28,799,863	22,076,231	149,948
Denver	3,187,962	4,451,952	3,185,925	10,825,839	8,422,717	...
Oklahoma City	646,386	3,630,988	861,305	6,138,679	3,880,159	...
Omaha	6,534,583	10,987,009	1,401,083	18,922,675	17,046,319	1,412,500
DALLAS	29,565,708	120,896,877	0	150,462,585	149,224,965	11,252,712
El Paso	262,477	1,458,093	404,946	2,125,516	2,048,477	...
Houston	2,205,500	3,295,695	1,126,030	6,627,225	6,207,363	...
San Antonio	482,284	2,674,490	1,581,919	4,738,694	3,704,407	...
SAN FRANCISCO	15,599,928	68,246,884	17,739,084	101,585,896	78,444,830	...
Los Angeles	3,891,887	51,126,648	8,398,066	63,416,601	54,877,791	...
Portland	415,924	5,682,337	1,254,537	7,352,798	6,163,927	...
Salt Lake City	480,222	4,903,818	1,467,539	6,851,579	3,964,109	...
Seattle	324,772	2,686,325	1,891,936	4,903,032	2,792,471	...
Total	**157,258,687**	**914,154,822**	**208,635,149**	**1,280,048,658**	**1,025,742,686**	**28,363,291**

1. Details may not sum to totals because of rounding.
2. Includes expenditures for construction at some offices, pending allocation to appropriate accounts.
3. Excludes charge-offs of $17,698,968 before 1952.
4. Covers acquisitions for banking-house purposes and bank premises formerly occupied and being held pending sale.

9. Operations in Principal Departments of Federal Reserve Banks, 1989–92

Operation	1992	1991	1990	1989
Millions of pieces (except as noted)				
Loans (thousands)	8	11	15	22
Currency received and counted	20,166	19,711	19,462	19,857
Currency verified and destroyed	7,506	6,254	6,561	6,319
Coin received and counted	8,660	9,462	12,072	12,668
Checks handled				
U.S. government checks	493	503	547	541
Postal money orders	181	166	162	147
All other	19,054	18,743	18,595	18,014
Issues, redemptions, and exchanges of U.S. Treasury and federal agency securities	76	52	44	40
Transfer of funds	68	65	63	60
Automated clearinghouse transactions				
Commercial[1]	1,327	1,119	915	741
Government	531	521	520	441
Food stamps redeemed	4,183	3,439	2,875	2,334
Millions of dollars				
Loans	29,427	64,597	194,538	229,358
Currency received and counted	277,681	265,473	252,430	246,598
Currency verified and destroyed	96,744	77,496	65,863	59,985
Coin received and counted	1,275	1,354	1,734	1,828
Checks handled				
U.S. government checks	588,311	610,106	623,008	635,064
Postal money orders	20,188	17,716	16,485	14,284
All other	13,241,785	12,164,175	12,514,201	12,321,576
Issues, redemptions, and exchanges of U.S. Treasury and federal agency securities	142,768,966	119,114,811	102,332,172	98,130,603
Transfer of funds	199,175,034	192,254,895	199,067,200	182,575,303
Automated clearinghouse transactions				
Commercial[1]	7,597,811	6,188,185	4,173,667	3,840,462
Government	859,774	723,426	486,809	391,463
Food stamps redeemed	21,452	17,888	14,517	11,714

1. Data for years preceding 1991 do not include items sent to the Reserve Banks by the New York Automated Clearing House.

10. Federal Reserve Bank Interest Rates, December 31, 1992

Bank	Loans to depository institutions			
	Adjustment credit[1]	Seasonal credit[2]	Extended credit[3]	
			First 30 days of borrowing	After 30 days of borrowing[4]
All Federal Reserve Banks	3.0	3.2	3.0	3.7

1. Adjustment credit is available on a short-term basis to help depository institutions meet temporary needs for funds that cannot be met through reasonable alternative sources. After May 19,1986, the highest rate established for loans to depository institutions may be charged on adjustment credit loans of unusual size that result from a major operating problem at the borrower's facility.

2. Seasonal credit is available to help smaller depository institutions meet regular, seasonal needs for funds that cannot be met through special industry lenders and that arise from a combination of expected patterns of movement in their deposits and loans. The discount rate on seasonal credit takes into account rates on market sources of funds and ordinarily is reestablished on the first business day of each two-week reserve maintenance period; however, it is never lower than the discount rate applicable to adjustment credit. See section 201.3(b)(1) of Regulation A.

3. Extended credit is available to depository institutions, if similar assistance is not reasonably available from other sources, when exceptional circumstances or practices involve only a particular institution or when an institution is experiencing difficulties adjusting to changing market conditions over a longer period of time. See section 201.3(b)(2) of Regulation A.

4. Extended-credit loans outstanding more than thirty days ordinarily will be charged a flexible rate somewhat above rates on market sources of funds; however, the rate will always be at least fifty basis points above the discount rate applicable to adjustment credit. In no case will the rate be less than the basic discount rate plus fifty basis points. The flexible rate is reestablished on the first business day of each two-week reserve maintenance period. At the discretion of the Federal Reserve Bank, the flexible rate may be charged on extended-credit loans that are outstanding less than thirty days.

11. Reserve Requirements of Depository Institutions[1]

Type of deposit[2]	Requirements	
	Percent of deposits	Effective date
Net transaction accounts[3]		
$0 million–$46.8 million	3	12/15/92
More than $46.8 million	10	12/15/92
Nonpersonal time deposits[4]	0	12/27/90
Eurocurrency liabilities[5]	0	12/27/90

1. Reserve requirements in effect on December 31, 1992. Required reserves must be held in the form of deposits with Federal Reserve Banks or vault cash. Nonmember institutions may maintain reserve balances with a Federal Reserve Bank indirectly on a pass-through basis with certain approved institutions. For previous reserve requirements, see earlier editions of the *Annual Report* or the *Federal Reserve Bulletin.* Under provisions of the Monetary Control Act, depository institutions include commercial banks, mutual savings banks, savings and loan associations, credit unions, agencies and branches of foreign banks, and Edge corporations.

2. The Garn–St Germain Depository Institutions Act of 1982 (Public Law 97–320) requires that $2 million of reservable liabilities of each depository institution be subject to a zero percent reserve requirement. The Board is to adjust the amount of reservable liabilities subject to this zero percent reserve requirement each year for the succeeding calendar year by 80 percent of the percentage increase in the total reservable liabilities of all depository institutions measured on an annual basis as of June 30. No corresponding adjustment is to be made in the event of a decrease. On December 15, 1992, the exemption was raised from $3.6 million to $3.8 million. The exemption applies in the following order: (1) net negotiable order of withdrawal (NOW) accounts (NOW accounts less allowable deductions); and (2) net other transaction accounts. The exemption applies only to accounts that would be subject to a 3 percent reserve requirement.

3. Transaction accounts include all deposits against which the account holder is permitted to make withdrawals by negotiable or transferable instruments, payment orders of withdrawal, and telephone and preauthorized transfers in excess of three per month for the purpose of making payments to third persons or others. However, money market deposit accounts (MMDAs) and similar accounts subject to the rules that permit no more than six preauthorized, automatic, or other transfers per month, of which no more than three can be checks, are not transaction accounts (such accounts are savings deposits).

The Monetary Control Act of 1980 requires that the amount of transaction accounts against which the 3 percent reserve requirement applies be modified annually by 80 percent of the percentage change in transaction accounts held by all depository institutions, determined as of June 30 each year. Effective December 15, 1992 for institutions reporting quarterly and December 22, 1992 for institutions reporting weekly, the amount was increased from $42.2 million to $46.8 million.

4. For institutions that report weekly, the reserve requirement on nonpersonal time deposits with an original maturity of less than 1½ years was reduced from 3 percent to 1½ percent for the maintenance period that began December 13, 1990, and to zero for the maintenance period that began December 27, 1990. The reserve requirement on nonpersonal time deposits with an original maturity of 1½ years or more has been zero since October 6, 1983.

For institutions that report quarterly, the reserve requirement on nonpersonal time deposits with an original maturity of less than 1½ years was reduced from 3 percent to zero on January 17, 1991.

5. The reserve requirement on Euroccurency liabilities was reduced from 3 percent to zero in the same manner and on the same dates as were the reserve requirement on nonpersonal time deposits with an original maturity of less than 1½ years (see note 4).

12. Initial Margin Requirements under Regulations T, U, G, and X[1]

Percent of market value

Effective date	Margin stocks	Convertible bonds	Short sales, T only[2]
1934, Oct. 1	25–45	...	...
1936, Feb. 1	25–55	...	...
Apr. 1	55	...	...
1937, Nov. 1	40	...	50
1945, Feb. 5	50	...	50
July 5	75	...	75
1946, Jan. 21	100	...	100
1947, Feb. 21	75	...	75
1949, Mar. 3	50	...	50
1951, Jan. 17	75	...	75
1953, Feb. 20	50	...	50
1955, Jan. 4	60	...	60
Apr. 23	70	...	70
1958, Jan. 16	50	...	50
Aug. 5	70	...	70
Oct. 16	90	...	90
1960, July 28	70	...	70
1962, July 10	50	...	50
1963, Nov. 6	70	...	70
1968, Mar. 11	70	50	70
June 8	80	60	80
1970, May 6	65	50	65
1971, Dec. 6	55	50	55
1972, Nov. 24	65	50	65
1974, Jan. 3	50	50	50

1. These regulations, adopted by the Board of Governors pursuant to the Securities Exchange Act of 1934, limit the amount of credit to purchase and carry "margin securities" (as defined in the regulations) when such value (100 percent) and the maximum loan value of credit is collateralized by securities. Margin requirements on securities other than options are the difference between the market value (100 percent) and the maximum loan value of collateral as prescribed by the Board. Regulation T was adopted effective October 15, 1934; Regulation U, effective May 1, 1936; Regulation G, effective March 11, 1968; and Regulation X, effective November 1, 1971.

On January 1, 1977, the Board of Governors for the first time established in Regulation T the initial margin required for writing options on securities, setting it at 30 percent of the current market value of the stock underlying the option. On September 30, 1985, the Board changed the required margin on individual stock options, allowing it to be the same as the option maintenance margin required by the appropriate exchange or self-regulatory organization; such maintenance margin rules must be approved by the Securities and Exchange Commission. Effective June 6, 1988, the SEC approved new maintenance margin rules, permitting margins to be the current market value of the option plus 20 percent of the market value of the stock underlying the option.

2. From October 1, 1934, to October 31, 1937, the requirement was the margin "customarily required" by the brokers and dealers.

13. Principal Assets and Liabilities and Number of Insured Commercial Banks, by Class of Bank, June 30, 1992 and 1991[1]

Asset and liability items shown in millions of dollars

Item	Total	Member banks			Nonmember banks
		Total	National	State	
	June 30, 1992				
Loans and investments	2,486,738	1,798,362	1,441,254	357,107	688,376
Gross loans	1,799,154	1,320,465	1,073,000	247,464	478,689
Net loans	1,790,741	1,315,292	1,068,991	246,301	475,449
Investments	687,584	477,897	368,254	109,643	209,687
U.S. Treasury and federal agency securities	549,931	386,690	300,265	86,425	163,240
Other	137,654	91,207	67,989	23,218	46,447
Cash assets, total	189,728	147,810	119,433	28,377	41,917
Deposits, total	2,319,688	1,662,383	1,345,048	317,335	657,305
Interbank	48,564	41,470	30,253	11,217	7,094
Other transaction	669,774	493,715	396,573	97,142	176,060
Other nontransaction	1,858,303	1,304,338	1,065,272	239,066	553,965
Equity capital	243,416	174,633	136,537	38,097	68,783
Number of banks	11,623	4,638	3,689	949	6,985
	June 30, 1991				
Loans and investments	2,446,295	1,775,794	1,437,167	338,627	670,500
Gross loans	1,850,168	1,369,674	1,122,113	247,561	480,495
Net loans	1,839,449	1,362,474	1,116,269	246,205	476,976
Investments	596,126	406,121	315,054	91,067	190,006
U.S. Treasury and federal agency securities	453,556	310,837	244,436	66,400	142,719
Other	142,571	95,284	70,618	24,666	47,287
Cash assets, total	191,698	147,153	120,294	26,859	44,545
Deposits, total	2,294,866	1,646,375	1,342,707	303,668	648,491
Interbank	45,049	38,180	29,268	8,912	6,870
Other demand	604,250	444,835	360,547	84,288	159,415
Other time and savings	1,868,539	1,316,914	1,080,994	235,920	551,625
Equity capital	221,957	157,296	123,632	33,664	64,661
Number of banks	12,085	4,889	3,902	987	7,196

1. All insured commercial banks in the United States.
Details may not sum to totals because of rounding.

14. Reserves of Depository Institutions, Federal Reserve Bank Credit, and Related Items—Year-End 1918–92, and Month-End 1992[1]

Millions of dollars

Period	Factors supplying reserve funds										
	Federal Reserve Bank credit outstanding								Gold stock[5]	Special drawing rights certificate account	Treasury currency outstanding[6]
	U.S. Treasury and federal agency securities			Loans	Float[2]	All other[3]	Other Federal Reserve assets[4]	Total			
	Total	Bought outright	Held under repurchase agreement								
1918	239	239	0	1,766	199	294	0	2,498	2,873	...	1,795
1919	300	300	0	2,215	201	575	0	3,292	2,707	...	1,707
1920	287	287	0	2,687	119	262	0	3,355	2,639	...	1,709
1921	234	234	0	1,144	40	146	0	1,563	3,373	...	1,842
1922	436	436	0	618	78	273	0	1,405	3,642	...	1,958
1923	134	80	54	723	27	355	0	1,238	3,957	...	2,009
1924	540	536	4	320	52	390	0	1,302	4,212	...	2,025
1925	375	367	8	643	63	378	0	1,459	4,112	...	1,977
1926	315	312	3	637	45	384	0	1,381	4,205	...	1,991
1927	617	560	57	582	63	393	0	1,655	4,092	...	2,006
1928	228	197	31	1,056	24	500	0	1,809	3,854	...	2,012
1929	511	488	23	632	34	405	0	1,583	3,997	...	2,022
1930	739	686	43	251	21	372	0	1,373	4,306	...	2,027
1931	817	775	42	638	20	378	0	1,853	4,173	...	2,035
1932	1,855	1,851	4	235	14	41	0	2,145	4,226	...	2,204
1933	2,437	2,435	2	98	15	137	0	2,688	4,036	...	2,303
1934	2,430	2,430	0	7	5	21	0	2,463	8,238	...	2,511
1935	2,431	2,430	1	5	12	38	0	2,486	10,125	...	2,476
1936	2,430	2,430	0	3	39	28	0	2,500	11,258	...	2,532
1937	2,564	2,564	0	10	19	19	0	2,612	12,760	...	2,637
1938	2,564	2,564	0	4	17	16	0	2,601	14,512	...	2,798
1939	2,484	2,484	0	7	91	11	0	2,593	17,644	...	2,963
1940	2,184	2,184	0	3	80	8	0	2,274	21,995	...	3,087
1941	2,254	2,254	0	3	94	10	0	2,361	22,737	...	3,247
1942	6,189	6,189	0	6	471	14	0	6,679	22,726	...	3,648
1943	11,543	11,543	0	5	681	10	0	12,239	21,938	...	4,094
1944	18,846	18,846	0	80	815	4	0	19,745	20,619	...	4,131
1945	24,252	24,252	0	249	578	2	0	15,091	20,065	...	4,339
1946	23,350	23,350	0	163	580	1	0	24,093	20,529	...	4,562
1947	22,559	22,559	0	85	535	1	0	23,181	22,754	...	4,562
1948	23,333	23,333	0	223	541	1	0	24,097	24,244	...	4,589
1949	18,885	18,885	0	78	534	2	0	19,499	24,427	...	4,598
1950	20,778	20,725	53	67	1,368	3	0	22,216	22,706	...	4,636
1951	23,801	23,605	196	19	1,184	5	0	25,009	22,695	...	4,709
1952	24,697	24,034	663	156	967	4	0	25,825	23,187	...	4,812
1953	25,916	25,318	598	28	935	2	0	26,880	22,030	...	4,894
1954	24,932	24,888	44	143	808	1	0	25,885	21,713	...	4,985
1955	24,785	24,391	394	108	1,585	29	0	26,507	21,690	...	5,008
1956	24,915	24,610	305	50	1,665	70	0	26,699	21,949	...	5,066
1957	24,238	23,719	519	55	1,424	66	0	25,784	22,781	...	5,146
1958	26,347	26,252	95	64	1,296	49	0	27,755	20,534	...	5,234
1959	26,648	26,607	41	458	1,590	75	0	28,771	19,456	...	5,311
1960	27,384	26,984	400	33	1,847	74	0	29,338	17,767	...	5,398
1961	28,881	30,478	159	130	2,300	51	0	31,362	16,889	...	5,585
1962	30,820	28,722	342	38	2,903	110	0	33,871	15,978	...	5,567
1963	33,593	33,582	11	63	2,600	162	0	36,418	15,513	...	5,578
1964	37,044	36,506	538	186	2,606	94	0	39,930	15,388	...	5,405

For notes see last two pages of table.

14.—Continued

Factors absorbing reserve funds											
Currency in circulation	Treasury cash holdings[7]	Deposits, other than reserves, with Federal Reserve Banks: Treasury	Deposits, other than reserves, with Federal Reserve Banks: Foreign	Deposits, other than reserves, with Federal Reserve Banks: Other	Other Federal Reserve accounts[4]	Required clearing balances	Other Federal Reserve liabilities and capital[4]	Member bank reserves[8]: With Federal Reserve Banks	Member bank reserves[8]: Currency and coin[9]	Member bank reserves[8]: Required[10]	Member bank reserves[8]: Excess[10]
4,951	288	51	96	25	118	0	0	1,636	0	1,585	51
5,091	385	51	73	28	208	0	0	1,890	0	1,822	68
5,325	218	57	5	18	298	0	0	1,781	0	0	0
4,403	214	96	12	15	285	0	0	1,753	0	1,654	99
4,530	225	11	3	26	276	0	0	1,934	0	0	0
4,757	213	38	4	19	275	0	0	1,898	0	1,884	14
4,760	211	51	19	20	258	0	0	2,220	0	2,161	59
4,817	203	16	8	21	272	0	0	2,212	0	2,256	–44
4,808	201	17	46	19	293	0	0	2,194	0	2.250	–56
4,716	208	18	5	21	301	0	0	2,487	0	2,424	63
4,686	202	23	6	21	348	0	0	2,389	0	2,430	–41
4,578	216	29	6	24	393	0	0	2,355	0	2,428	–73
4,603	211	19	6	22	375	0	0	2,471	0	2,375	96
5,360	222	54	79	31	354	0	0	1,961	0	1,994	–33
5,388	272	8	19	24	355	0	0	2,509	0	1,933	576
5,519	284	3	4	128	360	0	0	2,729	0	1,870	859
5,536	3,029	121	20	169	241	0	0	4,096	0	2,282	1,814
5,882	2,566	544	29	226	253	0	0	5,587	0	2,743	2,844
6,543	2,376	244	99	160	261	0	0	6,606	0	4,622	1,984
6,550	3,619	142	172	235	263	0	0	7,027	0	5,815	1,212
6,856	2,706	923	199	242	260	0	0	8,724	0	5,519	3,205
7,598	2,409	634	397	256	251	0	0	11,653	0	6,444	5,209
8,732	2,213	368	1,133	599	284	0	0	4,026	0	7,411	6,615
11,160	2,215	867	774	586	291	0	0	12,450	0	9,365	3,085
15,410	2,193	799	793	485	256	0	0	13,117	0	11,129	1,988
20,499	2,303	579	1,360	356	339	0	0	12,886	0	11,650	1,236
25,307	2,375	440	1,204	394	402	0	0	14,373	0	12,748	1,625
28,515	2,287	977	862	446	495	0	0	15,915	0	14,457	1,458
28,952	2,272	393	508	314	607	0	0	16,139	0	15,577	562
28,868	1,336	870	392	569	563	0	0	17,899	0	16,400	1,499
28,224	1,325	1,123	642	547	590	0	0	20,479	0	19,277	1,202
27,600	1,312	821	767	750	106	0	0	16,568	0	15,550	1,018
27,741	1,293	668	895	565	714	0	0	17,681	0	16,509	1,172
29,206	1,270	247	526	363	746	0	0	20,056	0	19,667	389
30,433	1,270	389	550	455	777	0	0	19,950	0	20,520	–570
30,781	761	346	423	493	839	0	0	20,160	0	19,397	763
30,509	796	563	490	441	907	0	0	18,876	0	18,618	258
31,158	767	394	402	554	925	0	0	19,005	0	18,903	102
31,790	775	441	322	426	901	0	0	19,059	0	19,089	–30
31,834	761	481	356	246	998	0	0	19,034	0	19,091	–57
32,193	683	358	272	391	1,122	0	0	18,504	0	18,574	–70
32,591	391	504	345	694	841	0	0	18,174	310	18,619	–135
32,869	377	485	217	533	941	0	0	17,081	2,544	18,988	637
33,918	422	465	279	320	1,044	0	0	17,387	2,544	18,988	96
35,338	380	597	247	393	1,007	0	0	17,454	3,262	20,071	645
37,692	361	880	171	291	1,065	0	0	17,049	4,099	20,677	471
39,619	612	820	229	321	1,036	0	0	18,086	4,151	21,663	574

14. Reserves of Depository Institutions, Federal Reserve Bank Credit, and Related Items—Year-End 1918–92 and Month-End 1992[1]—Continued

Millions of dollars

Period	Factors supplying reserve funds										
	Federal Reserve Bank credit outstanding								Gold stock[5]	Special drawing rights certificate account	Treasury currency outstanding[6]
	U.S. Treasury and federal agency securities			Loans	Float[2]	All other[3]	Other Federal Reserve assets[4]	Total			
	Total	Bought outright[12]	Held under repurchase agreement								
1965.....	40,768	40,478	290	137	2,248	187	0	43,340	13,733	...	5,575
1966.....	44,316	43,655	661	173	2,495	193	0	47,177	13,159	...	6,317
1967.....	49,150	48,980	170	141	2,576	164	0	52,031	11,982	...	6,784
1968.....	52,937	52,937	0	186	3,443	58	0	56,624	10,367	...	6,795
1969.....	57,154	7,154[3]	0	183	3,440	64	2,743	64,584	10,367	...	6,852
1970.....	62,142	62,142	0	335	4,261	57	1,123	67,918	10,732	400	7,147
1971.....	70,804	69,481	1,323	39	4,343	261	1,068	76,515	10,132	400	7,710
1972.....	71,230	71,119	111	1,981	3,974	106	1,260	78,551	10,410	400	8,313
1973.....	80,495	80,395	100	1,258	3,099	68	1,152	86,072	11,567	400	8,716
1974.....	85,714	84,760	954	299	2,001	999	3,195	92,208	11,652	400	9,253
1975.....	94,124	92,789	1,335	211	3,688	1,126	3,312	102,461	11,599	500	10,218
1976.....	104,093	100,062	4,031	25	2,601	991	3,182	110,892	11,598	1,200	10,810
1977.....	111,274	108,922	2,352	265	3,810	954	2,442	118,745	11,718	1,250	11,331
1978.....	118,591	117,374	1,217	1,174	6,432	587	4,543	131,327	11,671	1,300	11,831
1979.....	126,167	124,507	1,660	1,454	6,767	704	5,613	140,705	11,172	1,800	13,083
1980.....	130,592	128,038	2,554	1,809	4,467	776	8,739	146,383	11,160	2,518	13,427
1981.....	140,348	136,863	3,485	1,601	1,762	195	9,230	153,136	11,151	3,318	13,687
1982.....	148,837	144,544	4,293	717	2,735	1,480	9,890	63,659	11,148	4,618	13,786
1983.....	160,795	159,203	1,592	918	1,605	418	8,728	172,464	11,121	4,618	15,732
1984.....	169,627	167,612	2,015	3,577	833	0	12,347	186,384	11,096	4,618	16,418
1985.....	191,248	186,025	5,223	3,060	988	0	15,302	210,598	11,090	4,718	17,075
1986.....	221,459	205,454	16,005	1,565	1,261	0	17,475	241,760	11,084	5,018	17,567
1987.....	231,420	226,459	4,961	3,815	811	0	15,837	251,883	11,078	5,018	18,177
1988.....	247,489	240,628	6,861	2,170	1,286	0	18,803	269,748	11,060	5,018	18,799
1989.....	235,417	233,300	2,117	481	1,093	0	39,631	276,622	11,059	8,518	19,620
1990.....	259,786	241,432	18,354	190	2,566	0	39,880	302,421	11,058	10,018	20,404
1991.....	288,429	272,531	15,898	218	1,026	0	34,524	324,197	11,059	10,018	21,038
1992.....	308,518	300,424	8,094	675	3,350	0	30,278	342,820	11,056	8,018	21,503

1. For a description of figures and discussion of their significance, see *Banking and Monetary Statistics, 1941–1970* (Board of Governors of the Federal Reserve System, 1976), pp. 507–23. Components may not sum to totals because of rounding.

2. Beginning in 1960, figures reflect a minor change in concept; see *Federal Reserve Bulletin*, vol. 47 (February 1961), p. 164.

3. Principally acceptances and, until August 21, 1959, industrial loans, authority for which expired on that date.

4. For the period before April 16, 1969, includes the total of Federal Reserve capital paid in, surplus, other capital accounts, and other liabilities and accrued dividends, less the sum of bank premises and other assets, and was reported as "Other Federal Reserve accounts"; thereafter, "Other Federal Reserve assets" and "Other Federal Reserve liabilities and capital" are shown separately.

5. Before January 30, 1934, includes gold held in Federal Reserve Banks and in circulation.

6. Includes currency and coin (other than gold) issued directly by the Treasury. The largest components are fractional and dollar coins. For details see "Currency and Coin in Circulation," *Treasury Bulletin*.

7. Coin and paper currency held by the Treasury, as well as any gold in excess of the gold certificates issued to the Reserve Bank.

8. Beginning in November 1979, includes reserves of member banks. Edge corporations, and U.S. agencies and branches of foreign banks. Beginning on November 13, 1980, includes reserves of all depository institutions.

9. Between December 1, 1959, and November 23, 1960, part was allowed as reserves; thereafter all was allowed.

10. Estimated through 1958. Before 1929, data were available only on call dates (in 1920 and 1922 the call date was December 29). Beginning on September 12, 1968, the amount is based on close-of-business figures for the reserve period two weeks before the report date.

14.—Continued

Factors absorbing reserve funds											
		Deposits, other than reserves, with Federal Reserve Banks						Member bank reserves[8]			
Currency in circulation	Treasury cash holdings[7]	Treasury	Foreign	Other	Other Federal Reserve accounts[4]	Required clearing balances	Other Federal Reserve liabilities and capital[4]	With Federal Reserve Banks	Currency and coin[9]	Required[10]	Excess[10,13]
42,056	760	668	150	355	211	0	0	18,447	4,163	22,848	−238
44,663	1,176	416	174	588	−147	0	0	19,779	4,310	24,321	−232
47,226	1,344	1,123	135	563	−773	0	0	21,092	4,631	25,905	−182
50,961	695	703	216	747	−1,353	0	0	21,818	4,921	27,439	−700
53,950	596	1,312	134	807	0	0	0	22,085	5,187	28,173	−901
57,903	431	1,156	148	1,233	0	0	1,986	24,150	5,423	30,033	−460
61,068	460	2,020	294	999	0	0	2,131	27,788	5,743	32,496	1,035
66,516	345	1,855	325	840	0	0	2,143	25,647	6,216	32,044	98[13]
72,497	317	2,542	251	1,419[14]	0	0	2,669	27,060	6,781	35,268	−1,360
79,743	185	2,113	418	1,275[14]	0	0	2,935	25,843	7,370	37,011	−3,798
86,547	483	7,285	353	1,090	0	0	2,968	26,052	8,036	35,197	−1,103[15]
93,717	460	10,393	352	1,357	0	0	3,063	25,158	8,628	35,461	−1,535
103,811	392	7,114	379	1,187	0	0	3,292	26,870	9,421	37,615	−1,265
114,645	240	4,196	368	1,256	0	0	4,275	31,152	10,538	42,694	−893
125,600	494	4,075	429	1,412	0	0	4,957	29,792	11,429	44,217	−2,835
136,829	441	3,062	411	617	0	0	4,671	27,456	13,654	40,558	675
144,774	443	4,301	505	781	0	117	5,261	25,111	15,576	42,145	−1,442
154,908	429	5,033	328	1,033	0	436	4,990	26,053	16,666	41,391	1,328
171,935	479	3,661	191	851	0	1,013	5,392	20,413	17,821	39,179	−945
183,796	513	5,316	253	867	0	1,126	5,952	20,693	n.a.	n.a.	n.a.
197,488	550	9,351	480	1,041	0	1,490	5,940	27,141	n.a.	n.a.	n.a.
211,995	447	7,588	287	917	0	1,812	6,088	46,295	n.a.	n.a.	n.a.
230,205	454	5,313	244	1,027	0	1,687	7,129	40,097	n.a.	n.a.	n.a.
247,649	395	8,656	347	548	0	1,605	7,683	37,742	n.a.	n.a.	n.a.
260,453	450	6,217	589	1,298	0	1,626	8,486	36,701	n.a.	n.a.	n.a.
286,965	561	8,960	369	242	0	1,963	8,147	36,695	n.a.	n.a.	n.a.
307,780	636	17,697	968	1,706	0	3,955	8,113	25,458	n.a.	n.a.	n.a.
334,757	508	7,492	206	372	0	5,901	7,984	26,178	n.a.	n.a.	n.a.

11. Beginning December 1, 1966, includes federal agency obligations held under repurchase agreements and beginning September 29, 1971, includes federal agency issues bought outright.

12. Beginning in 1969, includes securities loaned—fully guaranteed by U.S. government securities pledged with Federal Reserve Banks—and excludes securities sold and scheduled to be bought back under matched sale-purchase transactions.

13. Beginning with week ending November 15, 1972, includes $450 million of reserve deficiencies on which Federal Reserve Banks are allowed to waive penalties for a transition period in connection with bank adaptation to Regulation J as amended, effective November 9, 1972. Allowable deficiencies are as follows (beginning with first statement week of quarter, in millions): 1973—Q1, $279; Q2, $172; Q3, $112; Q4, $84; 1974—Q1, $67; Q2, $58. The transition period ended with the second quarter of 1974.

14. For the period before July 1973, includes certain deposits of domestic nonmember banks and foreign-owned banking institutions held with member banks and redeposited in full with Federal Reserve Banks in connection with voluntary participation by nonmember institutions in the Federal Reserve System program of credit restraint.

As of December 12, 1974, the amount of voluntary nonmember bank and foreign-agency and branch deposits at Federal Reserve Banks that are associated with marginal reserves are no longer reported. However, two amounts are reported: (1) deposits voluntarily held as reserves by agencies and branches of foreign banks operating in the United States and (2) Eurodollar liabilities.

15. Adjusted to include waivers of penalties for reserve deficiencies, in accordance with change in Board policy effective November 19, 1975.

14. Reserves of Depository Institutions, Federal Reserve Bank Credit, and Related Items—Year-End 1918–92, and Month-End 1992[1]—Continued

Millions of dollars

Period	Factors supplying reserve funds										
	Federal Reserve Bank credit outstanding								Gold stock[5]	Special drawing rights certificate account	Treasury currency outstanding[6]
	U.S. Treasury and federal agency securities			Loans	Float[2]	All other[3]	Other Federal Reserve assets[4]	Total			
	Total	Bought outright[12]	Held under repurchase agreement								
1992											
Jan. ..	272,243	268,579	3,664	112	246	0	34,051	306,651	11,058	10,018	21,060
Feb. ..	271,383	271,383	0	62	294	0	32,040	303,779	11,058	10,018	21,099
Mar. ..	273,561	271,756	1,805	52	634	0	32,512	306,759	11,058	10,018	21,138
Apr. ..	273,855	273,855	0	115	548	0	31,175	305,694	11,057	10,018	21,175
May ..	276,802	276,558	244	150	387	0	29,021	306,360	11,057	10,018	21,210
June ..	282,593	282,593	0	1,359	484	0	31,030	315,466	11,060	10,018	21,257
July ..	281,594	281,594	0	256	398	0	31,860	314,107	11,059	10,018	21,286
Aug. ..	287,777	280,108	7,669	244	530	0	31,230	319,780	11,059	10,018	21,298
Sept. .	301,868	287,066	14,802	299	301	0	33,000	335,467	11,058	10,018	21,342
Oct. ..	288,411	288,411	0	80	567	0	31,111	320,169	11,060	10,018	21,377
Nov. ..	301,740	298,230	3,510	35	−285	0	29,424	330,914	11,059	10,018	21,433
Dec. ..	308,518	300,424	8,094	675	3,350	0	30,278	342,820	11,056	8,018	21,503

14.—Continued

Factors absorbing reserve funds												
		Deposits, other than reserves, with Federal Reserve Banks						Member bank reserves[8]				
Currency in circulation	Treasury cash holdings[7]	Treasury	Foreign	Other	Other Federal Reserve accounts[4]	Required clearing balances	Other Federal Reserve liabilities and capital[4]	With Federal Reserve Banks	Currency and coin[9]	Required[10]	Excess[10,13]
299,879	684	10,828	321	251	0	4,275	7,629	24,920			
301,374	698	5,477	264	231	0	4,381	7,222	26,307			
303,212	711	6,846	262	364	0	4,458	8,098	25,023			
306,373	705	4,692	206	260	0	4,756	7,906	23,046			
309,719	682	5,583	217	224	0	5,152	8,716	18,351			
310,935	612	13,630	219	249	0	5,194	9,416	17,546			
314,338	578	6,923	264	220	0	5,275	8,846	20,027	n.a.	n.a.	n.a.
316,136	539	6,232	297	254	0	5,472	9,275	23,950			
317,314	522	21,297	438	275	0	5,606	8,275	24,159			
320,363	505	4,413	415	317	0	5,615	7,271	23,724			
327,281	525	6,985	229	296	0	5,682	7,759	24,667			
334,757	508	7,492	206	372	0	5,901	7,984	26,178			

15. Changes in Number of Banking Offices in the United States, 1992[1]

Type of office and change	Total	Commercial banks[2]						State-chartered savings banks[4]	
		Total	Member			Nonmember			
			Total	National	State	Insured	Non-insured[3]	Insured	Non-insured
Banks, Dec. 31, 1991	12,629	12,269	4,838	3,809	1,029	7,159	272	360	0
Changes during 1992									
New banks	94	94	49	43	6	29	16	0	0
Ceased banking operation	−180	−157	−71	−51	−20	−62	−24	−23	0
Banks converted into branches	−420	−416	−207	−165	−42	−208	−1	−4	0
Other[5]	111	25	10	−22	32	−2	17	86	0
Net change	−395	−454	−219	−195	−24	−243	8	59	0
Banks, Dec. 31, 1992	**12,234**	**11,815**	**4,619**	**3,614**	**1,005**	**6,916**	**280**	**419**	**0**
Branches and additional offices, Dec. 31, 1991	55,921	53,000	34,810	28,315	6,495	18,080	110	2,921	0
Changes during 1992									
De novo	1,677	1,560	1,074	856	218	483	3	117	0
Banks converted into branches	420	414	255	197	58	159	0	6	0
Discontinued	−1,313	−1,192	−935	−810	−125	−238	−19	−121	0
Sale of branch	0	30	−93	−130	37	123	0	−30	0
Other[5]	−264	−68	358	−365	723	−419	−7	−196	0
Net change[5]	520	744	659	−252	911	108	−23	−224	0
Branches and additional offices, Dec. 31, 1992	**56,441**	**53,744**	**35,469**	**28,063**	**7,406**	**18,188**	**87**	**2,697**	**0**

1. Preliminary. Final data will be available in the *Annual Statistical Digest, 1992*, forthcoming.
2. Includes stock savings banks, nondeposit trust companies, private banks, industrial banks, and nonbank banks.
3. As of Dec. 31, 1988, includes noninsured national trust companies.
4. Formerly called mutual savings banks.
5. Includes interclass changes.

16. Mergers, Consolidations, and Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors, 1992

Crestar Bank, Richmond, Virginia *to acquire the assets and liabilities of* **twenty-four branches of Perpetual Savings Bank, FSB, McLean, Virginia, through its wholly owned subsidiary, CRFC VA Interim Federal Savings Bank, Richmond, Virginia**[1]

SUMMARY REPORT BY THE ATTORNEY GENERAL
No report received. Request for report on the competitive factors was dispensed with, as authorized by the Bank Merger Act, to permit the Federal Reserve System to act immediately to safeguard the depositors of the branches of Perpetual Savings Bank.[2]

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (1/10/92)
The applicant has assets of $10.3 billion; the target institutions have assets of $1.9 billion. The OTS has recommended immediate action by the Federal Reserve System to prevent the probable failure of Perpetual Savings Bank.

Wesbanco Bank Wheeling, Wheeling, West Virginia *to merge with* **Bank of Follansbee, Follansbee, West Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL (12/16/91)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (1/10/92)
The applicant has assets of $302.9 million; the target institution has assets of $18.0 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Fleet Bank–NH, Nashua, New Hampshire *to merge with* **Atlantic Trust Company, Newington, New Hampshire**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (1/30/92)
The applicant has assets of $1.7 billion; the target institution has assets of $21.2 million. The State has recommended immediate action by the Federal Reserve System to prevent the probable failure of Atlantic Trust.

Clear Lake Bank and Trust, Clear Lake, Iowa *to acquire the assets and liabilities of the* **Garner, Iowa, branch of Home Federal Savings and Loan Association, Algon, Iowa**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (1/31/92)
The applicant has assets of $83.7 million; the target institution has assets of $6.7 million. The OTS has recommended immediate action by the Federal Reserve System to prevent the probable failure of Home Federal Savings and Loan Association.

Iowa Trust and Savings Bank, Emmetsburg, Iowa *to acquire the* **Emmetsburg, Iowa, branch of Home Federal Savings and Loan Association, Algona, Iowa**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (1/31/92)
The applicant has assets of $43 million; the target institution has assets of $6 million. The OTS has recommended immediate action by the Federal Reserve System to prevent the probable failure of Home Federal Savings and Loan Association.

Rapides Bank & Trust Company, Alexandria, Louisiana *to acquire the assets and liabilities of the* **Alexandria and Pineville branches of Pelican Homestead Savings Association, Metairie, Louisiana**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

1. The institution or group of institutions named before the italicized words is referred to subsequently as the applicant, and the institution or group of institutions named after the italicized words is referred to subsequently as the target institution or target institutions.

2. Hereafter, the entry for the summary report by the Attorney General will read, "Request for report dispensed with as authorized by the Bank Merger Act," for cases in which the Attorney General's report on the competitive factors was dispensed with, as authorized by the Bank Merger Act, to permit the Federal Reserve System to act immediately to safeguard depositors.

16. Mergers, Consolidations, and Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors, 1992—Continued

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (1/31/92)
The applicant has assets of $422.4 million; the target institutions have assets of $1.5 billion. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of Pelican Homestead Savings Association.

Titonka Savings Bank, Titonka, Iowa *to acquire the* **Forest City, Iowa, branch of Home Federal Savings and Loan Association, Algona, Iowa**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (1/31/92)
The applicant has assets of $49 million; the target institution has assets of $4 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of Home Federal Savings and Loan Association.

Bank of Suffolk, Suffolk, Virginia *to acquire the assets and liabilities of the* **Whaleyville, Virginia, branch of Sovran Bank, N.A., Richmond, Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL (1/14/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (2/5/92)
The applicant has assets of $51.3 million; the target institution has assets of $9.3 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Chemical Bank, New York, New York, *to acquire four branches of* **Anchor Savings Bank, FSB, Hewlett, New York, through its wholly owned subsidiary CBC Interim Federal Savings Bank 2, New York, New York**

SUMMARY REPORT BY THE ATTORNEY GENERAL (11/25/91)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (2/5/92)
The applicant has assets of $107.9 billion; the target institutions have assets of $181.0 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

The Provident Bank of Kentucky, Alexandria, Kentucky *to merge with* **Peoples Federal Savings & Loan Association of Bellevue, Bellevue, Kentucky, through Provident Bank of Boone County, Bellevue, Kentucky, a wholly owned subsidiary; and with Suburban Federal Savings & Loan Association of Covington, Kentucky, through Provident Bank of Kenton County, Covington, Kentucky, a wholly owned subsidiary**

SUMMARY REPORT BY THE ATTORNEY GENERAL (1/28/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (2/28/92)
The applicant has assets of $79.6 million; the target institutions have assets of $116 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

The State Bank and Trust Company, Defiance, Ohio *to acquire the assets and liabilities of the* **Delta, Lyon, and Wauseon branches of The Society Bank and Trust Company, Toledo, Ohio**

SUMMARY REPORT BY THE ATTORNEY GENERAL (1/28/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/3/92)
The applicant has assets of $183.7 million; the target institutions have assets of $42.4 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

CivicBank of Commerce, Oakland, California *to acquire the assets and liabilities of the* **Walnut Creek and Fremont branches of American Bank & Trust Company, San Jose, California**

16.—Continued

SUMMARY REPORT BY THE ATTORNEY GENERAL (2/4/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/5/92)
The applicant has assets of $349 million; the target institutions have assets of $37.9 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Centura Bank, Rocky Mount, North Carolina *to merge with* **First Federal Savings Association, Raleigh, North Carolina**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/6/92)
The applicant has assets of $2.5 billion; the target institution has assets of $87.4 million. The parties do not operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

First Virginia Bank of Augusta, Staunton, Virginia *to acquire the assets and liabilities of the* **Staunton branch of CorEast Federal Savings Bank, Richmond, Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/6/92)
The applicant has assets of $73.5 million; the target institution has assets of $13.4 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

Central Virginia Bank, Powhatan, Virginia *to acquire the assets and liabilities of the* **Powhatan branch of CorEast Federal Savings Bank, Richmond, Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/6/92)
The applicant has assets of $72.9 million; the target institution has assets of $9.7 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

Central Fidelity Bank, Richmond, Virginia *to acquire the assets and liabilities of the* **Blacksburg, Virginia, branch of CorEast Federal Savings Bank, Richmond, Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/6/92)
The applicant has assets of $6.7 billion; the target institution has assets of $16.8 million. The parties operate in the same market. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

First Virginia Bank–Southwest, Roanoke, Virginia *to acquire the assets and liabilities of* **eight branches of CorEast Federal Savings Banks, Richmond, Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/6/92)
The applicant has assets of $345.1 million; the target institutions have assets of $236.0 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

First Virginia Bank–Piedmont, Lynchburg, Virginia *to acquire the assets and liabilities of* **three Lynchburg, Virginia, branches of CorEast Federal Savings Bank, Richmond, Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/6/92)
The applicant has assets of $170.3 million; the target institutions have assets of $57.8 million. The RTC has recommended immediate action

16. Mergers, Consolidations, and Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors, 1992—Continued

by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

First Virginia Bank–Franklin County, Lynchburg, Virginia *to acquire the assets and liabilities of the* **Hardy, Virginia, branch of CorEast Federal Savings Bank, Richmond, Virginia**

Summary Report by the Attorney General
Request for report dispensed with as authorized by the Bank Merger Act.

Basis for Approval by the Federal Reserve (3/6/92)
The applicant has assets of $121.6 million; the target institution has assets of $5.8 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

The State Bank of the Alleghenies, Covington, Virginia *to acquire the assets and liabilities of the* **Clifton Forge, Virginia, branch of CorEast Federal Savings Bank**

Summary Report by the Attorney General
Request for report dispensed with as authorized by the Bank Merger Act.

Basis for Approval by the Federal Reserve (3/6/92)
The applicant has assets of $74.5 million; the target institution has assets of $17.8 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

First Virginia Bank–Highlands, Covington, Virginia *to acquire the assets and liabilities of the* **Covington, Virginia, branch of CorEast Federal Savings Bank, Richmond, Virginia**

Summary Report by the Attorney General
Request for report dispensed with as authorized by the Bank Merger Act.

Basis for Approval by the Federal Reserve (3/6/92)
The applicant has assets of $115.1 million; the target institution has assets of $10 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

Regency Bank, Richmond, Virginia *to acquire the assets and liabilities of the* **Richmond, Virginia, branch of CorEast Federal Savings Bank, Richmond, Virginia**

Summary Report by the Attorney General
Request for report dispensed with as authorized by the Bank Merger Act.

Basis for Approval by the Federal Reserve (3/6/92)
The applicant has assets of $46.8 million; the target institution has assets of $7.9 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

First State Bank of Arkansas, Trumann, Arkansas *to acquire the assets and liabilities of the* **Trumann, Arkansas, branch of United Federal Savings and Loan Association, Jonesboro, Arkansas**

Summary Report by the Attorney General
Request for report dispensed with as authorized by the Bank Merger Act.

Basis for Approval by the Federal Reserve (3/13/92)
The applicant has assets of $32.8 million; the target institution has assets of $3.4 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of CorEast Federal Savings Bank.

Commercial Bank of Florida, Miami, Florida *to acquire the assets and liabilities of the* **South Dixie, Bird Road, and Sunset West branches of Professional Federal Savings Bank**

Summary Report by the Attorney General
Request for report dispensed with as authorized by the Bank Merger Act.

Basis for Approval by the Federal Reserve (3/13/92)
The applicant has assets of $144.5 million; the target institutions have assets of $119.5 million. The State has recommended immediate action by the Federal Reserve System to prevent the probable failure of Professional Federal Savings Bank.

Chemical Bank, New York, New York *to merge with* **Central Federal Savings Bank, Mineola, New York**

Summary Report by the Attorney General
Request for report dispensed with as authorized by the Bank Merger Act.

16.—Continued

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/13/92)
The applicant has assets of $138.9 million; the target institution has assets of $485 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Minden Bank & Trust Company, Minden, Louisiana *to merge with* **Webster Bank & Trust Company, Minden, Louisiana**

SUMMARY REPORT BY THE ATTORNEY GENERAL (1/7/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/13/92)
The applicant has assets of $124.1 million; the target institution has assets of $35.9 million. The parties operate in the same banking market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Plaza Bank of Miami, Miami, Florida *to acquire the assets and liabilities of the* **Coral Gables and Sunshine branches of Professional Federal Savings Bank, Coral Gables, Florida**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/13/92)
The applicant has assets of $60.1 million; the target institutions have assets of $18.2 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of Professional Federal Savings Bank.

First Virginia Bank–Central Maryland, Bel Air, Maryland *to acquire the assets and liabilities of the* **Catonsville, Maryland, branch of Augusta Federal Savings Association, Baltimore, Maryland**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/13/92)
The applicant has assets of $274.4 million; the target institution has assets of $9.9 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of Augusta Federal Savings Association.

SouthTrust Bank of Pinellas County, St. Petersburg, Florida *to acquire the assets and liabilities of the* **New Port Richey branch of Mid State Federal Savings Bank, Hudson, Florida**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/16/92)
The applicant has assets of $305.2 million; the target institution has assets of $13.3 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of Mid State Federal Savings Bank.

Meridian Bank, Reading, Pennsylvania *to merge with* **Bell Federal Savings Bank, Upper Darby, Pennsylvania**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/20/92)
The applicant has assets of $9.7 billion; the target institution has assets of $471.0 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of Bell Federal Savings Bank.

The Provident Bank *to merge with* **Merit Savings Association through Merit Savings Bank, both of Cincinnati, Ohio**

SUMMARY REPORT BY THE ATTORNEY GENERAL (3/11/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/20/92)
The applicant has assets of $3.4 billion; the target institution has assets of $107.9 million. Applicant and Thrift operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

The Provident Bank, Cincinnati, Ohio *to merge with* **Thrift Savings and Loan Co., Cincinnati, Ohio**

16. Mergers, Consolidations, and Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors, 1992—Continued

SUMMARY REPORT BY THE ATTORNEY GENERAL (3/20/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/20/92)
The applicant has assets of $3.4 billion; the target institution has assets of $132.2 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Mercantile Bank of Kansas City, Kansas City, Missouri *to acquire the assets and liabilities of the* **Independence Center branch of Home Federal Savings Association of Kansas City, Missouri**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/20/92)
The applicant has assets of $552 million; the target institution has assets of $72 million. The OTS has recommended immediate action by the Federal Reserve System to prevent the probable failure of Home Federal Savings Association.

Peoples State Bank of Plainview, Plainview, Minnesota *to merge with* **Eastwood Bank St. Charles, St. Charles, Minnesota**

SUMMARY REPORT BY THE ATTORNEY GENERAL (3/20/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (3/23/92)
The applicant has assets of $42.6 million; the target institution has assets of $8.9 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Valley Bank of Nevada *to merge with* **Security Pacific Bank Nevada, N.A., both of Las Vegas, Nevada**

SUMMARY REPORT BY THE ATTORNEY GENERAL (3/20/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (4/29/92)
The applicant has assets of $3.2 billion; the target institution has assets of $971.6 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

First Source Bank, South Bend, Indiana *to merge with* **Farmers State Bank of Wyatt, Wyatt, Indiana**

SUMMARY REPORT BY THE ATTORNEY GENERAL (4/7/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (5/7/92)
The applicant has assets of $1.2 billion; the target institution has assets of $83 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Mercantile Bank of Kansas City *to merge with* **American Bank, Kansas City, and American Bank of Platte County, both of Kansas City, Missouri**

SUMMARY REPORT BY THE ATTORNEY GENERAL (4/14/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (5/18/92)
The applicant has assets of $552 million; the target institutions have assets of $352 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Comerica Bank, Detroit, Michigan *to merge with* **Manufacturers Bank, N.A., Detroit, Michigan**

SUMMARY REPORT BY THE ATTORNEY GENERAL (5/6/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (5/19/92)
The applicant has assets of $12.2 billion; the target institution has assets of $12.0 billion. The parties operate in the same market.

16.—Continued

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Commercial Trust and Savings Bank, Mitchell, South Dakota *to merge with* **Sanborn County Bank, Woonsocket, South Dakota**

SUMMARY REPORT BY THE ATTORNEY GENERAL
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (5/27/92)
The applicant has assets of $141.6 million; the target institution has assets of $17.9 million. The parties do not operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Manufacturers and Traders Trust Company, Buffalo, New York *to merge with* **Central Trust Company, Rochester, New York, and Endicott Trust Company, Endicott, New York**

SUMMARY REPORT BY THE ATTORNEY GENERAL (4/16/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (6/1/92)
The applicant has assets of $7.0 billion; the target institutions have assets of $1.4 billion. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Banco Popular de Puerto Rico, New York, New York *to acquire the assets and liabilities of* **American Savings Bank, New York, New York**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (6/12/92)
The applicant has assets of $8.9 million; the target institution has assets of $622.1 million. The State has recommended immediate action by the Federal Reserve System to prevent the probable failure of American Savings Bank.

Bank of New York, New York, New York *to acquire the assets and liabilities of* **six branches of American Savings Bank, White Plains, New York, and three branches of Riverhead Savings Bank, Riverhead, New York**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (6/12/92)
The applicant has assets of $37.3 million; the target institutions have assets of $691 million. The State has recommended immediate action by the Federal Reserve System to prevent the probable failure of American Savings Bank and Riverhead Bank.

Johnstown Bank & Trust Company, Johnstown, Pennsylvania *to merge with* **People Bank One, West Lebanon, Pennsylvania**

SUMMARY REPORT BY THE ATTORNEY GENERAL (6/21/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (7/1/92)
The applicant has assets of $530.4 million; the target institution has assets of $18 million. The parties do not operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

The Bank of Hampton Roads, Chesapeake, Virginia *to merge with* **Coastal Virginia Bank, Virginia Beach, Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL (5/5/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (7/9/92)
The applicant has assets of $50.5 million; the target institution has assets of $17.4 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Central Fidelity Bank, Richmond, Virginia *to merge with* **Investors Federal Savings Bank, Richmond, Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

16. Mergers, Consolidations, and Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors, 1992—Continued

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (7/10/92)
The applicant has assets of $6.8 billion; the target institution has assets of $875.4 million. The RTC has recommended immediate action by the Federal Reserve System to prevent the probable failure of Investors Federal.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

City Center Bank of Colorado, Denver, Colorado *to merge with* **Security Bank of Colorado, Aurora, Colorado**

SUMMARY REPORT BY THE ATTORNEY GENERAL (7/21/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (8/5/92)
The applicant has assets of $18.8 million; the target institution has assets of $10.9 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Old Kent Bank & Trust Company, Grand Rapids, Michigan *to acquire the assets and liabilities of* **five branches of Great Lakes Bancorp, Lansing, Michigan**

SUMMARY REPORT BY THE ATTORNEY GENERAL (8/3/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (8/28/92)
The applicant has assets of $3.8 billion; the target institutions have assets of $66 million. Applicant and Branches operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Merrill Merchants Bank, Bangor, Maine *to acquire the assets and liabilities of* **seven branches of Fleet Bank of Maine, Portland, Maine**

SUMMARY REPORT BY THE ATTORNEY GENERAL (8/27/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (9/15/92)
The applicant, a de novo bank, and the target institutions have assets of $73.6 million. The parties operate in the same market.

The George Mason Bank, Fairfax, Virginia *to merge with* **The Washington Bank, Falls Church, Virginia**

SUMMARY REPORT BY THE ATTORNEY GENERAL
Request for report dispensed with as authorized by the Bank Merger Act.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (9/18/92)
The applicant has assets of $266.2 million; the target institution has assets of $23.8 million. The State has recommended immediate action by the Federal Reserve System to prevent the probable failure of The Washington Bank.

Demotte State Bank, Demotte, Indiana *to acquire the assets and liabilities of the* **Knox, Indiana, branch of Ameritrust National Bank, Elkhart, Indiana**

SUMMARY REPORT BY THE ATTORNEY GENERAL (9/2/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (9/29/92)
The applicant has assets of $104 million; the target institution has assets of $6.5 million. The parties do not operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Mellon Bank (MD), Rockville, Maryland *to acquire the assets and liabilities of* **eight branches of Standard Federal Savings Bank, Gaithersburg, Maryland**

SUMMARY REPORT BY THE ATTORNEY GENERAL (9/8/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (10/2/92)
The applicant has assets of $257 million; the target institutions have assets of $313.6 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

16.—Continued

Centura Bank, Rocky Mount, North Carolina *to acquire the assets and liabilities of the* **South Glen Burnie Road branch of People Federal Savings Bank, Wilmington, North Carolina**

SUMMARY REPORT BY THE ATTORNEY GENERAL (10/5/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (10/7/92)
The applicant has assets of $2.6 billion; the target institution has assets of $2.7 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Custer County Bank, Westcliffe, Colorado *to acquire the assets and liabilities of the* **Fountain branch of Green Mountain Bank, Lakewood, Colorado**

SUMMARY REPORT BY THE ATTORNEY GENERAL (9/8/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (10/9/92)
The applicant has assets of $8 million; the target institution has assets of $10 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Meridian Bank, Reading, Pennsylvania *to merge with* **The Peoples National Bank of Lebanon, Lebanon, Pennsylvania**

SUMMARY REPORT BY THE ATTORNEY GENERAL (10/5/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (10/26/92)
The applicant has assets of $10.3 billion; the target institution has assets of $142.8 billion. The parties do not operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Barnett Bank of Highlands County, Sebring, Florida; Barnett Bank of Naples, Naples, Florida; Barnett Bank of Pasco County, Holiday, Florida; Barnett Bank of Pinellas County, St. Petersburg, Florida; Barnett Bank of Polk County, Lakeland, Florida; Barnett Bank of Southwest Florida, Sarasota, Florida; Barnett Bank of Tallahassee, Tallahassee, Florida; Barnett Bank of Volusia County, Deland, Florida; and Barnett Bank of West Florida, Pensacola, Florida *to acquire the assets and liabilities of* **branches of First Florida Bank, N.A., Tampa, Florida**

SUMMARY REPORT BY THE ATTORNEY GENERAL
None received.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (10/28/92)
The applicants have assets of $9.2 billion; the target institutions have combined assets of $2.1 billion. In each case, the acquiring bank and the branches whose assets and liabilities were to be acquired operate in the same market.

In each case, the banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Farmers State Bank of Worden, Worden, Montana *to merge with* **The First National Bank in Hysham, Hysham, Montana**

SUMMARY REPORT BY THE ATTORNEY GENERAL (10/1/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (10/29/92)
The applicant has assets of $12.7 million; the target institution has assets of $8.9 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Centura Bank, Rocky Mount, North Carolina *to merge with* **Brevard Federal Savings and Loan Association, Brevard, North Carolina**

SUMMARY REPORT BY THE ATTORNEY GENERAL (9/8/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (11/18/92)
The applicant has assets of $2.6 billion; the target institution has assets of $130.9 million. The parties do not operate in the same market.

16. Mergers, Consolidations, and Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors, 1992—Continued

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

The Merchants Bank of New York, New York, New York *to merge with* **First New York Bank for Business, New York, New York**

Summary Report by the Attorney General
Request for report dispensed with as authorized by the Bank Merger Act.

Basis for Approval by the Federal Reserve (11/13/92)
The applicant has assets of $683 million; the target institution has assets of $418 million. The State has recommended immediate action by the Federal Reserve System to prevent the probable failure of First New York Bank for Business.

Old Kent Bank, Elmhurst, Illinois *to merge with* **UnibancTrust/Dupage, Chicago, Illinois, and First Federal of Elgin, FSA, Elgin, Illinois**

Summary Report by the Attorney General (10/21/92)
The proposed transaction would not be significantly adverse to competition.

Basis for Approval by the Federal Reserve (11/17/92)
The applicant has assets of $1.2 billion; the target institutions have assets of $263.4 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

The Bank of New York, New York, New York *to acquire the assets and liabilities of the* **retail operations of Barclays Bank of New York, New York, New York**

Summary Report by the Attorney General (10/7/92)
The proposed transaction would not be significantly adverse to competition.

Basis for Approval by the Federal Reserve (11/4/92)
The applicant has assets of $41.3 billion; the target operations have assets of $2.1 billion. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

The Peoples Bank and Trust Company, Selma, Alabama *to merge with* **The Citizens Bank, Prattville, Alabama**

Summary Report by the Attorney General (9/27/92)
The proposed transaction would not be significantly adverse to competition.

Basis for Approval by the Federal Reserve (11/27/92)
The applicant has assets of $218.7 million; the target institution has assets of $45.3 million. The parties do not operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Equibank, Pittsburgh, Pennsylvania *to acquire* **Integra National Bank/Pittsburgh, Pittsburgh, Pennsylvania**

Summary Report by the Attorney General
The proposed transaction would not be significantly adverse to competition.

Basis for Approval by the Federal Reserve (11/30/92)
The applicant has assets of $2.8 billion; the target institution has assets of $5.3 billion. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Fifth Third Bank, Cincinnati, Ohio *to acquire the assets and liabilities of the* **Chillicothe and Oxford, Ohio, branches of Home Savings Bank of America, FSB, Irwindale, California**

Summary Report by the Attorney General
The proposed transaction would not be significantly adverse to competition.

Basis for Approval by the Federal Reserve (12/8/92)
The applicant has assets of $5.6 billion; the target institutions have assets of $400 million. The parties do not operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Bank of Neosho, Neosho, Missouri *to merge with* **Anderson State Bank, Anderson, Missouri, and Citizens State Bank, Granby, Missouri**

Summary Report by the Attorney General (12/2/92)
The proposed transaction would not be significantly adverse to competition.

16.—Continued

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (12/16/92)
The applicant has assets of $92.8 million; the target institutions have assets of $213 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Belcaro Bank, Glendale, Colorado *to merge with* **Denver Tec Bank, Denver, Colorado, and The Professional Bank of Colorado, Englewood, Colorado**

SUMMARY REPORT BY THE ATTORNEY GENERAL (11/24/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (12/16/92)
The applicant has assets of $40.6 million; the target institutions have assets of $24.9 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Peoples Bank, Bloomington, Illinois *to merge with* **Lexington Bank, Lexington, Illinois**

SUMMARY REPORT BY THE ATTORNEY GENERAL (12/15/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (12/21/92)
The applicant has assets of $356.6 million; the target institution has assets of $93.6 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

First United Bank, Aurora, Colorado *to merge with* **The Bank of Parker, Parker, Colorado**

SUMMARY REPORT BY THE ATTORNEY GENERAL (12/1/92)
The proposed transaction would not be significantly adverse to competition.

BASIS FOR APPROVAL BY THE FEDERAL RESERVE (12/23/92)
The applicant has assets of $29.8 million; the target institution has assets of $19.2 million. The parties operate in the same market.

The banking factors and considerations relating to the convenience and needs of the community are consistent with approval.

Mergers Approved Involving Wholly Owned Subsidiaries of the Same Bank Holding Company

The following transactions involve banks that are subsidiaries of the same bank holding company. In each case, the summary report by the Attorney General indicates that the transaction would not have a significantly adverse effect on competition because the proposed merger is essentially a corporate reorganization. The Board of Governors, the Federal Reserve Bank, or the Secretary of the Board of Governors, whichever approved the application, determined that the competitive effects of the proposed transaction, the financial and managerial resources and prospects of the banks concerned, as well as the convenience and needs of the community to be served were consistent with approval.

Institution [1]	Assets (millions of dollars)	Date of approval
Chemical Bank, New York, New York	107,888	1/30/92
Merger		
Chemical Bank Delaware, Wilmington, Delaware	1,754	
Old Kent Bank and Trust Company, Grand Rapids, Michigan	3,500	1/29/92
Merger		
Old Kent Bank of Lansing, N.A., Lansing, Michigan	48	

16. Mergers, Consolidations, and Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors, 1992—Continued

Institution[1]	Assets (millions of dollars)	Date of approval
Eastern Michigan Bank, Croswell, Michigan (formerly State Bank of Croswell)	93	2/11/92
Merger		
Sanilac County Bank, Deckerville, Michigan	38	
Texas State Bank, McAllen, Texas	186	2/24/92
Merger		
Mid Valley Bank, Weslanco, Texas	92	
Harlingen State Bank, Harlingen, Texas	101	
Tri–State Bank, Denver, Colorado	50	3/10/92
Merger		
Boulder Tri–State Bank, Boulder, Colorado	16	
First of America Bank–Ann Arbor, Ann Arbor, Michigan	742	4/13/92
Merger		
First of America Bank–Livingston, Howell, Michigan	157	
Citizens Fidelity Bank and Trust Co., Louisville, Kentucky	5,630	4/22/92
Merger		
Citizens Fidelity Bank and Trust Co. of Hardin County, Elizabethtown, Kentucky	218	
Caliber Bank, Phoenix, Arizona	245	5/15/92
Merger		
Bank of America Arizona, Phoenix, Arizona (30 branches)	1,400	
Security Pacific Bank Arizona, Phoenix, Arizona (10 branches)	554	
Farmers State Bank & Trust Company of Superior, Superior, Nebraska	44	5/22/92
Merger		
Hardy State Bank, Hardy, Nebraska	8	
First of American Bank, Ann Arbor, Michigan	904	5/29/92
Merger		
First of America Bank–Plymouth, N.A., Plymouth, Michigan	119	
Vectra Bank, Denver, Colorado	24	7/16/92
Merger		
Vectra Bank, Denver, Colorado	21	
Vectra Bank of Lakewood, Lakewood, Colorado	17	
Vectra Bank of Thornton, Thornton, Colorado	12	
Vectra Bank of Wheat Ridge, Wheat Ridge, Colorado	9	
Vectra Bank of Federal Heights, Federal Heights, Colorado	14	
Citizens Fidelity B&T Company, Louisville, Kentucky	5,930	7/17/92
Merger		
Citizens Fidelity B&T Company, LaGrange, Kentucky	137	

16.—Continued

Institution [1]	Assets (millions of dollars)	Date of approval
Farmers State Bank of Western Illinois, New Windsor, Illinois	46	7/27/92
Merger		
Bank of Alexis, Alexis, Illinois	16	
City Center Bank of Colorado, Aurora, Colorado	20	8/5/92
Merger		
Security Bank of Colorado, Aurora, Colorado	11	
Fleet Bank of New York, Albany, New York	5,910	8/21/92
Merger		
Fleet Bank of New York, N.A., Buffalo, New York	3,951	
Bank One Champaign–Urbana, Monticello, Illinois	209	9/3/92
Merger		
Bank One, Monticello, Monticello, Illinois	88	
Cole Taylor Bank, Chicago, Illinois	1,258	10/9/92
Merger		
Cole Taylor Bank/Yorktown, Lombard, Illinois	119	
First Interstate Bank of Commerce, Billings, Montana (the successor of First Interstate Bank of Billings, Montana)	296	10/26/92
Merger		
First Interstate Bank of Missoula, N.A., Missoula, Montana	195	
First Interstate Bank of Hardin, Hardin, Montana	46	
First Interstate Bank of Miles City, Miles City, Montana	40	
First Interstate Bank of Billings Heights, Billings, Montana	34	
First Interstate Bank of West Billings, Billings, Montana	45	
First Interstate Bank of Colstrip, Colstrip, Montana	12	
First Interstate Bank of South Missoula, Missoula, Montana (a de novo bank)		
Community Bank and Trust Company, Forest City, Pennsylvania	176	12/17/92
Merger		
First National Bank of Nicholson, Nicholson, Pennsylvania	122	

1. Each proposed transaction was to be effected under the charter of the first named bank. The entries are in chronological order of approval. Some transactions include the acquisition of only certain assets and liabilities of the affiliated bank.

Mergers Approved Involving a Nonoperating Institution with an Existing Bank

The following transactions have no significant effect on competition; they merely facilitate the acquisition of the voting shares of a bank (or banks) by a holding company. In such cases, the summary report by the Attorney General indicates that the transaction will merely combine an existing bank with a nonoperating institution; in consequence, and without regard to the acquisition of the surviving bank by the holding company, the merger would have no effect on competition. The Board of Governors, the Federal Reserve Bank, or the Secretary of the Board, whichever approved the application, determined that the proposal would, in itself, have no adverse competitive effects and that the financial factors and considerations relating to the convenience and needs of the community were consistent with approval.

16. Mergers, Consolidations, and Acquisitions of Assets or Assumptions of Liabilities Approved by the Board of Governors, 1992—Continued

Institution[1]	Assets (millions of dollars)[2]	Date of approval
Interim Central Bank, Claysburg, Pennsylvania	...	2/26/92
Merger		
Central Bank, Claysburg, Pennsylvania	228	
Orange Interim Bank, Rocky Mount, North Carolina	...	9/24/92
Merger		
Centura Banks, Rocky Mount, North Carolina	2,600	
The KSB Bank, Killbuck, Ohio	...	10/22/92
Merger		
The Killbuck Savings Bank Company, Killbuck, Ohio	125	

1. Each proposed transaction was to be effected under the charter of the first-named bank. The entries are in chronological order of approval.

2. Where no assets are listed, the bank is newly organized and not in operation.

Federal Reserve Directories and Meetings

Board of Governors of the Federal Reserve System

December 31, 1992

Members

	Term expires
ALAN GREENSPAN of New York, *Chairman*[1]	January 31, 2006
DAVID W. MULLINS, JR., of Arkansas, *Vice Chairman*[1]	January 31, 1996
WAYNE D. ANGELL of Kansas	January 31, 1994
SUSAN M. PHILLIPS of Iowa	January 31, 1998
LAWRENCE B. LINDSEY of Virginia	January 31, 2000
JOHN P. LAWARE of Massachusetts	January 31, 2002
EDWARD W. KELLEY, JR., of Texas	January 31, 2004

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Bob Stahly Moore, *Special Assistant to the Board*
Lynn Fox, *Special Assistant to the Board*
Winthrop P. Hambley, *Special Assistant to the Board*
Diane E. Werneke, *Special Assistant to the Board*

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DIVISION OF CONSUMER AND COMMUNITY AFFAIRS

Griffith L. Garwood, *Director*
Glenn E. Loney, *Associate Director*
Dolores S. Smith, *Associate Director*
Maureen P. English, *Assistant Director*
Irene S. McNulty, *Assistant Director*

DIVISION OF BANKING SUPERVISION AND REGULATION

Richard Spillenkothen, *Director*
Stephen C. Schemering, *Deputy Director*
Don E. Kline, *Associate Director*
Frederick M. Struble, *Associate Director*
William A. Ryback, *Associate Director*
Herbert A. Biern, *Deputy Associate Director*
Roger T. Cole, *Deputy Associate Director*
James I. Garner, *Deputy Associate Director*
Howard Amer, *Assistant Director*
Gerald A. Edwards, Jr., *Assistant Director*
James D. Goetzinger, *Assistant Director*
Laura M. Homer, *Assistant Director*
James V. Houpt, Jr., *Assistant Director*
Jack P. Jennings, *Assistant Director*
Michael G. Martinson, *Assistant Director*
Rhoger H Pugh, *Assistant Director*
Sidney M. Sussan, *Assistant Director*
Molly S. Wassom, *Assistant Director*

1. The designations as Chairman and Vice Chairman expire on March 2, 1996, and July 22, 1995, respectively, unless the service of these members of the Board shall have terminated sooner.

Division of International Finance

Edwin M. Truman, *Staff Director*
Larry J. Promisel, *Senior Associate Director*
Charles J. Siegman, *Senior Associate Director*
Dale W. Henderson, *Associate Director*
David H. Howard, *Senior Adviser*
Donald B. Adams, *Assistant Director*
Peter Hooper III, *Assistant Director*
Karen H. Johnson, *Assistant Director*
Ralph W. Smith, Jr., *Assistant Director*

Division of Research and Statistics

Michael J. Prell, *Director*
Edward C. Ettin, *Deputy Director*
William R. Jones, *Associate Director*
Thomas D. Simpson, *Associate Director*
Lawrence Slifman, *Associate Director*
David J. Stockton, *Associate Director*
Martha Bethea, *Deputy Associate Director*
Peter A. Tinsley, *Deputy Associate Director*
Myron L. Kwast, *Assistant Director*
Patrick M. Parkinson, *Assistant Director*
Martha S. Scanlon, *Assistant Director*
Joyce K. Zickler, *Assistant Director*
John J. Mingo, *Adviser*
Levon H. Garabedian, *Assistant Director (Administration)*

Division of Monetary Affairs

Donald L. Kohn, *Director*
David E. Lindsey, *Deputy Director*
Brian F. Madigan, *Assistant Director*
Richard D. Porter, *Assistant Director*
Normand R.V. Bernard, *Special Assistant to the Board*

Office of Staff Director for Management

S. David Frost, *Staff Director*
William C. Schneider, Jr., *Project Director, National Information Center*
Portia W. Thompson, *Equal Employment Opportunity Programs Officer*

Division of Human Resources Management

David L. Shannon, *Director*
John R. Weis, *Associate Director*
Anthony V. DiGioia, *Assistant Director*
Joseph H. Hayes, Jr., *Assistant Director*
Fred Horowitz, *Assistant Director*

Office of the Controller

George E. Livingston, *Controller*
Stephen J. Clark, *Assistant Controller*
Darrell R. Pauley, *Assistant Controller*

Division of Support Services

Robert E. Frazier, *Director*
George M. Lopez, *Assistant Director*
David L. Williams, *Assistant Director*

Division of Information Resources Management

Stephen R. Malphrus, *Director*
Bruce M. Beardsley, *Deputy Director*
Marianne M. Emerson, *Assistant Director*
Po Kyung Kim, *Assistant Director*
Raymond H. Massey, *Assistant Director*
Edward T. Mulrenin, *Assistant Director*
Day W. Radebaugh, Jr., *Assistant Director*
Elizabeth B. Riggs, *Assistant Director*
Richard C. Stevens, *Assistant Director*

Division of Federal Reserve Bank Operations and Payment Systems

Clyde H. Farnsworth, Jr., *Director*
David L. Robinson, *Deputy Director*
Charles W. Bennett, *Assistant Director*
Jack Dennis, Jr., *Assistant Director*
Earl G. Hamilton, *Assistant Director*
Jeffrey C. Marquardt, *Assistant Director*
John H. Parrish, *Assistant Director*
Louise L. Roseman, *Assistant Director*
Florence M. Young, *Assistant Director*

Office of the Inspector General

Brent L. Bowen, *Inspector General*
Barry R. Snyder, *Assistant Inspector General*

Federal Open Market Committee

December 31, 1992

Members

ALAN GREENSPAN, *Chairman*, Board of Governors
E. GERALD CORRIGAN, *Vice Chairman*, President, Federal Reserve Bank of New York
WAYNE D. ANGELL, Board of Governors
THOMAS M. HOENIG, President, Federal Reserve Bank of Kansas City
JERRY L. JORDAN, President, Federal Reserve Bank of Cleveland
EDWARD W. KELLEY, JR., Board of Governors
JOHN P. LAWARE, Board of Governors
LAWRENCE B. LINDSEY, Board of Governors
THOMAS C. MELZER, President, Federal Reserve Bank of St. Louis
DAVID W. MULLINS, JR., Board of Governors
SUSAN M. PHILLIPS, Board of Governors
RICHARD F. SYRON, President, Federal Reserve Bank of Boston

Alternate Members

EDWARD G. BOEHNE, President, Federal Reserve Bank of Philadelphia
SILAS KEEHN, President, Federal Reserve Bank of Chicago
ROBERT D. MCTEER, JR., President, Federal Reserve Bank of Dallas
JAMES H. OLTMAN, First Vice President, Federal Reserve Bank of New York
GARY H. STERN, President, Federal Reserve Bank of Minneapolis

Officers

DONALD L. KOHN,
Secretary and Economist
NORMAND R.V. BERNARD,
Deputy Secretary
JOSEPH R. COYNE,
Assistant Secretary
GARY P. GILLUM,
Assistant Secretary
J. VIRGIL MATTINGLY,
General Counsel
ERNEST T. PATRIKIS,
Deputy General Counsel
MICHAEL J. PRELL,
Economist
EDWIN M. TRUMAN,
Economist
JOHN M. DAVIS,
Associate Economist
RICHARD G. DAVIS,
Associate Economist
THOMAS E. DAVIS,
Associate Economist
DAVID E. LINDSEY,
Associate Economist
ALICIA H. MUNNELL,
Associate Economist
LARRY J. PROMISEL,
Associate Economist
CHARLES J. SIEGMAN,
Associate Economist
THOMAS D. SIMPSON,
Associate Economist
DAVID J. STOCKTON,
Associate Economist

WILLIAM J. MCDONOUGH, *Manager of the System Open Market Account*
MARGARET L. GREENE, *Deputy Manager for Foreign Operations, System Open Market Account*
JOAN E. LOVETT, *Deputy Manager for Domestic Operations, System Open Market Account*

During 1992 the Federal Open Market Committee held eight meetings (see Record of Policy Actions of the Federal Open Market Committee in this REPORT.)

Federal Advisory Council

December 31, 1992

Members

District 1—IRA STEPANIAN, *Chairman and Chief Executive Officer*, Bank of Boston, Boston, Massachusetts

District 2—CHARLES S. SANFORD, JR., *Chairman*, Bankers Trust Company, New York, New York

District 3—TERRENCE A. LARSEN, *Chairman, President, and Chief Executive Officer*, CoreStates Financial Corp., Philadelphia, Pennsylvania

District 4—JOHN B. MCCOY, JR., *Chairman, President, and Chief Executive Officer*, Banc One Corporation, Columbus, Ohio

District 5—EDWARD E. CRUTCHFIELD, *Chairman and Chief Executive Officer*, First Union Corporation, Charlotte, North Carolina

District 6—E. B. ROBINSON, JR., *Chairman and Chief Executive Officer*, Deposit Guaranty Bank, Jackson, Mississippi

District 7—EUGENE A. MILLER, *Chairman, President, and Chief Executive Officer*, Comerica Incorporated, Detroit, Michigan

District 8—DAN W. MITCHELL, *Chairman and Chief Executive Officer*, Old National Bancorp, Evansville, Indiana

District 9—JOHN F. GRUNDHOFER, *Chairman, President, and Chief Executive Officer*, First Bank System, Inc., Minneapolis, Minnesota

District 10—DAVID A. RISMILLER, *Chairman, President, and Chief Executive Officer*, FirsTier Financial, Inc., Omaha, Nebraska

District 11—RONALD G. STEINHART, *Chairman and Chief Executive Officer*, Team Bank, Dallas, Texas

District 12—RICHARD M. ROSENBERG, *Chairman and Chief Executive Officer*, Bank of America, San Francisco, California

Officers

RONALD G. STEINHART, *President*

TERRENCE A. LARSEN, *Vice President*

HERBERT V. PROCHNOW, *Secretary*

WILLIAM J. KORSVIK, *Associate Secretary*

Directors

CHARLES S. SANFORD, JR.

JOHN B. MCCOY

E. B. ROBINSON, JR.

The Federal Advisory Council met on February 13–14, May 7–8, September 10–11, and November 5–6, 1992. The Board of Governors met with the council on February 4, May 8, September 11, and November 6, 1992. The council, which is composed of one representative of the banking industry from each of the twelve Federal Reserve Districts, is required by law to meet in Washington at least four times each year and is authorized by the Federal Reserve Act to consult with, and advise, the Board on all matters within the jurisdiction of the Board.

Consumer Advisory Council

December 31, 1992

Members

BARRY A. ABBOTT, *Partner*, Morrison & Foerster, San Francisco, California

JOHN R. ADAMS, *Corporate Vice President and Compliance Officer*, CoreStates Financial Corporation, Philadelphia, Pennsylvania

JOHN A. BAKER, *Senior Vice President*, Equifax, Inc., Atlanta, Georgia

VERONICA E. BARELA, *Executive Director*, NEWSED Community Development Corporation, Denver, Colorado

MULUGETTA BIRRU, *Executive Director*, Urban Redevelopment Authority of Pittsburgh, Pittsburgh, Pennsylvania

GENEVIEVE BROOKS, *Deputy Borough President*, Office of the Bronx Borough President, Bronx, New York

TOYE L. BROWN, *Director*, Massachusetts Bay Transportation Authority, Boston, Massachusetts

CATHY CLOUD, *Enforcement Program Director*, National Fair Housing Alliance, Washington, D.C.

MICHAEL D. EDWARDS, *President*, Prairie Security Bank, Yelm, Washington

GEORGE C. GALSTER, *Visiting Senior Research Associate*, The Urban Institute, Washington, D.C.

E. THOMAS GARMAN, *Professor of Consumer Studies*, Virginia Polytechnic Institute and State University, Blacksburg, Virginia

DONALD A. GLAS, *President*, First State Federal Savings and Loan Association, Hutchinson, Minnesota

DEBORAH B. GOLDBERG, *Reinvestment Specialist*, Center for Community Change, Washington, D.C.

MICHAEL M. GREENFIELD, *Professor of Law*, Washington University, St. Louis, Missouri

JOYCE HARRIS, *President and Chief Executive Officer*, Telco Community Credit Union, Madison, Wisconsin

GARY S. HATTEM, *Vice President*, Community Development Group, Bankers Trust Company, New York, New York

JULIA E. HILER, *Executive Vice President*, Sunshine Mortgage Corporation, Marietta, Georgia

HENRY JARAMILLO, JR., *President*, Ranchers State Bank, Belen, New Mexico

KATHLEEN E. KEEST, *Staff Attorney*, National Consumer Law Center, Boston, Massachusetts

EDMUND MIERZWINSKI, *Consumer Advocate*, U.S. Public Interest Research Group, Washington, D.C.

BERNARD F. PARKER, JR., *Executive Director*, Community Resource Projects, Detroit, Michigan

JEAN POGGE, *Vice President*, Development Deposits, South Shore Bank, Chicago, Illinois

JOHN V. SKINNER, *President and Chief Executive Officer*, Jewelers Financial Services, Inc., Irving, Texas

NANCY HARVEY STEORTS, *President*, Nancy Harvey Steorts and Associates, Dallas, Texas

LOWELL N. SWANSON, *President (Retired)*, United Finance Company, Portland, Oregon

MICHAEL W. TIERNEY, *Program Director*, Local Initiatives Support Corporation, Washington, D.C.

Consumer Advisory Council—Continued

Officers

COLLEEN D. HERNANDEZ, *Chairman*
Executive Director, Kansas City Neighborhood Alliance, Kansas City, Missouri

DENNY D. DUMLER, *Vice Chairman*
Senior Vice President, Colorado National Bank, Denver, Colorado

The Consumer Advisory Council met with members of the Board of Governors on March 26, June 11, and October 29, 1992. The council is composed of academics, state government officials, representatives of the financial industry, and representatives of consumer and community interests. It was established pursuant to the 1976 amendments to the Equal Credit Opportunity Act to advise the Board on consumer financial services.

Thrift Institutions Advisory Council

December 31, 1992

Members

DANIEL C. ARNOLD, *Director*, Farm & Home Financial Corporation, Houston, Texas

JAMES L. BRYAN, *President and Chief Executive Officer*, TEXINS Credit Union, Richardson, Texas

VANCE W. CHEEK, *President and Chief Executive Officer*, Home Federal Bank, FSB, Johnson City, Tennessee

BEATRICE D'AGOSTINO, *Chairman, President, and Chief Executive Officer*, New Jersey Savings Bank, Somerville, New Jersey

LYNN W. HODGE, *President and Chief Executive Officer*, United Savings Bank, Inc., Greenwood, South Carolina

THOMAS J. HUGHES, *President*, Navy Federal Credit Union, Merrifield, Virginia

RICHARD A. LARSON, *Chairman and Chief Executive Officer*, West Bend Savings Bank, West Bend, Wisconsin

PRESTON MARTIN, *Chairman and Chief Executive Officer*, WestFed Holdings, Inc., San Francisco, California

RICHARD D. PARSONS, *Chairman and Chief Executive Officer*, The Dime Savings Bank of New York, FSB, New York, New York

THOMAS R. RICKETTS, *Chairman, President, and Chief Executive Officer*, Standard Federal Bank, Troy, Michigan

EDMOND M. SHANAHAN, *President and Chief Executive Officer*, Bell Federal Savings and Loan Association, Chicago, Illinois

WOODBURY C. TITCOMB, *President and Chief Executive Officer*, Peoples Bancorp of Worcester, Inc., and Peoples Savings Bank, Worcester, Massachusetts

Officers

LYNN W. HODGE, *President*

DANIEL C. ARNOLD, *Vice President*

The members of the Thrift Institutions Advisory Council met with the Board of Governors on March 6, May 29, August 14, and November 13, 1992. The council, which is composed of representatives from credit unions, savings and loan associations, and savings banks, consults with and advises the Board on issues pertaining to the thrift industry and on various other matters within the Board's jurisdiction.

Officers of Federal Reserve Banks, Branches, and Offices

December 31, 1992[1]

BANK, Branch, or *facility*	Chairman[2] / Deputy Chairman	President / First Vice President	Vice President in charge of Branch
BOSTON[3]	Richard N. Cooper Jerome H. Grossman	Richard F. Syron Cathy E. Minehan	
NEW YORK[3]	Ellen V. Futter Maurice R. Greenberg	E. Gerald Corrigan James H. Oltman	
Buffalo	Herbert L. Washington		James O. Aston
PHILADELPHIA	Peter A. Benoliel Jane G. Pepper	Edward G. Boehne William H. Stone, Jr.	
CLEVELAND[3]	John R. Miller A. William Reynolds	Jerry L. Jordan William H. Hendricks	
Cincinnati	Marvin Rosenberg		Charles A. Cerino[4]
Pittsburgh	Robert P. Bozzone		Harold J. Swart[4]
RICHMOND[3]	Anne Marie Whittemore Henry J. Faison	Robert P. Black Jimmie R. Monhollon	
Baltimore	John R. Hardesty, Jr.		Ronald B. Duncan[4]
Charlotte	Anne M. Allen		Walter A. Varvel[4]
Culpeper			John G. Stoides[4]
ATLANTA	Edwin A. Huston Leo Benatar	Robert P. Forrestal Jack Guynn	Donald E. Nelson[4]
Birmingham	Nelda P. Stephenson		Fred R. Herr[4]
Jacksonville	Lana Jane Lewis-Brent		James D. Hawkins[4]
Miami	Michael T. Wilson		James T. Curry III
Nashville	Harold A. Black		Melvyn K. Purcell
New Orleans	Victor Bussie		Robert J. Musso
CHICAGO[3]	Richard G. Cline Robert M. Healey	Silas Keehn William C. Conrad	
Detroit	J. Michael Moore		Roby L. Sloan[4]
ST. LOUIS	H. Edwin Trusheim Robert H. Quenon	Thomas C. Melzer James R. Bowen	
Little Rock	James R. Rodgers		Karl W. Ashman
Louisville	Daniel L. Ash		Howard Wells
Memphis	Seymour B. Johnson		Raymond Laurence
MINNEAPOLIS	Delbert W. Johnson Gerald A. Rauenhorst	Gary H. Stern Thomas E. Gainor	
Helena	J. Frank Gardner		John D. Johnson

BANK, Branch, or *facility*	Chairman[2] Deputy Chairman	President First Vice President	Vice President in charge of Branch
KANSAS CITY	Burton A. Dole, Jr. Herman Cain	Thomas M. Hoenig Henry R. Czerwinski	
Denver	Barbara B. Grogan		Kent M. Scott
Oklahoma City	Ernest L. Holloway		David J. France
Omaha	Sheila Griffin		Harold L. Shewmaker
DALLAS	Leo E. Linbeck, Jr. Cece Smith	Robert D. McTeer, Jr. Tony J. Salvaggio	
El Paso	Alvin T. Johnson		Sammie C. Clay
Houston	Judy Ley Allen		Robert Smith III[4]
San Antonio	Roger R. Hemminghaus		Thomas H. Robertson
SAN FRANCISCO	James A. Vohs Robert F. Erburu	Robert T. Parry Patrick K. Barron	
Los Angeles	Donald G. Phelps		John F. Moore[4]
Portland	William A. Hilliard		E. Ronald Liggett[4]
Salt Lake City	Gary G. Michael		Andrea P. Wolcott
Seattle	George F. Russell, Jr.		Gordon R. G. Werkema[4]

1. A current list of these officers appears each month in the *Federal Reserve Bulletin*.
2. The Chairman of a Federal Reserve Bank, by statute, serves as Federal Reserve Agent.
3. Additional offices of these Banks are located at Lewiston, Maine; Windsor Locks, Connecticut; Cranford, New Jersey; Jericho, New York; Utica at Oriskany, New York; Columbus, Ohio; Columbia, South Carolina; Charleston, West Virginia; Des Moines, Iowa; Indianapolis, Indiana; and Milwaukee, Wisconsin.
4. Senior Vice President.

Conference of Chairmen

The Chairmen of the Federal Reserve Banks are organized into the Conference of Chairmen, which meets to consider matters of common interest and to consult with, and advise, the Board of Governors. Such meetings, attended also by the Deputy Chairmen, were held in Washington on May 27 and 28, and on December 3 and 4, 1992.

The members of the Executive Committee of the Conference of Chairmen during 1992 were Anne Marie Whittemore, Chairman; Delbert W. Johnson, Vice Chairman; and Richard N. Cooper, member.

On December 4, 1992, the Conference elected its Executive Committee for 1993, naming Delbert W. Johnson as Chairman, Ellen V. Futter as Vice Chairman, and Burton A. Dole, Jr., as the third member.

Conference of Presidents

The presidents of the Federal Reserve Banks are organized into the Conference of Presidents, which meets periodically to consider matters of common interest and to consult with, and advise, the Board of Governors.

Thomas C. Melzer, President of the Federal Reserve Bank of St. Louis, served as Chairman of the Conference in 1992, and Robert T. Parry, President of the Federal Reserve Bank of San Francisco, served as its Vice Chairman. Frances E. Sibley, of the Federal Reserve Bank of St. Louis, served as its Secretary, and Robert L. Feinberg, of the Federal Reserve Bank of San Francisco, served as its Assistant Secretary.

On October 26, 1992, the Conference elected Robert T. Parry as its Chairman for 1993–94 and Richard F. Syron, President of the Federal Reserve Bank of Boston, as its Vice Chairman.

Conference of First Vice Presidents

The Conference of First Vice Presidents of the Federal Reserve Banks was organized in 1969 to meet periodically for the consideration of operations and other matters.

William H. Hendricks, First Vice President of the Federal Reserve Bank of Cleveland, served as Chairman of the Conference for 1992, and William H. Stone, First Vice President of the Federal Reserve Bank of Philadelphia, served as its Vice Chairman. Creighton R. Fricek, of the Federal Reserve Bank of Cleveland, served as its Secretary, and Milissa Tadeo of the Federal Reserve Bank of Philadelphia, served as its Assistant Secretary.

On October 13, 1992, the Conference elected William H. Stone, First Vice President of the Federal Reserve Bank of Philadelphia, as its Chairman for 1993, and James H. Oltman, First Vice President of the Federal Reserve Bank of New York, as its Vice Chairman.

Directors

The following list of directors of Federal Reserve Banks and Branches shows for each director the class of directorship, the director's principal business affiliation, and the date the director's term expires. Each Federal Reserve Bank has nine members on its board of directors: three Class A and three Class B directors, who are elected by the stockholding member banks, and three Class C directors, who are appointed by the Board of Governors of the Federal Reserve System.

Class A directors represent the stockholding member banks in each Federal Reserve District. Class B and Class C directors represent the public and are chosen with due, but not exclusive, consideration to the interests of agriculture, commerce, industry, services, labor, and consumers; they may not be officers, directors, or employees of any bank or bank holding company. In addition, Class C directors may not be stockholders of any bank or bank holding company.

For the election of Class A and Class B directors, the Board of Governors classifies the member banks of each Federal Reserve District into three groups. Each group, which comprises banks with similar capitalization, elects one Class A director and one Class B director. The Board of Governors designates one Class C director as chairman of the board of directors and Federal Reserve Agent of each District Bank and appoints another Class C director as deputy chairman.

Federal Reserve Branches have either five or seven directors, a majority of whom are appointed by the parent Federal Reserve Bank; the others are appointed by the Board of Governors. One of the directors appointed by the Board is designated annually as chairman of the board of that Branch in a manner prescribed by the parent Federal Reserve Bank.

For the name of the chairman and deputy chairman of the board of directors of each Reserve Bank and of the chairman of each Branch, see the preceding table, "Officers of Federal Reserve Banks, Branches, and Offices."

DISTRICT 1—Boston

Class A

		Term expires Dec. 31
Terrence Murray	Chairman of the Board, President, and Chief Executive Officer, Fleet/Norstar Financial Group, Inc., Providence, Rhode Island	1992
David A. Page	President, Ocean National Bank of Kennebunk, Kennebunk, Maine	1993
Robert M. Silva	President, Chief Executive Officer, and Director, The Citizens National Bank, Putnam, Connecticut	1994

Class B

Joan T. Bok	Chairman of the Board, New England Electric System, Westborough, Massachusetts	1992
Stephen R. Levy	Chairman of the Board and Chief Executive Officer, Bolt Beranek and Newman, Inc., Cambridge, Massachusetts	1993
Edward H. Ladd	Chairman and Chief Executive Officer, Standish, Ayer and Wood, Inc., Boston, Massachusetts	1994

Class C

Richard N. Cooper	Maurits C. Boas Professor of International Economics, Harvard University, Cambridge, Massachusetts	1992
John E. Flynn	Executive Director, The Quality Connection, East Dennis, Massachusetts	1993
Jerome H. Grossman	Chairman of the Board and Chief Executive Officer, New England Medical Center, Inc., Boston, Massachusetts	1994

DISTRICT 2—New York

Class A

Victor J. Riley, Jr.	Chairman of the Board, President, and Chief Executive Officer, KeyCorp, Albany, New York	1992
Barbara Harding	Chairman of the Board and Chief Executive Officer, Phillipsburg National Bank and Trust Company, Phillipsburg, New Jersey	1993
Thomas G. Labrecque	Chairman and Chief Executive Officer, The Chase Manhattan Bank, N.A., New York, New York	1994

Class B

John A. Georges	Chairman of the Board and Chief Executive Officer, International Paper, Purchase, New York	1992

		Term expires Dec. 31
DISTRICT 2, *Class B*—Continued		
Rand V. Araskog	Chairman, President, and Chief Executive Officer, ITT Corporation, New York, New York	1993
Robert E. Allen	Chairman and Chief Executive Officer, American Telephone and Telegraph Company, Basking Ridge, New Jersey	1994
Class C		
Cyrus R. Vance	Presiding Partner, Simpson Thacher & Bartlett, New York, New York	1992
Ellen V. Futter	President, Barnard College, New York, New York	1993
Maurice R. Greenberg	Chairman and Chief Executive Officer, American International Group, Inc., New York, New York	1994
BUFFALO BRANCH		
Appointed by the Federal Reserve Bank		
Wilbur F. Beh	President, Atlanta National Bank, Atlanta, New York	1992
Susan A. McLaughlin	General Credit Manager, Eastman Kodak Company, Rochester, New York	1993
Charles M. Mitschow	Senior Executive Vice President, Regional Banking, Marine Midland Bank, N.A., Buffalo, New York	1994
Richard H. Popp	Operating Partner, Southview Farm, Castile, New York	1994
Appointed by the Board of Governors		
Herbert L. Washington	HLW Fast Track, Inc., Rochester, New York	1992
Joseph J. Castiglia	President and Chief Executive Officer, Pratt & Lambert, Inc., Buffalo, New York	1993
Donald L. Rust	Plant Manager, General Motors Powertrain Division, Tonawanda Engine Plant, Buffalo, New York	1994
DISTRICT 3—PHILADELPHIA		
Class A		
Samuel A. McCullough	Chairman of the Board and Chief Executive Officer, Meridian Bancorp, Inc., Reading, Pennsylvania	1992
Gary F. Simmerman	President and Chief Executive Officer, United Jersey Bank/South, N.A., Cherry Hill, New Jersey	1993

		Term expires Dec. 31
DISTRICT 3, *Class A*—Continued		
H. Bernard Lynch	President and Chief Executive Officer, The First National Bank of Wyoming, Wyoming, Delaware	1994
Class B		
David W. Huggins	President, RMS Technologies, Inc., Marlton, New Jersey	1992
James M. Mead	President, Capital Blue Cross, Harrisburg, Pennsylvania	1993
James A. Hagen	Chairman, President, and Chief Executive Officer, Consolidated Rail Corporation, Philadelphia, Pennsylvania	1994
Class C		
Peter A. Benoliel	Chairman of the Board, Quaker Chemical Corporation, Conshohocken, Pennsylvania	1992
Jane G. Pepper	President, The Pennsylvania Horticultural Society, Philadelphia, Pennsylvania	1993
Donald J. Kennedy	Business Manager, International Brotherhood of Electrical Workers, Local Union No. 269, Trenton, New Jersey	1994

DISTRICT 4—CLEVELAND

Class A		
Frank Wobst	Chairman of the Board and Chief Executive Officer, Huntington Bancshares Incorporated, Columbus, Ohio	1992
Alfred C. Leist	Chairman, President, and Chief Executive Officer, Apple Creek Banking Company, Apple Creek, Ohio	1993
William T. McConnell	President, The Park National Bank, Newark, Ohio	1994
Class B		
Laban P. Jackson, Jr.	Chairman, Clearcreek Properties, Lexington, Kentucky	1992
Verna K. Gibson	Business Consultant, Columbus, Ohio	1993
Douglas E. Olesen	President and Chief Executive Officer, Battelle Memorial Institute, Columbus, Ohio	1994
Class C		
A. William Reynolds	Chairman and Chief Executive Officer, GenCorp, Fairlawn, Ohio	1992
John R. Hodges	President, Ohio AFL–CIO, Columbus, Ohio	1993
John R. Miller	Former President and Chief Operating Officer, The Standard Oil Company (Ohio), Cleveland, Ohio	1994

		Term expires Dec. 31
DISTRICT 4—Continued		
Cincinnati Branch		
Appointed by the Federal Reserve Bank		
Clay Parker Davis	President and Chief Executive Officer, Citizens National Bank, Somerset, Kentucky	1992
Jack W. Buchanan	President, Sphar & Company, Inc., Winchester, Kentucky	1993
Harry A. Shaw, III	Chairman and Chief Executive Officer, Huffy Corporation, Dayton, Ohio	1993
Marvin J. Stammen	President and Chief Executive Officer, Second National Bank, Greenville, Ohio	1994
Appointed by the Board of Governors		
Eleanor Hicks	Hicks & Kinley, Cincinnati, Ohio	1992
Marvin Rosenberg	Partner, Towne Properties, Ltd., Cincinnati, Ohio	1993
Raymond A. Bradbury	Chairman, Martin County Coal Corporation, Inez, Kentucky	1994
Pittsburgh Branch		
Appointed by the Federal Reserve Bank		
William F. Roemer	Chairman and Chief Executive Officer, Integra Financial Corporation, Pittsburgh, Pennsylvania	1992
George A. Davidson, Jr.	Chairman and Chief Executive Officer, Consolidated Natural Gas Company, Pittsburgh, Pennsylvania	1993
I. N. Rendall Harper, Jr.	President and Chief Executive Officer, American Micrographics Company, Inc., Monroeville, Pennsylvania	1993
David S. Dahlmann	President and Chief Executive Officer, Southwest National Corporation, Greensburg, Pennsylvania	1994
Appointed by the Board of Governors		
Robert P. Bozzone	President and Chief Executive Officer, Allegheny Ludlum Corporation, Pittsburgh, Pennsylvania	1992
Sandra L. Phillips	Executive Director, Pittsburgh Partnership for Neighborhood Development, Pittsburgh, Pennsylvania	1993
Jack B. Piatt	Chairman of the Board, Millcraft Industries, Inc., Washington, Pennsylvania	1994

		Term expires Dec. 31
DISTRICT 5—RICHMOND		
Class A		
A. Pierce Stone	Chairman, President, and Chief Executive Officer, Virginia Community Bank, Louisa, Virginia	1992
James G. Lindley	Chairman, President, and Chief Executive Officer, South Carolina National Bank, Columbia, South Carolina	1993
Webb C. Hayes IV	President, The Palmer National Bank, Washington, D.C.	1994
Class B		
R. E. Atkinson, Jr.	Chairman, Dilmar Oil Company, Inc., Florence, South Carolina	1992
Paul A. DelaCourt	Chairman, The North Carolina Enterprise Corporation, Raleigh, North Carolina	1993
L. Newton Thomas, Jr.	Retired Senior Vice President, ITT/Carbon Industries, Inc., Charleston, West Virginia	1994
Class C		
Henry J. Faison	President, Faison Associates, Charlotte, North Carolina	1992
Stephen Brobeck	Executive Director, Consumer Federation of America, Washington, D.C.	1993
Anne Marie Whittemore	Partner, McGuire, Woods, Battle & Boothe, Richmond, Virginia	1994
BALTIMORE BRANCH		
Appointed by the Federal Reserve Bank		
Richard M. Adams	Chairman and Chief Executive Officer, United Bankshares, Inc., Parkersburg, West Virginia	1992
Daniel P. Henson III	Senior Development Director, Struever Bros., Eccles & Rouse, Inc., Baltimore, Maryland	1993
Thomas J. Hughes	President, Navy Federal Credit Union, Vienna, Virginia	1994
F. Levi Ruark	Chairman of the Board and President, The National Bank of Cambridge, Cambridge, Maryland	1994
Appointed by the Board of Governors		
John R. Hardesty, Jr.	President, Preston Energy, Inc., Kingwood, West Virginia	1992
Michael R. Watson	President, Association of Maryland Pilots, Annapolis, Maryland	1993
Rebecca Hahn Windsor	Chairman and Chief Executive Officer, Hahn Transportation, Inc., New Market, Maryland	1994

Term expires Dec. 31

DISTRICT 5—Continued

CHARLOTTE BRANCH

Appointed by the Federal Reserve Bank

David B. Jordan	Vice Chairman, Chief Executive Officer, and Director, Security Capital Bancorp, Salisbury, North Carolina	1992
Jim M. Cherry, Jr.	President and Chief Executive Officer, Williamsburg First National Bank, Kingstree, South Carolina	1993
Dorothy H. Aranda	President, Dohara Associates, Inc., Hilton Head Island, South Carolina	1994
L. Glenn Orr, Jr.	Chairman, President, and Chief Executive Officer, Southern National Corporation, Lumberton, North Carolina	1994

Appointed by the Board of Governors

Anne M. Allen	President, Anne Allen & Associates, Inc., Greensboro, North Carolina	1992
William E. Masters	President, Perception, Inc., Easley, South Carolina	1993
Harold D. Kingsmore	President and Chief Operating Officer, Graniteville Company, Graniteville, South Carolina	1994

DISTRICT 6—ATLANTA

Class A

W. H. Swain	Chairman of the Board, First National Bank, Oneida, Tennessee	1992
James B. Williams	Chairman and Chief Executive Officer, SunTrust Banks, Inc., Atlanta, Georgia	1993
Simpson Russell	Chairman and Chief Executive Officer, The First National Bank of Florence, Florence, Alabama	1994

Class B

J. Thomas Holton	President, Sherman International Corporation, Birmingham, Alabama	1992
Andre M. Rubenstein	Chairman of the Board and Chief Executive Officer, Rubenstein Brothers, Inc., New Orleans, Louisiana	1993
Victoria B. Jackson	President and Chief Executive Officer, DSS/ProDiesel, Nashville, Tennessee	1994

Class C

Leo Benatar	Chairman of the Board and President, Engraph, Inc., Atlanta, Georgia	1992

		Term expires Dec. 31
DISTRICT 6, *Class C*—Continued		
Edwin A. Huston	Senior Executive Vice President-Finance, Ryder System, Inc., Miami, Florida	1993
Hugh M. Brown	President and Chief Executive Officer, BAMSI, Inc., Titusville, Florida	1994
BIRMINGHAM BRANCH		
Appointed by the Federal Reserve Bank		
Robert M. Barrett	Chairman and President, The First National Bank of Wetumpka, Wetumpka, Alabama	1992
Julian W. Banton	Chairman, President, and Chief Executive Officer, SouthTrust Bank of Alabama, N.A., Birmingham, Alabama	1993
Marlin D. Moore, Jr.	Chairman, Pritchett-Moore, Inc., Tuscaloosa, Alabama	1994
Columbus Sanders	President, Consolidated Industries, Inc., Huntsville, Alabama	1994
Appointed by the Board of Governors		
Nelda P. Stephenson	President, Nelda Stephenson Chevrolet, Inc., Florence, Alabama	1992
Donald E. Boomershine	President, Better Business Bureau of Central Alabama, Inc., Birmingham, Alabama	1993
Shelton E. Allred	Chairman of the Board, President, and Chief Executive Officer, Frit Incorporated, Ozark, Alabama	1994
JACKSONVILLE BRANCH		
Appointed by the Federal Reserve Bank		
Merle L. Graser	Chairman and Chief Executive Officer, First National Bank of Venice, Venice, Florida	1992
Hugh H. Jones, Jr.	Chairman of the Board and Chief Executive Officer, Barnett Bank of Jacksonville, N.A., Jacksonville, Florida	1993
Perry M. Dawson	President and Chief Executive Officer, Suncoast Schools Federal Credit Union, Tampa, Florida	1994
Arnold A. Heggestad	William H. Dial Professor and Director, College of Business Administration, University of Florida, Gainesville, Florida	1994
Appointed by the Board of Governors		
Lana Jane Lewis-Brent	President, Paul Brent Designer, Inc., Panama City, Florida	1992
Joan Dial Ruffier	Member, Florida Board of Regents, Orlando, Florida	1993
Samuel H. Vickers	President, Chairman, and Chief Executive Officer, Design Containers, Inc., Jacksonville, Florida	1994

Term expires Dec. 31

DISTRICT 6—Continued

MIAMI BRANCH

Appointed by the Federal Reserve Bank

E. Anthony Newton	President, Island National Bank of Palm Beach, Palm Beach, Florida	1992
Steven C. Shimp	President, O-A-K/Florida, Inc., Fort Myers, Florida	1993
Pat L. Tornillo, Jr.	Executive Vice President, United Teachers of Dade, Miami, Florida	1993
Roberto G. Blanco	Vice Chairman and Chief Financial Officer, Republic National Bank of Miami, Miami, Florida	1994

Appointed by the Board of Governors

R. Kirk Landon	Chairman and Chief Executive Officer, American Bankers Insurance Group, Miami, Florida	1992
Michael T. Wilson	President, Vinegar Bend Farms, Inc., Belle Glade, Florida	1993
Dorothy C. Weaver	Executive Vice President, Intercap Investments, Inc., Coral Gables, Florida	1994

NASHVILLE BRANCH

Appointed by the Federal Reserve Bank

James D. Harris	President and Chief Executive Officer, Brentwood National Bank, Brentwood, Tennessee	1992
Williams E. Arant, Jr.	President and Chief Executive Officer, First National Bank of Knoxville, Knoxville, Tennessee	1993
William Baxter Lee III	Chairman and President, Southeast Services Corporation, Knoxville, Tennessee	1994
Marguerite W. Sallee	President and Chief Executive Officer, Corporate Child Care Management Services, Nashville, Tennessee	1994

Appointed by the Board of Governors

Harold A. Black	Professor and Head, Department of Finance, College of Business Administration, University of Tennessee, Knoxville, Tennessee	1992
Vacancy		1993
James R. Tuerff	President and Chief Executive Officer, American General Life and Accident Insurance Company, Nashville, Tennessee	1994

Term expires Dec. 31

DISTRICT 6—Continued

NEW ORLEANS BRANCH

Appointed by the Federal Reserve Bank

Earl W. Lundy	Chairman of the Board and Chief Executive Officer, First National Bank of Vicksburg, Vicksburg, Mississippi	1992
Howard C. Gaines	Chairman, President, and Chief Executive Officer, First National Bank of Commerce, New Orleans, Louisiana	1993
Joel B. Bullard, Jr.	President, Joe Bullard Automotive Companies, Mobile, Alabama	1994
Kay L. Nelson	Managing Director, Nelson Capital Corporation, New Orleans, Louisiana	1994

Appointed by the Board of Governors

Lucimarian Tolliver Roberts	President, Mississippi Coast Coliseum Commission, Pass Christian, Mississippi	1992
Victor Bussie	President, Louisiana AFL–CIO, Baton Rouge, Louisiana	1993
Jo Ann Slaydon	President, Slaydon Consultants and Insight Productions and Advertising, Baton Rouge, Louisiana	1994

DISTRICT 7—CHICAGO

Class A

B. F. Backlund	Chairman of the Board and Chief Executive Officer, Bartonville Bank, Peoria, Illinois	1992
David W. Fox	Chairman, President, and Chief Executive Officer, The Northern Trust Corporation and The Northern Trust Company, Chicago, Illinois	1993
Stefan S. Anderson	Chairman, President, and Chief Executive Officer, First Merchants Bank, N.A., Muncie, Indiana	1994

Class B

Paul J. Schierl	Financial Consultant, Green Bay, Wisconsin	1992
A. Charlene Sullivan	Associate Professor of Management, Krannert Graduate School of Management, Purdue University, West Lafayette, Indiana	1993
Thomas C. Dorr	President and Chief Executive Officer, Dorr's Pine Grove Farm Co., Marcus, Iowa	1994

Class C

Richard G. Cline	Chairman, President, and Chief Executive Officer, NICOR, Inc., Naperville, Illinois	1992

		Term expires Dec. 31
DISTRICT 7, *Class C*—Continued		
Robert M. Healey	President, Chicago Federation of Labor and Industrial Union Council, AFL–CIO, Chicago, Illinois	1993
Duane L. Burnham	Chairman and Chief Executive Officer, Abbott Laboratories, Abbott Park, Illinois	1994
DETROIT BRANCH		
Appointed by the Federal Reserve Bank		
Norman F. Rodgers	President and Chief Executive Officer, Hillsdale County National Bank, Hillsdale, Michigan	1992
Charles E. Allen	President and Chief Executive Officer, Graistone Realty Advisors, Inc., Detroit, Michigan	1993
William E. Odom	Chairman, Ford Motor Credit Company, Dearborn, Michigan	1993
Daniel R. Smith	Chairman and Chief Executive Officer, First of America Bank Corporation, Kalamazoo, Michigan	1994
Appointed by the Board of Governors		
J. Michael Moore	Chairman of the Board and Chief Executive Officer, Invetech Company, Detroit, Michigan	1992
Beverly A. Beltaire	President, PR Associates, Inc., Detroit, Michigan	1993
John D. Forsyth	Executive Director, University of Michigan Hospitals, Ann Arbor, Michigan	1994
DISTRICT 8—ST. LOUIS		
Class A		
W. E. Ayres	Chairman of the Board, Simmons First National Bank of Pine Bluff, Pine Bluff, Arkansas	1992
Ray U. Tanner	Chairman, Director, and Chief Executive Officer, Jackson National Bank, Jackson, Tennessee	1993
Henry G. River, Jr.	President and Chief Executive Officer, First National Bank in Pinckneyville, Pinckneyville, Illinois	1994
Class B		
Frank M. Mitchener, Jr.	President, Mitchener Farms, Inc., Sumner, Mississippi	1992
Warren R. Lee	President, W. R. Lee & Associates, Inc., Louisville, Kentucky	1993
Sandra B. Sanderson-Chesnut	President and Chief Executive Officer, Sanderson Plumbing Products, Inc., Columbus, Mississippi	1994

		Term expires Dec. 31
DISTRICT 8—Continued		
Class C		
H. Edwin Trusheim	Chairman and Chief Executive Officer, General American Life Insurance Company, St. Louis, Missouri	1992
Janet McAfee Weakley	President, Janet McAfee, Inc., St. Louis, Missouri	1993
Robert H. Quenon	Mining Consultant, St. Louis, Missouri	1994
LITTLE ROCK BRANCH		
Appointed by the Federal Reserve Bank		
Patricia M. Townsend	President, Townsend Company, Stuttgart, Arkansas	1992
James V. Kelley	Chairman, President and Chief Executive Officer, First United Bancshares, Inc., El Dorado, Arkansas	1993
Mahlon A. Martin	President, Winthrop Rockefeller Foundation, Little Rock, Arkansas	1993
Barnett Grace	Chairman and Chief Executive Officer, First Commercial Bank, N.A., Little Rock, Arkansas	1994
Appointed by the Board of Governors		
James R. Rodgers	Airport Manager, Little Rock Regional Airport, Little Rock, Arkansas	1992
L. Dickson Flake	President, Barnes, Quinn, Flake & Anderson, Inc., Little Rock, Arkansas	1993
Robert Daniel Nabholz, Jr.	Chief Executive Officer, Nabholz Construction Corporation, Conway, Arkansas	1994
LOUISVILLE BRANCH		
Appointed by the Federal Reserve Bank		
Morton Boyd	Chairman and Chief Executive Officer, First Kentucky National Corporation, Louisville, Kentucky	1992
Robert M. Hall	Owner, Mike Hall Farm, Seymour, Indiana	1993
Charles D. Storms	President and Chief Executive Officer, Red Spot Paint and Varnish Company, Inc., Evansville, Indiana	1993
Douglas M. Lester	Chairman, President, and Chief Executive Officer, Trans Financial Bancorp, Inc., Bowling Green, Kentucky	1994
Appointed by the Board of Governors		
Daniel L. Ash	President, Louisville Energy and Environment Corporation, Louisville, Kentucky	1992

		Term expires Dec. 31
DISTRICT 8, LOUISVILLE BRANCH		
Appointed by the Board of Governors—Continued		
John A. Williams	Chairman and Chief Executive Officer, Computer Services, Inc., Paducah, Kentucky	1993
Laura M. Douglas	Legal Director, Metropolitan Sewer District, Louisville, Kentucky	1994
MEMPHIS BRANCH		
Appointed by the Federal Reserve Bank		
Michael J. Hennessey	President, Munro & Company, Inc., Wynne, Arkansas	1992
Thomas M. Garrott	President and Chief Operating Officer, National Bank of Commerce and National Commerce Bancorporation, Memphis, Tennessee	1993
Larry A. Watson	Chairman of the Board and President, Liberty Federal Savings Bank, Paris, Tennessee	1993
Lewis F. Mallory, Jr.	President and Chief Executive Officer, National Bank of Commerce of Mississippi, Starkville, Mississippi	1994
Appointed by the Board of Governors		
M. Rita Schroeder	President, St. Francis Hospital, Memphis, Tennessee	1992
Seymour B. Johnson	Owner, Kay Planting Company, Indianola, Mississippi	1993
Vacancy		1994
DISTRICT 9—MINNEAPOLIS		
Class A		
Rodney W. Fouberg	Chairman of the Board, Farmers and Merchants Bank and Trust Co., Aberdeen, South Dakota	1992
Charles L. Seaman	President and Chief Executive Officer, First State Bank of Warner, Warner, South Dakota	1993
William W. Strausburg	Chairman and Chief Executive Officer, First Bank Montana, N.A., and General Manager, First Bank-Regional Banking Group, Billings, Montana	1994
Class B		
Bruce C. Adams	Partner, Triple Adams Farms, Minot, North Dakota	1992
Earl R. St. John, Jr.	President, St. John Forest Products, Inc., Spalding, Michigan	1993
Duane E. Dingmann	President, Trubilt Auto Body, Inc., Eau Claire, Wisconsin	1994
Class C		
Gerald A. Rauenhorst	Chairman of the Board and Chief Executive Officer, Opus Corporation, Minneapolis, Minnesota	1992

Term expires Dec. 31

DISTRICT 9, *Class C*—Continued

Delbert W. Johnson	President and Chief Executive Officer, Pioneer Metal Finishing, Minneapolis, Minnesota	1993
Jean D. Kinsey	Professor, Consumption and Consumer Economics, Department of Agricultural and Applied Economics, University of Minnesota, St. Paul, Minnesota	1994

HELENA BRANCH

Appointed by the Federal Reserve Bank

Donald E. Olsson, Jr.	Executive Vice President, Ronan State Bank, Ronan, Montana	1992
Nancy M. Stephenson	Executive Director, Neighborhood Housing Services, Great Falls, Montana	1992
Beverly D. Harris	President, Empire Federal Savings and Loan Association, Livingston, Montana	1993

Appointed by the Board of Governors

J. Frank Gardner	President, Montana Resources, Inc., Butte, Montana	1992
James E. Jenks	Jenks Farms, Hogeland, Montana	1993

DISTRICT 10—KANSAS CITY

Class A

Harold L. Gerhart, Jr.	Chairman and Chief Executive Officer, First National Bank, Newman Grove, Nebraska	1992
Roger L. Reisher	Co-Chairman of the Board, FirstBank Holding Company of Colorado, Lakewood, Colorado	1993
Charles I. Moyer	Chairman and Chief Executive Officer, The First National Bank of Phillipsburg, Phillipsburg, Kansas	1994

Class B

Frank A. McPherson	Chairman of the Board and Chief Executive Officer, Kerr-McGee Corporation, Oklahoma City, Oklahoma	1992
Don E. Adams	Buffalo, Oklahoma	1993
Frank J. Yaklich, Jr.	President and Chief Executive Officer, CF & I Steel Corporation, Pueblo, Colorado	1994

Class C

Herman Cain	President and Chief Executive Officer, Godfather's Pizza, Inc., Omaha, Nebraska	1992
Thomas E. Rodriguez	President and General Manager, Thomas E. Rodriguez & Associates, P.C., Aurora, Colorado	1993

		Term expires Dec. 31
DISTRICT 10, *Class C*—Continued		
Burton A. Dole, Jr.	Chairman of the Board and President, Puritan-Bennett Corporation, Overland Park, Kansas	1994
DENVER BRANCH		
Appointed by the Federal Reserve Bank		
Henry A. True III	Partner, True Companies, Casper, Wyoming	1992
Peter R. Decker	President, Decker & Associates, Denver, Colorado	1993
Clifford E. Kirk	President, First National Bank of Gillette, Gillette, Wyoming	1994
Richard I. Ledbetter	President and Chief Executive Officer, First National Bank of Farmington, Farmington, New Mexico	1994
Appointed by the Board of Governors		
Sandra K. Woods	Vice President, Corporate Real Estate, Adolph Coors Company, Golden, Colorado	1992
Gilbert Sanchez	President, New Mexico Highlands University, Las Vegas, New Mexico	1993
Barbara B. Grogan	President, Western Industrial Contractors, Inc., Denver, Colorado	1994
OKLAHOMA CITY BRANCH		
Appointed by the Federal Reserve Bank		
Gordona Duca	President and Owner, Gordona Duca, Inc., Realtors, Tulsa, Oklahoma	1992
John Wm. Laisle	President and Chief Executive Officer, MidFirst Bank, SSB, Oklahoma City, Oklahoma	1992
C. Kendric Fergeson	Chairman of the Board and Chief Executive Officer, The National Bank of Commerce, Altus, Oklahoma	1993
Appointed by the Board of Governors		
Victor R. Schock	Executive Director, Credit Counseling Services of Oklahoma, Inc., Tulsa, Oklahoma	1992
Ernest L. Holloway	President, Langston University, Langston, Oklahoma	1993
OMAHA BRANCH		
Appointed by the Federal Reserve Bank		
John R. Cochran	President and Chief Executive Officer, Norwest Bank Nebraska, N.A., Omaha, Nebraska	1992
Donald A. Leu	President and Chief Executive Officer, Consumer Credit Counseling Service, Omaha, Nebraska	1993

		Term expires Dec. 31
DISTRICT 10, OMAHA BRANCH		
Appointed by the Federal Reserve Bank—Continued		
Thomas H. Olson	President and Chief Executive Officer, Lisco State Bank, Lisco, Nebraska	1993
Appointed by the Board of Governors		
Sheila Griffin	Special Advisor to the Governor of the State of Nebraska for International Trade, Lincoln, Nebraska	1992
LeRoy W. Thom	President, T-L Irrigation Company, Hastings, Nebraska	1993

DISTRICT 11—DALLAS

Class A		
Robert G. Greer	Chairman of the Board, Tanglewood Bank, N.A., Houston, Texas	1992
T. C. Frost	Chairman of the Board, Frost National Bank, San Antonio, Texas	1993
Eugene M. Phillips	Chairman of the Board and President, The First National Bank of Panhandle, Panhandle, Texas	1994
Class B		
Gary E. Wood	President, Texas Research League, Austin, Texas	1992
J. B. Cooper, Jr.	Farmer, Roscoe, Texas	1993
Peyton Yates	President, Yates Drilling Company and Executive Vice President, Yates Petroleum Corporation, Artesia, New Mexico	1994
Class C		
Leo E. Linbeck, Jr.	Chairman of the Board and Chief Executive Officer, Linbeck Construction Corporation, Houston, Texas	1992
Vacancy		1993
Cece Smith	General Partner, Phillips-Smith Specialty Retail Group, Dallas, Texas	1994

EL PASO BRANCH

Appointed by the Federal Reserve Bank		
Wayne Merritt	Chairman of the Board and President, Texas National Bank of Midland, Midland, Texas	1992
Veronica K. Callaghan	Vice President and Principal, KASCO Ventures, Inc., El Paso, Texas	1993
Ben H. Haines, Jr.	President and Chief Operating Officer, First National Bank of Dona Ana County, Las Cruces, New Mexico	1993
Hugo Bustamante, Jr.	Owner and Chief Executive Officer, ProntoLube, El Paso, Texas	1994

Term expires Dec. 31

DISTRICT 11, EL PASO BRANCH—Continued

Appointed by the Board of Governors

W. Thomas Beard III	President, Leoncita Cattle Company, Alpine, Texas	1992
Diana S. Natalicio	President, The University of Texas at El Paso, El Paso, Texas	1993
Alvin T. Johnson	Senior Vice President, Management Assistance Corporation of America, El Paso, Texas	1994

HOUSTON BRANCH

Appointed by the Federal Reserve Bank

Jenard M. Gross	President, Gross Builders, Inc., Houston, Texas	1992
Walter E. Johnson	President and Chief Executive Officer, Southwest Bank of Texas, Houston, Texas	1993
Clive Runnells	President and Director, Runnells Cattle Company, Bay City, Texas	1993
Tieman H. Dippel, Jr.	Chairman of the Board and President, Brenham Bancshares, Inc., Brenham, Texas	1994

Appointed by the Board of Governors

Judy Ley Allen	Partner and Administrator, Allen Investments, Houston, Texas	1992
Milton Carroll	Chairman of the Board and Chief Executive Officer, Instrument Products, Inc., Houston, Texas	1993
Isaac H. Kempner III	Chairman of the Board, Imperial Holly Corporation, Sugar Land, Texas	1994

SAN ANTONIO BRANCH

Appointed by the Federal Reserve Bank

Gregory W. Crane	Chairman of the Board, President, and Chief Executive Officer, Broadway National Bank, San Antonio, Texas	1992
Javier Garza	Executive Vice President, The Laredo National Bank, Laredo, Texas	1993
Sam R. Sparks	President, Sam R. Sparks, Inc., Progreso, Texas	1993
T. Jack Moore III	Owner and Manager, T.J. Moore Lumber Inc., Ingram, Texas	1994

Appointed by the Board of Governors

Lawrence E. Jenkins	Vice President (Retired), Lockheed Missiles and Space Company, Inc., Austin, Texas	1992
Erich Wendl	President and Chief Executive Officer, Maverick Markets, Inc., Corpus Christi, Texas	1993

		Term expires Dec. 31
DISTRICT 11, SAN ANTONIO BRANCH		
Appointed by the Board of Governors—Continued		
Roger R. Hemminghaus	Chairman, President, and Chief Executive Officer, Diamond Shamrock, Inc., San Antonio, Texas	1994

DISTRICT 12–SAN FRANCISCO

Class A		
Warren K. K. Luke	President and Director, Hawaii National Bancshares, Inc., and Vice Chairman of the Board and Chief Executive Officer, Hawaii National Bank, Honolulu, Hawaii	1992
Richard L. Mount	Chairman, President, and Chief Executive Officer, Saratoga Bancorp, Saratoga, California	1993
William E. B. Siart	President, First Interstate Bancorp, Los Angeles, California	1994
Class B		
E. Kay Stepp	Advisor to the Chairman, Former President, and Chief Operating Officer, Portland General Electric, Portland, Oregon	1992
John N. Nordstrom	Co-Chairman of the Board, Nordstrom, Inc., Seattle, Washington	1993
William L. Tooley	Chairman, Tooley & Company, Investment Builders, Los Angeles, California	1994
Class C		
Robert F. Erburu	Chairman of the Board and Chief Executive Officer, The Times Mirror Company, Los Angeles, California	1992
James A. Vohs	Chairman and Chief Executive Officer (Retired), Kaiser Foundation Health Plan, Inc., and Kaiser Foundation Hospitals, Oakland, California	1993
Judith M. Runstad	Partner and Managing Director, Foster Pepper and Shefelman, Seattle, Washington	1994

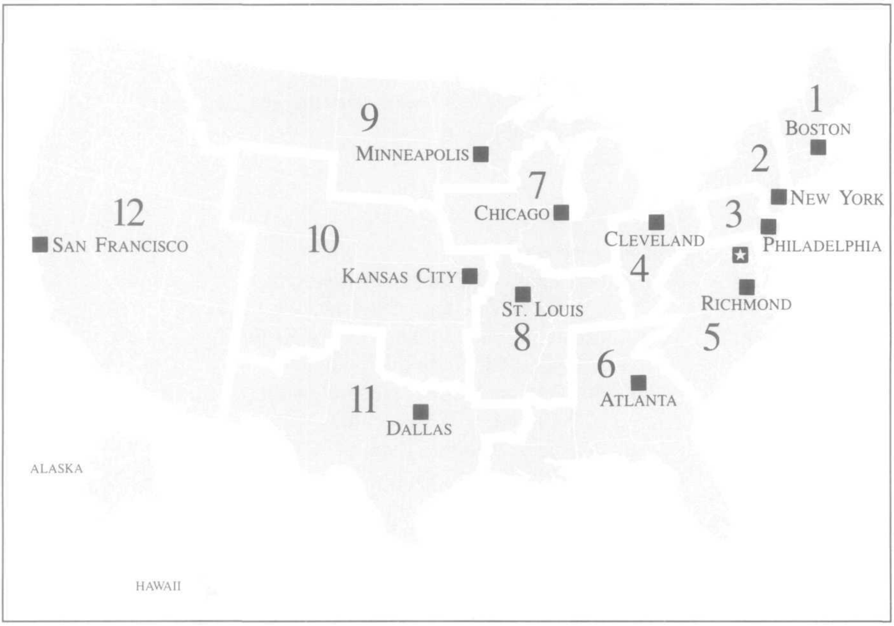
LOS ANGELES BRANCH

Appointed by the Federal Reserve Bank		
Fred D. Jensen	Executive Director, Long Beach Local Development Corporation, Long Beach, California	1992
Anita Landecker	Regional Vice President, Local Initiatives Support Corporation, Los Angeles, California	1993

		Term expires Dec. 31
DISTRICT 12, LOS ANGELES BRANCH		
Appointed by the Federal Reserve Bank—Continued		
Antonia Hernandez	President and General Counsel, Mexican American Legal Defense and Educational Fund, Los Angeles, California	1994
William S. Randall	Chief Executive Officer, Southwest Region, First Interstate Bank, Phoenix, Arizona	1994
Appointed by the Board of Governors		
Anne L. Evans	Owner, Developer, and Operator, Evans Hotels, San Diego, California	1992
Donald G. Phelps	Chancellor, Los Angeles Community College District, Los Angeles, California	1993
David L. Moore	President and Chief Executive Officer, Western Growers Association, Irvine, California	1994
PORTLAND BRANCH		
Appointed by the Federal Reserve Bank		
Elizabeth K. Johnson	President, TransWestern Helicopters, Inc., Scappoose Industrial Airpark, Scappoose, Oregon	1992
Cecil W. Drinkward	President, Hoffman Construction Company, Portland, Oregon	1993
Stephen G. Kimball	Chairman, President, and Chief Executive Officer, Baker Boyer Bancorp, Walla Walla, Washington	1993
Stuart H. Compton	Chairman, Pioneer Trust Bank, N.A., Salem, Oregon	1994
Appointed by the Board of Governors		
Wayne E. Phillips, Jr.	Vice President, Phillips Ranch, Inc., Baker, Oregon	1992
Ross R. Runkel	Professor of Law, Willamette University Center for Dispute Resolution, Salem, Oregon	1993
William A. Hilliard	Editor, *The Oregonian*, Portland, Oregon	1994
SALT LAKE CITY BRANCH		
Appointed by the Federal Reserve Bank		
Ronald S. Hanson	Director of the Board and Member of the Executive Committee, Zions First National Bank, Salt Lake City, Utah	1992
Curtis H. Eaton	Vice President; Manager, Community Banking Area; and Member of the Board of Directors, First Security Bank of Idaho, N.A., Twin Falls, Idaho	1993
Virginia P. Kelson	Partner, Ralston Consulting Group, Salt Lake City, Utah	1993
Gerald R. Sherratt	President, Southern Utah University, Cedar City, Utah	1994

		Term expires Dec. 31
DISTRICT 12, SALT LAKE CITY BRANCH—Continued		
Appointed by the Board of Governors		
Gary G. Michael	Chairman and Chief Executive Officer, Albertson's, Inc., Boise, Idaho	1992
Constance G. Hogland	Executive Director, Boise Neighborhood Housing Services, Inc., Boise, Idaho	1993
H. Roger Boyer	Chairman of the Board, The Boyer Company, Salt Lake City, Utah	1994
SEATTLE BRANCH		
Appointed by the Federal Reserve Bank		
H. H. Larison	President and Chief Executive Officer, Columbia Paint & Coatings, Spokane, Washington	1992
B. R. Beeksma	Chairman of the Board, InterWest Savings Bank, Oak Harbor, Washington	1993
Gerry B. Cameron	President and Chief Executive Officer, U.S. Bank of Washington, N.A., Seattle, Washington	1993
Robert P. Gray	President, National Bank of Alaska, Anchorage, Alaska	1994
Appointed by the Board of Governors		
Emilie A. Adams	President and Chief Executive Officer, Better Business Bureau, Seattle, Washington	1992
George F. Russell, Jr.	Chairman, Frank Russell Company, Tacoma, Washington	1993
William R. Wiley	Senior Vice President, Technology Management; and Director, Pacific Northwest Division, Battelle Memorial Institute, Richland, Washington	1994

Maps of the Federal Reserve System



LEGEND

Both pages

- ■ Federal Reserve Bank city
- ⊡ Board of Governors of the Federal Reserve System, Washington, D.C.

Facing page

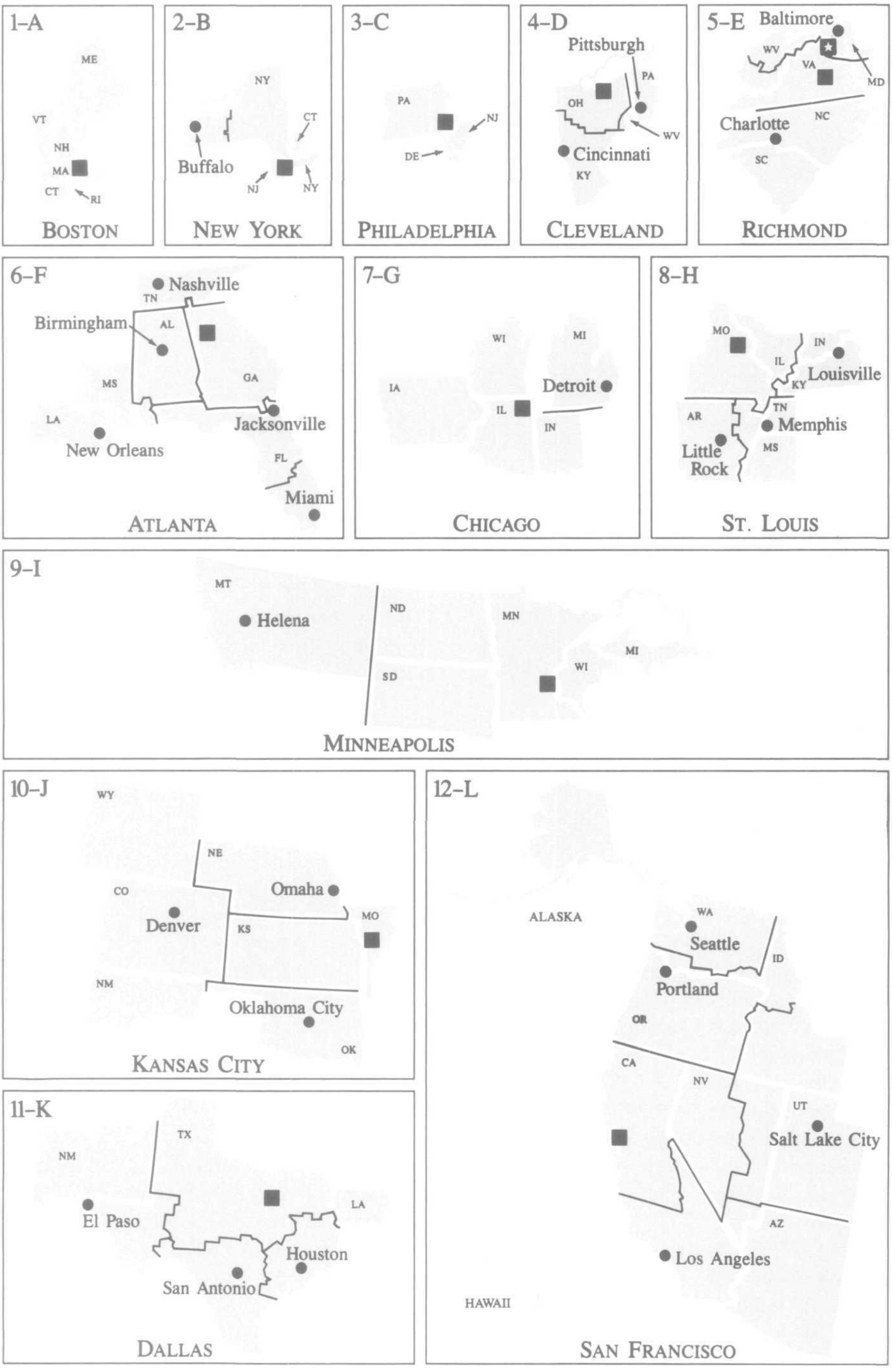
- • Federal Reserve Branch city
- — Branch boundary

NOTE

The Federal Reserve officially identifies Districts by number and Reserve Bank city (shown on both pages) and by letter (shown on the facing page).

In District 12, the Seattle Branch serves Alaska, and the San Francisco Bank serves Hawaii.

The System serves commonwealths and territories as follows: the New York Bank serves the Commonwealth of Puerto Rico and the U.S. Virgin Islands; the San Francisco Bank serves American Samoa, Guam, and the Commonwealth of the Northern Mariana Islands. The maps show the boundaries within the System as of year-end 1992.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