

Meeting of the Federal Open Market Committee

August 18, 1987

Minutes of Actions

A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington, D. C., on Tuesday, August 18, 1987, at 9:00 a.m.

PRESENT: Mr. Greenspan, Chairman
Mr. Corrigan, Vice Chairman
Mr. Angell
Mr. Boehne
Mr. Boykin
Mr. Heller
Mr. Johnson
Mr. Keehn
Mr. Kelley
Ms. Seger
Mr. Stern

Messrs. Black, Forrestal, and Parry, Alternate
Members of the Federal Open Market Committee

Messrs. Guffey, Melzer, and Morris, Presidents of the Federal
Reserve Banks of Kansas City, St. Louis, and Boston,
respectively

Mr. Kohn, Secretary and Staff Adviser
Mr. Bernard, Assistant Secretary
Mrs. Loney, Deputy Assistant Secretary
Mr. Bradfield, General Counsel
Mr. Oltman, Deputy General Counsel
Mr. Truman, Economist (International)

Messrs. Lang, Lindsey, Prell, Rolnick, Rosenblum,
Scheld, Siegman, and Simpson, Associate Economists

Mr. Sternlight, Manager for Domestic Operations, System
Open Market Account

Mr. Cross, Manager for Foreign Operations, System
Open Market Account

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Mr. Coyne, Assistant to the Board, Board of Governors
Mr. Gemmill, Staff Adviser, Division of International
Finance, Board of Governors
Mrs. Zickler, Assistant Director, Division of Research
and Statistics, Board of Governors
Ms. Low, Open Market Secretariat Assistant, Office of
Board Members, Board of Governors

Mr. Hendricks, First Vice President, Federal Reserve Bank
of Cleveland

Mr. Fousek, Executive Vice President, Federal Reserve Bank
of New York

Messrs. Balbach, Beebe, Broaddus, J. Davis, T. Davis,
Ms. Munnell, Mr. Thieke, and Ms. Tshinkel, Senior
Vice Presidents, Federal Reserve Banks of St. Louis,
San Francisco, Richmond, Cleveland, Kansas City,
Boston, New York, and Atlanta, respectively

By unanimous vote, Alan Greenspan was elected to serve as Chairman
of the Committee until the first meeting of the Committee after February 29,
1988.

By unanimous vote, the minutes of actions taken at the meeting of
the Federal Open Market Committee held on July 7, 1987, were approved.

By unanimous vote, System open market transactions in foreign
currencies during the period July 7, 1987, through August 17, 1987, were
ratified.

By unanimous vote, System open market transactions in government
securities and federal agency obligations during the period July 7, 1987,
through August 17, 1987, were ratified.

By unanimous vote, paragraph 1(a) of the Authorization for Domestic
Open Market Operations was amended to raise from \$6 billion to \$12 billion
the dollar limit on intermeeting changes in System account holdings of U.S.
government and federal agency securities for the intermeeting period ending
on September 22, 1987.

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

The information reviewed at this meeting suggests on balance that economic activity is expanding at a moderate pace in the current quarter. In July, total nonfarm payroll employment rose considerably further; the increase included continuing large gains in the service-producing sector and a sizable advance in manufacturing. The civilian unemployment rate fell slightly further to 6.0 percent. Industrial production increased strongly in July after rising moderately on balance in the first half of the year. Consumer spending grew at a reduced pace earlier in the year but retail sales posted large increases in June and July. Housing starts were unchanged in July and remained at their reduced second-quarter level. Recent indicators of business capital spending point to some strength, particularly in equipment outlays. The rise in consumer and producer prices has been moderate in recent months, but for the year to date prices generally have risen more rapidly than in 1986, primarily reflecting sizable increases in prices of energy and non-oil imports. Wage increases have remained relatively moderate in recent months.

In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies was unchanged on balance since the meeting of the Committee on July 7. In the second quarter the merchandise trade deficit in current dollars was about the same as in the first quarter.

The monetary aggregates grew slowly in July. For 1987 through July, expansion of both M2 and M3 has been below the lower ends of the ranges established by the Committee for the year, while growth in M1 has been well below its pace in 1986. Expansion in total domestic non-financial debt has moderated this year. Most long-term interest rates have risen somewhat since the July meeting; in short-term markets, Treasury bill rates also have increased somewhat while private rates are little changed. Stock prices have risen substantially since the latest meeting.

The Federal Open Market Committee seeks monetary and financial conditions that will foster reasonable price stability over time, promote growth in output on a sustainable basis, and contribute to an improved pattern of international transactions. In furtherance of these objectives the Committee agreed at its meeting in July to reaffirm the ranges established in February for growth of 5-1/2 to 8-1/2 percent for both M2 and M3, measured from the fourth quarter of 1986 to the fourth quarter of 1987. The Committee agreed that growth in these aggregates around the lower ends of their ranges may be appropriate in light of developments with respect to velocity and signs of the potential for some strengthening in underlying inflationary pressures, provided that economic activity is expanding at an acceptable pace. The monitoring range for growth in total domestic nonfinancial debt set in February for the year was left unchanged at 8 to 11 percent.

For 1988, the Committee agreed on tentative ranges of monetary growth, measured from the fourth quarter of 1987 to the fourth quarter of 1988, of 5 to 8 percent for both M2 and M3. The Committee provisionally set the associated range for growth in total domestic nonfinancial debt at 7-1/2 to 10-1/2 percent.

With respect to M1, the Committee recognized that, based on experience, the behavior of that aggregate must be judged in the light of other evidence relating to economic activity and prices; fluctuations in M1 have become much more sensitive in recent years to changes in interest rates, among other factors. Because of this sensitivity, which has been reflected in a sharp slowing of the decline in M1 velocity over the first half of the year, the Committee again decided at the July meeting not to establish a specific target for growth in M1 over the remainder of 1987 and no tentative range was set for 1988. The appropriateness of changes in M1 this year will continue to be evaluated in the light of the behavior of its velocity, developments in the economy and financial markets, and the nature of emerging price pressures. The Committee welcomes substantially slower growth of M1 in 1987 than in 1986 in the context of continuing economic expansion and some evidence of greater inflationary pressures. The Committee in reaching operational decisions over the balance of the year will take account of growth in M1 in the light of circumstances then prevailing. The issues involved with establishing a target for M1 will be carefully reappraised at the beginning of 1988.

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In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. Somewhat greater reserve restraint would, or slightly lesser reserve restraint might, be acceptable depending on indications of inflationary pressures, the strength of the business expansion, developments in foreign exchange markets, as well as the behavior of the aggregates. This approach is expected to be consistent with growth in M2 and M3 over the period from June through September at annual rates of around 5 percent. Growth in M1, while picking up from recent levels, is expected to remain well below its pace during 1986. The Chairman may call for Committee consultation if it appears to the Manager for Domestic Operations that reserve conditions during the period before the next meeting are likely to be associated with a federal funds rate persistently outside a range of 4 to 8 percent.

It was agreed that the next meeting of the Committee would be held on September 22, 1987.

The meeting adjourned.

Secretary