

Meeting of the Federal Open Market Committee

December 15-16, 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., starting on Tuesday, December 15, 1987, at 3:15 p.m., and continuing on Wednesday, December 16, 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 <sup>1</sup>  
Mr. Kelley  
Ms. Seger  
Mr. Stern

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

Messrs. Guffey, Melzer and Morris,<sup>2</sup> 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. Patrikis, Deputy General Counsel  
Mr. Truman, Economist (International)

Messrs. Lang, Lindsey, Prell, Rolnick, Rosenblum, Scheld,<sup>1</sup>  
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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1/ Present for Wednesday session; participated in Tuesday session via telephone conference from the Federal Reserve Bank of Chicago.

2/ Entered meeting after action to approve minutes of meeting held on November 3, 1987.

Mr. Coyne, Assistant to the Board, Board of Governors  
Mr. Promisel, Senior Associate Director, Division of  
International Finance, Board of Governors  
Mr. Slifman, Associate Director, Division of Research  
and Statistics, Board of Governors  
Mr. Madigan,<sup>1</sup> Assistant Director, Division of Monetary  
Affairs, Board of Governors  
Mr. Small,<sup>1</sup> Economist, Division of Monetary Affairs,  
Board of Governors  
Ms. Low, Open Market Secretariat Assistant, Division of  
Monetary Affairs, Board of Governors  
  
Mr. Guynn, First Vice President, Federal Reserve Bank  
of Atlanta

Messrs. Balbach, Beebe, Broaddus, J. Davis, T. Davis,  
and Ms. Tschinkel,<sup>2</sup> Senior Vice Presidents,  
Federal Reserve Banks of St. Louis, San Francisco,  
Richmond, Cleveland, Kansas City, and Atlanta,  
respectively

Messrs. Frydl and McNees, Vice Presidents, Federal Reserve  
Banks of New York and Boston, respectively

Mr. Guentner, Manager, Federal Reserve Bank of New York

Ms. Rosenbaum,<sup>3</sup> Research Officer, Federal Reserve Bank of  
Atlanta

By unanimous vote, the minutes of actions taken at the meeting  
of the Federal Open Market Committee held on November 3, 1987, were approved.

Secretary's Note: The following actions were taken at the  
Wednesday session.

By unanimous vote, System open market transactions in foreign  
currencies during the period November 3, 1987 through December 15, 1987,  
were ratified.

By unanimous vote, System open market transactions in government  
securities and federal agency obligations during the period November 3, 1987,  
through December 15, 1987, were ratified.

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1/ Attended portion of meeting on Tuesday.

2/ Attended Wednesday session only.

3/ Attended Tuesday session only.

By unanimous vote, paragraph 1(a) of the Authorization for Domestic Open Market Operations was amended to raise from \$6 billion to \$9 billion the dollar limit on intermeeting changes in System Account holdings of U.S. government and federal agency securities for the intermeeting period ending February 10, 1988.

With Mr. Johnson and Ms. Seger dissenting, 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 economic information reviewed at this meeting largely reflected the influence of developments that were under way before the financial disturbances of mid-October. The extent to which those disturbances would affect the economy remained uncertain. Information available for the current quarter suggested that the expansion in economic activity was moderating from a brisk pace in the third quarter. Total nonfarm payroll employment rose strongly further over October and November, with the manufacturing sector recording relatively large gains. The civilian unemployment rate, at 5.9 percent in November, remained close to its level since mid-year. Industrial production also increased considerably further over October and November, following sizable advances since late spring. Retail sales edged up in November after two months of substantial declines. Recent indicators of business capital spending suggested modest further growth after a surge in the third quarter. Housing starts rose somewhat in November, after slowing in October, but were little changed from the average pace in the second and third quarters. The nominal U.S. merchandise trade deficit in October appeared to have deteriorated substantially from the average rate in the third quarter. The rise in broad measures of prices and wages in recent months generally has been close to that experienced earlier in the year.

Financial markets remained somewhat unsettled. Stock and bond prices continued to fluctuate over a relatively wide range during the period since the previous Committee meeting on November 3. On balance, share prices fell somewhat further in this period. Changes in long-term yields were mixed while short-term interest rates rose, especially on short-maturity private market instruments. The trade-weighted foreign exchange value of the dollar in terms of the other G-10 currencies declined considerably further.

The monetary aggregates weakened in November after strengthening in October in conjunction with a temporary surge in demands for transaction balances and other liquid assets in the latter part of that month. For 1987 through November, expansion of M2 fell somewhat further below the lower end of the range established by the Committee for the year, while growth of M3 remained around the lower end of its range. Growth of M1 was close to that of nominal GNP for the year to date and expansion in total domestic nonfinancial debt remained well within the Committee's monitoring range for the year.

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 might 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 was 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 in July 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 had 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 would 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 welcomed 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 indicated in July that in reaching operational decisions over the balance of the year it would 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.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. The Committee recognizes that still sensitive conditions in financial markets and uncertainties in the economic outlook may continue to call for a special degree of flexibility in open market operations. Taking account of conditions in financial markets, somewhat lesser reserve restraint or somewhat greater reserve restraint would be acceptable depending on the strength of the business expansion, indications of inflationary pressures, developments in foreign exchange markets, as well as the behavior of the monetary aggregates. The contemplated reserve conditions are expected to be consistent with growth in M2 and M3 over the period from November through March at annual rates of about 5 percent and 6 percent, respectively. Over the same period, growth in M1 is expected to remain relatively limited. 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.

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It was agreed that the next meeting of the Committee would be held on February 9-10, 1988.

The meeting adjourned.

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Secretary