FEDERAL RESERVE press release

For Use at 4:30 p.m. February 12, 1988

The Federal Reserve Board and the Federal Open Market Committee today released the attached record of policy actions taken by the Federal Open Market Committee at its meetings on December 15-16, 1987, and January 5, 1988.

Such records for each meeting of the Committee are made available a few days after the next regularly scheduled meeting and are published in the Federal Reserve Bulletin and the Board's Annual Report. The summary descriptions of economic and financial conditions they contain are based solely on the information that was available to the Committee at the time of the meeting.

Attachment

RECORD OF POLICY ACTIONS OF THE
FEDERAL OPEN MARKET COMMITTEE

Meeting Held on December 15-16, 1987

1. Domestic policy directive

The data on the economy reviewed at this meeting largely reflected the impact of developments that were under way before the stock market collapse in mid-October. The ultimate effects of the decline in stock prices and associated developments in financial markets remained uncertain. Available data suggested that growth in output was moderating from a brisk pace in the third quarter. Spending indicators pointed to a considerable slowing in the expansion of domestic private final demands in the current quarter. Prices and wages continued to increase at about the same pace as in earlier months of the year.

Industrial production rose 0.4 percent in November, following a strong rise in the previous month. In November, gains were widespread with the exception of the motor vehicles industry. Capacity utilization in mining, manufacturing, and utilities rose slightly further in November, and the overall rate in manufacturing was at its highest level since August 1984.

Total nonfarm payroll employment continued to rise strongly over October and November. The manufacturing sector again recorded relatively large gains, with hiring increases widespread across durable and nondurable goods industries. At the same time, job growth in service industries continued at a brisk pace. Aggregate hours worked by production and nonsupervisory workers remained on a strong uptrend. The civilian unemployment rate fell back to 5.9 percent in November.

Growth in consumer spending appeared to have weakened thus far in the fourth quarter, mainly because of a drop in purchases of new cars after incentive programs ended in September, although sales of other items also were weak. Retail sales edged up in November after two months of substantial declines. Spending on furniture and appliances fell sharply in September and October and moved lower again in November. Outlays for apparel recovered a bit in November, but spending on general merchandise registered another decline.

Housing starts rebounded in November but their average level in October and November remained somewhat below the averages in the second and third quarters. The improvement in November reflected a sharp rise in the multi-family category, which had dropped noticeably in October. Single-family starts edged up, supported by lower interest rates, but remained below their third-quarter average. The number of permits issued was about unchanged in November.

The expansion in business fixed investment appeared to have decelerated markedly from the exceptional pace of the third quarter. Outlays for capital equipment were damped by the drop in auto sales and a sharp decline in purchases of heavy trucks. Outside of motor vehicles, equipment demand remained strong early in the current quarter. Nominal shipments of nondefense capital goods, although down somewhat in October, remained above the third-quarter average. In addition, new orders moved up further, suggesting that shipments were likely to retain some momentum in the near term. Spending for nonresidential structures softened in recent months; petroleum drilling appeared to have leveled off, and nonresidential construction put-in-place declined somewhat in September and October.

Inventory investment was strong in October. Nonetheless, factory stocks remained low relative to sales by historical standards. In the auto sector, production exceeded sales in both October and November, and dealer stocks again rose to relatively high levels. At other retail trade establishments, inventory accumulation slowed in October.

The nominal U.S. merchandise trade deficit appeared to have deteriorated substantially in October from the average rate in the third quarter, reflecting in part large seasonal swings in both exports and imports. Exports were up slightly in October; about half of the increase was accounted for by a strong seasonal rise in agricultural products. The rise in nonagricultural exports was concentrated in shipments of a variety of products to Canada while exports of commercial aircraft dropped. Imports rose considerably in October. Most of the increase was in non-oil products, particularly machinery imports and imports of passenger cars from Japan, Canada, and Korea.

Economic growth in the major foreign industrial countries increased markedly in the third quarter. Real GNP rose substantially in Japan mainly because of a large increase in domestic demand, although net exports made a small positive contribution to growth; expansion in residential investment was particularly strong. German GNP, which had declined over the first half of the year, also increased sharply largely in response to domestic demand. Industrial production data for October showed some further expansion of activity in Japan and Germany. Available data suggested that GDP growth in the third quarter was strong in France, the United Kingdom, and Canada, as well.

The rise in most broad measures of prices and wages in recent months generally was close to that experienced earlier in the year. Retail energy prices dropped in October, and crude oil prices edged down in recent weeks. However, apart from energy, increases in consumer prices picked up recently, including higher prices for food, new cars, apparel, and rents. At the producer level, prices of finished goods turned down in October, but prices for intermediate and crude materials remained on a strong uptrend.

At its meeting on November 3, the Committee adopted a directive that called for maintaining the degree of pressure on reserve positions that had been sought around the time of that meeting. The Committee recognized that the volatile conditions in financial markets, including potential shifts in demands for liquidity, and uncertainties in the economic outlook might continue to call for a special degree of flexibility in open market operations. Taking account of conditions in financial markets, the members decided that somewhat lesser reserve restraint would, or slightly greater reserve restraint might, 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 intermeeting range for the federal funds rate was reduced by one percentage point to 4 to 8 percent.

During the interval since the November meeting, reserves continued to be supplied on a more flexible basis than usual to help maintain relatively steady conditions in the money market at a time of unusual sensitivity and uncertainty in financial markets generally. Adjustment plus seasonal borrowing tended to be relatively low and averaged about $225 million during the two maintenance periods ending December 2. As evidence of a reduced willingness to borrow accumulated, such borrowing behavior was accommodated through provision of nonborrowed reserves in order to keep money market conditions from firming. Borrowing declined somewhat further so far in the latest maintenance period. After expanding at a double-digit pace in October, total and nonborrowed reserves contracted in November, reflecting a drop in required reserves associated in large measure with the reversal of the post-crash bulge in transactions accounts and a lower average level of demands for excess reserves.

Federal funds traded mainly in the 6-3/4 to 6-7/8 percent range over the intermeeting period, close to the average level around the time of the November meeting. Most other short-term rates rose somewhat on balance. The increases apparently reflected some ebbing of preferences for liquidity as financial markets calmed further. In addition, expectations of further ease in monetary policy tended to diminish as incoming data suggested continued, albeit moderate, expansion in the economy and as the dollar fell in foreign exchange markets. To some extent rates on very short-term instruments increased because of positioning in advance of anticipated pressures in money markets around the year-end. Yields on long-term Treasury securities were up about 20 basis points after early November, while corporate bond yields rose half that much. In contrast, municipal bond yields and mortgage rates fell over the intermeeting period. Stock prices declined slightly further on balance. In general, while financial markets appeared to be functioning more normally, they remained unsettled with occasional episodes of unusually wide price swings and of flights to liquidity and quality echoing the experience after mid-October.

Since the November meeting, the foreign exchange value of the dollar declined about 5 percent on a weighted-average basis in terms of the other G-10 currencies. The dollar came under pressure early in the period, partly because of market disappointment over U.S. efforts to reduce the budget deficit. In early December concerted reductions in official interest rates by Germany and several other European countries temporarily boosted the dollar; over the entire intermeeting period short-term interest rates declined about 1/2 percentage point, on average, in major foreign industrial countries, while long-term rates were down slightly on balance. However, the dollar's decline resumed, especially after the very disappointing U.S. trade figures for October were released on December 10.

The monetary aggregates weakened substantially in November. While some of the weakness reflected a runoff of the bulge in demand deposits that followed the stock market plunge in October, demand deposits dropped below early October levels. Other checkable deposits also decreased. With the nontransactions portion of M2 expanding only sluggishly, the level of M2 was about unchanged in November. Only small time deposits and money fund shares showed any strength, as their yields remained attractive relative to rates on market instruments and liquid deposits. To supplement weak growth in core deposits, banks and thrift institutions issued managed liabilities at a robust pace in November, and flows into institution-only money funds moved up sharply, as returns on these funds lagged the downward movement of market rates in late October. Even so, M3 expanded at an annual rate of only 4-3/4 percent. For the year through November, M2 and M3 grew respectively at rates well below and at the lower ends of the 5-1/2 to 8-1/2 percent annual ranges established by the Committee. M1 growth also slowed sharply this year. The reduced growth of these aggregates and a turnaround of their velocities appeared to be attributable primarily to the rebound in interest rates and opportunity costs in 1987 after steep declines in 1985 and 1986.

The staff projection continued to point to relatively sluggish growth in economic activity during the first part of 1988 and to some pickup later in the year. The contour of the projection was dominated by the anticipated effects of the decline in stock prices and the accompanying developments in financial markets, although these effects now were projected to be more muted than was expected in early November. In the context of recent decisions to reduce the federal budget deficit, fiscal policy would exert a moderately restraining impact on aggregate demand. As in the previous projection, consumer spending was projected to slow in coming quarters, but to strengthen later in 1988 as most of the adjustment to the lower level of stock market wealth was completed. Growth in spending for plant and equipment was likely to slow in response to the sluggish pace of domestic sales--offset only in part by further growth in export sales--and the resulting diminished requirements for additional capacity. The decline in mortgage interest rates was expected to stimulate a modest improvement in residential construction. The external sector would provide a substantial positive contribution to activity over the entire projection horizon. Prices were likely to rise at a moderate rate in 1988. Energy prices were expected to be flat, but nonpetroleum import prices were projected to continue to place upward pressure on inflation and nominal gains in compensation were anticipated to increase. However, continuing efforts to improve competitiveness were expected to damp real wages and labor costs over the projection horizon.

In the Committee's discussion of the economic situation and outlook, members referred to conflicting signs with regard to the prospective strength of the business expansion. On the one hand, employment and production had been well maintained in recent months and financial markets had calmed since late October. To date, the sharp decline in stock prices appeared to have had little impact on domestic business activity, perhaps because it had merely reversed a runup in earlier months of the year and because it was associated with a reduction in market interest rates. Moreover, recent declines in the foreign exchange value of the dollar would help to sustain the improvement in net exports. In these circumstances, business investment also might remain fairly strong. Members cited favorable reports from businesses in many parts of the country that tended to support an optimistic outlook for overall business activity, although some areas or industries had recovered only slightly thus far from relatively depressed conditions. On the negative side, a number of members observed that the risks to the economy were in the direction of slower growth than foreseen in the staff forecast. Consumer spending in particular had been relatively weak, as evidenced by recent trends and the apparent need for widespread discounting to buttress sales. Moreover, growth in disposable incomes was believed likely to remain relatively sluggish, and together with an already low saving rate and rising consumer debt burdens would tend to retard expansion in retail sales. It also was noted that the full effects of the decline in stock prices might not yet have been felt. In addition, money growth had been quite weak, and at some point the slow growth might be reflected in incomes and spending. Several members commented that current projections were subject to a great deal of uncertainty, especially in light of still unusually sensitive conditions in domestic financial markets and the uncertain prospects for the dollar and the nation's foreign trade balance.

The members gave considerable attention during the discussion to the outlook for foreign trade and its implications for domestic economic activity. Recent data on nominal net exports were disappointing, but real net exports had shown considerable improvement so far this year. Gains in exports were especially encouraging. The data indicating an improved real trade balance were supported by members' observations from around the country. Many business contacts were reporting greatly enhanced export opportunities as a result of the dollar's depreciation, although there were exceptions, and they also indicated that their ability to compete in domestic markets against imported goods had improved. The members generally agreed that the foreign trade sector was positioned to make an appreciable contribution to sustained expansion in domestic economic activity at a time when growth in overall domestic demands might be weakening. However, the likely extent of actual gains from trade would depend to some degree on the strength of the economies of foreign industrial nations.

In further discussion members observed that, given the higher rate of utilization of domestic capital and labor resources, substantial improvement in the nation's trade balance implied the need for relatively restrained growth in domestic demands over time as more production was diverted to export markets. The adjustment in trade, which appeared inevitable in light of the unsustainable size of the current trade deficit and the rapid growth in the nation's external indebtedness, appeared feasible over time without causing major disruptions in domestic business activity. However, such an adjustment would require the implementation of appropriate fiscal, monetary, and trade policies by the United States and its major trading partners.

Turning to the outlook for inflation, some members commented that inflationary expectations seemed to have abated to some extent since the collapse in stock prices during October. The depreciation of the dollar would continue to exert upward pressures on domestic prices, but increases in wages and other costs did not appear to be worsening, and in the view of some members inflation might be in the process of easing. Concern was expressed by a number of members, however, that wage and price pressures might well intensify if the economy were to expand at an appreciably faster pace than many members currently expected or if the dollar were to decline substantially in the foreign exchange markets.

At its meeting in July the Committee reviewed the basic policy objectives that it had set in February for growth of the monetary and debt aggregates in 1987 and established tentative objectives for expansion of those aggregates in 1988. For the period from the fourth quarter of 1986 to the fourth quarter of 1987, the Committee reaffirmed the ranges established in February involving growth of 5-1/2 to 8-1/2 percent for both M2 and M3. Given developments through mid-year, the Committee agreed in July that growth in these aggregates around the lower ends of their ranges might be appropriate, depending on the circumstances. The monitoring range for expansion in total domestic nonfinancial debt also was left unchanged at 8 to 11 percent for 1987. For 1988 the Committee agreed on tentative reductions of 1/2 percentage point to growth ranges of 5 to 8 percent for both M2 and M3. The Committee also reduced the associated range for growth in total domestic nonfinancial debt by 1/2 percentage point to 7-1/2 to 10-1/2 percent for 1988. With respect to M1, the Committee decided at the July meeting not to set a specific target for the remainder of 1987 or to establish a tentative range for 1988. It was understood that all the ranges for 1988 were provisional and that they would be reviewed in early 1988 in the light of intervening developments. The issues involved with establishing a target for M1 would be carefully reappraised at the same time.

At this meeting the Committee held a preliminary discussion of issues relating to its target ranges for monetary growth in 1988. The behavioral characteristics of the aggregates in recent years were reviewed. Considerable attention was devoted to the question of whether or not to establish a target for M1 or some possible alternative such as M1A or the monetary base. While no decisions were made at this meeting, the members were not currently inclined to reestablish a range for M1, given the continued large interest rate sensitivity of the demand for this aggregate and the associated wide swings in its velocity. The Committee will complete its review of these issues and decide on its target ranges for 1988 at the February meeting.

In the Committee's discussion of policy for the next intermeeting period, most of the members agreed that on balance economic and financial developments called for unchanged conditions of reserve availability. Such a policy was viewed as consistent with continuing growth in the economy at a moderate pace. The members recognized that financial markets remained unsettled despite the emergence of a much calmer atmosphere since the latter part of October, and they believed that money market conditions might be subject to considerable volatility around the year-end. In this situation most of the members felt that open market operations should continue to be conducted with a special degree of flexibility and should give considerable weight to conditions in the money market, at least over the nearer term, to accommodate shifting demands for liquidity and reserves and to temper potentially excessive fluctuations in short-term markets. However, most of the members also favored looking for opportunities to move toward more normal procedures for implementing policy if financial markets continued to stabilize.

In the majority view the risks associated with either firming or easing under current circumstances outweighed the potential benefits. It was noted, for example, that any significant firming would have unsettling effects on domestic financial markets and the associated rise in interest rates would pose considerable risks to the economic expansion. At the same time, many members felt that any appreciable easing would not be desirable currently, especially in light of the dollar's weakness and the risks to domestic financial markets and the economy that a sharp further decline in the dollar would incur. Other members weighed such risks differently, including one member who concluded that monetary policy should move toward somewhat easier reserve conditions in light of the potential for appreciably slower growth in the economy, given in this view the prospects for substantially reduced growth in domestic demands and the possibility that improvement in the nation's foreign trade balance would not provide a sufficient offset. In light of the differences among the members with regard to policy for the short run, including the Committee's operating procedures in the near term, and the uncertainties surrounding financial markets and the economy, it was understood that the members might need to consult on policy implementation before the next scheduled meeting on February 9-10, 1988.

Several members expressed some concern about the generally sluggish growth in the monetary aggregates since the early months of the year, including indications of little or no growth in M2 in recent weeks and much slower expansion in M3 than had been expected earlier. The members recognized that the relationship between monetary growth and economic performance had been very imprecise in recent years. Nonetheless, money growth and the economy were not unrelated and the reemergence of a stronger linkage could not be ruled out. In these circumstances, a continuation of sluggish growth of the monetary aggregates needed to be monitored closely as a potential danger signal with regard to the sustainability of the economic expansion.

The members also focused on the question of possible adjustments in policy implementation during the intermeeting period. A majority felt that there should be no presumptions about the likely direction of such adjustments, if any. In their view the risks that economic and financial developments might differ significantly from current expectations were fairly evenly balanced in both directions. A number of other members believed that the Committee should remain especially alert to developments that might call for somewhat easier reserve conditions. In particular, these members felt that incoming information regarding the performance of the economy should be evaluated with particular care for evidence of a possible slowing in the expansion. The members recognized that the performance of the dollar in foreign exchange markets might have a key bearing on policy implementation in this period. No member wanted to tie monetary policy exclusively to the dollar, but some strongly emphasized that further substantial depreciation in the dollar could have highly adverse repercussions on domestic financial markets and the economy.

During this meeting the members reviewed the Committee's operating procedures. These had been directed toward greater emphasis on stabilizing money market conditions since the stock market collapse in October and had given relatively less attention to the implementation of a specified degree of pressure on reserve positions. The members generally agreed that the Committee should return to its earlier operating procedures. The latter were seen to possess a number of advantages, including greater scope for market forces to be reflected in money market conditions. Given the still sensitive conditions in financial markets, however, the members expressed a range of views with regard to the appropriate timing of a return to the Committee's former operating procedures. Some endorsed the prompt implementation of those procedures. However, a majority felt that a gradual shift toward greater emphasis on reserve objectives should be implemented during the intermeeting period. Such an approach would continue to give some attention to moderating fluctuations in money market conditions but would tolerate somewhat greater fluctuations than had occurred in recent weeks. A few members disagreed and indicated a preference for retaining the recent operating procedures at least for now. These members emphasized that a normal or predictable relationship between the provision of reserves and money market conditions had not been reestablished and was not likely to reemerge in the near term, at least in the period through the year-end when interest rates and reserves were expected to be subject to considerable variations associated with the bank statement date. The procedures could be reviewed in early January and a decision delayed until then.

At the conclusion of the Committee's discussion, all but two of the members indicated their support of a directive that called for maintaining the existing degree of pressure on reserve positions and that would phase open market operations into a more normal approach to policy implementation keyed increasingly to a desired degree of reserve pressure while giving less emphasis than recently to money market conditions. The members recognized that the conduct of open market operations might continue to require a special degree of flexibility, given still quite sensitive conditions in financial markets and the uncertainties in the business outlook. Taking account of conditions in financial markets, the members indicated that somewhat less or somewhat more reserve restraint would be acceptable, depending on the strength of the business expansion, indications of inflation, the performance of the dollar in foreign exchange markets, with consideration also taken of the behavior of the monetary aggregates. If current reserve conditions were maintained, the members expected growth in M2 and M3 to pick up from the pace in recent months to annual rates of about 5 percent and 6 percent respectively over the four-month period from November to March. Growth of M1 was expected to remain relatively limited over the same period; because of the substantial uncertainty that continued to surround the outlook for M1, the Committee continued its practice of not specifying a numerical expectation for its growth. The members agreed that the intermeeting range for the federal funds rate, which provides a mechanism for initiating consultation of the Committee when its boundaries are persistently exceeded, should be left unchanged at 4 to 8 percent.

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

> 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.

Votes for this action: Messrs. Greenspan Corrigan, Angell, Boehne, Boykin, Heller, Keehn, Kelley, and Stern. Votes against this action: Mr. Johnson and Ms. Seger.

Mr. Johnson dissented because he believed that policy implementation should continue to focus on maintaining generally stable conditions in the money market, at least through the year-end, pending the emergence of more settled conditions in financial markets and a more predictable relationship between reserve objectives and money market conditions. He also preferred a directive that gave greater weight to the possibility for some easing, given potential developments during the intermeeting period.

Ms. Seger dissented because she favored some slight easing of reserve conditions in light of her concern about the downside risks in the economy, especially in the context of sluggish growth in reserves and the monetary aggregates over an extended period. She also wanted to continue to focus on money market conditions in System open market operations and in particular to counter upward pressures on short-term interest rates.

2. Authorization for Domestic Open Market Operations.

Effective December 17, 1987, the Committee approved a temporary increase of $3 billion, to $9 billion, in the limit between Committee meetings on changes in System Account holdings of U.S. government and federal agency securities specified in paragraph 1(a) of the Authorization for Domestic Operations. The increase was effective for the intermeeting period ending with the close of business on February 10, 1988.

> Votes for this action: Messrs. Greenspan, Corrigan, Angell, Boehne, Boykin, Heller, Johnson, Keehn, Kelley, Ms. Seger, and Mr. Stern. Votes against this action: None.

This action was taken on the recommendation of the Manager for Domestic Operations. The Manager advised that the normal leeway of $6 billion for changes in System Account holdings of securities probably would not be sufficient to accommodate desirable reductions in the intermeeting period because of seasonal declines in currency in circulation and required reserves.

On January 5, 1988, the Committee held a meeting by telephone conference to review monetary and financial developments since mid-December and to assess the Committee's decisions at the December meeting to begin to redirect its operating procedures towards more emphasis on achieving a desirable degree of pressure on reserve positions. In the period after the stock market collapse in October, open market operations had been guided to an important extent by the objective of restoring and sustaining stability in the money market, and less attention was given than previously to the implementation of objectives relating to reserve conditions.

In the Committee's discussion most of the members agreed that with the further passage of time since the October disturbances in financial markets and with year-end pressures in the money market now unwinding, further progress could be made toward restoring the Committee's earlier approach to open market operations. The members recognized that conditions in financial markets were still somewhat unsettled and that the relationship between reserves and money market conditions had not been reestablished on a fully normal or predictable basis. In the circumstances and in light of the uncertainties in the economic outlook, it was agreed that some amount of flexibility might continue to be needed in the conduct of open market operations.

To reflect and endorse the further progress toward the operating procedures in use before mid-October, the Committee decided to amend the relevant reference in the operational paragraph of its directive issued at its December meeting. The amendment encompassed solely a change in emphasis relating to operating procedures and did not include any change in the Committee's short-run policy objectives.

At the conclusion of this telephone meeting, the Committee voted to change the operational paragraph of its directive to read as follows:

> In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. The Committee agrees that the passing of time and the year-end should permit further progress toward restoring a normal approach to open market operations, although still sensitive conditions in financial markets and uncertainties in the economic outlook may continue to call for some flexibility in 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.

> Votes for this action: Messrs. Greenspan, Corrigan, Angell, Boehne, Boykin, Heller, Johnson, Keehn, Kelley, and Stern. Vote against this action: Ms. Seger.

Ms. Seger dissented because she continued to believe that open market operations should be directed toward some slight easing. She also felt that financial markets remained too unsettled to warrant any shift at this time in operational procedures toward more emphasis on reserve objectives.