

Meeting of Federal Open Market Committee

July 15, 1982

A meeting of the Federal Open Market Committee was held on Thursday, July 15, 1982. This was a telephone conference meeting, and each individual was in Washington, D. C., except as otherwise indicated in parentheses in the following list of those participating.

PRESENT: Mr. Volcker, Chairman
Mr. Solomon, Vice Chairman (New York)
Mr. Balles (San Francisco)
Mr. Black (Richmond)
Mr. Ford (Atlanta)
Mrs. Horn (Cleveland)
Mr. Martin
Mr. Partee
Mrs. Teeters

Messrs. Guffey (Kansas City), Keehn (Chicago), Roos (St. Louis), and Timlen (New York), Alternate Members of the Federal Open Market Committee

Messrs. Boehne (Philadelphia), Boykin (Dallas), and Corrigan (Minneapolis), Presidents of the Federal Reserve Banks of Philadelphia, Dallas, and Minneapolis, respectively

Mr. Axilrod, Staff Director
Mr. Altmann, Secretary
Mr. Bernard, Assistant Secretary
Mrs. Steele, Deputy Assistant Secretary
Mr. Bradfield, General Counsel
Mr. Oltman (New York), Deputy General Counsel
Mr. Kichline, Economist

Messrs. J. Davis (Cleveland), Keran (San Francisco), Koch (Atlanta), Prell, Siegman, and Zeisel, Associate Economists

Mr. Cross (New York), Manager for Foreign Operations, System Open Market Account

Mr. Sternlight (New York), Manager for Domestic Operations, System Open Market Account

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Mr. Coyne, Assistant to the Board of Governors

Mr. McIntosh (Boston), First Vice President, Federal Reserve Bank of Boston

Messrs. T. Davis (Kansas City), Eisenmenger (Boston), and Stern (Minneapolis), Senior Vice Presidents, Federal Reserve Banks of Kansas City, Boston, and Minneapolis, respectively

Messrs. Broaddus (Richmond), Burger (St. Louis), Nichols (Chicago), and Soss, Vice Presidents, Federal Reserve Banks of Richmond, St. Louis, Chicago, and New York, respectively

Mr. Lang (Philadelphia), Research Officer, Federal Reserve Bank of Philadelphia

Mr. Pearce (Dallas), Assistant Vice President, Federal Reserve Bank of Dallas

Transcript of Federal Open Market Committee Conference Call
of July 15, 1982

MR. ALTMANN. Murray Altmann here in the Board room. As usual, I will call the roll by District. Gentlemen, we are broadcasting. If there's any change from the attendance that you have wired to me, please so indicate as I go down the list. [Secretary's note: Attendance roll was called]. Thank you very much. We expect to have in the Board room the Chairman, Governors Martin, Partee, and Teeters, and some staff. If you'll stand by, I expect the Chairman to be here any minute.

SPEAKER(?). Murray, do you have a number for us to call if we are disconnected?

MR. ALTMANN. Yes. Should you be disconnected, call 202-452-3042 and we'll try to get you back on as quickly as possible. Thank you. Let me ask one question: Is there anybody who did not receive the wire that I sent not very long ago? Good, I'm glad not to hear any response.

MR. PARTEE. Paul is now here.

CHAIRMAN VOLCKER. Are you ready? Well, ladies and gentlemen, greetings. I sent out this wire. I'm sorry I am so late but I thought it might be helpful just to get some words in front of us so we know what we're voting on, assuming we want to go in this direction. [Secretary's note: A copy of the draft language sent to Committee participants is included in the Appendix.] Before getting there we might just have a little updating on where we stand in the more immediate sense. We have been putting a little money in the market, as you know, and putting borrowings down. That would have been implied by the money supply developments, in any event, and we were more alert to do so than we might otherwise have been--to keep a little ahead of the market in putting some money in. I don't think the market reacted all that well. For a while rates went down and then there wasn't much carry-through and some reversal. I don't know quite where we are at the moment. We ended up with borrowings at around \$500 million last week, if I recall correctly. They were a little lower than I might have aimed at on path grounds alone but, since we're in the process of increasing the nonborrowed reserves path in any event in response to the money supply figures, they probably will be still lower this week.

The latest money supply figure is not nearly as favorable, unfortunately, as the preliminary indication. It appears to be [an increase of] between \$5-1/2 and \$6 billion--that's just among us--which is certainly in the range of market expectations, and it's not a bad number put together with those of the past couple of weeks. It shows, I think, essentially no July bulge. What it shows is an erratic downward movement last week replaced by an erratic upward movement this week, both in demand deposits rather than in NOW accounts where the bulge was supposed to come. So, in itself it doesn't look like a confirmation of a bulge. It's not really. I suspect the money supply in the first week in July will be slightly below the June average level. As you recall we were anticipating a bulge in July. I guess it's too soon to say that that possibility is eliminated entirely. But the kind of pattern we foresaw would have

allowed for a pretty big increase in July and then much smaller increases in August and September. July would have to be bigger than projected at the moment to get up to the path evenly distributed over the 3 months. And that is a basis for increasing nonborrowed reserves even apart from disturbances we have had elsewhere in the market.

I don't know what I can say about the Penn Square fallout. Having heard of the name of this bank only a couple of weeks ago, I have tried to forget it. But I think the obvious thing to say is that we haven't heard the last of it. We have had some repercussions in scattered banks, particularly in the Southwest, of a more or less direct nature in uninsured deposit withdrawals. We have some local banks that were affected by the participations themselves. But the bigger questions, of course, are how the large participants will fare and how it will affect the whole tone of the market--the nervousness in the market about financial institutions in general. We have not had a rapidly unravelling situation but it is far from a normal situation and there is a lot of tentativeness in the market, particularly with respect to the obligations of the institutions directly affected. And enormous numbers of rumors are being generated, which get reported to me regularly, about other financial or nonfinancial institutions. I think there is an undertone of nervousness in the market. That is a very general summary. I don't know whether Mr. Axilrod wants to say anything more precisely and then we'll turn to Mr. Sternlight.

MR. AXILROD. No, Mr. Chairman. You covered the aggregates: In the first two weeks of July, [ending] the 7th and the 14th, the level is just about equal to the June level; M1 is running well below the path level for July which was up around \$454 billion. So, it's running around \$3 billion below that path level.

VICE CHAIRMAN SOLOMON. What do you mean, Steve?

MR. AXILROD. Well, the Committee adopted a path for that aggregate for June through September of around 5 percent. We allowed for a bit of a bulge in July--not much, around 7 percent--and the average level in July, to hit that, would be close to \$454 billion. It's running around \$451 billion. That's all I really meant.

VICE CHAIRMAN SOLOMON. The \$451 billion includes the \$5.8 billion [increase] we will be publishing?

MR. AXILROD. Yes. For another reference point, the top of the range for July would have been \$452.7 billion, so we're running well below that also.

CHAIRMAN VOLCKER. Slightly below. Mr. Sternlight.

MR. STERNLIGHT. I'll only add, Mr. Chairman, that the fed funds rate has come down some in the past week, averaging about 13-1/8 percent rather than the 14 percent plus levels of the previous week. And it's also in that 13 to 13-1/8 percent area today.

CHAIRMAN VOLCKER. Are there any questions or comments on recent developments? I assume all this discounting of the receiver certificates is going on smoothly or otherwise--

VICE CHAIRMAN SOLOMON. Which Districts have received them? We haven't had any in New York.

MR. BRADFIELD. Mr. Chairman, there has only been one issued and that was to the Wright Patman Credit Union. There haven't been any issued in addition to that.

CHAIRMAN VOLCKER. There have been a number of inquiries, haven't there?

MR. AXILROD et. al. Yes.

MR. GUFFEY. In Kansas City we've had a number of inquiries. But in talking with the FDIC people, apparently they haven't been very diligent in getting these certificates out.

CHAIRMAN VOLCKER. Issued?

MR. GUFFEY. It's not in the hands of the holder.

CHAIRMAN VOLCKER. Well, let's turn to completing the meeting that we had earlier and the portion on the longer-term ranges. The language I sent you attempted to encapsulate my interpretation of what we said. What I have in mind in adopting the decision is that instead of just flatly having ranges in the directive--it appears essentially as boilerplate in the directive--we would repeat the ranges as usual but add this bit of gloss to it. Of course, something similar would also appear in the report we make to the Congress and in my testimony. But I think it's just as well to put this--whatever we agree on--in the record so that there is some reflection of the interpretation in the directive boilerplate as well as just the bare numbers.

MR. ROOS. When will the testimony be?

CHAIRMAN VOLCKER. Tuesday.

VICE CHAIRMAN SOLOMON. Paul, in regard to the last sentence: "The Committee also indicated that it was tentatively planning to adopt the same ranges for 1983," it seems to me that there might be some slight advantage in saying instead "The Committee also indicated in view of present uncertainties that it was tentatively planning to continue the same ranges."

MS. TEETERS. We're always uncertain at this time of the year.

MR. MARTIN. I think that argues against our maintaining a position that we need flexibility.

MR. PARTEE. Tony, I prefer the second phrase of that sentence, which you didn't read, as the reason for our being tentative. That's a pretty good phrase--that we'll be watching carefully and we certainly will feel free to reserve on those ranges after we have looked at the second half of the year.

CHAIRMAN VOLCKER. Do you see any significance in saying continue the same ranges and saying--

VICE CHAIRMAN SOLOMON. Yes, I do. I had the feeling that "adopt" sounds like a firmer judgment as to the target ranges we want in '83 whereas "continued" sounds like a holding action. I think it was the sense of the FOMC at its meeting that if we were going to do a revision, we would skew it downwards. It would be easier to do that then whereas it would be hard to do an upward revision, and that is why we were continuing the same ranges tentatively. I don't know why but I have the feeling that "continued" sounds better than "adopt."

CHAIRMAN VOLCKER. I haven't any strong feeling about it. I think we ought to have separate votes when we get around to the vote-- I guess that has been the tradition--for the remainder of this year and for next year. Since you raised the issue, let's discuss next year and get that settled for a tentative decision anyway. The point here, and there was of course a lot of support for it before, was that we would retain the same range in the knowledge--and this would be in the report too--that continuing the same range gives us ample scope for an actual reduction, if that seems appropriate. And that would be mentioned. I don't think it has to be mentioned here but it is mentioned in the Humphrey-Hawkins report, and my testimony says there is nothing inconsistent about this and having lower actual growth next year, if that's what we want to do. But it is worded to make it a little more tentative than usual. That was the effort, and if "continue" helps, that doesn't bother me. Any other comment on 1983?

MR. BLACK. Mr. Chairman, Bob Black. I'd rather knock off a half point at the top. I just think [retaining the 1982 ranges for 1983] might raise unnecessary doubts about the degree of seriousness we attach to the targets. At the same time, we could also pull up the bottom. I don't think anybody would want anything as low as 2-1/2 percent. I realize this would narrow the range from what most people prefer, but I believe 3 to 5 percent would have a more salutary market impact than what you have stated.

MS. HORN. Mr. Chairman, this is Karen Horn. Just to follow along on Bob's comments, I have some concern about changing the policy that we've had for some time now of [reducing the M1 range by] 1/2 percentage point each year, or even indicating with this tentativeness our thoughts about changing that policy for fear that it might be a signal to the markets that in fact this Committee was contemplating a significant change in policy. And at this time I think either very soft language with regard to not changing the target ranges or actually saying something about lowering the targets by 1/2 point might instill more confidence in the market.

CHAIRMAN VOLCKER. Well, I have a little problem, which I mentioned in my own testimony, in that someday this velocity may not increase so rapidly. If we had, let's say, 5 percent [M1 growth] next year--which may turn out to be right and it may turn out to be lower than that--that assumes, in order to get any kind of economic recovery next year, that we have to have a higher-than-trend velocity figure. It would have to be well up into the ranges of what we get with a good recovery and rising interest rates. I gulp a little at this stage in saying that that is necessarily consistent with even the projections that we have, in the light of all the uncertainties that exist about this. We sit here and imply--if we want growth above 5 percent, which I guess is what you're saying--that we have to have about a 4 or 5 percent increase in velocity through the year to get real growth in

the economy of 3-1/2 to 4-1/2 percent. That's assuming that velocity is absolutely normal. And I don't know that we can make that assumption.

MR. FORD. Paul, this is Bill Ford in Atlanta. I want to express myself on the side of the last two speakers but add to what you're saying. I'd be inclined to go ahead with our program that we established a couple years ago of continuing to try to notch the target down a half point a year but perhaps add on the caveat you just expressed that we are anticipating a normal cyclical positive factor to [unintelligible] for adequate growth in the economy, and should it develop--

CHAIRMAN VOLCKER. I think we have to say that anyway. A 1/2 percentage point [reduction] isn't enough to make a difference there. It just aggravates the problem.

MR. FORD. In any case I would prefer to stay with the program at this point, with a caveat that allows some leeway on--

CHAIRMAN VOLCKER. The program is not to reduce the money supply forever; it's to get rid of inflation and have a little growth.

MR. FORD. I don't really believe that a 5 percent increase is as low as we ultimately want it to be. I don't know if you regard that as the lowest we ever want growth in the money supply to be in the future.

CHAIRMAN VOLCKER. I don't know. If velocity ended up at zero, I wouldn't want to end up much lower than that.

MR. FORD. Yes, that's right. But normally we don't see velocity at zero when we are where we should be in terms of the stage of the cycle.

MR. PARTEE. We certainly did in the first half, Bill. In fact it was negative. I'm led now, on the basis of the comments of the last several speakers, to support Tony in changing that word to "continue" rather than "adopt." I have two reasons for it. One is that, substantively, I'd be opposed to narrowing the range. Remember that the midpoint of the present range is 4-1/4 percent. There is lots of room for reduction if we want to specify that we're going to be more toward the middle or that we [look at the full] range rather than that we are shooting for the upper part of it as we have this year. But more importantly, in order to maintain our options, I think it would be significant to say that we'll continue with the current ranges until we see some reason for varying them on the basis of the second-half experience. If, as Karen suggests, we reduce the top by a half point and, as Bob suggests, we increase the bottom by a half point, we will be giving a sense of specificity to the plan that then becomes extremely difficult to get out of. I'm very much opposed to that kind of doodling with the numbers at this point.

MR. FORD. The way I see it, Chuck, what you're proposing, as it is in the telegram, is doodling with the numbers because the market is anticipating that we're going to continue to bring the planned rate of expansion in the aggregates downward for some time yet. I don't think anybody I've talked to in the market thinks that even 5 percent

is the ultimately appropriate rate of growth in the aggregates. So the doodling in my view is the one that does not reduce the rate 1/2 percentage point. That's the change in policy.

MR. PARTEE. But the point is, Bill, that we have plenty of room to make the policy more restrictive within the present ranges. And by saying we're going to continue the present ranges, we retain the option to review the information from the second half. I certainly agree with Paul that if we're not going to have any increase in velocity, I'm going to support a sizable increase in the money supply next year. And I don't know whether that will be the case or not.

MR. BLACK. Chuck, this is Bob Black. [Unintelligible] on your position that we have room to do what we want in the existing ranges. The thing that bothers me is what the market will think if we haven't made at least some little move in the direction we've all stated we wanted to move.

MS. TEETERS. Mr. Chairman, I'm worried about a different proposition here, and that is: If we signal that we're going to lower the money supply next year--and we have never changed our [July] projections made 18 months ahead of time--it seems to me that the market would take that as signalling that we want interest rates to go up and that there is an even greater probability of interest rates going up as the recovery proceeds.

MR. BOEHNE. This is Ed Boehne. If I had my druthers, I wouldn't even set a 1983 target at this point. There is an unusual amount of uncertainty, but we do have--

CHAIRMAN VOLCKER. We tried that once but it didn't work.

MR. BOEHNE. --but we do have to set it. I think we'd want to have some language and a position here that gives us as much flexibility as possible. And saying that we're going to stick with the current ranges until circumstances dictate otherwise should convey that notion. If we begin taking a half point off from whatever, that conveys a degree of precision that we don't have--and I don't think anybody else has--with respect to the economy in 1983.

CHAIRMAN VOLCKER. Well, I happen to agree with that rather strongly. The weight of the opinion last time was to [adopt the same ranges for 1983]. We've heard from a couple of objectors. Do I assume that the others who were in favor of doing this remain in favor of it?

MR. MARTIN. I would certainly come in, along with Tony and others, on the side of talking about a continuance of the ranges. Several of us have referred to the market. If we wish to be a little more literal and a bit short termed and realistic, the market people are now talking about illiquidity; they're talking about what bank is going to fail next; they're talking about surprises from the corporate sector. The market has an unusual degree of uncertainty and indeed fear right now. For us to drop the top of the range would indicate, I believe, to many of these individuals and firms and banks and overseas holders of dollars that we are not taking seriously the downside risk

inherent in an unstable, illiquid market and set of corporations. I think that would be the wrong signal to send to them now.

MR. BALLEES. Paul, this is John Ballees. In thinking of the proposal Tony made, I'd like to piggyback on it and perhaps offer some language in the sentence that we're talking about simply by referring to the phrase you used: "In view of present uncertainties the Committee also indicated it was tentatively planning to retain the same ranges for 1983," etc.

MR. ROOS. This is Larry Roos. I would be most agreeable with the wording of the wire that was sent out to us. I don't think anyone, including the markets, thinks that a half point one way or the other is an achievable objective. I think there is a downside risk. I certainly feel that we should continue to attempt to control the money supply to bring down inflation. But if money really came in on the low side of either of these suggested targets, I think that might do in aggregate targeting forever and ever and we'd have another softening in the economy. So, I would opt for the wording that was in the wire and whether we use "continue" or "adopt" I don't think makes too much difference.

MR. BLACK. Let me emphasize that I'm not talking about the lower end, Larry, in case I misled you on that. I'm talking about the high side.

MR. ROOS. Well, Bob, the way we set these ranges in light of the strength in recent years is not as important as where we end up within a range that's either a half point higher or lower on either [end] or [whether we] indicate that we will shoot for the upper part of it, which I think would be satisfactory. I have no trouble with the wire as is.

CHAIRMAN VOLCKER. Are there any other comments? I conclude in the absence of any other comments that the majority wants something about the way it is, with some little fiddling with the language, and we'll test that later. But let us look at it in light of the near term. The first question is whether we keep the targets the same [for this year]. Any comment on just that point? This is not language, now; this is simply saying we're going to keep the same targets that we set in February. To some people it may depend on what the subsequent language says.

MS. TEETERS. You're talking about '82?

CHAIRMAN VOLCKER. I'm talking about '82 now.

VICE CHAIRMAN SOLOMON. I have mixed feelings on that section that says we would tolerate some kind of--

CHAIRMAN VOLCKER. I'm only talking about the numbers at this point.

MR. PARTEE. I think that we have to leave them where they are, although I certainly believe that we ought to err on the high side in our actual performance because it would be too much of a shock to the market--not the city of Washington but the market--to change

them. So I would support, as we discussed at the meeting, leaving them where they are and erring on the high side.

MR. BLACK. I agree with Chuck.

MR. BALLEES. I agree with Chuck as well.

MR. KEEHN. I agree with that also.

CHAIRMAN VOLCKER. Any objections? Well, we'll turn to the supplementary language now, but I'm presuming that we will keep the same ranges.

MR. BALLEES. John Balles, Paul. There's just one little fine point here that you might want to consider. I like the way the language is now and it would be acceptable to me as it is, only fine-tuning it a bit. In the second half of the sentence that reads "and would tolerate for some period of time growth above the target range should unusual precautionary demands for money and liquidity arise," would you want to consider saying "continue to arise"?

CHAIRMAN VOLCKER. My only problem with that is that right now we're within the targets. I certainly will argue in my testimony that we had unusual demands earlier in the year, that we may still have them, and that we have to be wary about them. But--I'm being very technical in some sense--we presumably allowed for that in our operations and right now we're within the target. Just as you were talking I thought of a more neutral word instead of "arise." First of all, let me say that in the absence of hearing anything else on the numbers, we are now passing to the gloss. If we say "should unusual precautionary demands in money and liquidity be evident," that's rather neutral as to whether they are now or have been or will be. It's not so future looking.

MR. BALLEES. That would be better in my view because the word "arise" implies that there are not yet any.

CHAIRMAN VOLCKER. Yes, I understand your point. And the only reason I am a little hesitant about it is that if we have those unusual demands now, why aren't we above the target?

VICE CHAIRMAN SOLOMON. Paul, with regard to that second half of the sentence "and would tolerate for some period of time," etc. first of all, not only is your suggestion of "be evident" instead of "arise" a good one, but also I'm a little concerned about not having an adjective in front of the word "growth." It seems to me that an adjective--something like "modest"--before the word "growth" is necessary. I wouldn't go as far as Nancy went in the last FOMC meeting as to indicate how much growth above we would accept, but I think there ought to be an implication that we're not talking about unlimited growth. I'm a little concerned about the way some people might read that.

CHAIRMAN VOLCKER. Well, we're in a dilemma here. I don't disagree with what you're saying in some sense. We can put in the word "somewhat" or "some modest" growth. On the other hand, [I'm] trying to get away from this feeling in the market that every time we're \$1 billion above target--or even \$5 billion above if it came out

that way at some point--that it's something terrible and we're immediately going to react to get it down. So, if we put in the words "modest growth" or "somewhat above" or something--

MR. CORRIGAN. I have a little of the same uneasiness. I don't want to muddy us up with another suggestion but one thing that might take care of both of these concerns would be after the comma to say "and would continue to evaluate developments in the light of any evidence of unusual precautionary demands." Maybe I'm splitting hairs, but to me that would suggest a posture not unlike what in fact we did during the first half of the year and it might also get at Tony's point a little in suggesting that we're not talking about letting this go crazy on us.

VICE CHAIRMAN SOLOMON. I think it's a little too cryptic, Jerry. I don't know that that would be more clear both to the Congress and the market than saying something like "would tolerate for some period of time." That's just my initial instinct on that.

MR. PARTEE. Well, it also calls into question the notification process to Congress if we have evaluated and decided. That is, if a reevaluation indicates that the range should be different, we're supposed to tell the Congress that. The way it's written here we are giving ourselves a little cap over the range that is specified. I would associate myself with those who want to say "somewhat above." I think "modest" has the wrong ring to it because it's not modest if it's above and it might need to be, before a little time, a considerable figure. I also would like to suggest just a little notching up in the nomenclature here. Rather than saying that growth toward the top end of the range would be "acceptable," I would like to say that it would be "appropriate, given the low base" and then I would say with regard to the second phrase that growth somewhat above the upper end of the range would be "acceptable" not "tolerable," if this unusual liquidity demand persists.

MR. FORD. I think those are good suggestions.

CHAIRMAN VOLCKER. I don't know; that goes a little far. It sounds a little more aggressive.

MR. PARTEE. My problem, Paul, is that I think this is too grudging.

CHAIRMAN VOLCKER. Well, this is a fine distinction we are dealing with here at any case. I think the market will read "acceptable" as saying growth is going to be up there. But I don't know what is going to happen.

MR. PARTEE. Acceptable if this condition persists.

CHAIRMAN VOLCKER. The "acceptable" doesn't bother me so much in the second part; it's the "appropriate" pinning us right to the top end of the range in the first part of the sentence. We don't know what is going to happen.

MR. FORD. Paul, this is Bill Ford. I think the last language that Chuck Partee said just might do it [unintelligible].

There's a real chance of it being interpreted as dealing with the [unintelligible] demand.

MR. BLACK. Mr. Chairman, Bob Black. Let me try something; I don't whether it will appeal to anybody or not. After the comma say "and indicated that it would tolerate growth somewhat above the target ranges temporarily, should extraordinary liquidity pressures arise."

MR. FORD. I'd feel a lot more comfortable with something like Bob said.

CHAIRMAN VOLCKER. I'm not sure my ear heard any substantive difference in that.

MS. TEETERS. The "unusual precautionary demands for money" is what was taken out.

MR. BLACK. What bothers me, Mr. Chairman, is the precautionary part. One can certainly make a good case for it, but I don't think we can prove that. I think we have clear liquidity pressures; we all know that. I guess I'm worried about our rationalizing too much of an overshoot by saying that demand for money has shifted when we really don't have any empirical evidence that it has.

MR. FORD. One more thing on that, Paul. I'd like to hear what Pres Martin says about that because his comments earlier about what the market thinks were interesting to me, and I've been very worried, as everybody is, about the possibility of another Penn Square or some other institutions that we don't know about or even some institutions that we do know about. That's where I see the distinction in what Mr. Black is saying: that the market emphasizes [unintelligible] and that if there are real liquidity problems evident, then none of us is going to be in favor of clamping down on the market and threatening or precipitating a financial crisis.

CHAIRMAN VOLCKER. I must interject. I see no substantive difference. If there's an unusual demand for liquidity whether we call it precautionary or liquidity, I don't know what the distinction is. If you're making a distinction, I think you have to raise the targets. If the economy needs more liquidity, it needs more liquidity and we should raise the targets.

MR. FORD. We're talking about the liquidity problems in--

CHAIRMAN VOLCKER. The term "liquidity problems" to me means that people will temporarily want to run into money, which is what precautionary balances mean.

VICE CHAIRMAN SOLOMON. I must say, even though there isn't a large difference, that I think Bob Black's language implies a much greater willingness by the Fed to "cave in," so to speak, if there is a liquidity problem in the economy, whereas what we are saying is that if the velocity of circulation is less than what it normally would be because of precautionary demands as well as demands for money and liquidity, we will factor that in. So, I think that we stay more consistently and soundly based on technical grounds if we stay with the same language; Bob Black's language implies a much greater

willingness to ease monetary policy if the real economy continues to be in difficulty. Some people might expect almost an immediate easing, given the present liquidity situation.

CHAIRMAN VOLCKER. I guess that's my sense of it, too. The economy clearly has liquidity problems and if we're worried about those liquidity problems just in the general sense we ought to be raising the targets.

MR. BLACK. Mr. Chairman, I'd put in the adjective "extraordinary" liquidity problems. I think that really restates our willingness, as always, to serve as lender of last resort either through the discount window or by supplying reserves. I think about financial institutions and businesses in real trouble beyond what we've yet seen, whereas the idea of precautionary balances--

CHAIRMAN VOLCKER. We have got trouble beyond what we've yet seen; I tell you, we have trouble.

MR. BLACK. If it gets that bad, I'd have no problems with doing this; but if we just think we have a shift in the demand curve and we really don't have any statistics to [support] that--. I'd be reluctant to leave that precautionary demand wording in there because what we have had was not enough to make me want to overshoot the targets up to now. But I can easily see, as you seem to be concerned about it, that we could have problems where I'd want to overshoot.

MR. PARTEE. Well, I don't know. You seem to be mixing the discount window with aggregate monetary policy, Bob, in a way that is tricky. I would assume that if we made [available] extraordinary use of the window in the period to come, we would at that level of analysis also attempt to offset that in the open market. Are you suggesting that we wouldn't offset it in the open market?

MR. BLACK. I was saying that there are some institutions that might have liquidity problems which we couldn't reach through the discount window because they don't have eligibility to borrow and that we might have to put [more liquidity in the market] for somebody else to supply their liquidity to them.

MR. PARTEE. And there is, of course, the effect on the public or the general populace of the perception of these problems. The public may run to more liquidity and it's not an institution. It may be the public, which in response to its perception of problems in the institutions, goes into cash or goes out of market securities into M2 forms and that kind of thing. And we have to allow for that, it seems to me. As far as the first half of this year is concerned, I've no doubt, given the level of economic activity, that there was a change in the demand for money. There was an increase in precautionary demands. Virtually all of the increase in M1 was in NOW accounts. That, I think, is very, very strong evidence.

MR. BLACK. I think that's thoughtful, Chuck, but most [unintelligible] advantages there are. Last year we were saying that financial innovations justified a low rate of growth in M1 and I wasn't convinced of that. And when I see the same people on the other side of the issue, I'm not convinced this year of that.

SPEAKER(?). What's the precautionary lag?

MR. BLACK. [Unintelligible], I think. We probably had done it last year and it was too low. That's, of course, something that I can't prove; but no one has disproved it either.

CHAIRMAN VOLCKER. We have had a massively expansionary policy this year!

MR. PARTEE. As reflected in all the credit that's flowing and the sharp drop in interest rates and the ease in markets!

MR. BLACK. If we think the demand curve has shifted and we try to offset it and it hasn't--if it has shifted back--we are going to create a monetary disturbance. If it does shift and we don't detect it, we will create a monetary disturbance.

CHAIRMAN VOLCKER. That's our dilemma.

MR. BLACK. Either way, we're going to mess things up!

MR. MARTIN. Even more than they are today!

MR. PARTEE. Thank you, Mr. Patman!

MR. MARTIN. Mr. St Germain, I believe you meant to say!

CHAIRMAN VOLCKER. Are there any other comments? Does anybody else feel strongly about some part of this? We have to return to Mr. Partee's suggestion, I think, and analyze that. But are there any other comments to be put in the hopper here?

MR. BLACK. One comment, Mr. Chairman, and I'll say nothing else at all. The language that I threw out was intended to suggest that we would abandon our targets only in case of a clear emergency. I guess I didn't do that with my language and I would accept gladly any language that would do that.

CHAIRMAN VOLCKER. Mr. Partee suggested changing it basically by taking out the word "acceptable" and replacing it with "appropriate." I think the market will read this as it is worded as our being quite content with the top of the range, but he converts it technically into aiming at very close to the top of the range.

MR. PARTEE. Let's make it "appropriate to be in the upper half of the range."

CHAIRMAN VOLCKER. That's no change from what we said six months ago. That doesn't say it's wrong, but this is precisely what we are doing. I don't know what precise wording we used, but the indication was that we expected [growth] to be in the upper part of the range.

VICE CHAIRMAN SOLOMON. I'd like to support Chuck's suggestion. I think it's very consistent with our posture. We would be very unhappy--I think substantively unhappy--if growth came in significantly lower than that. It seems to me, in view of the

undershooting last year and in view of the situation in the economy, that coming in close to the top is appropriate.

CHAIRMAN VOLCKER. Well, I don't know. That's probably right or I wouldn't use this language. But if we get a distinct surge in the economy and interest rates are going down and somehow M1 is not at the top of the range, I wouldn't be too unhappy. I don't know that that's going to happen; I don't think it's going to happen. But stranger things have happened.

[Secretary's note: The transcript for this conference call ended at this point. The two decisions on the longer-term ranges reached at this telephone meeting were recorded in the Committee's Record of Policy Actions as shown below:

- (1) The Committee reaffirmed the following ranges for growth of the monetary aggregates over the year from the fourth quarter of 1981 to the fourth quarter of 1982 that it had adopted in early February: for M1, 2-1/2 to 5-1/2 percent; for M2, 6 to 9 percent; and for M3, 6-1/2 to 9-1/2 percent. The associated range for bank credit was 6 to 9 percent. At the same time, the Committee agreed that growth in the monetary and credit aggregates around the top of the indicated ranges would be acceptable in the light of the low base period for the M1 target and other factors, and that it would tolerate for some period of time growth somewhat above the target range should unusual precautionary demands for money and liquidity be evident in the light of current economic uncertainties.

Votes for this action: Messrs. Volcker, Solomon, Black, Ford, Mrs. Horn, Messrs. Martin, and Partee. Vote against this action: Mrs. Teeters. Absent and not voting: Messrs. Gramley, Rice and Wallich.

- (2) The Committee indicated that for 1983 it was tentatively planning to continue the current ranges for 1982, but would review that decision carefully in the light of developments over the remainder of 1982. The vote for this action was unanimous.

It was also noted in the policy record that Messrs. Gramley, Rice, and Wallich, who had been unable to attend this meeting but had been present for the main discussion of the longer-run ranges for monetary growth held at the meeting on June 30-July 1, associated themselves with the Committee with respect to the ranges for both 1982 and 1983.]

END OF MEETING