

REMARKS OF ROBERT P. MAYO
PRESIDENT, FEDERAL RESERVE BANK OF CHICAGO
BEFORE
THE GRADUATE SCHOOL OF BUSINESS'
"ADVANCED TOPICS IN BANKING"
UNIVERSITY OF CHICAGO
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WHEN GALE --- OR PERHAPS I SHOULD SAY PROFESSOR FREEMAN -- INVITED ME TO TALK WITH YOU THIS AFTERNOON HE GAVE ME ALMOST COMPLETE FREEDOM ON THE CHOICE OF TOPIC, SUGGESTING ONLY THAT I TALK ABOUT THE FEDERAL RESERVE. WHILE I APPRECIATE THE LATITUDE, I REALIZE THAT I COULD EASILY STRAY AWAY FROM THE TOPICS AND ISSUES THAT MOST CONCERN YOU. CONSEQUENTLY, I'LL TRY TO KEEP MY OPENING COMMENTS SHORT SO THAT YOU CAN RE-DIRECT ME, IF NECESSARY, THROUGH YOUR QUESTIONS. BESIDES, I WANT TO LEAVE TIME SINCE I KNOW FROM MY PAST EXPERIENCES HERE AT THE UNIVERSITY OF CHICAGO THAT I GAIN A GREAT DEAL FROM THE INTERCHANGE.

ABOUT TEN YEARS AGO, CARTER GOLEMBE WROTE A PIECE ON THE FEDERAL RESERVE SYSTEM IN WHICH HE SAID "THE LIFE OF A RESERVE BANK PRESIDENT MUST SEEM EMPTY. A RESERVE BANK PRESIDENT IS IN CHARGE OF FEEDING, HOUSING, AND KEEPING A LARGE NUMBER OF CLERICAL PERSONNEL WARM, DRY AND HAPPY ENOUGH SO THAT THE WORK GETS OUT AND FLOAT DOES NOT RISE UNDULY HIGH. INTERSPERSED WITH ALL THE LITTLE ROUTINE DECISIONS THAT SOMEONE HAS TO TAKE CARE OF AND WHICH WOULD BE UNSEEMLY FOR A SUBORDINATE TO DECIDE, IS THE GLORIFIED TRIP TO WASHINGTON TO AN OPEN MARKET COMMITTEE MEETING EVERY MONTH. THERE FOR A FEW BRIEF MOMENTS THE RESERVE BANK PRESIDENT REPORTS ON CONDITIONS IN HIS OWN FEDERAL RESERVE DISTRICT, GIVES HIS IMPRESSIONS OF NATIONAL ECONOMIC AND

FINANCIAL CONDITIONS AND SAYS WHAT HE WOULD RECOMMEND FOR FEDERAL RESERVE POLICY IF EVERYONE ELSE AGREES."

CARTER COULDN'T HAVE BEEN MORE WRONG. LIFE ISN'T EMPTY FOR ME AT THE CHICAGO FED NOR IS IT FOR ANY OF MY COLLEAGUES. IT IS, IN FACT, EXTREMELY FULL -- AND NOT WITH LITTLE ROUTINE DECISIONS. MANAGING A GROWING AND CHANGING PAYMENTS MECHANISM, MAINTAINING AN APPROPRIATE SUPERVISORY AND REGULATORY STANCE IN A CHANGED ENVIRONMENT AND FRAMING AN EFFECTIVE MONETARY POLICY FOR TODAY'S AND TOMORROW'S WORLD ARE CHALLENGING EFFORTS.

I WOULD LIKE TO TALK WITH YOU FOR A FEW MOMENTS ABOUT SOME OF THESE CHALLENGES. I REALIZE THAT MANY OF YOU ARE PROBABLY MORE INTERESTED IN MONETARY POLICY AND CERTAINLY I'LL DEVOTE SOME TIME TO THAT. BUT BEFORE DOING SO, I'D LIKE TO SHARE A FEW THOUGHTS WITH YOU ABOUT SOME OF THE OTHER ROLES OF THE FED. IN PARTICULAR, I'D LIKE TO MENTION THE SUBSTANTIVE PUBLIC POLICY ISSUES ASSOCIATED WITH THE FEDERAL RESERVE'S RESPONSIBILITIES IN THE PAYMENTS MECHANISM AND SUPERVISION AND REGULATION AREAS.

IT SEEMS TO ME THAT THE NON-MONETARY POLICY FUNCTIONS OF THE FED ARE TOO FREQUENTLY AND INCORRECTLY CONSIDERED NARROWLY WITHIN A STRICTLY OPERATIONAL CONTENT. FOR EXAMPLE, WITH REGARD TO CHECK CLEARING OR THE PAYMENTS MECHANISM, THE FED IS VIEWED, MUCH AS YOU WOULD A MANUFACTURING OR FINANCIAL FIRM, AS A PRODUCER OF PRODUCTS AND SERVICES. IT IS PRESUMED THAT THE PRODUCTS AND SERVICES AND IMPLICITLY EVEN THE QUANTITIES AND QUALITY CHARACTERISTICS ARE PRESCRIBED. THE ROLE OF THE FED IS SIMPLY TO MEET THESE PERFORMANCE REQUIREMENTS. BUT IN SPITE OF THIS IMPRESSION THE SPECIFIC OBJECTIVES AS WELL AS THE MEANS OF ATTAINING THEM IN MANY OF THE SO-CALLED OPERATING AREAS ARE MUCH MORE VAGUE IN THE FEDERAL RESERVE ACT THAN

THE MONETARY POLICY OR ECONOMIC STABILIZATION OBJECTIVES ARE.

THIS MEANS THAT MANY OF THE MAJOR DECISIONS OF THE FED ARE IN TERMS OF DECIDING WHAT IS DESIRABLE, WHAT ARE THE APPROPRIATE DIRECTIONS IN WHICH TO MOVE IN MEETING THE PUBLIC NEEDS. NOT THAT THE STRICTLY OPERATING DECISIONS TO ACHIEVE EFFICIENT PERFORMANCE MAY NOT BE DIFFICULT. THEY ARE AT TIMES. BUT THE MORE CHALLENGING AND MORE DIFFICULT AREAS ARE IN DETERMINING WHAT THE DIRECTION SHOULD BE.

THE PAYMENTS MECHANISM IS AN EXCELLENT CASE IN POINT. THE FEDERAL RESERVE HAS TRADITIONALLY HAD A ROLE AS A LINK BETWEEN THE SOME 14,000 COMMERCIAL BANKS IN THE COUNTRY FOR CLEARING AND SETTLING MONEY PAYMENTS. IN AN OPERATING SENSE, THE COMMUNICATION, ACCOUNTING AND SORTING ARRANGEMENTS FOR MOVING MONEY AND MONEY AUTHORIZATIONS BETWEEN EACH PAIR OF 14,000 BANKING INSTITUTIONS REQUIRES A FORMIDABLE COMPLEX OF MACHINERY TO SAY THE LEAST. IF IT WERE TO BREAK DOWN OR SHUT DOWN, CHECK BACKLOGS WOULD PILE UP AT THE RATE OF 30 - 40 MILLION ITEMS PER DAY. THE DOLLAR VOLUME OF TRANSFERS GOING THROUGH THE RESERVE ACCOUNTS AT THE FED ARE HUGE -- MORE THAN \$25 TRILLION A YEAR IN WIRE TRANSFERS ALONE AND ANOTHER \$4 TRILLION IN CHECKS.

FOR YEARS, INTEREST IN THIS MASSIVE MECHANISM WAS LARGELY LIMITED TO BANKERS AND THE FEDERAL RESERVE. WE PROCEEDED TO PROMULGATE REGULATIONS AND PROCEDURES DESIGNED TO INSURE ITS EFFICIENCY. IT SEEMED TO BE A SIMPLE CASE OF MEETING PERFORMANCE REQUIREMENTS WHICH EVERYONE KNEW -- MAKE THE CHECK AS CLOSE TO CURRENCY AND COIN AS POSSIBLE IN TERMS OF TIME AND ACCEPTABILITY.

BUT IN THE LAST FEW YEARS IT HAS BECOME OBVIOUS THAT THE STRICTLY OPERATIONAL VIEW OF THE PAYMENTS MECHANISM IS INAPPROPRIATE. BY THE MID 1960'S QUESTIONS WERE BEING RAISED ABOUT THE LONG-TERM VIABILITY OF A

PAYMENTS MECHANISM BASED ON PAPER FLOWS. GOVERNOR GEORGE MITCHELL BECAME AN OUTSPOKEN ADVOCATE OF EVALUATING AND INVESTIGATING ALTERNATIVE ARRANGEMENTS AND FORMS. THE DECISION NEXUS BEGAN TO SHIFT FROM IMPROVED EFFICIENCY OF THE EXISTING MECHANISM TO DIFFERENT MECHANISMS. WITH THAT SHIFT CAME A WHOLE NEW SET OF CONCERNS ABOUT IMPACTS ON THE PUBLIC, BUSINESS FIRMS, BANKS AND OTHER FINANCIAL INSTITUTIONS.

I HARDLY NEED TO TELL YOU HOW RAPIDLY THE PAYMENTS MECHANISM HAS BEEN CHANGING IN TERMS BOTH OF FORM OF PAYMENT AND INSTITUTIONAL PARTICIPATION. COMMERCIAL BANKS AND SOME OF THE NON-BANK FINANCIAL INSTITUTIONS HAVE MOVED AHEAD VIGOROUSLY IN DEVELOPING AND EXPERIMENTING WITH NEW TECHNIQUES. BUT THERE ARE DIFFERENCES NOW FROM EARLIER ATTEMPTS BY BANKS TO IMPROVE THE EFFICIENCY OF OPERATIONS. NOW THE STRUCTURE OF COMPETITION IN THE PAYMENTS AREA IS CHANGING — FORMS OTHER THAN BANKS ARE INVOLVED. AND NOW THERE IS A CLEARER IDENTIFICATION OF THE PUBLIC INTEREST.

AS YOU KNOW, CONGRESS HAS BECOME INVOLVED IN ORDER TO BALANCE THE MANY EQUITIES IN MONEY TRANSFERS FOR THE PUBLIC'S BENEFIT. THE COMMISSION ON ELECTRONIC FUNDS TRANSFER HAS BEEN SET UP AND IS ^{operating} BEGINNING TO OPERATE. ^{Commission would} THE LEGISLATION SHOULD BE HELPFUL IN ESTABLISHING PUBLIC INTEREST PRIORITIES AND IN CLARIFYING THE RESPONSIBILITIES OF VARIOUS PARTICIPANTS IN FUNDS TRANSFER. BUT THE ISSUES ARE DIFFICULT ONES. WHO SHOULD HAVE THE MAJOR RESPONSIBILITY FOR DEVELOPING AND OPERATING THE SYSTEM FOR HANDLING MONEY PAYMENTS? IS IT OR SHOULD IT BE A PRIVATE OR A PUBLIC FUNCTION? IS THE CONTINUATION OF A MIXED PRIVATE AND PUBLIC RESPONSIBILITY IN THE BEST PUBLIC INTEREST? IF THERE IS A CLEAR PUBLIC INTEREST, WHO SHOULD HAVE ACCESS.

THE FEDERAL RESERVE IS AND OBVIOUSLY WILL CONTINUE TO BE INVOLVED IN

THE DELIBERATIONS. BUT THE WORLD DOESN'T STAND STILL AND EVEN BEFORE THE FINAL CONCLUSIONS ARE PRESENTED, DECISIONS MUST BE MADE. AND EVEN THESE INTERIM DECISIONS REQUIRE THE BALANCING OF MANY ELEMENTS.

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TO CITE ONLY ONE, WE HAVE RECENTLY HAD TO STRUGGLE WITH THE ISSUE OF WHO SHOULD HAVE ACCESS TO THE MECHANISM HERE IN ILLINOIS. ON THE SURFACE IT IS PERHAPS A SIMPLE ONE. THE PAYMENTS MECHANISM SERVES A PUBLIC BENEFIT SO IT WOULD SEEM THAT THE S & L'S SHOULD HAVE ACCESS. BUT WHAT ABOUT EQUITY? MEMBER BANKS VIEW THEIR RESERVE ACCOUNTS AS "PAYING" FOR THE SERVICE. SHOULD THE S & L'S BE ABLE TO ENTER WITHOUT COST? THE ISSUE COULD BE EXPANDED. COST THE SERVICES AND PROVIDE TO ALL AT THE SAME PRICE. BUT ARE THE SOCIAL BENEFITS GREATER THAN THE COSTS AND, THEREFORE, SHOULD THE SERVICE BE SUBSIDIZED? AND SO ON, THE RAMIFICATIONS SEEM ALMOST ENDLESS AT TIMES, AFFECTING THE STRUCTURE OF FINANCIAL INSTITUTIONS AND THE PUBLIC INTEREST.

SO IN THIS AREA ALONE, MY DAYS ARE HARDLY EMPTY.

THE SUPERVISORY AND REGULATORY FUNCTION IS ANOTHER AREA THAT IS OBVIOUSLY LOADED WITH DECISIONS AS WELL. THE "HOTTEST" PUBLIC INTEREST ISSUE AROUND IS THE SAFETY AND SOUNDNESS OF BANKS. TO A DEGREE THE ISSUE MIGHT BE VIEWED AS STRICTLY OPERATIONAL -- THAT IS, THE PERFORMANCE OF THE EXAMINERS. BUT THIS AREA, TOO, IS LOADED WITH OTHER CRITICAL AND MAJOR ISSUES AS TO THE APPROPRIATE OBJECTIVES OF THE SUPERVISION PROCESS.

COMING FROM CHICAGO, YOU MIGHT ARGUE THAT BANKS SHOULD BE ALLOWED TO FAIL. I REALIZE THAT THAT IS A SIMPLISTIC STATEMENT OF A MAJOR ISSUE, BUT YOU KNOW WHAT I MEAN. PROBLEM SITUATIONS HAVE FREQUENTLY BEEN RESOLVED IN THE PAST THROUGH MERGER, NEW OWNERSHIP OR AN INFUSION OF

CAPITAL -- FAILURES IN A SENSE -- WITHOUT PUBLIC LOSS OR EVEN WITHOUT A RIPPLE IN THE FINANCIAL COMMUNITY. WHAT PRICE ARE WE WILLING TO PAY FOR THE ZERO LOSS CRITERIA THAT SOME NOW APPEAR TO BE ADVOCATING?

ONE APPROACH BEING TAKEN NOW IS TO MOVE TOWARD FULL DISCLOSURE BY BANKS. I AM NOT OPPOSED TO REASONABLE AND MEANINGFUL DISCLOSURE. PARTICIPANTS IN THE MARKET FOR BANK DEBT AND EQUITIES SHOULD BE ABLE TO DIFFERENTIATE ACCURATELY AMONG INSTITUTIONS AS TO SOUNDNESS, EARNINGS PROSPECTS AND MANAGEMENT CAPABILITY.

WHAT DISTURBS ME IS THAT WE HAVEN'T DEFINED OUR OBJECTIVES VERY CLEARLY -- IS IT A ZERO FAILURE RATE? NOR HAVE WE CLEARLY IDENTIFIED THAT THIS IS THE MOST EFFICIENT MEANS OF REACHING THAT OBJECTIVE.

IMPROPER DISCLOSURE CAN AROUSE NAIVE CONCERN THAT CAN ADVERSELY AFFECT THE BANK AND ULTIMATELY THE METHODS OF FINANCING IN OUR ECONOMY. ON ONE HAND INCREASED INFORMATION FOR THE INVESTOR MAY HELP HIM TO PROTECT HIS INVESTMENT, BUT, ON THE OTHER HAND IT MAY ALSO SET IN TRAIN USELESS AND INAPPROPRIATE SPECULATION ABOUT THAT AND OTHER INSTITUTIONS IN GENERAL. DOES THE PRIVATE BENEFIT OFFSET THE PUBLIC COST?

THE CONCERN WITH BANK SOUNDNESS HAS ALSO LED TO INCREASED INTEREST IN THE ISSUE OF REGULATORY STRUCTURE. WHILE A CASE MIGHT BE MADE FOR AN OVERHAUL OF OUR REGULATORY APPARTUS, I DO NOT FEEL THAT A RELATIONSHIP BETWEEN PRESUMED BANK PROBLEMS AND THE REGULATORY STRUCTURE HAS BEEN ESTABLISHED. THE FRANKLIN AND SAN DIEGO FAILURES DID NOT OCCUR BECAUSE OF OUR REGULATORY STRUCTURE.

OBVIOUSLY, THERE ARE MANY MORE ISSUES IN THIS AREA AS WELL. MY DAY ISN'T EMPTY.

I'D LIKE TO TURN NOW TO MONETARY POLICY. THIS WAS AN AREA IN WHICH I INTENDED TO SAY THE MOST BUT OBVIOUSLY I HAD A FEW THINGS TO SAY FIRST CUTTING INTO THE TIME. BUT LET ME SKETCH OUT A FEW THOUGHTS AND THEN IN THE DISCUSSION WHICH FOLLOWS I'LL TRY TO ROUND THEM OUT.

SINCE I'M HERE AT CHICAGO I FEEL COMFORTABLE IN ASSUMING THAT YOU KNOW THE MAJOR ISSUES IN FORMING AND IMPLEMENTING MONETARY POLICY. RATHER THAN ENUMERATING THEM AND RATHER THAN GOING THROUGH THE DECISION PROCESS -- USING A POSITIVE APPROACH SOME MIGHT SAY -- I'M GOING TO TAKE ON SEVERAL OF THE CRITICISMS OF FED PROCEDURES IN AN OBLIQUE MANNER. I DON'T INTEND THAT THE CRITICISMS BE STRAW MEN BUT AT THE SAME TIME I DON'T WANT TO ARGUE THAT THESE ARE NECESSARILY MILTON'S POSITIONS EITHER. LET'S JUST SAY THESE ARE SOME OF THE MORE COMMON CONCERNS ABOUT HOW WE FORMULATE AND IMPLEMENT MONETARY POLICY.

A GOOD PLACE TO BEGIN IS WITH THE SENATE-HOUSE CONCURRENT RESOLUTION 133. THIS RESOLUTION REQUIRES THE FEDERAL RESERVE TO CONSULT WITH CONGRESS WITH RESPECT TO THE GROWTH OF THE MONETARY AND CREDIT AGGREGATES FOR THE YEAR AHEAD. SOME HAVE TAKEN THIS AS THE MOST CONSTRUCTIVE CHANGE IN THE STRUCTURE OF MONETARY POLICY IN YEARS. WHILE THIS INCREASED OVERSIGHT HAS HAD SOME PLUSSES IN TERMS OF REMOVING SOME OF THE MYSTERY ASSOCIATED WITH WHAT THE OBJECTIVES OF THE FED ARE AND HAS DEMONSTRATED THAT THERE IS NO BASIS FOR VIEWING THE FED'S ACTIONS AS BEING INIMICAL TO THE PUBLIC INTEREST, IT IS NOT THAT IMPORTANT A DEVELOPMENT.

THE CONCURRENT RESOLUTION REQUIRES QUARTERLY REPORTS -- SOMETHING THAT WAS ALREADY BEING DONE ON EVEN A MORE FREQUENT BASIS -- ON LONGER TERM TARGETS -- SOMETHING ALREADY COVERED EXTENSIVELY IN FOMC DELIBERATIONS.

THE RESOLUTION DID NOT REQUIRE OR EVEN SUGGEST ANY CHANGE IN POLICY FORMULATION AND IMPLEMENTATION.

UNFORTUNATELY, SOME HAVE TAKEN THE PUBLICATION OF THE AGGREGATES IN MONEY AND CREDIT AS MEANING THAT THE FED WAS NOW "CONVERTED" TO FULL M_1 WATCHING. THEY IGNORED THE OTHER AGGREGATES AND THE STATEMENTS OF THE CHAIRMAN.

THE USE OF M_1 -- PARTICULARLY CURRENT FIGURES ON M_1 -- AS A MEASURE OF MONETARY POLICY MUST STILL BE USED WITH GREAT CAUTION. NEITHER I NOR MOST OF MY COLLEAGUES WOULD DENY THE NOTION THAT THERE IS A CONNECTION BETWEEN THE BEHAVIOR OF THE MONEY SUPPLY AND THE BEHAVIOR OF ECONOMIC ACTIVITY AND THERE IS A GOOD DEAL OF EVIDENCE TO SUPPORT IT. BUT I DO FEEL THAT THERE IS MORE CONFUSION THAN NECESSARY ABOUT THE EXTENT TO WHICH THIS CONCEPT ENTERS INTO MONETARY POLICY DELIBERATIONS, THE EXTENT TO WHICH THE FED CAN HIT SPECIFIC MONEY SUPPLY TARGETS OVER THE SHORT RUN, AND THE EXTENT TO WHICH THE FED SHOULD FOCUS ON THE MONEY SUPPLY RATHER THAN ON SUSTAINABLE ECONOMIC EXPANSION AS THE GOAL.

WITH RESPECT TO THE USE OF THE MONEY STICK IN POLICY DELIBERATIONS, I CAN ASSURE YOU THAT THE BEHAVIOR OF M_1 (AND OTHER MONETARY AGGREGATES) IS TAKEN INTO ACCOUNT VERY SERIOUSLY IN FED POLICY DELIBERATIONS. WE DO NOT, OF COURSE, ACCEPT THE SIMPLE VIEW THAT MONETARY GROWTH SHOULD OCCUR AT A CONSTANT RATE. THAT CONCEPT IMPLIES THAT MONETARY POLICY SHOULD NOT BE USED AS A COUNTERCYCLICAL ECONOMIC TOOL AT ALL. MANY WHO HAVE BECOME ENAMORED WITH A CONCEPT OF CONSTANT MONEY SUPPLY GROWTH HAVE FORGOTTEN THAT EVEN IF ATTAINABLE, SUCH AN APPROACH WOULD NOT PRODUCE ECONOMIC STABILITY. THUS, THE DISCRETIONARY USE OF MONETARY POLICY AND VARYING RATES OF MONEY GROWTH WEIGH HEAVILY IN THE POLICY-MAKING PROCESS.

THE EXTENT TO WHICH THE FED CAN HIT SPECIFIC MONEY TARGETS HAS ALSO BEEN A CONFUSING PART OF THE PUBLIC DEBATE. SINCE ALL WE HAVE TO DO IS CHANGE THE AMOUNT OF RESERVES, IT MIGHT APPEAR THAT THE FED HAS RATHER SPECIFIC CONTROL OF THE MONEY STOCK.

BUT THERE IS MUCH LESS CERTAINTY OF THE IMPACT OF A CHANGE IN RESERVES ON THE MONEY STOCK THAN MANY SUGGEST. A GIVEN INCREASE IN BANK RESERVES IS NOT NECESSARILY ACCOMPANIED BY AN EXPANSION IN MONEY EQUAL TO THE THEORETICAL POTENTIAL BASED ON THE REQUIRED RATIO OF RESERVES TO DEMAND DEPOSITS. WHAT HAPPENS TO THE QUANTITY OF MONEY WILL VARY, DEPENDING UPON THE REACTIONS OF THE COMMERCIAL BANKS AND THE PUBLIC. A NUMBER OF LEAKAGES MAY OCCUR. WHAT AMOUNT OF RESERVES WILL BE DRAINED INTO THE PUBLIC'S CURRENCY HOLDINGS, WHERE THE MULTIPLIER IS ONE, NOT EIGHT TIMES? TO WHAT EXTENT WILL THE INCREASE IN THE RESERVE BASE REMAIN UNUSED AS EXCESS RESERVES? WHICH BANKS WILL GAIN THE RESERVES? HOW MUCH WILL BE ABSORBED BY TIME DEPOSITS OR OTHER LIABILITIES NOT USUALLY DEFINED AS MONEY BUT AGAINST WHICH BANKS MUST ALSO HOLD RESERVES -- BUT WITH A MULTIPLIER MUCH GREATER THAN EIGHT TIMES? HOW SENSITIVE ARE THE BANKS TO CHANGES IN RESERVE PRESSURES EXERTED BY THE CENTRAL BANK? THE ANSWERS TO THESE QUESTIONS HOLD THE EXPLANATION OF WHY CHANGES IN THE MONEY SUPPLY MAY BE DIFFERENT THAN EXPECTED OR MAY RESPOND TO POLICY ACTION ONLY AFTER CONSIDERABLE TIME HAS ELAPSED.

UNFORTUNATELY, MANY IN THE FINANCIAL MARKETS HAVE BECOME SO ATTUNED TO WATCHING THE MONEY SUPPLY FIGURES THAT EVERY WEEKLY WIGGLE, EVERY CHANGE, IS SEIZED UPON AS A CHANGE IN MONETARY POLICY. BUT YET POLICY MAY NOT HAVE CHANGED ONE IOTA.

THE BIGGEST PROBLEM, IT SEEMS TO ME, IS THAT TOO MANY OBSERVERS HAVE FOCUSED ON CHANGES IN THE MONEY STOCK AS THOUGH IT WERE THE GOAL ITSELF. YET THE ULTIMATE GOALS OF MONETARY POLICY INVOLVE THE BEHAVIOR OF EMPLOYMENT, PRICES, ECONOMIC GROWTH, AND INTERNATIONAL TRADE AND PAYMENTS. SINCE MONETARY POLICY DOES NOT AFFECT THESE GOALS DIRECTLY WITH SUFFICIENT SPEED TO HELP THE FED MAKE POLICY DECISIONS, THE FED HAS TO RELY ON SOME INTERMEDIATE OBJECTIVES THAT CAN BE ACHIEVED MORE DIRECTLY AND RELATIVELY QUICKLY AND THAT HAVE SOME RELATIVELY PREDICTABLE RELATIONSHIP WITH THE ULTIMATE GOALS.

ONE OF THE INTERMEDIATE TARGETS IS CERTAINLY M_1 . BUT IT HAS MANY DRAWBACKS AS A EXCLUSIVE TARGET. IN THE PAST 20 YEARS, OUR COUNTRY HAS EXPERIENCED RAPID ADVANCES IN FINANCIAL TECHNOLOGY. WITH THE ADVENT OF CERTIFICATES OF DEPOSIT, BANK CREDIT CARDS, INTEREST-BEARING DEPOSITS THAT CAN BE USED FOR TRANSACTION PURPOSES, MONEY-MARKET MUTUAL FUNDS, AND AN INCREASE IN THE LEVEL OF SOPHISTICATION OF MANAGING CASH ASSETS ON THE PART OF THE GENERAL PUBLIC, THE DEMAND FOR CURRENCY AND CHECKING DEPOSITS HAS AND CONTINUES TO UNDERGO CHANGES. AS A RESULT, CHANGES IN THE RELATIONSHIP BETWEEN M_1 AND OUR GROSS NATIONAL PRODUCT MAY ALSO BE OCCURRING. SOME OF THESE CHANGES CAN BE PREDICTED FAIRLY ACCURATELY, BUT OTHERS CANNOT.

BECAUSE NO SINGLE DEFINITION OF MONEY DESCRIBES COMPLETELY THE SPENDABLE FUNDS HELD BY THE PUBLIC, THE FEDERAL RESERVE TAKES INTO CONSIDERATION THE BEHAVIOR OF A NUMBER OF MONETARY AND CREDIT AGGREGATES, INCLUDING TIME DEPOSITS AND EVEN DEPOSITS AT ALL FINANCIAL INSTITUTIONS. IN ADDITION TO THE MONETARY AGGREGATES, WE MUST ALSO MONITOR THE CONDITION OF FINANCIAL MARKETS -- THAT IS, MOVEMENTS IN INTEREST RATES AND THE LIQUIDITY NEEDS OF BUSINESSES AND FINANCIAL INSTITUTIONS. THEY IN TURN

REFLECT BUSINESS AND CONSUMER ATTITUDES AND ANTICIPATIONS IN A UNIQUE WAY. ATTENTION IS ALSO PAID TO DEVELOPMENTS IN THE FOREIGN EXCHANGE MARKETS. THE BEHAVIOR OF ALL THESE VARIABLES INETERS INTO THE DECISION-MAKING PROCESS -- AND WITH DIFFERING WEIGHTS DEPENDING ON DIFFERING ECONOMIC CONDITIONS.

BUT I WOULD LIKE TO MAKE IT CLEAR THAT WHILE ONGOING MONETARY POLICY DECISIONS MAKE USE OF MANY INPUTS, THE LONGER-TERM PATH OF MONETARY AGGREGATE GROWTH DOES HAVE SIGNIFICANCE. EXTENDED PERIODS OF TOO RAPID OR TOO SLOW A GROWTH OF THE MONETARY AGGREGATES WILL TAKE A TOLL IN MORE RAPID INFLATION OR IN MORE SLUGGISH RECOVERY. BECAUSE OF THIS, THE FEDERAL RESERVE CONCENTRATES ON SETTING MONETARY AGGREGATE TARGETS OVER LONGER PERIODS OF TIME.

ONE FINAL WORD ABOUT MY FULL DAYS. CARTER WAS WRONG, TOO, IN SUGGESTING A NOMINAL, EVEN A PERFUNCTORY ROLE OF THE RESERVE BANK PRESIDENTS IN THE MONETARY POLICY DECISION PROCESS. EACH OF US FEEL AND I AM CERTAIN CAN DEMONSTRATE THAT WE ARE FULL PARTICIPANTS.

I WOULD BE PLEASED TO RESPOND TO ANY QUESTIONS YOU MIGHT HAVE.