

TRANSCRIPT

FEDERAL OPEN MARKET COMMITTEE CONFERENCE CALL

November 8, 1976

Prefatory Note

This transcript has been produced from the original raw transcript in the FOMC Secretariat's files. The Secretariat has lightly edited the original to facilitate the reader's understanding. Where one or more words were missed or garbled in the transcription, the notation "unintelligible" has been inserted. In some instances, words have been added in brackets to complete a speaker's thought or to correct an obvious transcription error or misstatement.

Errors undoubtedly remain. The raw transcript was not fully edited for accuracy at the time it was produced because it was intended only as an aid to the Secretariat in preparing the record of the Committee's policy actions. The edited transcript has not been reviewed by present or past members of the Committee.

Aside from the editing to facilitate the reader's understanding, the only deletions involve a very small amount of confidential information regarding foreign central banks, businesses, and persons that are identified or identifiable. Deleted passages are indicated by gaps in the text. All information deleted in this manner is exempt from disclosure under applicable provisions of the Freedom of Information Act.

Meeting of Federal Open Market Committee

November 8, 1976

A meeting of the Federal Open Market Committee was held on Monday, November 8, 1976, at 10:00 a.m., at the call of Chairman Burns. 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.

PARTICIPATING: Mr. Burns, Chairman
Mr. Black (Richmond)
Mr. Coldwell (Dallas)
Mr. Gardner
Mr. Jackson
Mr. Kimbrel (Miami)
Mr. Lilly
Mr. Partee
Mr. Wallich
Mr. Winn (Cincinnati)
Mr. Guffey, Alternate
for Mr. Balles (Kansas City)
Mr. Timlen, Alternate
for Mr. Volcker (New York)

Mr. Baughman, Alternate Member of the
Federal Open Market Committee
(Dallas)

Mr. Broida, Secretary
Mr. Altmann, Deputy Secretary
Mr. Bernard, Assistant Secretary
Mr. O'Connell, General Counsel
Mr. Axilrod, Economist (Domestic
Finance)
Mr. Gramley, Economist (Domestic
Business)

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Messrs. Davis (New York), Kichline,
Parthemos (Richmond), and
Zeisel, Associate Economists

Mr. Sternlight, Deputy Manager for
Domestic Operations (New York)

Messrs. Coyne and Keir, Assistants
to the Board of Governors

Mr. Gemmill, Adviser, Division of
International Finance, Board
of Governors

Mrs. Farar, Economist, Open Market
Secretariat, Board of Governors

Mrs. Deck, Staff Assistant, Open
Market Secretariat, Board of
Governors

Mr. Doll, Senior Vice President,
Federal Reserve Bank of Kansas
City (Kansas City)

Messrs. Davis (Kansas City), Green
(Dallas), Snellings (Richmond),
and Willey (New York), Vice
Presidents, Federal Reserve
Banks of Kansas City, Dallas,
Richmond, and New York
respectively

Transcript of Federal Open Market Committee Conference Call of
November 8, 1976

CHAIRMAN BURNS. Gentlemen, this is Arthur Burns speaking. I take it that all members of the Committee or their duly appointed alternates are now assembled and we can proceed to our discussion of the longer--

MR. TIMLEN. Mr. Chairman, we cannot hear you in New York.

MR. BLACK. Nor in Richmond, Mr. Chairman.

CHAIRMAN BURNS. Well, let's see what is happening here. Can you hear me now?

[Others reply "yes."]

CHAIRMAN BURNS. Well, apparently all I have to do is to speak up; and I shall try. We held a preliminary discussion of our annual monetary growth range targets at the last meeting of our Committee, and in the course of that discussion, approximately half of the members expressed a preference for leaving the monetary growth rates for the year--starting in the third quarter of 1976 and ending in the third quarter of 1977--unchanged. Approximately the remaining one-half of the members of the Committee expressed a preference for lowering the upper limit of the growth range for M1 from 7 percent to 6-1/2 percent but leaving other specifications concerning monetary growth unchanged. Now, since these were the two prevailing views, I think it would be best if we concentrated our discussion on a choice between these two ways of specifying our monetary growth ranges for the coming year.

At the FOMC meeting, I argued that it would be desirable to lower the upper limit of the growth range of M1 from 7 percent to 6-1/2 percent. I have given a great deal of thought to this matter since our meeting, as I'm sure all of us have. My own basic view remains pretty much what it was. I think there is a good case for lowering the upper limit of M1 from 7 to 6-1/2 percent. And my basic reason is as follows: If a return to reasonable price stability in our country is to be obtained over the next few years, we will need to reduce our monetary growth rates quite substantially. Now, we have already done this during the past year, or year and a half, on a modest scale at our preceding meetings. Today, by taking one more small step toward reducing our annual growth range targets, we would clearly indicate to the outside world that we are still pursuing a moderate, prudent, consistent policy of promoting economic expansion and yet helping to unwind the inflation that is still plaguing our economy.

This argument is reinforced by a second consideration in my mind. Namely, that our average growth rate of M1 during the past year has been roughly 5 percent, that is, it has been at the lower limit of the range for M1. We have not used the upper part of the range for M1, and therefore a reduction of the upper limit of the range from 7 percent to 6-1/2 percent would not be at all inconsistent with, actually, a substantial increase in the growth of M1 during the coming year if the Committee so sought, and if events validated the Committee's decisions.

Nevertheless, I fully recognize that there is a significant objection that could be raised against lowering the upper limit of M1 to 6-1/2 percent. The objection is, or might well be, that

such a move would be misinterpreted by many, that it would be regarded as a restrictive monetary measure and that, at a time when the economy is pausing, so to speak, that such a time is hardly opportune for restrictive measures or for measures that could be so interpreted. I tried to weigh this objection, and my conclusion is as follows: First, we must do what we think is basically right for the economy. Second, we should not be deterred from doing so by the danger of misinterpretation. And third, we should be able to minimize misinterpretation by carefully interpreting what we are striving to accomplish.

So I thus find myself still recommending, as I did before, a reduction in the annual monetary growth range, or more precisely, the upper limit of that range, from 7 percent to 6-1/2 percent. In making this recommendation, it is only proper that I add that I thoroughly respect opposing arguments that can be, and--I'm sure before this meeting is concluded--will be made.

Now I would like to say a word about procedure. A telephonic conversation is difficult for all of us, and by maintaining a certain order we might facilitate our discussion. Now I am going to call first of all on Mr. Winn, and there's a good and obvious reason for doing so. Mr. Winn left our [preceding] meeting of the FOMC before the longer-range targets were discussed. Starting, then, at the lower end of the alphabet I will move next to the upper end of the alphabet and call on Mr. Black. Then I shall move to the next lowest end of the alphabet and call on Mr. Wallich and then to the next highest name on the alphabetic range and call on Mr. Coldwell, and so on in sequence.

And the order, therefore, in which I will call on members of the Committee is as follows: First, Mr. Winn, then Mr. Black, then Mr. Wallich, then Mr. Coldwell, then Mr. Timlen, then Gardner, then Partee, then Guffey, then Lilly, then Jackson, and then Kimbrel. Now as a result of the alphabetical rule that I am following, you will notice that the south will have the last voice and that perhaps is not altogether inappropriate at this season, and this will be the only quasi-political note, I hope, that will be struck at this meeting. We are ready now for you, Mr. Winn. Good morning to you, and good morning to all members of the Committee.

MR. WINN. My concern, Mr. Chairman, is not so much with the philosophy you have expressed, but you did not mention the problem of our floating base. And this is the problem that concerns me. That we really get a double reduction as the result of the third-quarter level versus our targets. And in view of the sophisticated nature of our criticism, I have a feeling that if we could take as our base our targeted objective for the third quarter rather than our achieved objective, then a reduction in the range from 7 to 6-1/2 percent would be appropriate.

But it seems to me that with our third-quarter base down, we're getting a double impact, which strikes me as a problem from which criticism could be more extreme than I would like to see at this time. Therefore, if the base could be the third-quarter objective rather than the achievement, 4-1/2 to 6-1/2 I think would be quite appropriate. In view of our base problem, it seems to me that we are indicating a reduction by sticking to the same range that we have for the previous quarter.

CHAIRMAN BURNS. Let me say a word about that. I think the question you raised is entirely appropriate, but I don't believe that we can, particularly in a telephone meeting, reconsider our procedure, and therefore I don't think that we ought to make any attempt at this

time to do anything about the base. But I think this would be a fitting subject for discussion in subsequent meetings. Now let me next call on Mr. Black. Good morning, Mr. Black.

MR. BLACK. Good morning, Mr. Chairman. I am almost 100 percent in accord with your recommendation, and I come out a little bit different, with 6 percent on the listing that the Board's staff provided us. In the past year we had an adjusted rate of 6.3 on the money supply; [then we] assumed from here on out to the third quarter of next year that we'd get 5.5, the midpoint of the range you proposed; and after a 1.2 adjustment to that, that gives you a figure of 6.7 net, I think a very realistic measure of what you get if we have acceleration of what we have had. I personally would hope that we'd get the low end of that range.

CHAIRMAN BURNS. Thank you, Mr. Black. I should have observed that members of the Committee, in addition to stating their views on the two alternatives on which we'll be concentrating, should feel free if they so desire, at the time when they speak, to call on Mr. Gramley or Mr. Axilrod to reply to any questions that they may have.

With that understanding, let me turn next to Mr. Wallich, please. I have the advantage now--I can look into Mr. Wallich's eye. We all have a certain difficulty, you know, talking to individuals whom we do not see face-to-face, but that's the nature of the telephonic conversation. Perhaps we should be grateful that such a thing is possible in our advanced technological age.

MR. WALLICH. This is Henry Wallich, can you hear me?

[Others reply "yes"]

MR. WALLICH. I have a great deal of difficulty with this decision. It seems to me that, during the brief period that has elapsed since the last meeting of the Committee, things have not improved. In some respects, failure to improve really means deterioration of the situation. I am quite concerned that we should not seem to be throwing off false signals; in particular, we shouldn't seem to be giving up in the effort to bring the aggregates down as a means of reducing inflation over the longer run.

Now there are two ways, really, one could go about this. One is to bring down the 7 percent for M1--the upper edge--to 6-1/2 and then make a statement explaining that it is not a restrictive action because that upper part of the range has never been used. The alternative way is to leave it where it is and make a statement to the effect that one is not thereby compromising one's long-run policy of bringing these aggregates down. I am somewhat impressed by Willis Winn's point about base drift. Without wanting to enter into discussion of the base, the fact is that in the last three months we haven't achieved the midpoint of our range, and I guess over the last six months, with 5.5 percent M1 growth, we have not quite achieved it.

CHAIRMAN BURNS. You're not overlooking the October figure are you?

MR. WALLICH. Well, October is strong, and we may well find our base drifting upward from whatever decision we may make now. My own preference is for leaving things as they are, with a statement at the hearing that we should not regard this as an ending of the effort to bring down the ranges but that, in the light of the economic situation and the length of the pause that we've experienced, it seems appropriate at least to give that [situation] a degree of recognition.

We're not raising anything but simply slowing down the rate at which we're bringing down the aggregates.

CHAIRMAN BURNS. Well, thank you, Mr. Wallich, and good morning, Phil.

MR. COLDWELL. Good morning, Mr. Chairman.

CHAIRMAN BURNS. And we're ready for you now.

MR. COLDWELL. Thank you. I've been doing some thinking about this because of some of the [unintelligible] you raised. I could accept a reduction in the M1 upper level from 7 to 6-1/2 percent, but I accept it more because of the impact that I read from the staff's memorandum on regulatory changes and the things that [those changes have] done to our M1 figures.

Contrary to that, however, if we're going to reduce that level, I would prefer to have a third alternative of raising M2 and M3 levels from where they are now to an 8 to 10 percent for M2, and 10 to 12 percent on M3, giving cognizance to the fact that we are still expecting to have more shifts out of the M1 level into the M2 and M3. I admit that it complicates our discussion, Mr. Chairman, but I do think that if you look out over this year or for the past two years, you've seen our past records being a very low level of M1 but [at] the upper level of the M2 and M3 ranges, particularly M3. And I guess if you ask for my preference, my preference is for the lowering of that M1 so that we don't get caught with a partly presumptuous feeling of change for other reasons rather than the basic economy and yet leaving us some leeway on the upper end. That's all I have.

CHAIRMAN BURNS. Thank you, Mr. Coldwell. Let us hear now from Mr. Timlen. Good morning, Mr. Timlen.

MR. TIMLEN. Good morning, Mr. Chairman. On balance, I personally favor some overt indication by the System of its continuing concern with the question of inflation. I am personally in favor of the reduction you have proposed in the upper range of the target for M1, from 7 to 6-1/2 percent, which focuses primarily on the long-range nature of these targets. Basically it's clear we are going through a pause in our economic situation, but I think we should be willing to look beyond that in setting our long-range targets. I'd also say, in defense of the technical argument put forward by the staff paper, the explanation of what has been happening to M1 gives further ground for the reduction moves.

CHAIRMAN BURNS. Thank you, Mr. Timlen. Mr. Gardner, let us hear from you now, please.

MR. GARDNER. Good morning. Can you hear me?

[Others reply "yes"]

MR. GARDNER. I'll try to be very brief. I'm impressed with the care and thought that goes into the Committee's deliberations. I look at the existing supply of money in the economy, and I see an ample supply of money. I don't believe that that has been a bar to any of our

progress this year. In my view, there's a consensus that we are indeed in a slowdown and a deteriorating condition. As a possible analysis, the measures that are appropriate are not, in my view, more monetary stimulus, because I don't believe that our economy or our progress is being held back. I think clearly we must face the future with an effort to reduce inflation.

I think it may be a very difficult time for us to announce a slight lowering in the top of the range, but I really think that that's our responsibility and our job, and therefore I would agree with a slight limiting or reduction in the long-range target for M1, and I think Governor Coldwell is entirely right in seeing mechanical and regulatory changes in the definition of M1, and we must put more attention on that subject. But nevertheless, I vote now for a 1/2 point reduction in the long-range M1 target.

CHAIRMAN BURNS. Thank you, Mr. Gardner. And we are now ready for Mr. Partee. Mr. Partee, may we hear from you?

MR. PARTEE. Thank you, Mr. Chairman. Gentlemen, can you hear me?

SPEAKER(?). Yes.

MR. PARTEE. Well, I came into the meeting this morning thinking that it would be a mistake to reduce the M1 target range even by a small amount given the performance of the economy, which I consider to be quite weak. I think we ought to hear from Lyle. My impression is that the fourth-quarter resurgence in GNP has not materialized in any way, and you know that if the pause continues long enough, it's no longer just a pause between expansions, but it may affect the expansion.

I think there's considerable doubt about the business situation right now. I also was opposed to reducing the target range for a technical reason. Willis Winn referred to one part of it, that is, that we [had] a third-quarter shortfall of appreciable dimension. But the other part of it is that, October, which [was] a very large month [for M1], adds to the fourth-quarter average, so that in fact the chances are that we're going to have a fourth-quarter average that is rather high in relation to the M1 range that we've been talking about. Though it's true that we've been talking about it for a year [unintelligible]. And I think Steve Axilrod ought to speak to that point just briefly.

But my real concern, as I stated at the meeting a couple of weeks ago, is with M2, which I think is way too low and is likely to prove the limiting force on monetary policy given the different configuration of interest rates that we're now living with and that may be in prospect yet for some months to come. When we drew up this M2 range of 7-1/2 to 9-1/2 percent, late last summer I guess it was, we were doing this on the basis of a staff expectation that interest rates would be rising throughout the fall and winter period and that the rise in interest rates would limit the natural growth in M2 because the market would be a stronger competitor than before. That has certainly not been true thus far.

Indeed, up to now we're quite high, I believe, in the M2 figures; we have been running that way for some months. There is no difference in October; in fact the October-November period is even stronger, something like 13-1/2 percent as I recall--13.1 percent for M2, which is way above the 7-1/2 to 9-1/2 percent range--and it is likely to remain so. And also there are a good

many economists that draw--rightly or wrongly--a parallel between M2 growth and nominal GNP on a more or less one-for-one basis. Well, the midpoint of an M2 of 7-1/2 to 9-1/2 is 8-1/2 percent, and an 8-1/2 percent increase in nominal GNP is considerably short of what we need assuming that we're going to have something like 5 percent inflation.

So to state my position in this rather difficult circumstance where all of us aren't together, my first preference would be to retain the current M1 target range of 4-1/2 to 7 and to raise M2 and M3 ranges back to where they were before, which is about a point increase. But I considered the second part of my desire more important than the first, mainly because of the substitution that is occurring, and that was pretty well demonstrated in that staff memo. Therefore, I would accept a somewhat lower M1 range in return for a higher M2 and M3 range. Thank you.

CHAIRMAN BURNS. Thank you, Mr. Partee. And now good morning, Mr. Guffey, and we're ready to hear from you.

MR. GUFFEY. I think my view is very similar to what Governor Gardner has already expressed, that is, that we are focusing in on the long-range targets at the moment. There seems to be little evidence that there is a lack of liquidity. Rather, the money supply is adequate in the economy, as evidenced by the continuing downward drift of interest rates over a rather substantial period of time. And I guess I would prefer at the moment, perhaps, to continue our downward movement in one or more of the aggregates, this time at least to be focusing in on M1. And I think it would be reasonable because we've been using only the lower portion of that particular range.

[In] testimony for the public view, I think it might be equally premised upon the fact that you do have a large latitude in M1, even if we are at 6-1/2 percent, to accommodate the necessary growth we see in the future. As a result, I guess I would opt for the lowering of the M1 upper range to 6-1/2 percent; it gives a better alignment, I suppose, between M1 and M3. So I think there is something to be said for, [at] some time in the future, taking a look at these outrageous upper ranges of M2 and M3. Now, at the moment, I would go with the 6-1/2 percent upper range on M1.

CHAIRMAN BURNS. Thank you, Mr. Guffey. We're now ready for you, Mr. Lilly.

MR. LILLY. Well, Mr. Chairman, I very much share Governor Partee's feelings. Before I do speak, however, I would like to hear what Lyle has to say and what Steve has to say in answer to Chuck's questions.

CHAIRMAN BURNS. Very good, would you be good enough to repeat your question, Mr. Partee, first to Mr. Gramley.

MR. PARTEE. Well, my question to Mr. Gramley was whether, indeed, the economic evidence hadn't been weak enough over the last month, or the last few weeks since the meeting, to now raise considerable question about the presumed increase in GNP in the fourth quarter that was in the Greenbook in the last meeting, and any other further comments he would like to make on the pattern of economic developments.

CHAIRMAN BURNS. All right, Mr. Gramley, may we have some brief comments from you now, in reply to Mr. Partee.

MR. GRAMLEY. Thank you, Mr. Chairman. I would agree with Governor Partee that the recent economic news has not been particularly encouraging, but it certainly hasn't been all bad. I suppose the most discouraging news we received was last Friday's report on labor market developments in October. In manufacturing, there were widespread declines in employment in aggregate man-hours, but the severity of those declines was partly due to strikes.

As a very rough guess, we think industrial output last month may have declined by several tenths of a percent, possibly as much as 1/2 percent. This continuing weakness in the industrial sector suggests continued efforts on the part of businesses to pare unwanted inventories. That interpretation, I think, is consistent with the figures we received for manufacturers' inventories in December, which showed a higher rate of accumulation than earlier in the summer and [unintelligible] inventory-sales ratios.

CHAIRMAN BURNS. This evidence is for what month?

MR. GRAMLEY. For the month of September. Manufacturing inventory for the month of September. On the positive side, there is some evidence that retail sales except for autos strengthened in October. The weekly retail sales figures have been moving up, and we received qualitative reports from a number of retailers indicating that they're relatively happy with their present inventory positions, and that sales of apparel have been quite good in October. We also had a good increase in September in new orders for nondefense capital goods.

I do think that we're probably looking at a smaller rise of real GNP in the fourth quarter than we had been projecting and possibly even a smaller increase than in the third. But if retail sales continue to improve and the outlook for capital goods continues to strengthen--if the indicators continue to show improvement--then I don't think this recent news of weakness need have significant implications for the longer-term outlook.

CHAIRMAN BURNS. Thank you, Mr. Gramley. Now, Mr. Partee, would you be good enough to repeat your question to Mr. Axilrod.

MR. PARTEE. Well, I have two questions, I believe. The first is, isn't it true that the M1 behavior in October, which wasn't fully anticipated in the Bluebook at the time of the meeting, now suggests a good deal stronger fourth-quarter rise on average than we've had before? My second question was, what about this M1-M2 relationship? Was that based on interest rate relationships that now seem unlikely to develop, at least in the period immediately ahead?

MR. AXILROD. In answer to the first question Governor Partee raised, at the time of the previous Committee meeting, we were anticipating a relatively moderate growth rate in October and a fourth-quarter growth rate in M1 of around 5 percent. It now looks as if the October growth rate will be around a 14 or 14-1/2 percent annual rate. And assuming a return to moderate growth rates for November and December--not much more than, for example, 5 or 6 percent in those months--we would anticipate a fourth-quarter growth rate in M1 of around 7 percent.

So given what's happened in October, we're about 2 percentage points higher on a quarterly average growth rate for M1. With regard to the relationships between M1 and M2, I would point out in answer to those questions that the M2 [base] and also the M3 base is drifting upward. It was pointed out that the M1 base is drifting downward, but in the third quarter, we had growth rates in M2 and M3 that were, respectively, just below and just above the top of the range. We expect less interest rate pressure in the future, and we would continue to expect that M2 and M3 would grow strongly relative to M1 as compared with previous estimates of that relationship, that is, we're now expecting more strength in M2 and M3 relative to M1. Thus, if the Committee retained the 4-1/2 to 7, we would expect M2 and M3 to go off track on the high side.

CHAIRMAN BURNS. Thank you, Mr. Axilrod and Mr. Gramley. And we're now ready to return to Mr. Lilly, please.

MR. LILLY. I need a piece of paraphernalia.

MR. PARTEE. Here it comes.

MR. LILLY. Well, I share the concern regarding the economy, and I also share the concern about the longer-range implications of allowing M1 to increase at too rapid a rate. However, I do feel at this point that if we bring the upper range of M1 down to 6-1/2, there ought to be an appropriate adjustment upwardly in M2 and M3. And I'm looking at alternative B, on page 5 of the Bluebook, which I would have M1 at 4-1/2 to 6[-1/2]--

CHAIRMAN BURNS. Can you just pause for a moment so that members of the Committee, to the extent that they are physically equipped to do so, [unintelligible] and locate their Bluebooks?

MR. LILLY. I'll be glad to read what I see in front of me.

CHAIRMAN BURNS. That would be helpful.

MR. LILLY. Alternative B as presently in front of you is M1, 4-1/2 to 7; M2, 8-1/2 to 10-1/2; and M3, 10 to 12. I would propose alternative B with one modification: M1, 4-1/2 to 6-1/2; M2, at 8-1/2 to 10-1/2; and M3 at 10 to 12.

CHAIRMAN BURNS. Thank you very much, Mr. Lilly. And now we'll hear from Mr. Jackson.

MR. JACKSON. Good morning, gentlemen. Like others that have spoken earlier, I have some concern about the present rate of growth in our economy. However, I am not quite as pessimistic as some of you would appear to be this morning. I do think that considering the present price prospects, we've got a dual dilemma. [One is the] need to be sure that we don't exacerbate [price prospects] in any way by our monetary policy--in fact, to go further than that, to do what we can to slow them down. But at the same time we have the problem that--given the shifting emphasis toward a higher price level--a smaller growth in the supply of funds actually produces a higher rate of restraint.

There is a great argument I can see in reducing the rate of growth in M1 for the future. Further, I can see a valid argument that somehow or another we need to break ourselves out of this recent habit of half of 1 percent reductions. Because otherwise it would take us forever to get down where we really ought to be, and that will require much more material reductions in rates. And another half a point reduction tends to give the color of custom and habit, which is the holy of holies in most economies, to the half-point rate of change. And to that extent there is some argument in my mind that says, stick to the 7 percent upper level, warn the public that more material reductions will be necessary in the future, and urge that perhaps a 1 percent reduction take place the following quarter. Just as evidence that this small amount of reduction can't be tolerated.

And also, I'm sold by Mr. Winn's shifting-base concept, and on balance I would prefer that we keep the 7 percent upper range for the present. However that would not say that I feel that a reduction to 6-1/2 would be something really worth fighting and arguing about one way or the other, because I think the merits on both sides of this argument are pretty well balanced. Material consequences are probably--it's how we say it, more than what we do, in this circumstance that strikes me as being the most important aspect of our targets announced to the Congress.

CHAIRMAN BURNS. Thank you, Mr. Jackson, we're now ready for the final statement that will be made at this stage of our discussion. Then Mr. Kimbrel, good morning, Mr. Kimbrel.

MR. KIMBREL. Good morning, Mr. Chairman and gentlemen. I too am concerned about the appearance of a possibly weaker economic situation from three months ago and maybe even the potential for some adverse publicity that we would encounter from lowering our long-range target. I find myself more impressed by our need not to compromise our responsibilities. In the last week or ten days, we have moved around the District a good deal, discussing with businessmen, and I have not detected in any area feelings that any of these men are suggesting that there's a lack of funds available, that the lack of these funds is in any way limiting their plans. There seems to be ample liquidity.

The other thing though that does appear to be concerning businessmen in our area is still the specter of inflation. And maybe, certainly in recent days, there seems to be almost a phobia that we are destined to have [price] controls. The limit of those controls is the only thing that seems to be yet unresolved. Well, then, I feel we have to move to think about our part in the contribution to the economy, and I think it [was] already alluded to that we'd be better served to remain consistent in our continuing a gradual reduction of our long-range targets.

I think that Federal Reserve policy is likely to be rather obvious and is rather obvious over the near term. I sense that the business community is rather eager for us to reassure them with some contributions to stability. It is against that background, Mr. Chairman, that I would like to see us continue our plan of reducing, gradually, the upper range. And I would like to see M1 move to 4-1/2 to 6-1/2. I expressed before, and say again, because of the usual quirks of the time deposits [unintelligible], it's not that bad on M2. I'm perfectly willing to accept some gradual increase there. But more importantly, today, I'd like to see us continue our practice of gradually moving down the M1 range to [in this case] 4-1/2 to 6-1/2.

CHAIRMAN BURNS. Now let me try to summarize the discussion that we've had thus far. A clear majority of the Committee would favor reducing the upper limit of M1 to 6-1/2 percent. However, in the case of several members of the Committee, that feeling has been accompanied by the thought that the upper limit of M2 and M3 might well be raised somewhat. I would now like to canvas the thinking of the Committee with regard to M2 and M3, not concentrating so much on numbers as on the thought of whether or not it would be desirable at this time to raise somewhat the upper limits of those two monetary magnitudes.

MR. JACKSON. Before that discussion takes place, Mr. Chairman, would it be possible to ask Mr. Axilrod a question?

CHAIRMAN BURNS. Mr. Jackson has suggested that before we turn to this discussion concerning M2 and M3, that a question be put to Mr. Axilrod, and Mr. Jackson would you be good enough to proceed.

MR. JACKSON. Mr. Axilrod, we have seen substantial growth in M2 and M3 in recent months as a consequence of the Regulation Q interest rate ceilings on certain classes of time and savings deposits. Is it your judgment that, if interest rates stay at the same level--and I recognize that's a hypothetical situation because we have no way of knowing--we're likely to continue to see the rapid rate of growth in M2 and M3 that we've seen in October and September and in more recent months? Or is that likely to level off in the future in relationship to the long-range prospects that we're discussing today?

MR. AXILROD. My judgment, Governor Jackson, would be that if interest rates stay where they are, that the rate of growth in M2 and M3 would moderate somewhat from its recent rate because I believe that, over time, the institutions would begin to have to at least be less aggressive in offering time deposits and probably would begin to lower offering rates, at least on the longer-maturing time deposits--perhaps not on the savings deposits, but certainly on time certificates--because over time they would find pressure. The long-term rates would begin dropping, the mortgage rates would begin dropping, and cost considerations, if nothing else, would begin to force institutions to lower offering rates and become less aggressive in their advertising. So I believe that as time goes on, the present very high rates of growth, even at current interest rates, would moderate somewhat.

CHAIRMAN BURNS. Mr. Partee would like to make a comment.

MR. PARTEE. Well, I think we need to have a little bit more clarification of the relative magnitudes, Steve, than you've given us. That is, if we look at the October-November projection, it's for 13 percent in M2, and I believe more than that in M3. So some moderation would be required to get us down within anybody's proposed longer-term range of growth for those quantities, particularly in the case of M3, which I think has been running strong now for a considerable number of months. So when you say a moderation, are you talking about a point or two or are you talking about something that would put you down, let's say, in the case of M2, [from] 13 to 8 or 9?

CHAIRMAN BURNS. Mr. Axilrod, please give a very brief reply since you're going to take a number out of the air.

MR. AXILROD. Well, we are reevaluating, of course, all these projections as of this very minute. And therefore, any number picked out of the air would be subject to revision. At the time of the last Committee meeting, the easiest alternative, which had only very moderate upward interest rate pressures, that is, alternative A, had M3 growth down around the 11 to 12 percent range in the early part of 1977, and going to around 11 by mid-1977; for M2, it had growth around 10 percent by mid-1977 and 11 percent in early 1977. I believe that this could be roughly what I would think the orders of magnitude are, but we are already reevaluating.

CHAIRMAN BURNS. Thank you, Mr. Axilrod, let us then turn to a discussion of the upper limit of M2 and M3. Messrs. Coldwell, Lilly, and Partee have already stated their views very clearly that they would prefer to see an increase in the upper limit of those two monetary magnitudes, and therefore I shall not call on them at this time. And I shall proceed to call on other members of the Committee, this time in straight alphabetical order, all of which has an element of justice in it since Mr. Winn, having been first at the start, will now be the last speaker. And we'll start now with Mr. Black.

MR. BLACK. Mr. Chairman, I'm impressed very much by Mr. Axilrod's argument. As I indicated earlier, the rate of growth of M1 over the past year--third quarter of last year to the first quarter of this year--was actually 4.4 percent. The midpoint of the long-term ranges we talked about was 5.5, and as I indicated, I was hoping that we could come in toward the lower end of that. I would prefer to stick with the ranges for M2 and M3 that we have now.

CHAIRMAN BURNS. Thank you, Mr. Black. Mr. Gardner, please.

MR. GARDNER. I do not wish to mix our signals, and I also believe that the relationship between M1 and M2 and M3, which gives the appearance of change, is something that this Committee should consider at considerable length. Therefore, I would prefer to lower the range in M1 and keep our M2 and M3 targets for the long range, knowing that the immediate projections will indicate that we will be at the quite high end of the range.

CHAIRMAN BURNS. Thank you, Mr. Gardner. Mr. Guffey next, please.

MR. GUFFEY. Thank you, Mr. Chairman. If it's true that we're starting at a point where we go to 6-1/2 on M1, I think that we have achieved a realignment of the three aggregates. In looking ahead, the end results of these are a full year away, and we anticipate upward movement in [unintelligible] growth, and thereby interest rates, which would make those M2 and M3 [unintelligible]. I would opt today for staying, by lowering the upper range for M1 and leaving M2 and M3 where they are at the moment.

CHAIRMAN BURNS. Thank you, Mr. Guffey. Mr. Jackson, please.

MR. JACKSON. Mr. Chairman, I would favor leaving the present ranges for M2 and M3 as they presently are stated to the public. It strikes me that the arguments that Mr. Winn made about the shifting base of M1 becomes especially pertinent [to] the effect of shifting the base of M2, which is at a much higher level. And thus, as we look at the prospects for increased growth based on this higher level, the present ranges are certainly more appropriate than an increase.

CHAIRMAN BURNS. Thank you, Mr. Jackson. Mr. Kimbrel, please.

MR. KIMBREL. Mr. Chairman, I could accept, I guess, a very, very modest increase in these, but I'm much more impressed that any such movement now would thoroughly confuse the market. I really believe it will be difficult for us to pass that message along. I prefer simply at this moment to reduce the upper range of M1.

CHAIRMAN BURNS. Thank you, Mr. Kimbrel. Mr. Timlen now.

MR. TIMLEN. I think it would be a very confusing signal to lower the upper range for M1 while raising the upper range for M2 and M3. I don't think that would convey the System's intent, and its present posture on inflation in long range. I think the general public would be totally confused by the technical explanation for raising M2 and M3, and it would obscure the real purpose, that is, lowering the upper range of M1. So I would not favor a change in M2 and M3.

CHAIRMAN BURNS. Thank you, Mr. Timlen. Mr. Wallich, please.

MR. WALLICH. I have less confidence, I think, than some of my colleagues in M2. It's becoming a broader and broader concept, becoming more monetary at its highly liquid end [with] transactions balances, and more investment type at the other end, where multiyear certificates are issued. Also, I'm aware that M1 is contained in M2, so that if there is some tendency of M1 to be understated by something like 2 percentage points, 1 percentage point of that reflects in M2.

But on the other hand, I'm not greatly concerned about the danger of conflicting signals. It seems to me that can be explained. What we're doing is a realignment; there probably is never a good time to make a realignment. But by raising the [broader] Ms while lowering the [narrower], I think we are, as far as the technicalities are concerned, making a realignment; as far as the economy is concerned, we are at least not reducing the expansive force of the economy, the monetary aggregates. In short, it seems to me that to raise M2 and M3 slightly would be a good move.

CHAIRMAN BURNS. Thank you, Mr. Wallich. Let us hear from Mr. Winn.

MR. WINN. I think I ought to associate myself with that position, Mr. Chairman, with Mr. Wallich's.

CHAIRMAN BURNS. As matters stand now five members of the Committee have indicated a preference for raising the upper limits of M2 and M3, six members of the Committee have indicated a preference for [keeping them] where they are, and for the moment, I'm not going to express a view on that issue. We're almost evenly divided.

Now I should say this to the Committee. At the last meeting of the FOMC, we reached a decision which I think was a proper decision, to take a formal vote on our longer-range targets. Before that, we had advice from our attorneys not to follow that procedure, but I think our attorneys have relented. In any case the Committee clearly expressed its view at the last meeting that a vote should be taken. Now that puts a heavy responsibility on each of us, and I think the responsibility, without elaborating the point, is especially heavy at this time in Federal Reserve history.

In view of that, while I am somewhat fearful that raising the upper limit of M2 and M3 will cause some confusion, I believe that the best chance of coming close to unanimity, if not actually attaining it--I hope we can attain it at this meeting--would be to vote on the following proposition: that the range for M1 be set at 4-1/2 to 6-1/2 percent for the coming year, and that the range for M2 be set at 7-1/2 to 10 percent and the range for M3 to be set at 9 to 11-1/2 percent--the reason for raising the upper limit of M2 and M3 being along the lines expounded most fully by Mr. Partee in the earlier part of our discussion. I suggest that we vote on that proposition: M1 at 4-1/2 to 6-1/2 percent, M2 at 7-1/2 to 10 percent, and M3 at 9 to 11-1/2 percent. But before taking an actual vote, does any member of the Committee wish to speak at this time? Mr. Partee would like to speak.

MR. PARTEE. Well, Mr. Chairman, I appreciate the substitute, the increase in the range, the slight increase in the range for M2 and M3, but I really don't think it is going to be sufficient to accommodate even what has been going on recently in the last several months. I would prefer to have seen the alternative B specs that Governor Lilly mentioned, which would mean another 1/2 percent on the upper end of both M2 and M3. And so, I think what's going to happen is that M2 is going to become a very limiting factor as time passes here, in addition to possibly M1 being a very limiting factor. And therefore I think there ought to be a little more on the upper side.

CHAIRMAN BURNS. At this time, I think I must state my views on this subject. While I have some sympathy with what Mr. Partee has said, he, like the rest of us, is guessing about the future. Moving up to the upper limit of M2 and M3 would indicate a direction of our thinking. We will have ample opportunity to modify our thinking, if that is desired, at subsequent meetings.

To move down the upper limit of M1 by 1/2 percentage point and to move up the upper limit of M2 and M3 by a full percentage point I think would be profoundly confusing. We would return, as far as M2 and M3 are concerned, to the upper limit that we set as early as April 1975. There would be a complete reversal, and I think it would be most unfortunate, and while I regret differing with my colleague so sharply, I would strongly urge the Committee not to do that, and I hope that Mr. Partee would go along. Is there any other comment that any member of the Committee would like to make at this time?

I think the differences between us now have become rather subtle and I hope that we can be reasonably close to unanimity if not actually unanimous. Any other comments? Mr. Wallich would like to make a comment.

MR. WALLICH. Well, I certainly agree, Mr. Chairman, I certainly agree that 1/2 percentage point in M2 does not make a vast amount of difference in the uncertainties that we face. I also agree that raising it by a full percentage point might be a signal of a change of mind. I just want to clarify that, in my thinking about a combination of lowering the upper end of M1 and raising the upper end of M2 and M3 by equal percentage points, we can interpret that as a technical realignment, leaving the overall immediate stance of policy unchanged--but the longer-term intention continues to be to bring them all down.

CHAIRMAN BURNS. I think that's a reasonable interpretation. We might not all agree with it, but I think it's a very reasonable interpretation. Is there any other comment at this time? If not, I'll ask our Secretary to call the roll.

MR. BROIDA.

Chairman Burns	Yes
President Black	Yes
Governor Coldwell	Yes
Governor Gardner	Yes
President Guffey	Yes
Governor Jackson	Yes
President Kimbrel	Yes
Governor Lilly	Yes
Governor Partee	Yes
Governor Wallich	Yes
President Winn	Yes
First Vice President Timlen	Yes

It's unanimous.

CHAIRMAN BURNS. Well, I think this is a good outcome, and the ability of this Committee to conciliate our differences, I think, is most encouraging, not only for today but for the long future. And, actually, we've not been very far apart at any time. I have nothing to add, except to express my thanks to members of the Committee. Would someone like to say anything at this time? I hear yes. Please.

MR. WINN. Mr. Chairman, can we address ourselves to some of these other issues, if we can reasonably in the near term, such as the base problems and some of these other issues that we've mentioned?

CHAIRMAN BURNS. Well, I think that these issues are so complex that we ought not to try to do that in a telephone conversation.

MR. WINN. I agree on that.

CHAIRMAN BURNS. But this is something that we must do. There are an accumulating number of technical issues--and I would say, particularly, the method of operating in the short run--that we need to examine with very great care, and I am waiting for the staff to give me a signal when they are ready, and I am urging the staff to try to be ready as soon as possible.

So I'll be in touch with the Committee, or Mr. Broida will be in touch. And I assure you, Mr. Winn, and I assure other members of the Committee, that these technical questions are not being neglected. They will be considered very carefully, they must be, by our Committee. There's nothing to add. Let me thank all of you.

END OF MEETING