

Meeting of the Federal Open Market Committee

March 31, 1987

Minutes of Actions

A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington, D. C., on Tuesday, March 31, 1987 at 9:00 a.m.

PRESENT: Mr. Volcker, Chairman  
Mr. Corrigan, Vice Chairman  
Mr. Angell  
Mr. Boehne  
Mr. Boykin  
Mr. Heller  
Mr. Johnson  
Mr. Keehn  
Ms. Seger  
Mr. Stern

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

Messrs. Guffey, Melzer, and Morris, Presidents of the Federal  
Reserve Banks of Kansas City, St. Louis, and Boston,  
respectively

Mr. Kohn, Secretary and Staff Adviser  
Mr. Bernard, Assistant Secretary  
Mrs. Loney, Deputy Assistant Secretary  
Mr. Bradfield, General Counsel  
Mr. Kichline, Economist  
Mr. Truman, Economist (International)

Messrs. Lang, Lindsey, Prell, Rolnick, Rosenblum,  
Scheld, Siegman, and Simpson, Associate Economists

Mr. Sternlight, Manager for Domestic Operations, System  
Open Market Account

Mr. Cross, Manager for Foreign Operations, System  
Open Market Account

Mr. Coyne, Assistant to the Board of Governors  
Mr. Gemmill, Staff Adviser, Division of International  
Finance, Board of Governors  
Mrs. Low, Open Market Secretariat Assistant, Office of  
Staff Director for Monetary and Financial Policy,  
Board of Governors

Messrs. Hendricks and Powell, First Vice Presidents,  
Federal Reserve Banks of Cleveland and San Francisco,  
respectively

Messrs. Broaddus, Burger, J. Davis, T. Davis, Ms. Munnell,  
Messrs. Scadding and Thieke, and Ms. Tschinkel,  
Senior Vice Presidents, Federal Reserve Banks of  
Richmond, St. Louis, Cleveland, Kansas City, Boston,  
San Francisco, New York, and Atlanta, respectively

Mr. R. Davis, Senior Economic Adviser, Federal Reserve  
Bank of New York

In the agenda for this meeting, it was reported that advices of the election of the following members and alternate members of the Federal Open Market Committee for the year commencing March 1, 1987, had been received and the named individuals had executed their oaths of office.

The elected members and alternate members were as follows:

E. Gerald Corrigan, President of the Federal Reserve Bank of New York, with Thomas M. Timlen, First Vice President of the Federal Reserve Bank of New York, as alternate;

Edward G. Boehne, President of the Federal Reserve Bank of Philadelphia, with Robert P. Black, President of the Federal Reserve Bank of Richmond, as alternate;

Silas Keehn, President of the Federal Reserve Bank of Chicago;

Robert H. Boykin, President of the Federal Reserve Bank of Dallas, with Robert P. Forrestal, President of the Federal Reserve Bank of Atlanta, as alternate;

Gary H. Stern, President of the Federal Reserve Bank of Minneapolis, with Robert T. Parry, President of the Federal Reserve Bank of San Francisco, as alternate.

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By unanimous vote, the following officers of the Federal Open Market Committee were elected to serve until the election of their successors at the first meeting of the Committee after February 29, 1988, with the understanding that in the event of the discontinuance of their official connection with the Board of Governors or with a Federal Reserve Bank, they would cease to have any official connection with the Federal Open Market Committee:

Paul A. Volcker	Chairman
E. Gerald Corrigan	Vice Chairman
Donald L. Kohn	Secretary and Staff Adviser
Normand R. V. Bernard	Assistant Secretary
Rosemary R. Loney	Deputy Assistant Secretary
Michael Bradfield	General Counsel
James H. Oltman	Deputy General Counsel
James L. Kichline	Economist
Edwin M. Truman	Economist (International)
Peter Fousek, Richard W. Lang, David E. Lindsey, Michael J. Prell, Arthur J. Rolnick, Harvey Rosenblum, Karl A. Scheld, Charles J. Siegman, and Thomas D. Simpson	Associate Economists

By unanimous vote, the Federal Reserve Bank of New York was selected to execute transactions for the System Open Market Account until the adjournment of the first meeting of the Committee after February 29, 1988.

By unanimous vote, Peter D. Sternlight and Sam Y. Cross were selected to serve at the pleasure of the Committee in the capacities of Manager for Domestic Operations, System Open Market Account, and Manager for Foreign Operations, System Open Market Account, respectively, on the understanding that their selection was subject to their being satisfactory to the Federal Reserve Bank of New York.

Secretary's note: Advice was subsequently received that the selections indicated above were satisfactory to the Federal Reserve Bank of New York.

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Secretary's note: On March 9, 1987, certain continuing rules, regulations, authorizations, and other instruments of the Committee had been distributed with the advice that, in accordance with procedures approved by the Committee, they were being called to the Committee's attention before the March 31 organization meeting to give members an opportunity to raise any questions they might have concerning them. Members were asked to so indicate if they wished to have any of the instruments in question placed on the agenda for consideration at this meeting, and no such requests were received. Accordingly, the instruments remained in effect in their existing forms. They are listed below:

1. Procedures for allocation of securities in the System Open Market Account.
2. Authority for the Chairman to appoint a Federal Reserve Bank as agent to operate the System Account in case the New York Bank is unable to function.
3. Resolutions providing for the continued operation of the Committee and for certain actions by the Reserve Banks during an emergency.
4. Resolution relating to examinations of the System Open Market Account.
5. Guidelines for the conduct of System operations in Federal agency issues.
6. Regulation relating to Open Market Operations of Federal Reserve Banks.
7. Rules of Organization, Rules Regarding Availability of Information, and Rules of Procedure.
8. Agreement with the U.S. Treasury to Warehouse Foreign Currencies.
9. Program for Security of FOMC Information.

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By unanimous vote the Authorization for Domestic Open Market Operations shown below was reaffirmed:

AUTHORIZATION FOR DOMESTIC OPEN MARKET OPERATIONS  
Reaffirmed March 31, 1987

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, to the extent necessary to carry out the most recent domestic policy directive adopted at a meeting of the Committee:

(a) To buy or sell U. S. Government securities, including securities of the Federal Financing Bank, and securities that are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States in the open market, from or to securities dealers and foreign and international accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the System Open Market Account at market prices, and, for such Account, to exchange maturing U. S. Government and Federal agency securities with the Treasury or the individual agencies or to allow them to mature without replacement; provided that the aggregate amount of U. S. Government and Federal agency securities held in such Account (including forward commitments) at the close of business on the day of a meeting of the Committee at which action is taken with respect to a domestic policy directive shall not be increased or decreased by more than \$6.0 billion during the period commencing with the opening of business on the day following such meeting and ending with the close of business on the day of the next such meeting;

(b) When appropriate, to buy or sell in the open market, from or to acceptance dealers and foreign accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the account of the Federal Reserve Bank of New York at market discount rates, prime bankers acceptances with maturities of up to nine months at the time of acceptance that (1) arise out of the current shipment of goods between countries or within the United States, or (2) arise out of the storage within the United States of goods under contract of sale or expected to move into the channels of trade within a reasonable time and that are secured throughout their life by a warehouse receipt or similar document conveying title to the underlying goods; provided that the aggregate amount of bankers acceptances held at any one time shall not exceed \$100 million;

(c) To buy U. S. Government securities, obligations that are direct obligations of, or fully guaranteed as to principal and interest by, any agency of the United States, and prime bankers acceptances of the types authorized for purchase under 1(b) above, from dealers for the account of the Federal Reserve Bank of New York under agreements for repurchase of such securities, obligations, or acceptances in 15 calendar days or less, at rates that, unless otherwise expressly authorized by the Committee, shall be determined by competitive bidding, after applying reasonable

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limitations on the volume of agreements with individual dealers; provided that in the event Government securities or agency issues covered by any such agreement are not repurchased by the dealer pursuant to the agreement or a renewal thereof, they shall be sold in the market or transferred to the System Open Market Account; and provided further that in the event bankers acceptances covered by any such agreement are not repurchased by the seller, they shall continue to be held by the Federal Reserve Bank or shall be sold in the open market.

2. In order to ensure the effective conduct of open market operations, the Federal Open Market Committee authorizes and directs the Federal Reserve Banks to lend U. S. Government securities held in the System Open Market Account to Government securities dealers and to banks participating in Government securities clearing arrangements conducted through a Federal Reserve Bank, under such instructions as the Committee may specify from time to time.

3. In order to ensure the effective conduct of open market operations, while assisting in the provision of short-term investments for foreign and international accounts maintained at the Federal Reserve Bank of New York, the Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York (a) for System Open Market Account, to sell U. S. Government securities to such foreign and international accounts on the bases set forth in paragraph 1(a) under agreements providing for the resale by such accounts of those securities within 15 calendar days on terms comparable to those available on such transactions in the market; and (b) for New York Bank account, when appropriate, to undertake with dealers, subject to the conditions imposed on purchases and sales of securities in paragraph 1(c), repurchase agreements in U. S. Government and agency securities, and to arrange corresponding sale and repurchase agreements between its own account and foreign and international accounts maintained at the Bank. Transactions undertaken with such accounts under the provisions of this paragraph may provide for a service fee when appropriate.

By unanimous vote paragraph 1D of the Authorization for Foreign Currency Operations was amended to raise from \$10 billion to \$12 billion the limit on the overall open position in all foreign currencies. With this amendment, the authorization reads as follows:

AUTHORIZATION FOR FOREIGN CURRENCY OPERATIONS

As Amended March 31, 1987

1. The Federal Open Market Committee authorizes and directs the Federal Reserve Bank of New York, for System Open Market Account, to the extent necessary to carry out the Committee's foreign currency directive and express authorizations by the Committee pursuant thereto, and in conformity with such procedural instructions as the Committee may issue from time to time:

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A. To purchase and sell the following foreign currencies in the form of cable transfers through spot or forward transactions on the open market at home and abroad, including transactions with the U. S. Treasury, with the U. S. Exchange Stabilization Fund established by Section 10 of the Gold Reserve Act of 1934, with foreign monetary authorities, with the Bank for International Settlements, and with other international financial institutions:

Austrian schillings  
Belgian francs  
Canadian dollars  
Danish kroner  
Pounds sterling  
French francs  
German marks  
Italian lire  
Japanese yen  
Mexican pesos  
Netherlands guilders  
Norwegian kroner  
Swedish kronor  
Swiss francs

B. To hold balances of, and to have outstanding forward contracts to receive or to deliver, the foreign currencies listed in paragraph A above.

C. To draw foreign currencies and to permit foreign banks to draw dollars under the reciprocal currency arrangements listed in paragraph 2 below, provided that drawings by either party to any such arrangement shall be fully liquidated within 12 months after any amount outstanding at that time was first drawn, unless the Committee, because of exceptional circumstances, specifically authorizes a delay.

D. To maintain an overall open position in all foreign currencies not exceeding \$12.0 billion. For this purpose, the overall open position in all foreign currencies is defined as the sum (disregarding signs) of net positions in individual currencies. The net position in a single foreign currency is defined as holdings of balances in that currency, plus outstanding contracts for future receipt, minus outstanding contracts for future delivery of that currency, i.e., as the sum of these elements with due regard to sign.

2. The Federal Open Market Committee directs the Federal Reserve Bank of New York to maintain reciprocal currency arrangements ("swap" arrangements) for the System Open Market Account for periods up to a maximum of 12 months with the following foreign banks, which are among those designated by the Board of Governors of the Federal Reserve System under Section 214.5 of Regulation N, Relations with Foreign Banks and Bankers, and with the approval of the Committee to renew such arrangements on maturity:

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<u>Foreign bank</u>	<u>Amount of arrangement (millions of dollars equivalent)</u>
Austrian National Bank	250
National Bank of Belgium	1,000
Bank of Canada	2,000
National Bank of Denmark	250
Bank of England	3,000
Bank of France	2,000
German Federal Bank	6,000
Bank of Italy	3,000
Bank of Japan	5,000
Bank of Mexico	700
Netherlands Bank	500
Bank of Norway	250
Bank of Sweden	300
Swiss National Bank	4,000
Bank for International Settlements:	
Dollars against Swiss francs	600
Dollars against authorized European currencies other than Swiss francs	1,250

Any changes in the terms of existing swap arrangements, and the proposed terms of any new arrangements that may be authorized, shall be referred for review and approval to the Committee.

3. All transactions in foreign currencies undertaken under paragraph 1(A) above shall, unless otherwise expressly authorized by the Committee, be at prevailing market rates. For the purpose of providing an investment return on System holdings of foreign currencies, or for the purpose of adjusting interest rates paid or received in connection with swap drawings, transactions with foreign central banks may be undertaken at non-market exchange rates.

4. It shall be the normal practice to arrange with foreign central banks for the coordination of foreign currency transactions. In making operating arrangements with foreign central banks on System holdings of foreign currencies, the Federal Reserve Bank of New York shall not commit itself to maintain any specific balance, unless authorized by the Federal Open Market Committee. Any agreements or understandings concerning the administration of the accounts maintained by the Federal Reserve Bank of New York with the foreign banks designated by the Board of Governors under Section 214.5 of Regulation N shall be referred for review and approval to the Committee.



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5. Foreign currency holdings shall be invested insofar as practicable, considering needs for minimum working balances. Such investments shall be in liquid form, and generally have no more than 12 months remaining to maturity. When appropriate in connection with arrangements to provide investment facilities for foreign currency holdings, U. S. Government securities may be purchased from foreign central banks under agreements for repurchase of such securities within 30 calendar days.

6. All operations undertaken pursuant to the preceding paragraphs shall be reported promptly to the Foreign Currency Subcommittee and the Committee. The Foreign Currency Subcommittee consists of the Chairman and Vice Chairman of the Committee, the Vice Chairman of the Board of Governors, and such other member of the Board as the Chairman may designate (or in the absence of members of the Board serving on the Subcommittee, other Board Members designated by the Chairman as alternates, and in the absence of the Vice Chairman of the Committee, his alternate). Meetings of the Subcommittee shall be called at the request of any member, or at the request of the Manager for Foreign Operations, for the purposes of reviewing recent or contemplated operations and of consulting with the Manager on other matters relating to his responsibilities. At the request of any member of the Subcommittee, questions arising from such reviews and consultations shall be referred for determination to the Federal Open Market Committee.

7. The Chairman is authorized:

A. With the approval of the Committee, to enter into any needed agreement or understanding with the Secretary of the Treasury about the division of responsibility for foreign currency operations between the System and the Treasury;

B. To keep the Secretary of the Treasury fully advised concerning System foreign currency operations, and to consult with the Secretary on policy matters relating to foreign currency operations;

C. From time to time, to transmit appropriate reports and information to the National Advisory Council on International Monetary and Financial Policies.

8. Staff officers of the Committee are authorized to transmit pertinent information on System foreign currency operations to appropriate officials of the Treasury Department.

9. All Federal Reserve Banks shall participate in the foreign currency operations for System Account in accordance with paragraph 3 G(1) of the Board of Governors' Statement of Procedure with Respect to Foreign Relationships of Federal Reserve Banks dated January 1, 1944.

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By unanimous vote, the Foreign Currency Directive shown below was reaffirmed:

FOREIGN CURRENCY DIRECTIVE  
Reaffirmed March 31, 1987

1. System operations in foreign currencies shall generally be directed at countering disorderly market conditions, provided that market exchange rates for the U. S. dollar reflect actions and behavior consistent with the IMF Article IV, Section 1.

2. To achieve this end the System shall:

- A. Undertake spot and forward purchases and sales of foreign exchange.
- B. Maintain reciprocal currency ("swap") arrangements with selected foreign central banks and with the Bank for International Settlements.
- C. Cooperate in other respects with central banks of other countries and with international monetary institutions.

3. Transactions may also be undertaken:

- A. To adjust System balances in light of probable future needs for currencies.
- B. To provide means for meeting System and Treasury commitments in particular currencies, and to facilitate operations of the Exchange Stabilization Fund.
- C. For such other purposes as may be expressly authorized by the Committee.

4. System foreign currency operations shall be conducted:

- A. In close and continuous consultation and cooperation with the United States Treasury;
- B. In cooperation, as appropriate, with foreign monetary authorities;  
and
- C. In a manner consistent with the obligations of the United States in the International Monetary Fund regarding exchange arrangements under the IMF Article IV.

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By unanimous vote, the Procedural Instructions with respect to Foreign Currency Operations shown below were reaffirmed:

PROCEDURAL INSTRUCTIONS WITH RESPECT TO  
FOREIGN CURRENCY OPERATIONS  

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Reaffirmed March 31, 1987

In conducting operations pursuant to the authorization and direction of the Federal Open Market Committee as set forth in the Authorization for Foreign Currency Operations and the Foreign Currency Directive, the Federal Reserve Bank of New York, through the Manager for Foreign Operations, System Open Market Account, shall be guided by the following procedural understandings with respect to consultations and clearance with the Committee, the Foreign Currency Subcommittee, and the Chairman of the Committee. All operations undertaken pursuant to such clearances shall be reported promptly to the Committee.

1. The Manager for Foreign Operations shall clear with the Subcommittee (or with the Chairman, if the Chairman believes that consultation with the Subcommittee is not feasible in the time available):

A. Any operation that would result in a change in the System's overall open position in foreign currencies exceeding \$300 million on any day or \$600 million since the most recent regular meeting of the Committee.

B. Any operation that would result in a change on any day in the System's net position in a single foreign currency exceeding \$150 million, or \$300 million when the operation is associated with repayment of swap drawings.

C. Any operation that might generate a substantial volume of trading in a particular currency by the System, even though the change in the System's net position in that currency might be less than the limits specified in 1B.

D. Any swap drawing proposed by a foreign bank not exceeding the larger of (i) \$200 million or (ii) 15 percent of the size of the swap arrangement.

2. The Manager for Foreign Operations shall clear with the Committee (or with the Subcommittee, if the Subcommittee believes that consultation with the full Committee is not feasible in the time available, or with the Chairman, if the Chairman believes that consultation with the Subcommittee is not feasible in the time available):

A. Any operation that would result in a change in the System's overall open position in foreign currencies exceeding \$1.5 billion since the most recent regular meeting of the Committee.

B. Any swap drawing proposed by a foreign bank exceeding the larger of (i) \$200 million or (ii) 15 percent of the size of the swap arrangement.

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3. The Manager for Foreign Operations shall also consult with the Subcommittee or the Chairman about proposed swap drawings by the System, and about any operations that are not of a routine character.

By unanimous vote, the minutes of actions taken at the meeting of the Federal Open Market Committee held on February 10-11, 1987, were approved.

By unanimous vote, System open market transactions in foreign currencies during the period February 11 through March 30, 1987, were ratified.

By unanimous vote, System open market transactions in government securities and agency obligations during the period February 11 through March 30, 1987, were ratified.

By unanimous vote, the Federal Reserve Bank of New York was authorized and directed, until otherwise directed by the Committee, to execute transactions in the System Account in accordance with the following policy directive:

The information reviewed at this meeting suggests on balance that economic activity has been expanding at a faster pace than in the fourth quarter, with output apparently strengthened by a rebuilding of business inventories and some improvement in foreign trade. Total nonfarm payroll employment rose strongly again in February. The civilian unemployment rate remained at 6.7 percent for the third consecutive month. Industrial production also increased appreciably further in February. Total retail sales have continued to fluctuate substantially from month to month, largely reflecting the uneven pattern of automobile sales, but on balance overall consumer spending has been relatively flat over the past several months. Housing starts strengthened further in February after rising in December and January to their highest level since late spring. Business capital spending appears to have weakened in early 1987. Consumer and producer prices

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rose more rapidly in early 1987, primarily reflecting sizable increases in energy prices. Labor cost increases have remained relatively moderate in recent months.

Growth of M2 and M3 has slowed substantially from the pace in December and January, and for 1987 to date expansion of these two aggregates appears to have been around the lower ends of their respective ranges established by the Committee for the year. Growth of M1, after moderating in January from an exceptionally rapid pace in late 1986, also has slowed markedly further. Expansion in total domestic nonfinancial debt appears to have moderated appreciably since year-end. Interest rates generally have fluctuated in a relatively narrow range since the February 10-11 meeting of the Committee, although they have firmed somewhat recently. At a meeting in the latter part of February, the Finance Ministers and Central Bank Governors of major industrial countries agreed to cooperate closely to foster stability of exchange rates around then-current levels. However, after mid-March, the trade-weighted value of the dollar against the other G-10 currencies declined further on balance, including a sizable decline against the yen.

The Federal Open Market Committee seeks monetary and financial conditions that will foster reasonable price stability over time, promote growth in output on a sustainable basis, and contribute to an improved pattern of international transactions. In furtherance of these objectives the Committee at its February meeting established growth ranges of 5-1/2 to 8-1/2 percent for both M2 and M3, measured from the fourth quarter of 1986 to the fourth quarter of 1987. The associated range for growth in total domestic nonfinancial debt was set at 8 to 11 percent for 1987.

With respect to M1, the Committee recognized that, based on experience, the behavior of that aggregate must be judged in the light of other evidence relating to economic activity and prices; fluctuations in M1 have become much more sensitive in recent years to changes in interest rates, among other factors. During 1987, the Committee anticipates that growth in M1 should slow. However, in the light of its sensitivity to a variety

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of influences, the Committee decided at the February meeting not to establish a precise target for its growth over the year as a whole. Instead, the appropriateness of changes in M1 during the course of the year will be evaluated in the light of the behavior of its velocity, developments in the economy and financial markets, and the nature of emerging price pressures.

In that connection, the Committee believes that, particularly in the light of the extraordinary expansion of this aggregate in recent years, much slower monetary growth would be appropriate in the context of continuing economic expansion accompanied by signs of intensifying price pressures, perhaps related to significant weakness of the dollar in exchange markets, and relatively strong growth in the broad monetary aggregates. Conversely, continuing sizable increases in M1 could be accommodated in circumstances characterized by sluggish business activity, maintenance of progress toward underlying price stability, and progress toward international equilibrium. As this implies, the Committee in reaching operational decisions during the year, might target appropriate growth in M1 from time to time in the light of circumstances then prevailing, including the rate of growth of the broader aggregates.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. Somewhat greater reserve restraint might be acceptable depending on developments in foreign exchange markets, taking into account the behavior of the aggregates, the strength of the business expansion, progress against inflation, and conditions in credit markets. This approach is expected to be consistent with growth in M2 and M3 over the period from March through June at annual rates of around 6 percent or less. Growth in M1 is expected to remain substantially below its pace in 1986. The Chairman may call for Committee consultation if it appears to the Manager for Domestic Operations that reserve conditions during the period before the next meeting are likely to be associated with a federal funds rate persistently outside a range of 4 to 8 percent.

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It was agreed that the next meeting of the Committee would be held on Tuesday, May 19, 1987.

The meeting adjourned.

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Secretary

Secretary's note: On April 22, 1987, the Committee approved an increase of \$3 billion, to \$9 billion, in the intermeeting limit on changes in System holdings of U.S. government and federal agency securities specified in paragraph 1(a) of the Authorization for Domestic Open Market Operations. On May 6, the Committee approved a further increase of \$2 billion, to \$11 billion, in the limit. These actions were effective immediately, for the period ending May 19, 1987.