FEDERAL RESERVE press release

For Use at 4:30 p.m. December 21, 1984

The Federal Reserve Board and the Federal Open Market Committee today released the attached record of policy actions taken by the Federal Open Market Committee at its meeting on November 7, 1984. This record also includes policy actions taken during the period between the meeting on November 7, 1984, and the next regularly scheduled meeting held on December 17-18, 1984.

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

Attachment

RECORD OF POLICY ACTIONS OF THE
FEDERAL OPEN MARKET COMMITTEE

Meeting Held on November 7, 1984

1. Domestic policy directive

The information reviewed at this meeting indicated a mixed pattern of developments but on balance suggested that economic activity was continuing to expand, though at a considerably more moderate pace than earlier in the year. Final demands appeared to have picked up a bit in early autumn after a lull during the summer. However, domestic production was apparently being damped by strong and growing competition from imported products and by partly related efforts in a few sectors to reduce inventories. Thus far in 1984, broad measures of prices generally have continued to rise at rates close to the reduced rates recorded in 1983.

Nonfarm payroll employment rose 440,000 in October, following average monthly gains of about 200,000 in the third quarter. The October advance was most pronounced in the service and retail trade industries, but employment in manufacturing also increased somewhat after falling sharply in September. The civilian unemployment rate was unchanged in October at 7.4 percent, as an increase in the civilian labor force offset a substantial rise in employment.

Industrial production fell 0.6 percent in September, after edging up 0.1 percent in August. About half of the September decline was due to a decrease in the production of motor vehicles, which had been affected

by a short strike and by continuing problems related to the availability of quality parts. Production of nondurable goods and construction supplies also fell, while output of equipment for business and defense continued to advance. Available information suggested that industrial production increased little in October.

Retail sales rebounded in September, rising an estimated 1.6 percent after two consecutive monthly declines. Gains were recorded at nearly all types of retail outlets and included sharp increases at stores selling largely discretionary items such as apparel and general merchandise. Sales of new domestic automobiles, curtailed by a variety of supply factors, were at an annual rate of about 7-3/4 million units in September and fell in October to a rate of around 7-1/4 million units.

Housing starts rose substantially in September after dropping in both July and August. The advance was broadly based: starts of single-family and multifamily units rose by similar margins, and all major geographic regions of the country recorded increases. Sales of new homes rose nearly 22 percent in September, more than offsetting the declines of the previous two months.

Business fixed investment picked up in September, with shipments of equipment and expenditures on nonresidential construction both expanding appreciably. Investment spending slowed considerably during the third quarter as a whole, however, following exceptional increases over the preceding year. Recent indicators of outlays and spending plans suggested a continuation of the slower expansion in business fixed investment, and

investment in inventories, which had risen relative to sales in recent months, also appeared to be slowing.

The producer price index for finished goods fell 0.2 percent in September and had remained essentially unchanged over the past two quarters. The consumer price index rose 0.4 percent in September, continuing its pattern of increasing in recent months at an annual rate of 4 to 5 percent. Various measures of wage inflation, including the index of average hourly earnings and the employment cost index, have continued to rise more slowly in 1984 than in 1983.

The foreign exchange value of the dollar fluctuated widely over the intermeeting period, rising to a new high in mid-October, but subsequently declining to a level about 2-3/4 percent below that prevailing at the time of the previous meeting. Factors contributing to the dollar's recent decline included an apparent perception among market participants of slower economic activity in the United States than previously anticipated and a judgment that U.S. interest rates might decline somewhat further. The U.S. foreign trade deficit in the third quarter was substantially above the rate in the first half of the year, as a sharp rise in non-oil imports exceeded further growth in exports.

At its meeting on October 2, 1984, the Committee had adopted a directive that called for maintaining the lesser degree of reserve restraint that had been sought in the weeks just before that meeting. The members expected that such an approach to policy implementation would be consistent with growth of M1, M2, and M3 at annual rates of about 6, 7-1/2, and 9

percent respectively for the period from September to December. The Committee agreed that somewhat lesser restraint would be acceptable in the event of significantly slower growth in the monetary aggregates, evaluated in relation to the strength of the business expansion and inflationary pressures, conditions in domestic and international financial markets, and the rate of credit growth. Conversely, greater restraint might be acceptable in the event of substantially more rapid monetary growth and indications of significant strengthening of economic activity and inflationary pressures. The intermeeting range for the federal funds rate was left unchanged at 8 to 12 percent.

Growth in the monetary aggregates strengthened in September from the sluggish pace in August. But data available for October indicated that M1 declined during the month; as a result, M1 was running well below the Committee's expectations for growth in the fourth quarter. Expansion in M2 was also below the Committee's expectations, although to a much lesser extent, while growth in M3 appeared to be at a pace somewhat above the Committee's expectations.

Expansion of total domestic nonfinancial debt moderated to an estimated annual rate of about 11-1/4 percent in September from an average pace of about 13 percent in the preceding two months. Government borrowing remained large, while private credit growth, though relatively strong, moderated. At commercial banks, credit expansion slowed as the pace of consumer lending slackened and growth in business borrowing eased. Thus far in 1984, total domestic nonfinancial debt appeared to be growing at a

rate appreciably above the Committee's monitoring range of 8 to 11 percent for the year.

Over much of the intermeeting interval borrowing by banks at the discount window averaged slightly below levels in the weeks preceding the meeting. However, despite indications of reduced pressure on reserve positions and narrowing spreads between the discount rate and short-term market rates, borrowing at times was sizable. Banks apparently became more willing borrowers at the window following the more cautious approach to reserve management, particularly on the part of large banks, that had developed in late spring. Toward the end of the intermeeting interval, open market operations were conducted to further reduce pressures to borrow in recognition of the extended weakness of M1, and to a degree M2, against the background of incoming economic and financial indicators suggesting, on balance, a marked slowing in the pace of economic expansion. As a result of these developments, together with market expectations of monetary easing and a drop in other short-term rates, the federal funds rate moved down irregularly from around 11 percent just before the October meeting to around 10 percent most recently, with trading on several days in the area of 9-1/2 percent or below. At the same time, other short-term rates fell about 1-1/4 to 1-1/2 percentage points over the period. Long-term rates on taxable securities generally declined about 3/4 percentage point, responding in part to expectations of an improved outlook for inflation as oil prices weakened as well as to the signs of moderating economic expansion. Most major banks reduced their "prime" lending rate in several

steps from 12-3/4 percent to 12 percent, and a few banks lowered their rate to 11-3/4 percent.

The staff projections presented at this meeting suggested that real GNP would grow somewhat more rapidly in the fourth quarter than in the third and that the expansion would continue at a moderate pace in 1985. Personal consumption expenditures were expected to pick up in the near term, and growth over the coming year was also expected to be sustained by continued expansion in business fixed investment, though at a much slower pace than in recent quarters, and by defense spending. The unemployment rate was projected to decline somewhat further over the period, and the rate of price increase was expected to rise a little from its recent pace if the dollar depreciates significantly on exchange markets following its strong rise during the past year.

In the Committee's discussion of the economic situation and outlook, members commented that a mixed pattern of developments had fostered increased uncertainty about the prospects for economic activity. While most agreed that the staff projection of moderate growth in real GNP was a reasonable expectation, much of the discussion focused on the risks of an appreciable deviation from the projection under prevailing circumstances. A few members believed that the chances of a deviation were tilted in the direction of somewhat faster expansion than the staff was projecting, but others expressed concern that the rate of growth might remain quite sluggish in the near term with some possibility of a rise in the rate of unemployment.

The outlook for consumer expenditures was cited as a key area of uncertainty. Several members felt that evidence of general improvement was still lacking after the summer slowdown. It was noted, however, that a number of retailers expected sales to improve in conjunction with the forthcoming holiday season. A failure of consumer spending to revive in line with expectations would have adverse implications for economic growth beyond the fourth quarter, as it would reinforce a recent tendency by businesses to curb their accumulation of inventories or possibly induce them to attempt to reduce previously acceptable inventory levels.

Members who were relatively optimistic about the prospects for economic activity noted the favorable impact that recent declines in interest rates were likely to have on interest-sensitive sectors of the economy such as housing. They also noted that the basic forces that had given impetus to the expansion over the last several quarters were still largely present. These included rising consumer incomes, a high degree of consumer confidence and relatively strong financial positions, a subdued rate of inflation, a favorable outlook for investment in plant and equipment, and a large federal deficit that, at least in the short run, provided a strong stimulus to the expansion. A number of members observed, however, that while underlying factors favored sustained expansion, the timing of a pickup in economic growth following the "pause" experienced in recent months remained uncertain and growth might well remain relatively sluggish in the current quarter. Moreover, even a substantial increase in retail sales over the period ahead might not contribute to significant

short-run improvement in domestic production to the extent that inventories were drawn down or that a rising share of sales was accounted for by imported goods. However, a strong rise in retail sales that tended to deplete inventories would have a favorable effect on production in 1985.

Members who were somewhat less optimistic about the economic outlook noted that the surge in imports was having a strong impact on a number of important domestic industries, both in terms of inhibiting their sales and curbing their investment plans. The current value of the dollar together with relatively weak economic growth in foreign countries were also inhibiting demands for U.S. exports. Moreover, some concern was expressed that rising consumer debt burdens might tend increasingly to curtail consumer spending.

Several members commented that the outlook for inflation remained relatively favorable. While inflationary expectations appeared to have subsided further in recent months, the need to be alert to inflationary potential remained. It was noted, for instance, that a sizable decline in the foreign exchange value of the dollar, if it were to occur, would in time exert upward pressure on domestic prices.

At its meeting in July, the Committee had reviewed and reaffirmed the basic policy objectives that it had established in January for growth of the monetary and credit aggregates in 1984 and had set tentative objectives for expansion in 1985. For the period from the fourth quarter of 1983 to the fourth quarter of 1984, the policy objectives included growth of 4 to 8 percent for M1 and 6 to 9 percent for both M2 and M3.

Through October, M1 grew at a rate in the lower half of the range for the year, M2 at a rate somewhat below the midpoint of its range, and M3 at a rate a bit above the upper limit of its range. For 1985 the Committee had established tentative ranges that included reductions of 1 and 1/2 percentage point from the upper limits of the 1984 ranges for M1 and M2, respectively, and no change in the range for M3. For both years the associated range for growth in total domestic nonfinancial debt was set at 8 to 11 percent.

During the Committee's discussion of policy implementation for the weeks immediately ahead, a number of members expressed concern about the persisting weakness in M1, especially in the context of the concurrent "pause" or "lull" in the economic expansion, and they saw a need for some easing of reserve conditions to encourage a resumption in M1 growth. Other members, while not necessarily disagreeing, nonetheless noted that the recent expansion of M2 had been much closer to the Committee's expectations and that growth in M3 had been somewhat faster. A few members cautioned against putting too much emphasis on M1 in light of its typically volatile behavior, the difficulties of achieving accurate seasonal adjustments, and the often unpredictable relationship of M1 to aggregate measures of economic performance.

Most members felt that the potential for a sharp upward surge in business activity had diminished appreciably for the time being and with it the possible need for a near-term reversal of easing steps already taken. On balance, nearly all of the members favored further easing from the reduced degree of reserve restraint sought recently. While preferences with regard

to the extent of such easing differed somewhat, a majority urged that the lesser restraint be implemented in limited steps, pending an evaluation of its impact on financial markets and of incoming information on the economy and the monetary aggregates. A number of members, who suggested slightly more aggressive steps, stressed that the risks of stimulating an intensification of inflationary pressures were relatively small under forseeable circumstances and that, on balance, more weight needed to be given to the risks of inadequate monetary and economic growth. With regard to the latter, some members noted that the economy appeared to have the capacity for somewhat faster expansion than was generally expected without generating significantly greater inflationary pressures.

A differing view placed more emphasis on prospects for some strengthening in economic activity, partly in light of the sizable declines in interest rates that had already occurred. In this view, little or no easing of reserve conditions would be desirable at this time, although the Committee needed to remain sensitive to possible indications of further weakness in monetary growth and in economic performance. It was pointed out that any very substantial decline of interest rates over the near term might have to be reversed later, with potentially unsettling consequences for financial markets and institutions, in order to restrain a resurgence of monetary growth and inflationary pressures.

In the course of the Committee's discussion, the members generally agreed that under prevailing economic and financial conditions, policy

implementation should be particularly alert to the possible need for adjustment toward lesser restraint. It was felt that any such adjustment should be made promptly, although not automatically, depending on the behavior of the monetary aggregates and continuing indications of relatively sluggish economic activity. In this view, policy implementation should be relatively tolerant, for a time, of a substantial rebound in monetary growth, given the unexpected weakness of M1 in October. Any adjustment of operations in a tightening direction should also depend upon clear evidence of substantial strengthening in economic activity.

Members noted that, along with other interest rates, the federal funds rate had declined appreciably during recent weeks. Accordingly, most of the members favored a reduction in the intermeeting range of the federal funds rate from the current 8 to 12 percent that had been set initially at the July meeting, thus technically providing a more symmetrical range around recent levels. The members regard the federal funds range as a mechanism for initiating Committee consultation when its boundaries are persistently exceeded.

At the conclusion of the Committee's discussion, all but one member indicated that they favored or could accept a directive that called for a somewhat reduced degree of restraint on reserve positions. The members expected such an approach to policy implementation to continue to be consistent with growth of M2 and M3 at annual rates of about 7-1/2 and 9 percent, respectively, as established at the early October meeting

for the period from September to December. Given the appreciable decline in M1 during October, its growth over the 3-month period was now expected to be at an annual rate of around 3 percent, down from the 6 percent rate anticipated at the October meeting. The members recognized the volatility of this monetary measure and indicated that more rapid growth would be acceptable for the quarter. Lesser restraint on reserve conditions would be sought if the monetary aggregates grew significantly below expectations, evaluated in the context of the strength of the business expansion and inflationary pressures, conditions in domestic and international financial markets, and the rate of growth in domestic nonfinancial debt. Conversely, greater restraint might be acceptable in the event of substantially more rapid growth in the monetary aggregates than was currently expected, provided such growth was associated with evidence that economic activity and inflationary pressures were strengthening significantly. It was agreed that the intermeeting range for the federal funds rate should be reduced by one percentage point to 7 to 11 percent.

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

> The information reviewed at this meeting indicates a mixed pattern of developments but on balance suggests that economic activity is continuing to expand, though at a considerably more moderate pace than earlier in the year. Nonfarm payroll employment rose substantially outside of manufacturing in October, following a moderate increase in September, and the civilian unemployment rate was unchanged at 7.4 percent. Industrial production fell in September, partly because of strikes, and available information suggests little increase in October. Retail sales and housing starts rebounded in September after two months of decline. Information

on outlays and spending plans suggests slower expansion in business fixed investment, following exceptionally rapid growth earlier, and inventory investment, having risen relative to sales in recent months, also appears to be slowing. Since the beginning of the year, broad measures of prices generally have continued to rise at rates close to, or somewhat above, those recorded in 1983, and the index of average hourly earnings has risen somewhat more slowly.

Growth of the monetary aggregates strengthened in September, but data available for October indicated that M1 declined during the month, growth of M2 slowed somewhat, and expansion of M3 picked up further. From the fourth quarter of 1983 through October, M1 grew at a rate in the lower half of the Committee's range for 1984, M2 at a rate somewhat below the midpoint of its longer-run range, and M3 at a rate a bit above the upper limit of its range. Growth in total domestic nonfinancial debt appears to be continuing above the Committee's monitoring range for the year, reflecting large government borrowing; private credit growth, though relatively strong, has moderated in recent months. Interest rates have fallen substantially further since the meeting of the Committee on October 2.

Over the past month, the foreign exchange value of the dollar against a trade-weighted average of major foreign currencies has continued to fluctuate widely, rising to a new high in mid-October but subsequently declining to somewhat below its level at the time of the previous meeting. The merchandise trade deficit in the third quarter was substantially above the first-half rate as a sharp rise in non-oil imports exceeded some further growth in exports.

The Federal Open Market Committee seeks to foster monetary and financial conditions that will help to reduce inflation further, promote growth in output on a sustainable basis, and contribute to an improved pattern of international transactions. In furtherance of these objectives the Committee agreed at the July meeting to reaffirm the ranges for monetary growth that it had established in January: 4 to 8 percent for M1 and 6 to 9 percent for both M2 and M3 for the period from the fourth

quarter of 1983 to the fourth quarter of 1984. The associated range for total domestic nonfinancial debt was also reaffirmed at 8 to 11 percent for the year 1984. It was anticipated that M3 and nonfinancial debt might increase at rates somewhat above the upper limits of their 1984 ranges, given developments in the first half of the year, but the Committee felt that higher target ranges would provide inappropriate benchmarks for evaluating longer-term trends in M3 and credit growth. For 1985 the Committee agreed on tentative ranges of monetary growth, measured from the fourth quarter of 1984 to the fourth quarter of 1985, of 4 to 7 percent for M1, 6 to 8-1/2 percent for M2, and 6 to 9 percent for M3. The associated range for nonfinancial debt was set at 8 to 11 percent.

The Committee understood that policy implementation would require continuing appraisal of the relationships not only among the various measures of money and credit but also between those aggregates and nominal GNP, including evaluations of conditions in domestic credit and foreign exchange markets.

In the implementation of policy in the short run, the Committee seeks to reduce somewhat existing pressures on reserve positions. This action is expected to be consistent with growth of M2 and M3 at annual rates of around 7-1/2 and 9 percent during the period from September to December. M1 is expected to grow over the period at an annual rate of around 3 percent, less than anticipated earlier in view of the decline in October. In light of that decline, more rapid growth of M1 would be acceptable. Lesser restraint on reserve positions would be sought in the event of significantly slower growth in the monetary aggregates, evaluated in relation to the strength of the business expansion and inflationary pressures, domestic and international financial market conditions, and the rate of credit growth. Conversely, greater restraint might be acceptable in the event of substantially more rapid monetary growth and indications of significant strengthening of economic activity and inflationary pressures. The Chairman may call for Committee consultation if it

appears to the Manager for Domestic Operations that pursuit of the monetary objectives and related reserve paths during the period before the next meeting is likely to be associated with a federal funds rate persistently outside a range of 7 to 11 percent.

Votes for this action: Messrs. Volcker, Solomon, Boehne, Boykin, Corrigan, Mrs. Horn, Messrs. Martin, Partee, Rice, Ms. Seger, and Mr. Wallich. Vote against this action: Mr. Gramley.

Mr. Gramley dissented from this action because he preferred a directive that called for maintaining approximately the existing degree of reserve restraint. Despite the pause in the current expansion, underlying forces in the economy, together with the decline in interest rates that had already occurred, were likely to produce a resumption of economic expansion in the reasonably near future. In those circumstances, he was concerned that further easing of reserve positions might lead to a significant decline in interest rates that would subsequently have to be reversed as economic activity and money growth picked up again.

2. Authorization for domestic open market operations.

During the intermeeting period, the Committee approved temporary increases in the $4 billion limit on changes between Committee meetings in System Account holdings of U.S. government and federal agency securities specified in paragraph 1(a) of the authorization for domestic open market operations. The first increase from $4 billion to $6 billion was effective on November 21, 1984, and the second from $6 billion to $8 billion on December 5, 1984. Both increases applied to the period ending with the close of business on December 18, 1984. They were approved on the recommendation

of the Manager for Domestic Open Market Operations. During the first part of the intermeeting period, substantial net purchases of securities were undertaken to provide reserves in association with seasonal increases in required reserves and in currency in circulation. The need to provide reserves through open market operations had been augmented this year by some reduction in borrowings on an extended basis at the Federal Reserve Banks. By November 21, immediately contemplated purchases would have nearly exhausted the $4 billion leeway in the authorization and the Manager believed that additional purchases were likely to be required before the next Committee meeting. Subsequently, in early December the Manager advised that a greater need to provide reserves than previously expected had arisen from a combination of factors, all working in the same direction, that included further declines in extended credit at the discount window, anticipated changes in vault cash, currency, and required reserves, and an increased pool of overnight investment funds of foreign official accounts.

Votes for the action effective November 21, 1984: Messrs. Volcker, Solomon, Boehne, Boykin, Corrigan, Gramley, Mrs. Horn, Messrs. Martin, Partee, Rice, Ms. Seger, and Mr. Wallich. Votes against this action: None.

Votes for the action effective December 5, 1984: Messrs. Volcker, Solomon, Boehne, Boykin, Corrigan, Gramley, Martin, Partee, Rice, Ms. Seger, Messrs. Wallich and Keehn. Votes against this action: None. (Mr. Keehn voted as alternate for Mrs. Horn.)