

Meeting of the Federal Open Market Committee
August 18, 1992

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, August 18, 1992, at 9:00 a.m.

PRESENT: Mr. Greenspan, Chairman
Mr. Corrigan, Vice Chairman
Mr. Angell
Mr. Hoenig
Mr. Jordan
Mr. Kelley
Mr. LaWare
Mr. Lindsey
Mr. Melzer
Mr. Mullins
Ms. Phillips
Mr. Syron

Messrs. Boehne, Keehn, McTeer, and Stern, Alternate
Members of the Federal Open Market Committee

Messrs. Black, Forrestal, and Parry, Presidents of
the Federal Reserve Banks of Richmond,
Atlanta, and San Francisco, respectively

Mr. Kohn, Secretary and Economist
Mr. Bernard, Deputy Secretary
Mr. Coyne, Assistant Secretary
Mr. Gillum, Assistant Secretary
Mr. Mattingly, General Counsel
Mr. Patrikis, Deputy General Counsel
Mr. Prell, Economist
Mr. Truman, Economist

Messrs. Balbach, J. Davis, R. Davis, T. Davis,
Ms. Munnell, Messrs. Promisel, Siegman,
Simpson, and Stockton, Associate Economists

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

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

MS. PHILLIPS. So moved.

CHAIRMAN GREENSPAN. Is there a second?

SPEAKER(?). Second.

CHAIRMAN GREENSPAN. Without objection. Thank you very much. Let's now move on to Bill McDonough and the foreign currency operations.

MR. MCDONOUGH. [Statement--see Appendix.]

CHAIRMAN GREENSPAN. Questions for Mr. McDonough?

MR. SYRON. Bill, the questions I have do not have to do with the tactics of what we're doing because I have full faith and very strong confidence in the tactics that we use in carrying out these operations. I have to confess, though, to being somewhat perplexed--and I'm sure there's an answer to this--about what our policy is and what we're trying to do here and to what extent. I just want to be reassured that what we're doing is in the interest of having more orderly markets and [is appropriate in regard to] its impact on the domestic securities market, more particularly the government bond market. Just looking at this round of [actions] and looking at the longer-term pressures, particularly if something were to happen with the German official rates, I worry about our credibility more broadly, not just in the foreign exchange market. If there's a risk, it's perhaps inappropriate if we are seen trying to do something that is impossible to do. So, I'm trying to figure out what we are really trying to accomplish here and over what time horizon. I'm also interested in your view as to what extent [the exchange market] is a factor that is taken into consideration in terms of short-term domestic policy. If we are concerned about the credibility of this institution, particularly at this point in time, we don't want to seem to be going in two opposite directions. I'd be interested in how you integrate these things.

MR. MCDONOUGH. I think one must distinguish in foreign exchange intervention between trying to protect a rate level and seeking to avoid markets being disorderly. Now, we have something of a [conundrum] with the Treasury on exchange rate policy; they, I believe, would be rather more interested in the rate. Our interest--certainly my own and the one I keep preaching to the Treasury with regard to what we ought to be doing--is that we should try to avoid disorderly markets. [It is only when] we make that second judgment that we will be effective in doing anything. As to the two interventions so far, I think the key tie-in to short-term domestic policy is that the Committee has a greater degree of freedom this morning than if the dollar were a great deal lower. Now, I have no idea what the deutschemark-dollar rate would be if we hadn't intervened. I think it's reasonable to say that it would be a good deal lower and the Committee might be worrying about the weakness of the dollar and any inhibiting factor that might be. Going forward, if one were to apply the test of "Is the market disorderly?" and "Would intervention do something about it?", it becomes more difficult the more we intervene. It's a tool that gets dull pretty quickly. One can really see the difference between the two interventions if you [count] the second two pieces as part of one. The first intervention

was very successful because nobody expected it to happen and we did it at a time of day when such intervention normally doesn't happen. It was as if there were a rookie pitcher on the mound and Babe Ruth was at the plate and they moved in the fences; it wasn't too hard. But now it would be really difficult because the market is sitting there waiting for us to come to them, and that's a very awkward position to be in if we are to accomplish something. So, my own view would be that at certain periods it gives the System greater flexibility in monetary policy and at other times it is not likely to be effective and could be counterproductive. Philosophically, that's where I am. Exactly how you apply that is difficult.

MR. SYRON. Do you think its effectiveness is diminished now as compared to the first [intervention]?

MR. MCDONOUGH. I guess the best test of that is that last Thursday the Treasury staff up to just below the Secretary was very inclined to want to intervene; I spent a fair amount of time trying to convince them that it wasn't a good idea. At one stage I moved in my good friend, Mr. Truman, to help. And the two of us I think dissuaded them largely, in addition to policy considerations, on the grounds that it just wouldn't work.

CHAIRMAN GREENSPAN. President Forrestal.

MR. FORRESTAL. Well, Mr. Chairman, I've heard the rationale of disorderly markets [as the reason for intervention], but I feel constrained to say that I was extremely surprised at this intervention, particularly the second and the third [operations]. Of course, I would respect the judgment of the Desk and Bill with regard to whether the markets were in fact disorderly. But we've had extensive discussions over the last year or so in the Committee about the effectiveness of sterilized intervention, and I thought it was the sense of this group that, unless we were going to follow intervention with some kind of substantive monetary policy move, intervention was not the policy of the Committee. I haven't been clear, Bill, whether or not this might have been instigated by the Treasury, but from your remarks I gathered that that was not entirely so. What really compounds the problem with respect to our credibility is having intervention and then having that followed by the Secretary's statement that he's looking for lower interest rates. That to me made us look extremely silly, to put it mildly. So, Mr. Chairman, I'm just confused as to what the policy of the Committee is. And I guess I'd be interested in knowing what really constitutes a disorderly market in the minds of the Desk. I didn't think hitting a postwar low or coming close to a postwar low with respect to the mark constituted a disorderly market, but maybe there are factors that I'm not aware of.

CHAIRMAN GREENSPAN. President Parry.

MR. PARRY. President Forrestal covered it.

CHAIRMAN GREENSPAN. Go ahead.

MR. JORDAN. I have a number of comments. As far as the Secretary's remarks, I remember that a decade ago we had a Secretary of the Treasury who was very emphatic in saying that we would not intervene and we would sell the foreign currencies that his

predecessor had bought; this always intrigued me. Bill, you emphasized surprise a number of times both in your prepared remarks and in your response to Dick Syron and that suggests to me that the rate effect was the key consideration. In fact, your last comment that it wouldn't work last Thursday suggests that the criterion is whether something is working or not working with regard to the rate effect. And I think President Forrestal's remarks about whether the intervention is sterilized or not becomes the key criterion. It seems to me that for this Committee to say on one side that we're in the mood to see our inventory of foreign currencies reduced, as reflected in some of the discussions since I've been here, and at the same time to raise questions about intervening or selling of foreign currencies would not be consistent. If the general attitude is that we would like to see our inventory of foreign currencies diminished and we're willing to communicate that we welcome opportunities to reduce U.S. holdings of foreign-denominated currencies, would that reduce the element of surprise--the benefits that you see to surprising the markets? Would the benefits be diminished if we are very open and acknowledge that when the market is receptive to our selling foreign currencies, we would do so? Also, one small point: In your first remark about our intervening with Canada when the European markets were closed, you said we "bought" DM. I think you meant "sold."

MR. MCDONOUGH. Sorry, I did mean "sold."

MR. JORDAN. Okay. Also, I understand why traders talk in terms of buying and selling dollars, but of course we're the central bank and we can't really buy dollars. So, when you ask for approval and say that we purchased \$385 million dollars, I would far prefer that you say we sold so many deutschemarks, but give the equivalent in dollars for the actual amount of the deutschemarks. I'd prefer that we talk in terms of buying and selling foreign currencies because we, of course, pay U.S. dollars.

CHAIRMAN GREENSPAN. Any further questions?

VICE CHAIRMAN CORRIGAN. Let me just make a further comment, partly in response to Bob Forrestal's and Dick Syron's point. I think the sentiment of the Committee is quite well recognized. I would say the Committee views intervention, however couched, with rather distinct displeasure, and that I think is clear enough. But I don't consider the kind of thing that Bill tried to describe to be practically or philosophically out of character with that distinct Committee orientation. I would say that if the orientation of the Committee is, to put it in its extreme form, that under no circumstances could there ever be intervention for any reason, I think that is a potentially dangerous posture. And while the orientation of the Committee is clear enough--I think it is well understood both within the Committee and in the markets--we have to be careful in terms of taking that orientation to the point where it is indeed seen as a statement of "never" because experience suggests that such a position is one that can come back to haunt us. So, I recognize and accept the sentiment and the distinct orientation of the Committee, but I personally would not be comfortable with the logical extremis of that position that says "never." I try never to say "never"!

CHAIRMAN GREENSPAN. Let me add to the general discussion here and broaden it to evaluate the question and the implications of

what sterilized intervention does and does not do. I think we're all pretty much aware that there is very little intervention can do in and of itself to affect the average of any exchange rate over a particular period of time. But the other side of that issue is not that we are going to get a stable set of bilateral currencies without any intervention at all because we're also aware that we've seen significant bubbles in exchange rates. We have seen what amounts to, in certain cases, panic selling and clear issues of disorderly markets. In principle, the same arguments [apply to] not intervening, on the logic that is implicit in the portfolio adjustment process with respect to sterilized intervention; the other side of that issue is that on occasion [the markets] clearly break down. And the evidence does suggest that when that occurs we in fact can affect the market. One has to ask how it is possible for intervention even of \$1 billion to move the dollar/mark relationship by four pfennigs. Clearly, that's not a fundamental issue. The question is: How in the world did that exchange rate for that particular period of time get that far down and be changed by a very small amount of intervention minutes later? The same argument that one employs to evaluate that is the argument that markets feed on themselves, get out of hand, and sometimes create some degree of instability. Nobody in this Committee that I have spoken to is of the view that intervention has any long-term consequences. But I do think the evidence is quite strong that it does on occasion have short-term consequences. I don't know what to make of it, but the comments within the market in the last two or three days--and I heard it on the radio this morning--are that the expectation that central banks might intervene has stabilized the currency. Now, I don't know whether that's true or false, but that type of market chatter which essentially is saying "Don't get locked into a position; be careful because you might get hit by the central banks" does tend to create a level of uncertainty in the market that is helpful. Some uncertainty is not; I would suspect that this is.

Now, I don't know in any individual instance whether [intervention] is useful or not. I think that Bill is right: That in this particular case we would now be sitting, at least for a while, with a much weaker dollar with spillover effects on dollar-denominated assets. Would that correct itself? Probably. But we are aware that there have been occasions in which disorderly markets crack the structure of the underlying base of the market and the market unfolds. That's what happened when the stock market broke in October 1987; the whole structure just broke down underneath. That wasn't a fundamental change--fundamental in the sense that there were external events. So, while it's terribly important that we stay away from

if we can find times when the market is perceived to be disorderly, [intervention may be useful]. And I would even define a disorderly market as one in which the shorts have become excessive--or longs, depending upon which side of the market it is. A true test as to whether or not the intervention worked or not is whether those people believe that they were wrong. In that case the markets will adjust. There's no science to this; I agree with Bill. The other day when the market was expecting us to intervene and it was self-evident that no matter what we did we could not succeed, we stayed out and I think that was wise. Were we to go back and intervene within the next two or three days, I think we would fail. It's only when the market begins to perceive that we're not going to be there that I think we have a shot at it. So, it's a tricky issue.

only conditions under which [intervention] can be effective--then a single isolated move probably requires marginal reinforcement at a later date or at some point merely to indicate that there is no pattern which is easy to [discern]. If we had done only the [first intervention operation] and then stopped completely, I'm not sure that we would have gotten the effects, [in terms of introducing a] degree of uncertainty about when central banks move. I was not one who believed at the time that the second intervention would accomplish very much other than what I just said. I was frankly surprised when in fact it did work immediately. I thought it would have a very mild effect; but in my judgment the point was that it would be useful merely to have that action there. For the same reason, I think it would be a terrible mistake to try to [intervene] now, because I think the markets are expecting us to do so. If we were to do it, it wouldn't have any effect. And it then becomes a tar baby to the market; we can't get ourselves out of it. Governor Angell.

MR. ANGELL. Well, even though I really support what you've said, Mr. Chairman, I find it unusual for me to be almost on the other side of you on this issue in that I have complained so often over six years regarding intervention. I need to make my position clear; I don't think it has been expressed by anyone yet. There are many ways that we go about conducting monetary policy. In that context, foreign exchange policy is a part of monetary policy. Monetary easing domestically tends to cause the value of a currency to depreciate versus other goods that are trading in the domestic market. Internationally, monetary ease tends to make a currency less valued against goods traded worldwide and against foreign currencies. The full scope of monetary policy then should enable us from time-to-time to use all aspects of this. Monetary policy is not the sole province of the Federal Reserve. When the Secretary of the Treasury makes remarks, in some sense that creates uncertainties in the market in regard to what U.S. policy is.

My own view is that the foreign exchange value of the dollar at this time is in a very precarious spot. It's not whether or not the market is very disorderly but whether or not it will become very disorderly. We have used monetary policy to take interest rates in the United States very low for domestic purposes compared to the monetary policy adopted by the Bundesbank in pursuit of their domestic policy. As a result of [the slope of] our yield curve out to 10 years [versus] the Bundesbank's yield curve out to 10 years, there is an arbitrated 10-year D-mark/dollar forward rate of 170. [Unintelligible] if the Bundesbank seems to be more concerned about inflation than we are, that would tend to make the forward D-mark stronger compared to the forward dollar. Now, we are in a spot, it seems to me, where we have to understand that what happens in the foreign exchange market is part and parcel of what happens to 10-year Treasury securities. If we were to ignore the foreign exchange relationship in a world with huge international capital [stocks], the international capital flows would occur in such a way as to cause an equilibrium adjustment of 10-year notes in the United States. It just can't be that the dollar will fall off a cliff [relative to] the D-mark and head down from 145 to 140 to 135; if that occurs, then at some point in time someone will say: "Hey, how in the world can the dollar get back to 170?" And there could be a serious breakdown such as what the Chairman suggested happened in [October] of 1987. To me we are very close to that kind of serious breakdown. I believe we

have accomplished a great deal of what we wanted to accomplish, which was to create an interest rate environment in the United States that was conducive to U.S. economic growth. I don't believe at this point that depreciating the dollar is going to work very much [in the direction of providing] stimulus to our foreign trade. It's part and parcel of all that we do, and I don't want to tie one of our hands behind our back at a critical moment in time. If someone says that they want us to use the right hand to do one thing and the left hand to do something else, then I will vote "no" as I did in the summer of [1989] when we were following an exactly opposite policy in foreign exchange intervention than we were in [domestic] monetary policy. Now, I support this program; it's a good program and I think we ought to be prepared to do more of it. But I support it because I do not want to take the foreign exchange value of the dollar down, which will cause import prices to rise and will not be conducive to progress on inflation. I don't want monetary ease. In a sense that could be a drastic kind of monetary policy ease that I believe could upset the markets. So, I guess that's a more extreme position than has been heard.

CHAIRMAN GREENSPAN. President McTeer.

MR. MCTEER. Governor Angell says that exchange rate policy is part of the context of monetary policy and obviously it is. I'm not clear to what extent we're in agreement on whether exchange rate policy comes under the jurisdiction of this Committee. Do we have a clear idea of who's in charge of exchange rate policy--the FOMC or the Treasury--or who's the junior partner and who's the senior partner?

CHAIRMAN GREENSPAN. This issue is pretty clear legally. The President of the United States and through him the Secretary of the Treasury--who if push came to shove statutorily could demand that we do certain things, not necessarily with our portfolio but on their behalf--is in charge. There's an ambiguity in the law with respect to whether we could act independently. I suspect that we could find a lawyer in this city who would say that we could buy deutschmarks while the Treasury is selling them. The operations have evolved over the years as a joint venture between the Treasury and the Federal Open Market Committee. Sometimes it has worked well; sometimes it has worked less than well. But in general the issue has very rarely come to a confrontation where we took a hard line position and the Treasury took a hard line position and there was no agreement, at least in my experience. Now, since Jerry [Corrigan] was about to talk in any event--and he has a longer experience in this than I do--I was curious to get his recollection on this issue.

VICE CHAIRMAN CORRIGAN. I think you're about right. Actually, the point I was going to make builds on this. Regardless of the precise legal authority in the relationship between the Treasury and the Federal Reserve, I think when it comes to this area we also have to recognize as a practical matter that there are other players or partners involved--namely, the monetary authorities or central banks in other countries. I think it's fair to say--and Ted or the Chairman or somebody has--that pretty much without exception the heads of all the major central banks probably in their own way would come pretty close to subscribing to the view that intervention over time doesn't do anything. But I think as a group they would also certainly come pretty close to associating themselves with a hybrid point of

view that would incorporate some of what Bill said, some of what Wayne said, some of what the Chairman, and maybe some of what I said. And I think I can say with absolute confidence that not one of them would associate themselves with the "never" school.

So long as that is the case--and I suspect, frankly, that it will always be the case--it would be very, very difficult as a practical matter for us literally to go it alone in a context in which we must maintain these relationships. Now, I think the evolving position of this Committee over the years has had an influence in shaping attitudes in other financial capitals on this very issue. But I must say that in my judgment it would be rather naive, quite apart from our relationship with the Treasury, to say that we could literally go it alone without running some very, very high risks one way or the other that such an attitude or policy would come back to haunt us in spades. It might not be on that issue but on some other issue. So, putting all the theology aside, I think one has to be sensitive to these relationship questions. Those relationship questions far transcend 15th Street or 14th Street or 16th Street, or wherever [the Treasury is located]. So, there is also that very pragmatic aspect of this, which is one of the reasons why I subscribe to that "never say never" school.

MR. ANGELL. Well, I agree that there's no question as to where the call is located legally in regard to exchange rate policy. But the monetary policy operations of this Committee can overwhelm any official exchange rate policy. That is, if we decide to buy Treasuries or buy deutschemarks--it doesn't make any difference--if we buy in the open market, we will overwhelm other foreign exchange objectives. So, this Committee has tremendous power when it comes to determining the outcome of the official position that is [decided] by the Secretary of the Treasury in consultation with the Chairman.

CHAIRMAN GREENSPAN. Let's hear from President Black and then shut this [discussion] down for now. This is the type of subject that we can [return to] if we like in our general planning sessions over the next couple of days. Even though it's not on the agenda, I'm sure it could very well surface. It is an important issue and I think we're coming to at least a temporary close on this question. I think it would be useful for us to go on after President Black has had his say.

MR. BLACK. Mr. Chairman, a while ago you said that statutorily the Treasury has the primary responsibility [for foreign exchange policy]. I believe it would be safe to say, wouldn't it, that it also has that primary responsibility under the Constitution, just as Congress has the power to coin money and regulate the value thereof, which gives us primacy in the monetary policy area.

CHAIRMAN GREENSPAN. Well, I think there is an ambiguity involved. The President's power comes from his Constitutional authority in international relationships.

MR. BLACK. That's what I was speaking of.

CHAIRMAN GREENSPAN. So, there's no question that there is a legal ambiguity surrounding this whole issue, which has never been pushed to fruition. I remember we reviewed this in considerable

detail a few years ago; and the tortured logic of some of the stuff that I saw was really [unintelligible]. The history of this issue is really bizarre.

MR. TRUMAN. In fact, Mr. Chairman, it's interesting that in that tortured history, going back to the early 1960s [when] the Treasury agreed to the interpretation of the Federal Reserve Act made at that time, they did not assert that all we did had to meet with the approval or the control of the Treasury. We understood at that time the need for cooperation, but that was not an element of the debate in the early 1960s. From time to time, there have been some discussions on that point, but it has never been asserted as far as I know that as a legal matter the Treasury had the power to order us what to do with our own portfolio.

CHAIRMAN GREENSPAN. Not with our own portfolio, but they certainly--

MR. TRUMAN. I agree 100 percent with Mr. Corrigan that we don't have the power, at least as a technical matter, to operate on our own. We'd be foolish to do so. And the [Committee's] directive under which all these operations [are conducted] does require us to operate in close and continuous consultation and cooperation with the Treasury and, as appropriate, with other monetary authorities, for the reasons that President Corrigan just articulated.

CHAIRMAN GREENSPAN. Would somebody like to move to ratify the actions of the Desk since the last meeting?

MR. ANGELL. So move.

VICE CHAIRMAN CORRIGAN. Second.

CHAIRMAN GREENSPAN. Without objection.

CHAIRMAN GREENSPAN. Let's move on to Peter Sternlight's report.

MR. STERNLIGHT. Thank you, Mr. Chairman. [Statement--see Appendix.]

CHAIRMAN GREENSPAN. Thank you. Questions for Peter? If not, would somebody like to move to ratify the actions of the Desk since the last meeting?

MR. KELLEY. So moved.

CHAIRMAN GREENSPAN. Without objection. They let you off the hook since this is a celebration of your last meeting! We now move on to Messrs. Prell and Truman.

MR. PRELL. I'm deferring to my colleague, Mr. Stockton, this morning in light of my absence through much of the period. He's more on top of the forecast.

MESSRS. STOCKTON and TRUMAN. [Statements--see Appendix.]

CHAIRMAN GREENSPAN. Are there questions for either gentleman?

MR. SYRON. Did I hear you say--this is almost an exercise at the margin--that if there were risks in either direction, particularly regarding employment, you think they might be on the negative side?

MR. STOCKTON. On the unemployment rate--

MR. SYRON. That's what I meant, on the unemployment rate.

MR. STOCKTON. There is probably some upside risk as we look at it.

MR. SYRON. So the risks wouldn't be center-weighted.

MR. MULLINS. You mentioned the housing starts figure, and I thought you mentioned that the permits looked pretty good.

MR. STOCKTON. What I indicated was that the permits for single-family starts in July inched up a bit but were only at their second-quarter average.

MR. MULLINS. Okay.

MR. STOCKTON. One wouldn't necessarily want to characterize them as--

MR. MULLINS. It looks pretty flat; maybe the multifamily [permits] were up a bit. What other evidence do we have? We've seen the big refinancing boom pick up in July again. How about actual purchases and starts? Do we have anecdotal evidence that we may be getting something going here?

MR. STOCKTON. The only other piece of anecdotal information that we have at this time is a preliminary August homebuilders survey which showed that their views about sales have moved back toward the levels of earlier in the year. So, they have picked up a bit. They didn't sag quite as sharply this spring as did starts and sales, but they moved back up a little.

MR. MULLINS. Okay.

MR. PRELL. On these July figures, I think last time in the Chart Show one of the exhibits I showed indicated that [the housing data] had been somewhat out of whack in the past several months. We were getting a much higher level of single-family starts than customarily goes with the level of new home sales we had observed. The level of starts in the latest month is well aligned with the permits--it had been running high relative to permits--and it's well aligned with the recent pace of new home sales. Our supposition is, though, that we are in a period when new home sales are rising. There will be some eating away of inventory. And attitudes are favorable for home buying apart from the concerns about the general economic environment. Certainly, home buyers perceive interest rates as being attractive. So we'll see permits and starts rising a little.

MR. MULLINS. The recent data on home sales really reflect decisions of a couple of months ago?

MR. PRELL. New home sales are reported fairly promptly after a sales contract is signed, but we don't have data for July. And there are slight lags; [sales are] a little behind when these lower interest rates should have had their effect.

MR. MULLINS. Thank you.

CHAIRMAN GREENSPAN. Governor Lindsey.

MR. LINDSEY. Dave, you mentioned some uncertainty about the unemployment rate forecast and, certainly, there is some. If we were probabilistic about this, what do you think the chances are that the unemployment rate will hit 8 percent?

MR. STOCKTON. Well, that's very conditional on what is likely to occur with overall activity over the remainder of the year. Eight percent, let's say, by the end of the year would require a pretty weak fourth quarter relative to where we are right now. But if you were to ask me whether that is a standard deviation away from the forecast we have here, clearly the answer would be "no."

MR. LINDSEY. I was trying to get a feel for your sense of the risks in the forecast. Whether they're balanced or not is one question; whether they're diffused or not is another.

MR. STOCKTON. Obviously, over the summer period we also have a bit of a difficult time, with the influx of teens in and out of the labor market, trying to pin down exactly where the unemployment rate is. We face that same uncertainty again this summer. So, in some sense there is a diffusion of estimates that always increases this time of the year and we are facing that as well. But I don't think there are any unusual risks to the unemployment rate apart from the fact that, as I mentioned in the briefing, the data that we actually have in hand right now show no signs of improvement in the labor market and are not signaling a step-up in activity. If you were to take that as a risk that we could be seeing just more of the same as we move through the second half of the year, I think there would be some risks that the unemployment could be higher.

CHAIRMAN GREENSPAN. Productivity is just doing too well!

MR. LINDSEY. Right, it leaves the less efficient workers unemployed!

MR. PRELL. The recent data have been favorable on balance for consumer spending. Car sales haven't been great, but retail sales have been good and orders for capital goods have been pretty good. There just isn't any reason to think that we are falling off from this somewhat erratic but generally steady trend of slow growth. We only have 2-1/2 percent growth [forecast] for the fourth quarter. If we were to fall short of that by a percentage point, the Okun's law relation would add only a touch to the unemployment rate. So, it gets back to what Dave has been emphasizing in terms of these uncertainties about the labor market relationship per se: What is happening with productivity and what is happening with labor market participation?

CHAIRMAN GREENSPAN. President Stern.

MR. STERN. Dave, while we're on this: What is your estimate of potential growth in the economy these days and how do you parcel that out?

MR. STOCKTON. At this point our estimate of potential would be 2 percent with roughly 1 percent in trend productivity and a 1 percent increase in labor input. That's a tad lower than where we were before we saw all the [unintelligible] revisions, which revised output growth down. So, we're just a little below.

CHAIRMAN GREENSPAN. Is there a tendency that that 1 percent might be higher?

MR. STOCKTON. On trend productivity? Yes, that's certainly a possibility, although currently when we're coming out of the business cycle trough--

CHAIRMAN GREENSPAN. We are? [Laughter]

MR. STOCKTON. --it's difficult to pin down what the trend in fact is. The good productivity performance that we've seen thus far in the recovery is not inconsistent with normal cyclical behavior if one were to assume a trend of 1 percent. That is in some sense how we infer what the trend is. But one could certainly say that at this stage we don't know how much of this restructuring is actually accomplishing some underlying improvement in trend productivity and how much of it is just simply using the existing work force more effectively as firms always do in a cyclical recovery. So, there's certainly a possibility that it could be better, but I wouldn't bet on it at this point. If one thinks back to where we were in the early '80s, coming out of that recession there was a tendency, I think, for many people to overestimate the improvement in productivity. There was talk then that the trend had improved to maybe 2 percent or in excess of 2 percent and it turned out to be a disappointment that as we progressed through the decade we didn't see that kind of improvement. So, I think it's always difficult when you see the good increases in productivity early on [in a recovery] to know exactly how much is trend and how much is cyclical.

CHAIRMAN GREENSPAN. President Jordan.

MR. JORDAN. In the last Greenbook you were more optimistic than private forecasters about long-term interest rates, though not quite as optimistic as what in fact has happened since the last meeting. On one side, given the sharp downward movement affecting intermediate- and long-term rates, I would have expected that to show through in economic activity. The other side is--at least from all the anecdotal reports I've heard and probably everybody is hearing--that there are more complaints about lower interest income to savers rather than [happiness about] lower interest expense to borrowers. Once again you have a projection that's more optimistic than private forecasters, [which is a view] that I share. I still think the 7.3 or 7.4 percent bond yield is much too high to be consistent with what is embodied in a [forecast of] 5.8 percent nominal GNP growth, [out] over a year and a half or so [unintelligible]. From this point how do you sort that out if we get a further substantial downward move in

intermediate and long rates versus if we get a significant backup and we give back what we've gained in the last six weeks?

MR. STOCKTON. I guess we'd come down pretty strongly on the side that we would imagine that lower intermediate- and long-term interest rates would be beneficial for overall activity. To be sure, lower interest rates always have an income effect in the household sector given that the household sector is a net creditor. But as I tried to indicate in my remarks, I think we have seen signs that the interest-sensitive sectors have responded to lower interest rates and would do so with greater force if rates were lower. I suppose a backup in long-term rates, assuming that the backup occurred for reasons other than purely inflation expectation reasons--

MR. JORDAN. Are you saying that even though this forecast is somewhat weaker--and I read it to be weaker than the last Greenbook--it is stronger than it would have been if we hadn't had the rally in the bond market?

MR. STOCKTON. Correct, and I think you can see that in the way that the forecast has changed. We have higher equipment spending in this forecast; we have some upward tilt now to net exports that we didn't have before and a little better consumer durables expenditures. But that has been offset in part by a bleaker outlook for the state and local sector and, given that we think the starting point here is weaker in some sense, weaker consumption outside of durable goods.

CHAIRMAN GREENSPAN. Any further questions for these gentlemen? If not, who would like to start our tour de table?
[President Boehne.]

MR. BOEHNE. I think "economic anemia" is how I would diagnose the Third District economy. Retailing is listless; manufacturing growth seems to be slowing; bank lending is soft. There is some activity in residential housing at the low end but not a lot in other areas. Commercial real estate has several more years of adjustment ahead. The District economy has settled into a slow-growth rut and the attitudes reflect that. People seem to think things will improve at some point, but the economy is just in that slow-growth pattern.

At the national level, it's very hard to find a sector that is going to act as an engine for a faster recovery. It's certainly not in exports; it's not in investment; it's not in consumption; it's not in government. I think we're just in a long, slow, corrective phase to the credit excesses and overbuilding of previous years. Clearly, as all forecasters are aware, this corrective phase will give way to faster growth at some point, but I think we need a lot of humility in forecasting just when that is going to be. My own gut feeling is that this corrective phase is going to last even longer than the Greenbook expects and that inflation correspondingly will be less than the Greenbook expects. I think the role of monetary policy in this environment is quite limited; we can stretch out the corrective phase, but we can't eliminate the need for it. If we get even slower growth than we have now or if growth appears to be heading negative, I think we would have little choice but to respond. But our options are really not all that plentiful at the moment.

CHAIRMAN GREENSPAN. President Parry.

MR. PARRY. Mr. Chairman, economic conditions in the West appear to have deteriorated further since our last meeting. Employment fell in June in all Twelfth District states except Utah. The number of jobs fell especially sharply in the state of California, at an annualized rate of 5.4 percent. And California employment remained weak in July, rising only slightly. California's budget problems are going to be yet another source of weakness in this troubled area. The implementation of the new budget--whenever it comes--will have a much greater negative impact than the stalemate itself. Most of the \$8 billion plus budget shortfall will be resolved through cuts in spending by state and local governments and schools, which will further weaken the state economy. Now, in addition to the \$8 billion plus [shortfall], we have a \$2 billion carryover from the prior year which is why in Part II of the Greenbook there is a reference to about \$11 billion. But there's another interesting point to be made, and that is that the estimate of the deficit for the current fiscal year is based upon a forecast that is old. They are going to be making a new forecast in a week or so and that's likely to show an even larger budget problem--probably \$2 billion above the current estimate of the problem for this fiscal year. There is a tremendous incentive for agreement in the next week so they don't have to deal with the \$2 billion problem that at this point is unofficial. Lawmakers from both parties are strenuously opposed to increasing state taxes, although fees at the state's universities have been raised substantially and some tax increases by local governments are possible as well.

Turning to the national economy, we continue to forecast a moderate expansion with most of the strength coming from sectors that are sensitive to interest rates and also to exchange rates. Our projection is somewhat stronger than that in the Greenbook, largely as a result of more inventory investment and also somewhat slower growth in imports. With activity continuing to fall below the economy's capacity, we expect further downward pressure on the inflation rate. In our opinion consumer price inflation is likely to fall from 3 percent this year to around 2-1/2 percent next year. While this scenario seems like a reasonable one, there clearly are downside risks to the real economy. As has been noted, the expected moderate expansion has seemed likely for a year now and has so far failed to materialize. Thank you.

CHAIRMAN GREENSPAN. What is the latest status of these vouchers or other IOUs that the state government is handing out?

MR. PARRY. Well, the problem now is that quite a few of the large financial institutions are unwilling to accept them. Consequently that means that some people who are receiving vouchers in effect have to stick them in the top drawer until they can be cashed in after a budget agreement or they can be given to an institution that will accept them or be returned to the state. For example, some businesses--I don't think this is very widespread--that receive money from the state because they sell things to the state are making their sales tax payments with these vouchers.

MR. BLACK. Including the 5 percent interest on them, I suppose?

MR. PARRY. Well, it depends on what the market is at that point. If they are just giving them the face value, then the state would in effect be picking up the 5 percent return.

MR. SYRON. Are they in M12?

MR. PARRY. I'm not sure where exactly they are!

MR. BLACK. Well, they ought to have some value on accrued interest I would assume.

MR. PARRY. Oh, they would. And the market, if you were to buy them, would reflect that.

CHAIRMAN GREENSPAN. If the state treasurer were smart, he wouldn't accept them; it's lousy paper! [Laughter]

MR. BLACK. That would seem a right unwelcomed message to send out.

MR. LINDSEY. Given that there's this large stock out there, does everyone come in and redeem them the same day? If so, where does the state get the money?

MR. ANGELL. They are interest-bearing notes.

MR. PARRY. Well, the budget agreement presumably raises funds to meet all expenditures, including expenditures now being made.

MR. LINDSEY. But the flow of that savings is over 12 months.

MR. PARRY. The only thing that's not in the budget as a revenue source I assume--and maybe it's being built in--is the accrued interest as these are held over a period of time. So, I think the money is there; there may be some timing differences. I don't see a problem unless I'm missing something.

CHAIRMAN GREENSPAN. President Keehn.

MR. KEEHN. Mr. Chairman, in terms of economic activity in the District, really there has been very little change since the last meeting. Some sectors are doing a little better but others not quite so well.

Much of the District's focus continues to be on the auto sector which has declined just a bit since the last meeting. The third-quarter production schedules, which earlier seemed pretty strong, have been reduced quite substantially, principally due to GM's cutback. Whereas originally the third-quarter schedules were set at about 18 percent over the third-quarter 1991 levels, they now have been reduced to about 11 percent [over the year-earlier level]. We would expect the effect of the auto sector, which earlier might have had an effect on third-quarter GDP of about 1 percent, to be reduced to about 1/2 percent. The fourth-quarter production schedules haven't been announced for all the manufacturers, but one I talked to has reduced its sales forecast for the fourth quarter from 14 million at an annual rate to 13-1/2 million. They feel in their case that the production risk is definitely on the down side.

Retail sales in the area continue to be very tough; merchandise will move but only at discounted prices. And the pricing techniques have become very, very aggressive. At least one retailer that I talked to had a pretty good early part of July; at the end of the month things turned sour and the lower sales levels have continued into August. Offsetting this, though, the steel business continues to be pretty good. The industry is operating at a rate of about 82 percent. One large Midwestern manufacturer is higher than that, at about 85 percent, and they now expect shipments for the year to come in at about 82 million tons, which in a comparative sense is not that bad a year. Part of the strength is based on lower imports. The industry, as you know, is involved in an effort to deal with tariffs, and that is having an effect; but also the export business has been pretty good. The heavy truck business also is showing some favorable signs. The order flow for Class A units has improved and customers for these units are feeling pretty good about their business. The industry expects to ship about 120,000 to 125,000 Class A units this year; that's up from 100,000 last year. Indeed, the current order rate is a little higher than that, and they expect the order rate to come out at the end of the year at about 140,000 units.

The residential housing business is also quite strong. New single-family home sales in the Midwest have been stronger than the national average. Housing starts on a seasonally adjusted basis, though down in the second quarter from an unusually strong first quarter, are still above levels for 1991. And given the reduction in mortgage rates, I think the attitudes about residential housing are pretty good.

In the agricultural sector, we've had a very significant change from the last meeting. We had plenty of rain in July and early August and at this point the crop outlook is really excellent. Crop prices reflect that; they're down quite significantly. And that negative effect on farm income is showing up in the sales of agricultural equipment. That industry is really having a very tough year: For example, year-to-date sales of 4-wheel drive tractors are down 37 percent; sales of large tractors are down 32 percent; and sales of combines are down about 36 percent. So, production schedules, which had already been reduced, are being reduced further. One large manufacturer expects that their fourth-quarter production schedules will be about 20 percent lower than last year.

On the inflation side, the news continues to improve. Upward price pressures just aren't part of anyone's thinking. Large manufacturers are putting tremendous pressure on their suppliers. In many cases, they are holding [down] price increases on their purchases to very low levels and in a couple of cases they actually are getting reductions. The pattern of prices on purchases over the last two or three years really has been very, very favorable.

While in an economic sense, in terms of the indicators, the news in the Midwest and indeed nationally is a bit mixed, I must say that I think there has been a deterioration in mental attitudes. Many of the people I talk to seem awfully grim. The uncertainty and the negative outlook are beginning to creep into business thinking and, therefore, I think the risks here are a bit on the down side. Using the analogy of the slow takeoff--and I think we've been experiencing this slow takeoff for an awfully long time--my worry is that we're

reaching the end of the runway. And in a policy sense, I think we better push forward on the throttle until we're sure we are clear off the ground.

CHAIRMAN GREENSPAN. President Forrestal.

MR. FORRESTAL. Thank you, Mr. Chairman. We've seen some slowing in the already modest pace of recovery in the Southeast, and the anecdotal information has become even less encouraging in recent weeks than it had been. The litany of bad news would go something like this: Consumer spending was not as strong in July as in previous months and auto sales in particular, which had shown some improvement, have been quite mixed in the last several weeks; manufacturers are reporting that both production and shipment levels have plateaued recently and fewer firms are reporting increases in new orders and shipments; and bank lending is very weak, and [the explanation] is on the demand side basically. Incidentally, on David Mullins's question related to mortgage financing, the anecdotal information available to me would suggest that while there has been a great spurt in refinancing in the Sixth District, very little of that is going into new home purchases. Growth in home sales and building has decelerated, as I've just indicated. Multi-family and commercial construction remain pretty grim; they're in the doldrums. One bright spot--and perhaps it's the only one in the District--is that business travel and tourism are up; that's basically in response to the airfare price wars. But that, of course, is coming at great expense to the airlines, which are a significant employer in the District. Foreign travel continues to be pretty good, too, as a result of the lower dollar.

So, in general, a slowdown appears to be in train in the Sixth District. While some optimism was evident just a few months ago, attitudes about the future have become quite negative or, to use the words somebody else just used, quite grim. Business people are seeing growing evidence of caution among consumers. And among consumers, there's a belief that the ongoing wave of consolidations and cost-cutting will lead to further layoffs even in industries that had been perceived to be recession-proof. So, in this environment very little business expansion is being planned in the region.

With respect to the national economy, like many others, we too have lowered our forecast for GDP for 1992. We do see a little stronger near-term growth than the Greenbook but not the acceleration that the Greenbook has for 1993. Our estimate of unemployment is around 7 percent at the end of next year; and consistent with that outlook, we've lowered our inflation numbers as well. On balance, it seems to me the risks to the forecast are now skewed to the down side. There is a lack of confidence out there and it goes beyond the political uncertainties; and that can further restrain consumer spending in the future. On the export side, perhaps we're getting some help from the weaker dollar, but growth among our major trading partners could fall short of the forecast given the policies that some of our trading partners appear to be committed to.

Since we have lowered our forecasts for both real GDP and inflation, it seems to me that perhaps it's time for us to reconsider our policy as well. To be sure, there is a lot of stimulus in the system, measured by almost every measure except M2. But we've seen

over the past year or longer that it is taking more easing than we had expected to achieve any results. So, I'm of the opinion, Mr. Chairman, that we should at least be open to considering a move toward ease. The excess supplies of resources at this point make me doubt that a significant acceleration in growth would lead quickly to increased inflation. Having said that about moving toward ease, I also recognize that this probably is not the week to do it.

CHAIRMAN GREENSPAN. President Syron.

MR. SYRON. Thank you, Mr. Chairman. Unfortunately, I think we're in an increasingly interesting situation here. As far as the District goes, in New England--consistent with what other people have said about their parts of the country--we had a little buoyancy before we lapsed into a softer state. It's hard to separate all the factors that are involved--there are always special factors--but there is no question that there's less buoyancy than before. We're not sinking fast, but there's certainly an increase in people's uneasiness. Some of this may be related to weather. The retail sector has been soft after some earlier encouragement; tourism is not very good. The mood is very gloomy, particularly as we get increased announcements of layoffs and further restructuring in employment. The tone of the labor market seems to have softened more recently, even I would say in the health care sector, which is one area where there had been significant [employment] increases. Looking at the manufacturing sector, the source of strength before was exports and to some extent [unintelligible] supplies for autos, but those are softening now. In housing, there is quite a lot of refinancing activity and some marginal improvement in ordered housing--certainly not houses built on speculation--but not very much.

The banking side is interesting. Our institutions have improved their balance sheets a fair amount and they are taking a more active stance toward encouraging loan demand. But they're not finding very much demand. I think some of it may have to do with the need to adjust pricing terms to get back to a longer-term equilibrium. Loan officers and many senior managers complain of still overly cautious borrowers; but really we just are not seeing very much demand. On that score, just as a side point, it was interesting to look at some data: When we pulled out New England from the U.S. data, our region contributed a fair amount to the softness in loan demand in the Northeast and also to the employment problems.

As far as the U.S. economy goes, I'm finding myself in broad agreement with the Greenbook. But if we look at previous forecasts over a substantial period of time, there has been a negative correlation in our errors. There's no question that at some point this will turn, but one never knows when that turning point will be. Now, I'm not critical of the forecasting process; changes are the [essence] of its nature. But when I look at what is going on, I simply don't see any cumulating strength at all in the economy. In different periods we see a little contribution from housing or exports and in some cases manufacturing, but nothing that really is coming together to accelerate into a consistent recovery. All of this is consistent with the notion of all the obstacles in this long, long cycle readjustment that we have, which many people have talked about. Another aspect to this--and I think it's why employment and what happens on the employment rate are key--is that people are writing

down their human capital as well as their physical assets. With each announcement of further restructuring they say: "Well, you see this new [unintelligible] you're talking about, what am I going to do longer run?" And in my own mind that makes it more difficult for us to have any estimate of what their equilibrium or desired liability structure is going to look like and to know when the saving rate is going to return to what they think is a "normal situation." People are very much in flux on this as they watch what is happening in the employment markets. For that reason, I really have concerns--not about the technical aspects of the forecast but looking at the forecast from a broader perspective--about how even this wretched and anemic forecast that we have can hold together. For example, a concern I have is that we think productivity will be a little stronger and we see a lot of continued impetus for restructuring, so the unemployment rate may well increase. As the unemployment rate increases, that is going to have an effect on people's view of their welfare and it could contribute to a further increase in the saving rate. Thus, I'd say that the outcome risks are slightly on the down side, though maybe not in a pronounced way. And certainly in my own mind the costs of an error one way or the other are much greater if the error is on the down side.

The second reason to question whether this forecast can happen--and there's nothing we can do about this--is that if you look at the broad society and the body politic, there is an increased impetus from either party for some sort of fiscal package, which is almost certain to be counterproductive in a long-run sense. I just think as we get into next year, regardless of who wins the election, that there's going to be an enormous amount of discontent with people saying they are just not going to accept a situation where we have very slow economic growth. There are a lot of people who are very, very concerned about their economic welfare in the long run. I'm not sure what we can do about this, but I see a lot of stimulus for [politicians] to develop fiscal packages, and that's a concern I have. I don't think our policy has been inappropriate; I think it has been appropriate. But I believe we're in a very, very tough situation; indeed, it's what I consider in a broader sense perhaps a somewhat unstable situation.

CHAIRMAN GREENSPAN. President Hoenig.

MR. HOENIG. Our District continues to show sluggish growth in most sectors except for real estate construction in some areas. As for the farm economy, it's stable but as you've heard elsewhere prices are down and that is bringing the prospects for our ag sector toward the down side as we go forward; there may even be a decrease in [farm] income depending on what the near-term future holds. Manufacturing in our District is flat. The aircraft industry is feeling the effects of slumping foreign sales. Our auto industry is not pushing production at all and that is showing through. In energy, we have had some pickup in the rig count, but that is a very sluggish industry and we are not going to see much economic activity coming from that sector. As far as the real estate area goes, our residential sector does show some strength. There is a considerable amount of refinancing. But we are also seeing new construction in some parts of our District, particularly in Denver where what is almost a boom situation in residential housing gives us some pause.

I would add a couple of anecdotal points. We have talked with bankers in our region and we also hear and observe that the problem is not that they are unwilling to make loans but [that there is little] demand for loans. But that is a very unique situation. Beyond that, though the banks will say demand [is the problem], where their [loans] have picked up or they want to add [loans], they have changed their underwriting on the margin--how many guarantees and how much collateral they require. In one instance when they did that we observed that they were able to add significant amounts of loans, some of it taken from other banks who wouldn't change their underwriting. I'm not talking necessarily about throwing out all caution, but just that some changes will make a difference. I think banks in our region as they anticipate the need to bring their capital levels up are keeping their underwriting standards higher than they might otherwise and are trying to build those capital levels; and it is showing through in terms of the level of their lending activity.

As far as the national economy goes, we have some differences with the Greenbook quarter-to-quarter, but overall our GDP projections are now similar. We've adjusted ours down and we've adjusted our inflation expectations down as well. I see the national economy, with the things that are going on right now, in a sluggish mode, and as I listen to comments here I think we can anticipate further sluggishness. The situation does in fact suggest that perhaps we need to take a more forceful action.

CHAIRMAN GREENSPAN. President Black.

MR. BLACK. Mr. Chairman, a while ago Si Keehn's analogy of an airplane reminded me of another mechanical analogy that I think is very pertinent here. In the days when we first began to install antipollution equipment on automobiles I used to get terribly frustrated trying to get the car started and running very smoothly. I've been experiencing the same sort of feeling about the economy with its fits and starts and near stalls. But eventually we usually did get the car to run pretty smoothly, and I'm satisfied that sooner or later we're going to have the economy moving up at a smoother pace. But I do think the downward revision that the staff has made in the forecast over the remainder of 1992 is clearly appropriate in view of the lackluster growth we've had in the economy since the end of the first quarter. My guess is that the risks of errors are about evenly divided between the up side and the down side. On the down side, for example, many of the factors that have been plaguing us in the recovery in recent months--such as the negative impact of this corporate restructuring, which I think augurs well for the long run but is terribly painful in the short run--are still around. But it does mean increasing efficiency in the long run. And I think the rise in productivity probably means a higher long-term growth potential than the 2 percent the staff is estimating. We also have the slowing in defense expenditures; we have situations abroad where the economies are not really growing very fast; we have the oversupply of office space and other commercial real estate. And maybe even more important in the minds of the consumer, there are a lot of non-economic worries such as crime and drugs and the breakdown of family values that I think have been making people less inclined to part with their dollars than they otherwise would be. I believe this sort of thing is going to be with us for quite a while and is going to exert a drag on economic activity in the period ahead, and the weight of the drag

could even increase. Of course, in addition to that we have the weakness in M2. We've explained a lot of that, I think, but I still have a nagging worry that there's some weakness there that we're really not explaining away by these special factors.

But then one can look at the up side of this and say that there are at least some signs now that this might turn into a typical recovery--albeit a much less rapid recovery than we've usually had--because of the decline in interest rates, which eventually I think is going to stimulate housing. My expectations got a little setback with the data released this morning. Certainly, sales of durable goods at the consumer level and also of producers durable equipment are going to be one of the stronger parts in the recovery when it comes. And that, of course, will stimulate jobs and economic growth. But having said that, I think it is important for us to recognize that there's a big downside risk and it's very serious. I'm getting at the same sort of thing that Dick Syron was talking about a while ago.

If these reduced Greenbook expectations turn out to be true, this could be pretty serious in terms of jeopardizing our strategy for getting to our long-term objectives. We need to give that some consideration in our setting of short-term policy goals today. Now, in the case of the long-term objective, I think the staff's estimate of the inflationary outlook is [about right]; we will certainly be moving closer to our goal by the end of 1994. That's obviously very encouraging to someone who thinks that the prime goal of monetary policy ought to be price stability. But in the context of the staff's outlook, it seems to me that this further progress is dependent upon continued sluggishness of any projected recovery even as far out as the second half of 1994. Maybe this continued softness is necessary in order to get inflation down further. But my own guess is that we can get the same kind of inflation results with stronger real growth in late 1993 and in 1994 if we maintain a visible commitment to our long-term objective of price stability, despite the current weakness in the economy. And I think we ought not miss any chances to say that that is our ultimate long-term goal even though we recognize that we have some short-term problems on the side of weakness in the economy right now.

CHAIRMAN GREENSPAN. President McTeer.

MR. MCTEER. There was a definite shift in the Eleventh District economy between the first and the second quarters, both in terms of economic activity and of mood. Measuring economic activity in terms of employment growth, in the first quarter of this year our employment was growing faster than the national average and in the second quarter employment was shrinking and not keeping up with the national average. We have shifted from being a source of strength to the national economy to being a source of weakness. As for mood, in conversations with directors, bankers, and business people there is the definite sense that all is not well with the economy, although most people are not urging further ease of monetary policy. I believe the view is that monetary policy has done its thing; it hasn't been very effective but we don't find many people thinking that further reductions in short-term interest rates will help very much. That's their view on the one hand, but in addition to that there is increasingly the cry from those who are aware of lower interest income and the impact that is having on a significant segment of the

population. On the question of mood, let me say that I've been around a number of bankers recently, more than usual, and I'd just like to report that they are a very unhappy, mad bunch of people. They feel beleaguered--especially the small banks. They recognize the FDICIA legislation as punitive legislation and they are really dreading the regulations that are going to come out of that. And they don't see any light at the end of the tunnel; they feel that they're in a business that is going down the toilet and nobody cares. Their numbers in the context of measures of health of banks are improving in the District. But after all these years of recovering they still aren't lending; they're still shrinking their lending [activity]. And I guess they're turning into bond funds; they're riding the yield curve right now.

CHAIRMAN GREENSPAN. President Stern.

MR. STERN. Thank you, Mr. Chairman. With regard to the District economy, I don't detect any underlying change in activity; I think it's still expanding quite modestly. There really isn't a lot of additional information to add to that. I might comment on a couple of recent developments to flesh that out a bit. I reported before on very strong sales along the northern tier of the District to Canadians coming across the border. That currently is in the process of slowing down, apparently because the Canadians are making it more onerous to get back into Canada with everything that one has purchased. But that was due to change for one reason or another eventually, and it has. There is a significant expansion in the paper industry under way again. A couple of new plants have been approved and construction will start shortly if it hasn't already. Finally, you've probably heard about the so-called "mega mall" that has opened up in the suburbs of the Twin Cities. It actually opened about a week ago. So far, it has exceeded expectations--at least the expectations of those of us whose expectations weren't too high. I haven't been out there, but the press reports that traffic has occasionally exceeded 100,000 people a day. There have been lines to get into the restaurants and some of the other entertainment venues and so forth. Whether anybody is buying anything beyond that I don't know, but at least by some measures it's off to a positive start.

With regard to the national economy, I'm certainly comfortable with the contours of the Greenbook forecast. It's always difficult in a circumstance like this, when you try to do bottom-up forecasting and look at consumption and investment and so forth, to talk yourself into believing that any of these sectors is going to be very strong in this environment. Yet my experience has been that just when I've talked myself into that, the economy surprises me on the high side. I have a hunch that isn't going to happen this time. Bob Black gave a pretty good litany of the problems that are restraining growth, and I think those are in place. For what it's worth, my guess is that it will probably take longer for those to diminish than we might expect. So, the general shape of the forecast portrayed in the Greenbook looks like a pretty good estimate to me. The good news, of course, is that the price and cost statistics are starting to come in more in line with the anecdotal reports we've discussed around here for quite some time. It seems to me that we've commented for quite some time that we have talked to a lot of business people and don't hear much about price or wage pressures and so forth and so on. It took quite some time for that to show up in the statistics. But now

it is at least starting to show up in a more convincing way, which suggests that we're making some progress in a principal and significant area.

CHAIRMAN GREENSPAN. President Melzer.

MR. MELZER. In our District I would say that the same shift that Bob McTeer described has occurred statistically. We are looking now at June numbers and I would describe the situation as one where we've had modest employment growth, manufacturing more or less flat or maybe slightly negative, and nonmanufacturing offsetting that. For the most recent three-month period, we actually have nonmanufacturing [activity] flattening out and modest employment declines. I would say that one of the areas in nonmanufacturing that is particularly weak from an employment point of view is construction and that's reflected in contracts--residential as well as nonresidential--although compared to a year ago we're still up very significantly in the residential area. Anecdotally, it's hard to place in time when some of this was detectable; it may have been a couple months ago. But basically I don't detect any major shift in sentiment toward the negative. I spoke with a handful of CFOs of some of our major companies, and in the retailing area the description I got was the same as what was mentioned earlier--I forget by whom, maybe Si--that the first couple of weeks of July were very strong and then sales slowed and [the slowdown] seemed to continue into August. The retailer who passed that along said to me that they're not sure but they think the Olympic coverage may have had something to do with that; he likened it to the CNN effect to some extent. Another retailer described things as generally volatile. Every time they think things may be coming together they have a downturn. From a profitability point of view, the largest of the retailers I've talked to had just reported a very strong quarter and they got it basically by controlling costs. On the manufacturing side, a major electrical equipment manufacturer described their consumer-driven business as very strong. They, too, reported very strong earnings, largely again a contribution of cost controls and so forth. I did talk to a chemical manufacturer as well; a lot of their chemical business is driven by the auto business and housing and that has been generally sluggish, with no particular signs of strength there. The capital goods side is described as sluggish, basically. Order backlogs are holding up but not growing very rapidly. So, the general picture I get from business people is that the environment hasn't changed dramatically.

With respect to monetary policy--just picking up on some of the comments that have been made, particularly Ed Boehne's in terms of what the role is for monetary policy in this sort of environment--I agree that monetary policy can't solve some of the structural problems that we're dealing with. And at least in my view, whether you look at interest rates or reserves, we're pursuing a very easy monetary policy right now: Short-term real rates are negative and reserves over the last two quarters have grown at almost a 17 percent annual rate compared to a four-year trend of about 4-1/2 percent. I know it's a very difficult period in which to get a handle on the thrust of monetary policy, but I think there's a lot of danger in focusing just on the real economy as our guide for what we ought to be doing--and that seems to be what is happening--and not trying to look at policy from some other perspectives. I think we've had some warnings in the

foreign exchange markets and in long-term credit markets from time-to-time depending on what statements are made--albeit those rates have come down--that we may be testing the limits of our credibility. And we could well find ourselves in a situation here given the season--and I gather some people are looking at the same facts and coming out a different door--where we're going to want all the credibility we can get. If we don't have any, since we're the only game in town in that respect, we could have some very serious problems.

CHAIRMAN GREENSPAN. Governor LaWare.

MR. LAWARE. Mr. Chairman, I'm increasingly concerned about what I view as the continued deterioration of the economic psychology of the country. I believe that psychology creates the conflicting signals which in turn contribute to the sluggish rate of recovery in which we find ourselves. Banks continue to be chary of aggressive lending, but their role in a more dramatic growth rate is also constrained by a very slack demand for credit by both consumers and businesses. Consumers, or at least a lot of them, are frightened and very cautious about taking on more debt to step up consumption. Businesses are still involved in balance sheet restructuring to equitize debt or refund debt to reduce debt service [costs]. That posture will not change until demand creates confidence in inventory production and capacity expansion. And perhaps more fundamental than any or all of the above is the sense of the country that we are adrift: That we are in an election year in the midst of domestic and international issues which differ from those of a few years ago and perhaps are more worrisome. Stubborn political and humanitarian issues both at home and abroad are frustrating because the diplomatic, economic, and military tools we might have resorted to in the past no longer are particularly applicable or available, especially in the absence of fiscal ammunition. And neither candidate has yet given us a clear idea of how he would approach the final solution to these problems.

In these circumstances, I believe monetary policy is at a juncture similar to the doctor who has moved his patient into intensive care, shot him full of antibiotics, given him multiple transfusions of whole blood, has an intravenous going with glucose, and is assisting respiration with shots of pure oxygen. The doctor can now only wait for all of that to take effect. Further intervention will probably not change the outcome. Patience is prudent and patience should be our watchword for now.

CHAIRMAN GREENSPAN. Governor Kelley.

MR. KELLEY. Mr. Chairman, the last meeting turned out to be a little traumatic for me. After holding forth at some length, I reversed myself less than 24 hours later on a discount rate vote. So today I'll just try to throw in a quick speculative thought. It seems to me that we're clearly in the same pattern that we've been in for some time now: a slow, struggling recovery that has been severely inhibited by the financial restructuring in both the financial and the nonfinancial sectors. To me so far--I would emphasize "so far"--this recovery has been going along at a pace that may be a bit disappointing; nevertheless, it's still acceptable because it seems to me that the long-term health of the economy demands that we get this restructuring successfully accomplished. In my view this financial

restructuring was going to happen and it could have been a great deal more traumatic than it is given the way things have evolved so far. I think we may be able to see in retrospect that monetary policy has been very effective indeed over the course of this era that we're in rather than ineffective as some have alleged.

Two things seem to be evolving and I'm hearing both of them around the table this morning. One is that the timing of this breakout to a higher level of growth seems to be getting stretched out. The second quarter was weaker than a lot of us had hoped it would be; the third quarter now looks as if it will be weaker than we had hoped, too. I think most of us are reducing our forecast for the fourth quarter. We haven't started lowering the first-quarter forecast yet, but we'll see about that! The second point is that we may be making more progress on inflation than many of us had ever dared to hope. Year-over-year [measures of] the CPI began to break around year-end 1990 and the first quarter of 1991 when we went through that recession period. The core CPI in the year 1990 according to the Greenbook was 5.3 percent; and the Greenbook projects 1994 at 2.5 percent even considering two back-to-back 3 percent growth years. So far, the history has been that in the first quarter of 1991 year-over-year the core CPI was at about 5-3/4 percent; now it's at 3-3/4 percent. That's a 200 basis points decline in the core rate of inflation over 18 months, and I think that's pretty impressive. Clearly, the very slow growth period and the increase in unemployment and the concern in the country that we've been experiencing has had an awful lot to do with that. Trying to put those together looking forward, it seems to me that if this sluggishness does continue to stretch out for a very long period of time, we may need to ask ourselves if we are beginning to be in danger of our disinflation trend overshooting and actually becoming a deflation, which could conceivably have pretty serious downside implications. I continue to believe that it's very important that this financial restructuring be completed. A great deal of progress is being made and I'm comfortable that our policy so far has been about right. We've been doing pretty respectably at balancing the needs for a lot of this restructuring to work through and still have as healthy an economy as possible. But having said that, I think this period does have to come to a conclusion at some appropriate point lest it start to feed on itself with some serious downside potential. That could turn out to be the issue that we're going to be grappling with a little later in the year, though probably not just yet.

CHAIRMAN GREENSPAN. President Jordan.

MR. JORDAN. Well, after listening to Bob Parry's report, it sounds as if I chose a very good time to leave California! It also turns out to have been a good time to go to the Midwest. If I were to go through and talk about sectors and industries we've been in contact with, it would sound very similar to what Si Keehn has said. There's really no difference there. The manufacturing area is doing quite well, much better than the nation as a whole in terms of employment. Industrial production, whether it's trucking or auto-related, is doing well. Residential housing, which I think is related to people's confidence and jobs, is very positive. Some areas in east Kentucky that had suffered very greatly for a long time in the '80s have virtually boom conditions now, with 4 percent unemployment, and are doing quite well. Agriculture had come through two very bad years and

farmers were very worried coming into this season. But we're getting such good volume numbers that it's dominating the price effects, and even the ag sector bankers are much better these days. In spite of all of that, attitudes remain lousy. When I confront individuals, especially nonbank business people but to some extent the small bankers as well, and ask why, they keep telling me about good numbers and then complain. They cite the political situation, mainly at the national level but sometimes at the state level. Companies continue to report: "My numbers are good, my orders are up, my sales are good, I've cut my costs, my profits are at a record, and I feel lousy about it." And they don't see much that can help them.

I have been struck by the difference in attitudes about inflation between the bank and the nonbank sectors. The nonbank side tells us that inflation is simply not an issue. Large and small businesses are saying that they have no expectation of raising their prices. It's a question of what the smallest declines are that they can get away with and if they can match the price pressure they're feeling with productivity gains and other cost reductions. One major company advises a great many smaller companies in the District and nationally and has told them all that any well-run business can reduce its prices by a percent given the gains in current productivity. They say they only want to buy from well-run businesses, so everybody should come in with bids that are no more than 5 percent less than before or else they shouldn't bother bidding. The bankers, though, continue to worry about inflation. Whether they're citing declines in short-term interest rates from easy policy or the fiscal side, which is more often the case, they're persistent in believing that inflation is heading back up and, with that, interest rates. When I asked if there was anything we could do to persuade them differently, they said "no." They're just not willing to be persuaded. The bankers will tell us that commercial loan demand is weak but consumer loan demand, especially for auto financing, is very strong throughout the District.

One of the positive things that I see happening in the adjustment process is that bankers in their search for lending opportunities are finding some very innovative ways throughout the District for doing minority housing lending, including enlisting the clergy as loan officers--conducting seminars and teaching them how to evaluate people's financials--and then making contributions to the religious organizations for every loan that is based on that. They also are reducing the amount they contribute on a formula based on delinquencies or default. A lot of volume is being generated by the activity, with a lot of good sentiment developing in the communities about how available the bankers are for exploring opportunities to do that kind of lending.

One major home improvement supplier said that we have a national boom going; people who aren't doing anything else are apparently remodeling their homes. And that is consistent with a story that I could take as another very positive development. There was an article saying that people, in a search for alternatives to what were characterized as the lousy yields one gets at the bank, in addition to doing home improvements are trying to start up new businesses. They gave a lot of examples of people opening restaurants or engaging in other distribution-type or light manufacturing activities because it's better than just leaving the money in the bank

earning 2 percent. And I would think that that is part of the adjustment process we would expect from price stability.

CHAIRMAN GREENSPAN. Vice Chairman.

VICE CHAIRMAN CORRIGAN. I'll start out by saying that while I agree with a lot of what John LaWare said, I'd make an argument that at the very least the patient is out of intensive care. I think we have made some progress. As far as the national outlook is concerned, our people see it pretty much as their Board staff associates do with the one exception, as has already been discussed, being the unemployment rate. And that, as has been suggested, is probably a crapshoot. Our people have it more in the 7-1/2 percent range at the end of next year. But the point is that regardless of whether it's 7 percent or something north of 7 percent, even taking the Board staff's forecast means nine consecutive quarters in which the unemployment rate will have been 7 percent or higher. There have been multiple comments about the gloomy atmosphere and, obviously, that [unemployment rate] in itself has a lot to do with it. A number of people have directly or indirectly touched on what is called a very broad political landscape; undoubtedly that has something to do with it too. But whatever weight one wants to put on those or other factors, I think the tone is pretty darn sour out there.

In terms of some of the underlying issues, the budget outlook even without any new magic is actually worse in the out years; on the basis of these latest figures some of that obviously reflects the level of economic activity itself, but it's not just the level of economic activity. A number of people have said that the inflation outlook is better; it is. A number of people have also said that price increases are not on the horizon or the radar scope for anybody, especially in manufacturing. I guess that's true except for the auto industry. I never quite understand those guys!

On the anecdotal side and the District side, I wish I had some brilliant new insight to offer but I don't. It's really just more of the same. I do think, as everybody has said one way or another, that we have this Catch-22 situation: Productivity is better, profits are better, and costs are better; but in part because those things are better, employment is worse, income is worse, and attitudes are worse. I think that to a very large degree is a result of cumulative pressures. My own sense of it, trying to put it all together, is that on net the risks are about balanced. That's about all I have to say, Mr. Chairman.

CHAIRMAN GREENSPAN. Governor Mullins.

MR. MULLINS. I would agree with the notion that has been expressed by a number of people that we're probably stuck in the same old ditch for a while, rocking back and forth trying to gain the momentum to escape the gravitational pull of this deleveraging phenomenon. I don't really have a serious argument with the Greenbook, although there is the question of the timing of our escape from this. I do wonder whether or not we are in a lurching pattern with two steps forward and one step back as opposed to a steady progression and gradual acceleration. I don't know how to write down a lurching pattern in the forecast. That's the difficult part, so I wouldn't argue with that. I tend to think the next lurch is likely to

be a bit forward, although I'm not so certain about that given the political climate. But I wouldn't be surprised to see third-quarter [GDP growth] a bit better than 2 percent following the reduction in long bond rates and our [interest] rate cuts. We have another round of mortgage refinancing going. Even if housing activity hasn't picked up, we've already seen some revival of retail sales, especially the discretionary GAF category. So, we might have a little better third quarter than the Greenbook projects. I still think we are likely to be stuck in the range of 1-1/2 to 2-1/2 percent growth for the foreseeable future until these balance sheet adjustments are sufficiently far along to allow sustained growth in spending or until this upward ratcheting process pushes employers beyond the limits of increasing production hours and overtime and into some hiring and some income growth. We continue to have the logic of pent-up demand waiting allegedly in the wings to be unleashed. But on the other side we also have the risk of cautious consumers increasing their saving rate. At this stage we have very little rigorous insight into how long we will be stuck in the sluggish growth rut or the trajectory on which we will emerge.

We are getting some G-7 companionship, as Ted mentioned, in this condition. Some countries are climbing out of recession into sluggish growth and others are descending from healthy growth. It is interesting to see the process of convergence among the G-7 nations with real growth in '92 converging in most countries to 1-1/2 percent, inflation at around 2 to 3 percent, and unemployment in the 8 to 10 percent range. And just as we have no U.S. sector to provide an engine, we seem to have no G-7 country as an engine. Fortunately, we're making progress on that, which might be useful at the margin.

Focusing on the near term, I do think we have another shot of stimulus in the pipeline as reinforced by the reduction in the long bond rate, which has descended barely through the lows of early January. The dollar has also descended. So, near term we have some stimulus. This could be just another pig in the python working its way through the system which, once digested, will leave a hungry economy in need of another feeding. That is the Arkansas version of the Chairman's seize-up model! [Laughter]

MR. LAWARE. They have pythons in Arkansas?

MR. MULLINS. They have a lot of pigs! [Laughter] So, it's unclear at this stage whether that is what is going on or whether we are getting on a more stable recovery [path].

I do agree that the disinflation trend is starting to take hold. Two years ago, as I mentioned last time, the unemployment rate was 5-1/2 percent and manufacturing capacity utilization was 83 percent. Unemployment didn't break out of the 5 percent range until the fourth quarter of 1990 and capacity utilization didn't break below 80 percent until the first quarter of 1991. So, we've had about a year and half of this slack and I think it's taking hold. We see it not only in the numbers on wage inflation and the CPI and PPI, but we see it in consumer attitudes. I think there is a new ethos of bargain hunting which has reflected on business in a healthy way. I would agree with the comments that businesses are gradually, and I would say grudgingly, accepting cost-cutting and productivity improvement as the status quo and a steady-state approach to business, rather than

restructuring and a brief painful period followed by price increases as the way to go. So, I think that is good news. Commodity prices also continue to exhibit no signs of price pressure. Gold attempted a brief breakout recently, you might have noticed, but then collapsed. I think we're likely on the threshold of some real progress here and, again, the reduction in long-term rates suggests this as well. I would point out, though, that despite the consumer bargain hunting, inflationary expectations among consumers as expressed in surveys such as the Michigan survey have not come down much. Those expectations are still very high in the 3 percent range, at around 3.9 percent. And the 5- to 10-year inflation expectation is about 5 percent, so that's still relatively high.

In terms of the market view of inflation, our 10-year rate, which is the international long rate, is now only 6-1/2 percent. It's 150 basis points below the German 10-year rate of 8 percent and that looks pretty good. Unfortunately, the 10-year rate is influenced by the shape of that yield curve and is heavily weighted by the short-end rates included in that. So, our 10-year rate is weighted down by the short end; the German rate is weighted up by their short end. If you look at the 1-year implicit forward rate 10 years out, the German rate is about 7-1/2 percent and ours is about 8-1/2 percent. So, our 10-year forward rate viewed at the end of that 10-year period is still about 100 basis points above the German rate. So, on consumer inflation and in the capital markets we may have a ways to go.

I think it would be interesting to try to assess the current stance of monetary policy. While that's interesting, I don't have much insight into it. There's not much new to say. I view real short-term rates as low, as around zero. I wouldn't quibble with a view that they were marginally negative. If we do get more progress on inflation expectations, we may revisit that issue to see whether there isn't a case for an adjustment of nominal rates, but I would not make such a case now. M2 in the current environment is very little help. We have attained some insight into the distortion caused by the yield curve, and it seems to me we can adjust analytically for that distortion by in effect adding back the M2 that has been pulled out of the yield curve to see what a corrected M2 would look like. If you do that exercise, you find that this corrected M2 still has been growing probably at 2 to 2-1/2 percent since the fourth quarter; it's still near the lower bound. So, that distortion does not explain all the slow growth, nor would I believe that all that disintermediation yield curve effect is benign. I think it may have some impact. The credit channel I believe is important, not just the money channel. You can also, of course, just add back the growth of the [institution-only] money funds; that would get M2 growth up to about 4 percent. When I look at those figures I don't see a case [for arguing] that we're too easy in those terms. A more direct approach is to look at nominal GDP targeting; we have been experiencing and are projecting very low growth in nominal GDP. Still, it seems to me that it's very hard to make a case that there's compelling evidence the economy is constrained by an overly restrictive monetary stance or lack of liquidity or rates that are too high. So, I think it's quite difficult to gauge effectively the stance of policy. Perhaps this does lend credence to the Chairman's alternative model of an economy responding to liquidity shocks rather than to a stable relationship with the monetary stance in a traditional sense.

The other thing I would say is that in this environment I would agree with those who continue to argue that there are concerns about going too far. I don't believe we have the ability to pursue aggressive fine-tuning effectively or to respond to a blip in the unemployment rate and avoid a bad quarter. That may sound odd since we've come from 10 percent down to 3-1/4 percent on the fed funds rate; that sounds like contra-cyclical policy. But I think the economy in the late '80s was growing rapidly, fed by debt and leveraging; and that process went into reverse to deleveraging and financial contraction. And it's wholly appropriate for the nominal rate structure to decline dramatically just to maintain an appropriate stance of monetary policy, which is not overly restrictive but is still consistent with progress toward price stability. I think that is what we've done in that adjustment. We haven't yet gone too far. If we do go too far, with the long and variable lags in monetary transmission mechanisms and the unreliable navigational aid of M2, we obviously risk losing an opportunity it has taken years to earn. So, that's something to be wary of.

A final reason to be concerned about our near-term policy is the long list of potential shocks and risks in the current environment. Bob Black presented the litany of restraints. I'd just like to mention some of the potential shocks and risks. We have military situations--potential military action in Iraq and Bosnia-Herzegovina--fragility in markets in Japan, weakness in the economies, markets, and foreign exchange relationships in Europe, and in the United States we have the dollar, the election, and of course the stock market. Moreover, I'm not at all sure we are completely out of the woods with regard to some of our large financial institutions. So, one argument is that these are downside risks to be concerned about; another is that we might save a little ammunition. Overall, the early returns on the July move are encouraging, especially in terms of the response of the long-term rate and another round of refinancing under way, which can help reduce [financial] burdens and accelerate the adjustments. I think we should continue to learn about this unusual economic environment, to do research into the forces at work here, and to work at understanding them. I would also argue that we need to be mindful of the risks, and I agree with those who suggest that the risks remain tilted toward the down side.

CHAIRMAN GREENSPAN. Governor Phillips.

MS. PHILLIPS. Thank you. On the one hand there has been some progress in the sense that I've managed to move myself from the bottom or the last on the list to talking at least before a few other folks! On the other hand, and even after listening to the Gipper last night, it's a little hard to find the bright spots--or maybe I should say the points of light. The economy and the monetary aggregates appear to have weakened since our last meeting. Maybe I should say the monetary aggregates have weakened and then the economy has weakened. In trying to locate likely sources of strength, I don't think we're going to see it from the consumer. Housing may be a potential source of strength, but with the unemployment uncertainty and because trying to get out of the recession into a stronger recovery situation has taken so long, it seems to me questionable that housing is going to provide the spark that we may need. And, certainly, the news from different parts of the country tends to be spotty. Investment spending is a possibility, but again that may be

somewhat constrained by the retrenching that we're seeing in business, the emphasis on efficiency, and just simply the slowdown in spending. The downward Greenbook revision in GDP for the third quarter is particularly disturbing in view of the fact that last time we did not assume there would be an easing. What this implies to me is that it has taken an easing to feed this restructuring process that we've all talked about and that we've all observed. It appears that it is deep-seated and more widespread than many of us might have thought. As for the unemployment situation, I tend to wonder whether or not there's more pain out there in the labor market than is evidenced even by the 7.7 percent [unemployment rate]. I cite that because people know there is more restructuring to occur; the defense cutback is really only getting started. The fact that it is taking such a long time to move [along] is protracting some of the pain. And I guess the question for us is how satisfied we are with this picture of slow growth and an economy that doesn't seem to be generating jobs.

So, for me, the risks seem decidedly on the down side. I certainly recognize the arguments that another easing may not help. On the other hand, the question is: What are the risks of another easing? Inflation doesn't appear to be flaring up. And maybe, as Governor Kelley mentioned, we are approaching the point where we have to start wondering if we are overshooting. The politics, the press, and the concern about timing are problems only if we make them problems. That is to say: If we allow ourselves to be dictated by whatever happens to be going on in a particular week, then it becomes a problem. We have to do what we think is right. And I don't think we should be waiting around for fiscal policy. That is tenuous at best. So, on balance, it seems to me that since last time the risks have moved more to the down side.

CHAIRMAN GREENSPAN. Governor Lindsey.

MR. LINDSEY. Thank you, Mr. Chairman. I woke up in a good mood and then I heard these words: listless, torpid, mixed, slowing, softer, sluggish, shrinking, flat, lousy, and sour. That was the report. The only good news was from Minneapolis. I read recently that TIAA is 40 percent owner of that mall. And given some of the trash they bought in the First District, I'm glad that at least something is running well. I don't know how much I'm going to stake on that.

I agree with Tom Melzer that we err when we look too much at the real economy. What I learned was that we were supposed to look at nominal GDP as our ultimate target objective and that money, particularly M2, might be a good intermediate target--which may not be true so much anymore--but that was only because it was a good guide to nominal GDP. When I look at that, I see we just ended over two years of nominal GDP growth at the 4-1/4 percent level and now it's dropping down to the 3-1/2 percent level at least for two quarters. And 3-1/2 percent is summed up as listless, deteriorating, mixed, slow, exhausted, sluggish, etc.; it's lousy. It is a number that is below any of our forecasts. In my view it should be sending off alarm bells as to what we are doing to the economy. We cannot control the mix between real and inflation, but we can control the sum of the two. And 3-1/2 percent is not the right sum in my mind. With all respect to Dr. LaWare, if I were on the operating table, I wouldn't want to counsel patience. The patient after all is the U.S. economy. Sitting

back and waiting for the outcome, when the outcome could be quite bad, is not something I would advise.

Therefore, I share the sentiments expressed here that our likely next move is a cut in nominal interest rates. The question is whether to do it now or later. The case for later I think is a good one. We have all kinds of risks out there in the next three or four months. Bill's report included the possibility that Germany may raise the Lombard rate. I'm not an expert on this, but my bet would be that that will cause a European currency crisis. The French are voting on Maastricht on September 20th; the polls are all moving in the direction of defeat. As a little follow-up, the Danes recently had a poll last week asking people how they would vote now on Maastricht and it was booted down 57 to 43, an even wider margin. The pound is now below where it was when we were certain that Kinnick would be the next Prime Minister. The Financial Times Stock Exchange [Index] is down; it has lost all of its gains since the election; there is certainly a possibility of a pound crisis. There's always a possibility of a lire crisis. The Japanese market is weak, down another 4 percent. The likely reaction to that is going to be an easing by the Japanese, which will put downward pressure on the yen. They've reacted to that by selling dollars and that is not going to help our situation. We have our own stock market problem. There is also the possibility of instability in any part of the world. I would add to Governor Mullins's list the USSR. We recently had a briefing by a friend of mine who is an oil market operator and he pointed out that we risk an oil supply shock due to unrest in the USSR. That certainly has not been factored into the market. So, those are all reasons to wait.

The best reason to [move] now I thought was summed up in Bill [McDonough's] report. The best time to act is when we surprise the markets. And because everyone "knows" we would never act this week, that may be the best time to act. I am agnostic on when we're going to act, but I would give long odds that the proper next move will be a cut.

CHAIRMAN GREENSPAN. Governor Angell.

MR. ANGELL. I wanted to hear all the news and I agree that Governor Lindsey has summarized it pretty well. There is almost a total lack of anyone who thinks the economy really is going to go charging ahead, and maybe that's the best news there is. I've had such low nominal GNP forecasts for so long that I'm glad finally to have some company with forecasts the same as mine. I think you're right also, Governor Lindsey, in looking at the international arena. That's not something we can control. Yet the U.S. dollar is still the major reserve currency for the world and the U.S. dollar is affected by activities that take place in the world. Even though the goods markets may be very imperfect, with a lot of protectionist devices out there, the capital markets are not imperfect and they do move very quickly. When we look at the question of whether or not the disinflation in the United States has gone too far and whether we are moving into deflation, the fact of the matter is that wholesale prices around the world on a year-over-year rate of change basis indicate much more disinflation as do prices in other G-10 countries than do prices in the United States. Of course, in Japan [prices have declined] year-over-year; but even in Germany, with the Bundesbank worried about inflation, the year-over-year change in wholesale prices

is lower than ours and very close to zero. It even looks as if the United Kingdom's disinflation rate is such that their year-over-year change in wholesale prices might slide under ours in a couple of months. Our year-over-year change in wholesale prices at 1.8 percent just doesn't show what I would call disinflation turning into deflation. So, I don't see how we can build the story that we're in a deflationary environment.

Clearly, we're in an environment in which economic conditions are very sluggish. To me this is to be expected. It seems to me that American households should want to alter their balance sheets and to increase their saving rate. And it seems to me that there is some prospect that the saving rate before we get to 1994 might move up beyond 5 percent from the low of 4 percent that we had a few years ago. We've seen it move on up to 5 percent and I think it quite likely could move up to 5-1/2 percent before 1994. That would mean then that the source of our growth would not be from the consumer sector as we might expect. As we look at the patient, Dr. LaWare, maybe we ought not just be patient but monitor a few things as we go along. I think we ought to monitor commodity prices and see that commodity prices do not turn downward. Gold has quite often led commodity prices; gold has bounced around some and is now in somewhat of a downward mode. I don't think we ought to ignore that leading signal which might be more important at this point than M2 in terms of our seeing where we're going. Frankly, if the price of gold were to take another strong leg down, I'm not sure but I might join Governor Lindsey in regard to where we ought to go. But I do believe that we need to be on a very secure price level stability base before we make the next easing move because, if the world doesn't know that we are committed to price level stability and we ease in that environment, we risk destabilizing financial markets around the world. Governor Phillips says: What do we have to lose? There's not much danger that the inflation the bankers are worried about is going to come charging back. But I do think in the environment that we're in that we could very well destabilize international capital markets and we might understand that the notion of sour is a whole lot better with the DOW at 3320 than if the DOW were losing 200 points a day. So, I think there's some strength out there. In addition to commodity prices, I want to monitor M2. I think M2 in the coming months is going to be very important because I've had an hypothesis that M2 is going to be guided more by what happens to intermediate rates [unintelligible].

CHAIRMAN GREENSPAN. Mr. Kohn.

MR. KOHN. Thank you, Mr. Chairman. I'll attempt to summarize my presentation in an effort to cut it down at least by a few minutes. That may make it slightly more incoherent than usual! [For Mr. Kohn's full statement, see Appendix.]

CHAIRMAN GREENSPAN. I think it would be helpful at this stage to get a judgment of the Committee on this particular point. Do you want to say anything in defense of any of your proposals for the last sentence of the operational paragraph?

MR. KOHN. Well, I tried last time and I got beaten up! The reason alternatives C and D are in the Bluebook is because of the issue that arose last time about writing down a monetary growth number

--particularly now that it would go through the end of the year--that was inconsistent with the range you just gave to the Congress. However, I went back and looked at the report and the testimony and I do believe that they are sufficiently ambiguous as to leave open the possibility that monetary growth would drop below the range. And that would be judged on the basis of incoming information about how velocity was behaving. So, I think a sentence along the lines of either "C" or "D" would line up with the report and testimony and the decision of the Committee at the last meeting that it didn't know enough, really, to change the existing growth rate [objective] for the year. So, I think you could do either "C" or "D."

CHAIRMAN GREENSPAN. Jerry Jordan.

MR. JORDAN. In helping us to choose among these, let me make a couple of comments about what I've heard and observed over the last few months. From the standpoint of an outsider, in the 1980s it seemed to me that you were in a pretty good position on two counts: Having had pretty good results both in getting a model that helped to alert the Committee on what M2 to expect and [thus] hitting the target and on interpreting what it meant in terms of velocity, P^* , and so on. Recently, at least since I've been here, we've only had two problems: One is that we don't know how to hit [the target]; and two is that we wouldn't know what it meant if we did. So, if you have to indicate a relative confidence, would you have greater confidence in your ability to indicate what money growth would be, given the funds rate or whatever, or what it means in terms of the velocity? Where are we supposed to indicate that we have more confidence? If we put in the statement about velocity, it implies that we have more confidence in that than we do in something we are supposed to hit.

MR. KOHN. That's a very difficult choice. Clearly, we have major questions about both of those. They go together; I can't separate those two questions; I can't answer one or the other. The way we do the forecast is to take the path for [nominal] income in the Greenbook and the path for interest rates implied in the Greenbook and ask what money growth would come out. That's how alternative B is put together. It's all part of the same process. I don't see it as two different questions.

MR. JORDAN. To me it is two different questions. But that's a matter of a framework or a model or control versus--

MR. KOHN. Well, the other question is: If the Committee said to Peter Sternlight that it wanted 2 percent M2 growth, give or take a percentage point, and didn't care what interest rates and income went with that, I believe Mr. Sternlight could achieve that over a period of six months or so. Now, we might get some very wild interest rate [movements] in the process and perhaps as a result wild [variations in] income growth; but if that's all the Committee cared about, I feel some confidence that within a tolerable range and over a sufficiently long period we could achieve the M2 growth that the Committee asked us to achieve.

MR. JORDAN. I interpret that to mean that you're more comfortable explaining the misses rather than putting the weight on hitting the target?

MR. KOHN. Yes.

CHAIRMAN GREENSPAN. Governor Angell.

MR. ANGELL. I'm uncomfortable with "C" because putting the velocity in there makes it seem that the resulting nominal GDP is exactly what our policy objective is, whereas my understanding is that we would like the resulting nominal GDP to be higher than it might be or than we might be able to make it to be. So, I would prefer just to do the straightforward "B;" I'm presuming with your revised numbers that you might be able to put a "2" in there. Is that right?

MR. KOHN. Yes, I think so.

MR. ANGELL. So, I'd prefer "B" with 2 percent in it.

CHAIRMAN GREENSPAN. President Melzer.

MR. MELZER. I would not favor "D." I had some sentiment for "C," but I am a little concerned about the precision that second sentence might imply. I don't have any problem with the concept of doing "C" and then saying we don't think we're going to make the ranges for the year. I don't have a suggested change, but I think the words here may imply more certainty about these relationships than we have; I think Wayne was saying the same thing. I could live with "B."

MR. KOHN. In support of that, we can certainly take many more words in the Policy Record itself to explain how the Committee decided to do what it did. We're not confined to [the wording in the directive]. So, the record would accommodate this relationship.

CHAIRMAN GREENSPAN. Let me cut this whole thing short. With that qualification, could we all accept "B" at this point?

MR. SYRON. Could you tell us a little more about the qualifications?

CHAIRMAN GREENSPAN. Why don't we do that unless somebody has some objection. If I hear none, I'll just assume that we will go with "B" with the addition that Don suggested.

MR. KOHN. The Policy Record would explain that the Committee recognized that this put [M2] on a trajectory where it might fall short but took into account a number of different things in choosing this without having to specify exactly--

CHAIRMAN GREENSPAN. Any general questions then to Don? Yes, Jerry.

MR. JORDAN. Following up on what Wayne Angell said earlier in his remarks about the rally of the market affecting the intermediate term: Don, I would have expected you to come back and say that in view of the market developments since the last meeting our model is now showing a lot stronger M2 growth. So, one of two things [must be true]: Either other things weren't equal or I was wrong in guessing which way that goes.

MR. KOHN. Well, you have the direction right; it's a question of what the size is, and in particular our models operate with some lag. So, a lot of this would be feeding through into the fourth quarter. It gives us more confidence. Yesterday, Governor Angell was challenging me on why I had any more growth under alternative A than I did under alternative B, given our recent experience. I think the decline in intermediate-term rates gives us a little more confidence that we'll get the 2 percent [M2 growth] or a little more in the fourth quarter under "B" and that we'll get some more under "A." So, I think it's the kind of thing that builds confidence. We had a shortfall in July--more than we expected--and we carried that shortfall forward but slanted up growth from here on out, partly based on the decline of intermediate-term rates.

CHAIRMAN GREENSPAN. Any further questions? If not, I'll start off on the policy issues. We've all been looking at various models. In the earlier go-around members made major additions to macroeconomic models by employing such concepts as economies in ditches, the end of runways, terminal patients, and the python in a pig, or is it vice-a-versa! [Laughter] I have two models which I've discussed previously, and I'd like to raise them again merely on the grounds that I think it's fairly apparent that the basic structural models that we employ of necessity are not capturing what essentially is going on in this environment.

The one we used in the Humphrey-Hawkins testimony is what I would call a somewhat benign model. It essentially argues that there has been a diversion of cash flows in both the household and the business sectors away from purchases of goods and services to debt repair, largely a reduction in debt. That obviously engenders a higher saving rate and a subdued level of economic activity. But it basically stipulates that the saving rate is stable at a higher-than-desired longer-term level, that the balance sheet repair will continue until balance sheets get into pretty good shape at which point the amount of diversion of cash flow that is required for the eventual [recovery finally] supplies enough money, then spills over into goods and services, and ends up in gross domestic product. That argument stipulates that if the balance sheet repair [process] is, say, to a substantial extent completed in the business sector and, say, halfway through in the household sector--which the data on debt service burdens somehow but very crudely imply--then one would conclude that we're over the major part of the adjustment or at least in the middle of it and are sort of going down hill. One would not expect it to be an all or nothing adjustment on the balance sheet until the balance sheet repair is complete, but rather the beginning of a gradual moving away from savings toward purchases of goods and services as the balance sheet repair gets 80 percent complete, then 90 percent, and eventually 100 percent. That argues for something not terribly different from the Greenbook projection: a rather moderate, subdued gross domestic product increase but with characteristics essentially as described in the Greenbook.

The alternate significantly less benign model is the one I raised at the last FOMC meeting. It differs from the first model in regard to the presumption about the extent of balance sheet stringency--which you may recall I characterized as having many of the characteristics of the 19th century type of economic processes in the periods when we had a major speculative increase in assets financed by

debt, followed by a decline in market value of assets, debt burdens becoming oppressive, and people effectively seizing up on their expenditures in an effort to pay off their debts and restore their balance sheets. The effect is an implosion in economic activity. I stipulated at the last FOMC meeting that one way of looking at this process that we are involved in and have been involved in for the last three years is that it is one in which we forestalled this [adjustment] by continuously injecting liquidity--or I should say basically injecting funds and reserves into the system. That stretched out the adjustment process and effectively worked toward ease and toward a sort of relaxing of the grip when we eased, but only for a limited period of time. That is, one can view the essential player in the economy as having a desire to repair the balance sheet very rapidly but the process was being stretched out so to speak by some form of tranquilizer or whatever we may call it. And that tranquilizer has a limited life expectancy so that when we ease we get an economy which is not collapsing but tending to stabilize. But we have to ease continuously in order to get the economy just to stand still and prevent it from seizing up and collapsing.

Now, at the moment I think we can be on either Model 1 or Model 2. If after the substantial amount of liquidity we have injected in the system we are still at a stage in which there is a significant endeavor to repair balance sheets at a pace that implicitly [consistent] with negative gross domestic product growth, then what we've heard around this table would lead us to conclude that the cumulative weakness is going to go an awful lot further. This leads me generally to conclude that what we have to do at this stage is just to watch what happens. I felt that the [strengthening in] the M2 data, which Don mentioned just this morning, was helpful. It's not going in the wrong direction. And it's at least not inconsistent with Model 1. If Model 1 is in fact working, then we've probably done enough at this stage and no further actions would be required on our part. But we don't know that; the reason we don't know that is that it is conceivable, for example, that when housing sales figures come out at the end of this month they may be revised down sharply for last month and the newest month may be down; and automobile sales may start to go south. And even though [businesses] have very significant cash flow and profitability, plant and equipment expenditures data, which we will be getting in several weeks, may provide at least an indication of what is going on in corporate planning. All of that will at least give us an indication of where this whole process is going.

Listening to various views of the Committee, I would suspect that one way or another a significant majority of us are somewhere around alternative B asymmetric toward ease, but with a general awareness that if the economy starts to look a little better or even just continues to grow, no action would be required. Action would be implied only under the condition that expectations begin to emerge which suggest that the expansion is going to be running under the Greenbook forecast or if we get further important downward revisions that are relevant. The basic reason I would argue in those terms is one that Governor Mullins raised: namely, that we're running out of ammunition for potentially dangerous episodes. We do have a stock market, whatever [index] it is we're looking at, which is quite high. And I would hate to be at a point where we couldn't do anything to respond to that market because we had expended all of the ammunition

available to us. But having said that, if in fact it is turning out that this malevolent Model 2 type of seizure is going on, I suspect we probably would have no choice at that point and would wish to move and hope that if we run out of bullets in the process that at least there's no one left to shoot at. So, that's my addition to a python-in-the-pig!

CHAIRMAN GREENSPAN. Governor Angell.

MR. ANGELL. That's acceptable to me.

CHAIRMAN GREENSPAN. Jerry Jordan.

MR. JORDAN. I have a question. I know this is a Board matter, not an FOMC matter, but in terms of using ammunition: With the projection for seasonal increases in reserves in addition to the continuing trend of reserveable deposits growing very rapidly, would the Board consider using the ammunition it has, i.e. the bullet of lower reserve requirements?

CHAIRMAN GREENSPAN. Do we have room right now?

MR. KOHN. I think if we lowered them in October we'd have to raise them in February. I would doubt very seriously that we'd have room to get to the next seasonal low point even after the actions we have taken. We could take a look at that this fall, but I'd be skeptical at this point.

MR. JORDAN. The statutory limit is 8 percent and I don't understand the operating point. Peter tried to explain this to me, too, and I simply don't understand it. But the legal ammunition is that you can go down to 8 percent without seeking new legislative authority.

CHAIRMAN GREENSPAN. The basic question is clearing balances.

MR. ANGELL. But if more banks were to choose to adopt the alternative clearing balances, that would alter that prospect, right?

MR. KOHN. Right. The key is to have a stable and predictable demand for central bank liabilities, whether it's the reserves or clearing balances, off which Peter can operate in his open market operations.

CHAIRMAN GREENSPAN. Vice Chairman.

VICE CHAIRMAN CORRIGAN. "B" asymmetric is fine with me.

CHAIRMAN GREENSPAN. President Parry.

MR. PARRY. "B" asymmetric.

CHAIRMAN GREENSPAN. Governor LaWare.

MR. LAWARE. Mr. Chairman, I don't see anything about symmetric language that forbids a change, but to have asymmetric language seems to me like giving you a loaded gun that is already cocked. I would really rather have symmetric language so that you

would have to have a consultation with this group before you cock the weapon and certainly before you pull the trigger. So, I would certainly strongly favor "B," but I would favor symmetric language.

CHAIRMAN GREENSPAN. President Syron.

MR. SYRON. I favor "B" asymmetric. To tell the truth, if we didn't have the situation of wanting to be consistent--I'd be afraid we'd lose credibility in the exchange market if we did something now--I might be inclined to do a little now. So, for that reason I'd prefer to be asymmetric and leave it on hold.

CHAIRMAN GREENSPAN. The only argument I would have against John LaWare is that I feel a little uncomfortable or awkward about having been symmetric then asymmetric and going back. My view is that the safety catch is on the gun, if you want to put it that way.

MR. LAWARE. But symmetric language as opposed to asymmetric language might also be interpreted as an expression of confidence. The asymmetric language is saying we expect trouble.

CHAIRMAN GREENSPAN. Do you have that confidence?

MR. LAWARE. Yes.

CHAIRMAN GREENSPAN. You do?

MR. LAWARE. Yes.

CHAIRMAN GREENSPAN. I'm delighted.

MR. LAWARE. Well, I'm lonesome but I'm delighted too!
[Laughter]

CHAIRMAN GREENSPAN. [Unintelligible.]

MR. LAWARE. I have a patient; I'm waiting for him to recover.

CHAIRMAN GREENSPAN. All doctors have patients! That wasn't very funny. Governor Kelley.

MR. KELLEY. "B" asymmetric is fine.

CHAIRMAN GREENSPAN. President Forrestal.

MR. FORRESTAL. Well, Mr. Chairman, I'm going to be even a little more lonesome than Dr. LaWare. I think your arguments are very persuasive for staying where we are. However, it does seem to me that we've had considerable slippage in economic activity from the first quarter. I see very few signs or areas of strength that will give us any forward momentum here. I ask myself the question, first of all: What good would easing do at this point? It's questionable I suppose. But on the other hand, it may help, and I don't see any substantial risks; in fact, I see very little risk in moving. So, I would prefer to make a move now.

CHAIRMAN GREENSPAN. I think the risk in question is how much ammunition we have left. That's the only risk I see.

MR. FORRESTAL. Well, we still have 2 percentage points to 0.

CHAIRMAN GREENSPAN. That's right and we may need it.

MR. FORRESTAL. We may need it. Well, I think I would prefer to shoot the bullet now with alternative A.

CHAIRMAN GREENSPAN. Okay. President Keehn.

MR. KEEHN. Mr. Chairman, I agree with Bob Forrestal. I would prefer to ease now in the direction of "A" but certainly find "B" with asymmetric language acceptable.

CHAIRMAN GREENSPAN. President Boehne.

MR. BOEHNE. "B" asymmetric.

CHAIRMAN GREENSPAN. President Jordan.

MR. JORDAN. I feel a lot more comfortable with several [recent] developments: the rebound in July in reserve growth, in the monetary base, and in M1, whereas everything was negative in June. And I would want to see that--especially [the growth in] reserves--continue to be positive. I wouldn't want foreign operations to show up and drain reserves. Partial analysis, of course, [indicates that] they do, but I would hope that would be offset, or sterilized, consciously or not either way. I would be with John LaWare on preferring symmetric language at this point because I think things are in motion except--and this is not a policy issue but a communications issue--if we went with symmetric now, when that is released in the middle of October after the next meeting I would expect that the headlines would read that the Committee had tightened. And that is enough to dissuade me from changing the directive even though my preference would be to do so.

CHAIRMAN GREENSPAN. President Stern.

MR. STERN. I support your proposal for "B" asymmetric.

CHAIRMAN GREENSPAN. President Hoenig.

MR. HOENIG. I would be more with President Forrestal's alternative now, but I would accept your argument of holding back and thus would accept "B" asymmetrical.

CHAIRMAN GREENSPAN. President Melzer.

MR. MELZER. I favor "B" symmetric, Alan. I won't go into a lot of reasons; it's essentially for the same reasons that I cited at the last meeting but I feel even more strongly about them. I think credibility is more of an issue now. Also, we just eased and, if you think about it in percentage terms, it was a 15 percent cut in the level of nominal rates; that's not insignificant. Finally, I think this view captures a number of people who want to ease right away, and

I just feel so strongly that that's the wrong thing to do that I guess it's hard for me to put myself in that group.

CHAIRMAN GREENSPAN. President Black.

MR. BLACK. Mr. Chairman, ordinarily I'm biased very much in favor of symmetric language but I think your reasoning on why we shouldn't switch from one to the other and then back again is compelling. So, I would say "B" asymmetric.

CHAIRMAN GREENSPAN. Governor Lindsey.

MR. LINDSEY. Mr. Chairman, I will support your directive. However, I'd like to associate myself with the views of Presidents Forrestal, Keehn, and Hoenig. There is the number of bullets and also the quality of bullets. I think a little bullet shot now because it's unexpected would have a big effect. So, had you not expressed your view, I would have been inclined to favor "A" and shoot 1/4 point now.

CHAIRMAN GREENSPAN. President McTeer.

MR. MCTEER. I support your recommendation.

CHAIRMAN GREENSPAN. Governor Mullins.

MR. MULLINS. I think "B" asymmetric is the appropriate stance given the current environment and the changes we've seen. I tend to support the stronger asymmetric stance.

CHAIRMAN GREENSPAN. Governor Phillips.

MS. PHILLIPS. I'd prefer "A" but will support "B" asymmetric.

CHAIRMAN GREENSPAN. I think we have a majority for "B" asymmetric toward ease. If you'll read the language--

MR. BERNARD. "In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might or slightly lesser reserve restraint would be acceptable in the intermeeting period." Moving on to page 14 to alternative "B" for the last sentence, but I'm not sure what Don's latest numbers are--

MR. KOHN. Taking account of today's data, 2 and 1/2 percent.

MR. BERNARD. "The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from June through December at annual rates of about 2 and 1/2 percent, respectively."

CHAIRMAN GREENSPAN. Take the roll.

MR. BERNARD.
CHAIRMAN GREENSPAN Yes
VICE CHAIRMAN CORRIGAN Yes
GOVERNOR ANGELL Yes
PRESIDENT HOENIG Yes
PRESIDENT JORDAN Yes
GOVERNOR KELLEY Yes
GOVERNOR LAWARE No
GOVERNOR LINDSEY Yes
PRESIDENT MELZER No
GOVERNOR MULLINS Yes
GOVERNOR PHILLIPS Yes
PRESIDENT SYRON Yes

CHAIRMAN GREENSPAN. Okay, thank you very much. We will adjourn for lunch.

END OF MEETING