

Federal Open Market Committee  
Conference Call  
February 28, 1994

PRESENT: Mr. Greenspan, Chairman  
Mr. McDonough, Vice Chairman  
Mr. Broaddus  
Mr. Jordan  
Mr. Kelley  
Mr. LaWare  
Mr. Lindsey  
Mr. Parry  
Ms. Phillips

Messrs. Hoenig, Melzer, and Oltman, Alternate  
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Mr. Coyne, Assistant Secretary  
Mr. Gillum, Assistant Secretary  
Mr. Mattingly, General Counsel  
Mr. Patrikis, Deputy General Counsel  
Mr. Prell, Economist  
Mr. Truman, Economist

Messrs. Beebe, Goodfriend, Lindsey, Siegman,  
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Messrs. Cox and McNees, Vice Presidents, Federal Reserve Banks of Dallas and San Francisco, respectively

Transcript of Federal Open Market Committee Conference Call of  
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CHAIRMAN GREENSPAN. Good afternoon everyone. As you may recall, we decided at our last FOMC meeting that it would be advisable somewhere in the middle of the intermeeting period to have a telephone conference, basically to review various aspects of ongoing developments. I would also like to take the occasion, as I conventionally do, to brief you on the G-7 meeting. I will tell you the bottom line is that not much went on. There is a significant Congressional hearing coming up, as you are aware, on the issue of regulatory consolidation, on which I'd like to spend a few minutes. But I thought it would be useful in our conventional manner in such conferences to start off with a review by the two Desks. Is Peter Fisher on?

MR. FISHER. Yes, I am.

CHAIRMAN GREENSPAN. Peter, could you take just a few minutes and bring us up to date on how you see what's going on in the exchange markets and, if Joan Lovett is there, I'd like to call on her as well.

MR. MCDONOUGH. She is also here, Mr. Chairman.

CHAIRMAN GREENSPAN. Okay.

MR. FISHER. I'll be going over developments in dollar/yen and dollar/marks since the Committee's last meeting. Initially, the dollar traded in a range against the yen above and around 108 as we approached the Clinton/Hosakawa meeting. In retrospect, there was a fair amount of complacency among the holders of long dollar positions prior to that meeting. Market participants had for some time been of the view that once that meeting was out of the way, dollar/yen could trade up toward 115. And they quite clearly held on to those long positions going into that Friday and through Friday. On Monday, Valentine's Day, as everyone is aware, we had an abrupt liquidation of those long dollar positions here in the New York market. The dollar/yen closed in Tokyo that day around the 105 level. In New York, we got to an intra-day low of around 101.5 and closed just above 102 in what was a very abrupt and massive sell-off of speculative long dollar positions. During the day, there was a half-hour period that was quite exciting, some 50-pip and 100-pip moves in the exchange market. But many bankers I spoke to thought the market had functioned very well; even in the very busiest half hour, people were able to get their business done. Since then we have had a rather choppy market. The speculative market participants have been trying to make and take profits on smaller positions and smaller moves in both directions, and this has given a certain choppiness to the market. Japanese exporters have left their offers in the market to sell dollars at the 105 and above level. The Bank of Japan has purchased over these last two weeks. And Japanese life insurance companies and other central banks also have been seen buying dollars against yen around the 103 and 104 levels.

Turning to dollar/mark trading, following the Committee's meeting and the Committee's action to raise interest rates, the dollar/mark moved up above 1.76 immediately and then came down in what I would describe as three stages, principally reflecting the

perception that the Bundesbank was slowing further the pace of its easing. First, it came down toward 1.75 on profit-taking and a lack of willingness of participants to extend long dollar positions until the market saw some further rate reduction by the Bundesbank. Then it came down to the 1.72 - 1.73 area following the movement in dollar/yen on Valentine's Day. That was not so much a sympathetic move as an alternative form of selling dollars. If you were anxious about adjusting your dollar/yen position or your overall long dollar position once the move had happened, you would more likely want to do so in dollar/marks than in dollar/yen. Finally, the dollar/mark came down to the 1.71 area on February 17th following the Bundesbank's action to lower the discount rate but not the Lombard rate and the RP rate. This was seen as a sort of nonrate rate cut in the exchange market, and there was a further closing out and liquidation of long dollar positions that brought the exchange rate down roughly to where it is now. Today, the Bundesbank announced that it would be having a variable rate RP tender, the results of which we should see tomorrow. This has given the dollar some small boost today but the market will really await the tender tomorrow. I'll stop there and see if there are any questions.

CHAIRMAN GREENSPAN. Any questions for Peter? If not, Joan, would you give us a rundown?

MS. LOVETT. Thank you, Mr. Chairman. Since the February 4th meeting, we've had an increase in interest rates pretty much across the board and that increase has surpassed the 25 basis point move that took place in the federal funds rate. Initially, the increase was centered in the shorter end of the market. I guess that is what one would have expected, given the short-end adjustment to a federal funds rate move, but then the longer end began to catch up. First, the market felt that it had to try to digest some of the new supply that was coming out of the Treasury's quarterly refunding, which took place the following week. The markets then began to adjust. The adjustment in the 10- and 30-year areas became somewhat more pronounced as market participants began to react to current interest rate prospects and future inflation prospects in a way that led them to wonder how far and how fast the Fed would have to move going forward. I guess some of that came about as people started getting more information about the fourth quarter. This is old news, but thoughts about the fourth-quarter GDP were being revised up. By tomorrow, there will be a new estimate for that and most of the thinking in the market is for a growth rate pretty close to 7 percent. Even in the first part of the year there was some thinking that perhaps there was an undercurrent of strength in the economy, a little more than the market may have anticipated earlier on. That lengthened this debate about just exactly what was happening or how to characterize something that's a neutral stance by the Fed as opposed to an accommodating stance.

Against that background, people began to anticipate some further moves down the road. There was then a tendency for people to try to make some sales on any market strength. So, when there was some good news coming out--what formerly would have been taken as good news for the market on some of the different price indexes--everybody seemed to be poised to go the same way. People generally were looking to lighten up their inventories and to come in on the curve, and the consequence of that was that there never really was any strength. The reaction that seemed to be taking place in other bond markets also was

something that people were paying pretty close attention to as some of the overseas bond markets began to erode. I think that led to an element of securities overhang that made people cautious and provided no incentive to step in on the buy side, given the fact that higher rates were seen as likely down the road. By the middle to the end of last week, the market reached yield levels that in the case of the 30-year bond just flirted with the 6-3/4 percent level, though it never pierced that level; on the 2-year notes, that level seemed to be 4-3/4 percent. At 4-3/4 percent, I guess there has been a feeling that an awful lot of near-term bad news has been priced into the market and that seems to have acted as a stabilizing influence. Friday and today the markets have been tending to stabilize and to do somewhat better, with many people out there expressing the view that there has been an overreaction in the market. And, at least on a near-term basis, the market acts oversold; therefore, that's potentially enough to give the market a steadier footing going forward. There are a lot of data coming out this week, and each day there will be something on the plate that the market will be looking at pretty closely, culminating with the employment report at the end of the week.

CHAIRMAN GREENSPAN. Questions for Joan?

MR. LINDSEY. Joan, you mentioned 7 percent; could you tell me when they think the long bond will get there?

CHAIRMAN GREENSPAN. No, she said 7 percent GDP growth.

MR. LINDSEY. Oh, I see.

CHAIRMAN GREENSPAN. That's the fourth-quarter estimate.

MR. LINDSEY. I'm sorry, I apologize.

CHAIRMAN GREENSPAN. Any other questions for Joan? Let me say that looking back at our action, it strikes me that we had a far greater impact than we anticipated. I think we partially broke the back of an emerging speculation in equities; it's still too soon to know whether or not that's true, but the evidence to date clearly suggests that that is at least a good possibility. In retrospect, we may well have done the same thing inadvertently in the bond market because what we were getting earlier were tremendously rapid declines in long-term rates. As we look back on this, I suspect that there was a significant overshoot in the markets. We pricked that bubble as well, I think. We also have created a degree of uncertainty; if we were looking at the emergence of speculative forces, which clearly were evident in very early stages, then I think we had a desirable effect.

Watching the market behave in the long end since our move just reinforces what Joan was discussing. I'm not certain that we can say at this stage that the modal forecast for growth in the first quarter has changed materially. But the probability that the growth rate in the first quarter will be significantly higher than previously expected may be higher while the probability that growth in the first quarter will be significantly below the expected modal forecast is clearly much lower. As a consequence, the average expectation for the first quarter clearly has increased. And in the typical way people do

forecasts, if the revised number for the fourth quarter of 1993 is quite a good deal higher than originally expected and the first quarter somewhat higher, one can be reasonably certain that that will start a process of upward revisions that are almost automatic. In part, I think that has been pushing the changed attitudes; and it's getting increasingly clear that the markets are expecting stronger growth than, say, back in November. In that sense, even with the 25 basis points, in this context of rising expectations of higher long-term real rates, we probably have imparted or have been associated with a larger degree of restraint than we had anticipated was likely to occur in the first quarter. Coming off this type of operation, my own view with respect to policy is that we're going to have to move again, obviously. I don't know when that will be, but I think it would be wise for us at this particular point to allow markets, which clearly have been shocked, to settle down before we move again. I would hope that we could review the outlook much more extensively at our next meeting in a few weeks. Frankly, I would be curious at this stage to know what Mike Prell and Dave Lindsey are looking at with respect to the economy and the markets. I also want to do a round table of opinion among the presidents. Mike.

MR. PRELL. Well, I thought I was off the hook when you said it would be worthwhile waiting a couple of weeks, because, at this point, we find it very difficult to read the trends through the noise of the recent data. Clearly, there have been some effects of weather on a variety of data series, which makes them very difficult to read. One can't even tell how much of the labor market data is a fluke, for example, given the fact that the January surveys occurred during a week that was affected by bad weather. And it appears we're going to get a repeat of that in February when there was bad weather in the survey week. So, we don't know how representative that week is of the month. But in any event, in brief summary, the consumer sector still seems to be reasonably firm. The nonauto retail sales for January were not particularly impressive, but there were upward revisions in November and December, so we were at a fairly high level. And while there's some question in some circles about the seasonal adjustment of the motor vehicle sales, all indications are that the motor vehicles sector is on very firm ground at this point in terms of demand. We're also getting a substantial increase in production; this quarter appears likely to exceed what we had built into our forecast in the last Greenbook.

In the residential sector, housing starts were down very sharply in January; permits were down less sharply but still fell appreciably. In all likelihood, that was largely a weather effect and probably did not reflect a fundamental shortfall in demand from what we were anticipating would be the picture in the first half of this year. These higher interest rates do raise a question that we'll have to address in our forecasting. If they were to persist, it would imply mortgage rates significantly higher than we had in our prior forecast. But if this is an environment in which expectations about the growth of the economy and employment prospects might be reasonably strong, then this shouldn't put a very great dent into residential construction going forward. We would expect to see the January sales figures affected by the bad weather and the February picture again may be weaker because of bad weather.

In the capital goods sector, the orders and shipments for January for nondefense capital goods were on the soft side--but not particularly so relative to what we would have expected in the wake of very big jumps in some volatile categories in December. I think the trends there still are distinctly upward, and we perceive the equipment sector to be a very strong contributor to the overall growth of the economy at this point. On the employment side, the initial claims have tended to be higher in recent weeks, and reading through our models, that would suggest that we're going to get another quite modest increase in payroll employment this week. But that's a very shaky tool for estimating these things. Industrial production was up 1/2 point in January; manufacturing activity was flat. We think that was largely a loss of manufacturing due to bad weather offset to some degree by increased utility power generation that is holding up the overall index. What indications we have to this point suggest that output in motor vehicle manufacturing and some other sectors is producing a decent gain in manufacturing activity in February. Certainly, the anecdotal evidence--purchasing managers' surveys and so on--suggests that the manufacturing sector is remaining quite robust in the current quarter.

Finally, on the inflation picture, the CPI was very good news, with a zero overall increase and up just 0.1 ex food and energy. It was certainly below our expectations. It was not a seasonal adjustment story because we had largely allowed for the change in the seasonal adjustment. Could it mean that we are on a better overall trend? Perhaps, but I don't want to read too much into the one month. Could it mean that in the short run we're not getting the so-called speed effect that we feared we might see in the aftermath of that surge in activity at the turn of the year? I guess it argues against that to some degree, but I would not rule out the possibility that we will see less favorable readings in the next few months. Certainly, there are hints in the manufacturing sector that the pressure is on capacity, and some segments are leaning to some firmness in prices. We see it in the materials prices for inputs reported by the manufacturing purchasing managers. There's a sense of some greater pricing leverage but it's not pervasive. We're inclined to think that the general news on pricing, along with the CPI figure, has been favorable, on balance. So, at this point, we would guess the first-quarter GDP, in large part because of the weather effects, might be somewhat weaker than the 4 percent we forecast in the Greenbook and the increases in the overall CPI and core CPI also might be a little less than we had forecast.

CHAIRMAN GREENSPAN. With the GDP somewhat strong and at least the measured labor input soft, I assume that says that productivity growth probably is going to register a reasonably strong number in the first quarter.

MR. PRELL. I think there are offsetting influences here. What I'm suggesting is that the GDP growth probably will be weaker in the first quarter than we had forecast before. The overall hours input--I don't know. We have a very substantial increase in hours in January. We're expecting to see the workweek retrace some of its increase and only a modest increase in payroll employment. There is the possibility that this may be one of the downside risks.

While we can't see it in the data yet, the disruptions may have shown up, effectively, as a weaker productivity and profits performance in the first quarter. Certainly, there were many salaried workers who were paid but did not get to work in the eastern part of the country in January and February; so, that might suggest some weakening of productivity. At this point we have a very hard time summing up these pieces.

CHAIRMAN GREENSPAN. That would be consistent with a weakening in GDP below expectations.

MR. PRELL. Right.

CHAIRMAN GREENSPAN. Any other questions for Mike? Susan.

MS. PHILLIPS. Mike, I was just meeting with a group of bankers from the state of Kentucky and one thing that they mentioned was that people who could not make it to work could claim unemployment insurance. Is that right?

MR. PRELL. Yes, and that's one of the difficulties in reading the recent data. We don't know how much of the increase in initial claims might be just a very transitory weather effect or whether it means that we're actually getting a slower trend increase in employment. One thing that argues against it being totally weather-related is the persistence of this sort of week-in and week-out being a little higher than before. But there are certainly some weeks that one could identify as in all likelihood having been affected by the bad weather and the earthquake in January. So, there's undoubtedly some weather element in these numbers.

CHAIRMAN GREENSPAN. Other questions for Mike? If not, let's hear from Dave Lindsey.

MR. D. LINDSEY. Mr. Chairman, the broader monetary aggregates appear to be weaker than we thought on the afternoon of the policy tightening when we tried to build in those effects. M2 appears to be declining at about a 1/2 percent annual rate in February. The falloff in mortgage prepayments this year is, we think, deducting some 2 percentage points from February M2 growth after boosting that growth late last year. In light of M2's growth of 2-1/4 percent in January, from the fourth quarter through February, M2 has expanded at a 1-1/2 percent annual rate, quite close to its pace last year and quite close to the pace we estimated, abstracting from the various special factors influencing it. M3 is weaker still in February than M2, declining at about a 6-1/4 percent annual rate after growing 1 percent in January. From the fourth quarter to February, M3 is declining at a 1/2 percent annual rate. Sharp declines in the money market mutual funds component of M3, however, explain virtually all of its decline in February. Bank credit is continuing to expand in February, in fact a little faster than in January--about 5 percent in February following 3 percent in January. But there is an artificial upward boost to both months' growth rates in bank credit coming from an accounting change that is boosting the "other securities component," non U.S. government securities. So, if anything, since bank credit grew 5 percent over all of last year, in an underlying sense it seems to be slowing some this year. The recent weakness in bank credit so far this year reflects runoffs in U.S. government securities and a flattening of

real estate loans after they showed pretty strong increases late last year. Business loans were quite strong in January but their growth apparently is slowing in February. My February interpretations for bank credit are still somewhat preliminary, as some of the month is still projected.

CHAIRMAN GREENSPAN. Questions for Dave? If not, would anyone like to start a go-around on one's sense of what is going on out there?

MR. BROADDUS. Mr. Chairman, this is Al Broaddus. I would just say that I thought your Humphrey-Hawkins testimony did a great job of laying out once again our longer-term strategy. The problem, as I see it now, is that the public and the markets are still unsure about the execution of that strategy and whether we really can achieve our longer-term goals. And I think that's at least partly responsible for some of the rise in long-term interest rates and the current uneasiness in financial markets. But I think it's very important that we do whatever we have to do to reduce uncertainty and build confidence in both our resolve and our ability to achieve our longer-term goals. Since we have to look forward, the central question is still whether or not the current stance of policy is too accommodative to be consistent with our longer-term strategy. I think it still is. In your testimony, I believe you pointed out that at the Committee's February meeting we concluded that short-term real rates at zero posed, to use your words, unacceptable risks that would generate future problems. I think that's still true. Real rates are only 1/4 point higher than they were and are still close to zero. And that's a problem. So, I think a case can be made for an immediate action to increase rates another notch. I'm perfectly happy to wait until the March meeting, but unless there's a big change in the economic and financial climate by then, I believe we will need to take a close look and move another notch. I recognize that there is some risk in this approach, but frankly I think the risk of not acting and falling behind the curve is greater. And the consequences of that could be quite bad.

MR. JORDAN. This is Jerry Jordan in Cleveland. I agree with the analysis of the way forecasts feed additional new forecasts in the private sector. Certainly, we have to backtrack to the way private sector analysts put their numbers together. They use the fourth-quarter numbers plus whatever expectations they have about the first quarter after they account for the weather factor. I think the revisions are going to be mainly in an upward direction. To the extent that they think the first quarter is adversely affected by weather or the earthquake, they will simply push that growth to later in the year and overall they'll see 1994 as stronger than they previously projected just a few months ago. And in that sense in a de facto way, our current policy stance is more expansionary than it was even before we acted when people had expectations about a less robust economy. I do not see the benefits that come from having the other shoe hanging over the market. We sort of tested that idea, and I don't see that we gained anything; it's still there. And there's a risk as we go forth to the next meeting that the expectation will build that we will act at the time of that next meeting and maybe afterwards. I don't know that that is constructive; this environment lends itself to a whole lot of rumoring and speculation and even of what could be perceived as leaks that are not healthy for us. So I

wish we had gone ahead and done the full 1/2 point at the last meeting. I would like us to go ahead and do the other 1/4 point now and not leave it until the next meeting. I don't see what we're going to learn in the next three weeks that's going to change anything.

CHAIRMAN GREENSPAN. Other comments?

VICE CHAIRMAN MCDONOUGH. Mr. Chairman, this is Bill McDonough from New York. The views expressed by Al Broaddus are rather consistent with my own. It is very likely, as you suggested yourself, that we will have to take a rather close look at where we stand on policy at the next meeting. However, I think it would be very much more advisable for us to wait until then than to do anything now. I do feel that the markets overreacted somewhat to a variety of news around the world, both in Europe and in the United States. We have had some very significant losses--not just that by Mr. Soros and company in the exchange and fixed-income markets but to some degree in equity markets as well. We're still dealing with very nervous markets, which we might confuse rather than convince. I understand Jerry Jordan's position; but the answer to his question is, without doubt, a matter of judgment. My own judgment is that we are better off to get the additional information that we could get on the economy in the next few weeks, and let the markets calm down to a degree, which I think they will do largely because they are oversold. In conclusion, I believe that the best course of action for us is watchful waiting with the likelihood that we would make the next policy decision--which could be a change of policy or not--when we are physically together at the next meeting.

MR. HOENIG. Mr. Chairman, this is Tom Hoenig. May I ask Bill or Joan a follow-up question? It has to do with the earlier comments about the uncertainty of this other shoe hanging over the market and the possibility of this creating uncertainty. Is it your feeling, Bill or Joan, that the markets, knowing what's out there, will self-correct between now and the next meeting or are we going to be dealing with this until we act again and bring some firmness to the market? That's really an area that's bothersome to me.

MS. LOVETT. A lot depends on how quickly people begin to discount a fair amount of adverse news. And in fact they have not reacted to some positive news. At this point, as Bill mentioned, they're oversold, so that expectations are bound with that and on timing of something like the March meeting. And I think it would just depend on whether the new information that comes out is stronger than has been discounted or not.

VICE CHAIRMAN MCDONOUGH. I generally agree with what Joan said. I think to a very large degree one is dealing with the psychology of markets. If we were to move now, I think we would be perceived to have decided that inflation was getting ahead of us and that we were fearful of being behind the curve. If that interpretation is accurate, which I think it is, I believe that a move now would not, in fact, make them believe that the other shoe has dropped but that there is a multfooted critter in the hotel room above. The only question is how many, and with what frequency, quite a number of other shoes will drop.

MR. PARRY. Mr. Chairman, this is Bob Parry. My view is that one certainly could justify an additional move. But quite frankly, whether it's right now or in a couple of weeks is not particularly important in my view. I worry a bit about how much of the increase in long-term rates is an increase in real rates or a change in inflationary expectations. I wonder what you or Dave Lindsey might think about this. I'm a little concerned, at least based upon some of the things I read, that perhaps an element in the increase in rates is a function of people's assessment that the inflationary prospects longer term are not as positive as they were perhaps a month or several months ago.

CHAIRMAN GREENSPAN. Bob, I would be inclined to think it's more likely a real increase, in part because it is showing up around the world. If you look at the pattern of long-term rates from December through the current period and you plot the German, French, American, and I suspect a couple of other rates, they fit remarkably closely. And it's hard to argue that inflation expectations are really beginning to pick up in Europe. That is one of the reasons why I raised in my Humphrey-Hawkins testimony the question of index bonds; it would be very useful at this stage to have an insight into that. My own guess at the moment is that this is more real than inflation expectations. And one of my reasons is that we may be imparting, through the long end of the market, more restraint to this recovery than I think we would have anticipated. But the truth of the matter is that I don't think we can know at this particular point. How the markets behave in the next several weeks will create some useful information in this regard.

MR. PARRY. Thank you.

MS. MINEHAN. Mr. Chairman, this is Cathy Minehan in Boston. We would also agree with the idea of waiting, with the expectation that there will be some settling down in the long bond market. We also view the data as a little suspect given that they are affected so much by weather and the earthquake. On a local front here, we are seeing very weak retail numbers with no pressure on prices. There is some strength in our manufacturing base, which isn't that large, but again with no pressure on prices whatsoever. So, while it's probably true that in the next few months there has to be some tightening, we would like to see some more numbers before we could feel good about raising rates.

CHAIRMAN GREENSPAN. Anyone else out there want to add anything?

MR. MELZER. Alan, this is Tom Melzer. I would just comment that I agree with your statement that we can't really know what's impacting longer-term rates--whether it's an increase in the real component or an increase in inflationary expectations. In any event, we can't do much about that except over the very long term; and that's in the way we affect inflation and inflationary expectations. So, in a sense, no matter what's going on out there, it doesn't diminish in my mind the fact that with respect to where the funds rate is, we are probably significantly out of position. And to the extent that we are, over longer periods of time that's going to mean very expansive growth rates of the narrower aggregates to hold the funds rate there, and in the long run that will have inflationary implications. So,

just as a general matter, I would associate myself with Al Broaddus. I think we're out of position and the sooner we get to what we perceive to be a neutral stance the better. I don't think there's any compelling need to make a move today on this call, but I do think we have to make these judgments based on a much longer-term view of where policy has been positioned over a period of time and where we need to get it, as opposed to the interpretation of short-term economic data, which I think will be distorted. We certainly have had major weather distortions in our District both in Louisville, as Susan Phillips mentioned before, and also more recently in southern Arkansas and northern Mississippi. So, there will be distortions to the data. The only other thing I would say in general--and I don't think anyone has done this but we should be mindful of it--is that talking the market down in this environment would not be well received by market participants. In fact, I think that would be viewed as an effort to substitute words for action. What really affects credibility at this stage is our action. So, in my mind, the less said and the more done the better.

CHAIRMAN GREENSPAN. Anyone else? If not, let me quickly review the G-7 meeting in Frankfurt. Most of the time was spent on Russia, both internally among the G-7 members and then in an extended meeting with the Russian group, which was invited to the meeting. One gained a sense of fairly considerable frustration as to the inability to get Russia to move on a more credible course. We talked a great deal about the issue of their being on a vicious cycle; that is, they're in a position where they can't get out of the problem, where their establishment of the safety net is embodied in the demand for products of a number of dinosaur companies that is falling. A reduction in production is not acceptable because there's no way to keep people employed; that leads the central bank into the dilemma of either supplying credit to the establishments to keep them going or creating a major increase in unemployment with no safety net effectively there. And there was, I must say, a degree of general discouragement within the G-7 as to how to break out of that cycle. We discussed the issue of finding a means to move the safety net out of the establishments into independent entities that exist in the western markets. But the interesting response that the IMF and the World Bank apparently got in endeavoring to suggest that in one way or another is that the Russians are not focusing on that. The Russians certainly don't want to use any borrowed money from the IMF and World Bank to finance the safety net because they tend to endorse the old classical view, which is not altogether awful, that one should borrow only when one is investing in something. So, I thought the general discussion among the G-7 members on Russia was quite animated but, frankly, it didn't carry the ball very far beyond where much of the discussion has been.

In the other part of the meeting, there was a lot of discussion about the economic outlook and about interest rates. Basically, the view as to the rise in rates worldwide was one of expected increased economic activity here, obviously. But there also was some sense that the economic outlook, even though less than spectacular, is picking up a bit in Europe and that's creating a bottoming in rates. There is a fairly broad view that this rise may be temporary and that the expansion may dip down later. The Japanese were quite pessimistic about the outlook; they didn't see any particular evidence of increases and, even though they had positive GDP forecasts, it's the weakest outlook I've heard coming from an official Japanese delegation at the G-7 that I can recall.

In the Congressional hearings that are coming up, we've had some discussions on consolidated regulation with the Treasury.

It's pretty obvious to me at this point that the general principles that we consider inviolate here are not accepted at this stage by Treasury. We view the question of the choice of the charter as a crucial issue to maintaining a safety valve in the regulatory system when we are dealing with statutes, which of necessity are very broad, and rulemaking, which has a very significant degree of arbitrariness to it and the potential for considerable misapplication of policy. Under those conditions, I think we see the need for choice and a safety valve as nonnegotiable. We also are concerned about the apparent degree to which the Treasury is coming in our direction officially as they will indicate in tomorrow's testimony. We consider it quite inadequate frankly; it doesn't in any way meet what we think is appropriate. I will be testifying pretty much on the basis of the IBAA speech that I made. That came out of a number of the discussions we've been having here. Frankly, I think that we're likely to go through four days of hearings in which a lot is said, but it will be clear that the banks have come pretty much in our direction. The issue that comes up, obviously, is this: If the whole purpose of this was improved efficiency and very specifically to address the problems expressed by banks, it's hard to argue that the proposal, for example, that John LaWare put out doesn't actually do that pretty much without undercutting the position of the central bank in our necessary systemic risk and monetary policy considerations. That's a consequence of maintaining the Federal Reserve as a major regulator and maintaining the issue of choice with the continuation of the dual banking system.

It's going to be an interesting set of hearings. It's not obvious to me that there is anything resembling a majority for the Treasury's position in the Senate Banking Committee. I think the vast majority of them are going to be arguing that the Treasury has to find an acceptable solution because the issues probably are too complex, basically, for them to deal with. I testify with the other regulators on Wednesday. Secretary Bentsen is up tomorrow. On Thursday, the various banking interest groups come on. On Friday the GAO will be making a presentation as will a number of economists who, one must presume, basically are in favor of the President's position and legal position or else why were they invited. So, that's basically the story. We'll know a great deal more about this a week from now. And

my suspicion is that we will either come to an agreement with the Treasury that we find acceptable or nothing very much is likely to happen. That's about it from me. Does anybody have any questions? If not, we look forward to the next meeting--is it March the 22nd?

MR. BERNARD. The 22nd.

CHAIRMAN GREENSPAN. March 22; hopefully, we'll have a go-around and get up-to-date insights on where it is we are and where it is we at the central bank want to be. So, I wish you all good night.

END OF SESSION