

Meeting of the Federal Open Market Committee

October 1, 1985

Minutes of Actions

A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington, D. C., on Tuesday, October 1, 1985, at 9:00 a.m.

PRESENT: Mr. Volcker, Chairman
Mr. Corrigan, Vice Chairman
Mr. Balles
Mr. Black
Mr. Forrestal
Mr. Keehn
Mr. Martin
Mr. Partee
Mr. Rice
Ms. Seger
Mr. Wallich

Mr. Guffey, Mrs. Horn, Messrs. Melzer and Morris, Alternate Members of the Federal Open Market Committee

Messrs. Boehne, Boykin, and Stern, Presidents of the Federal Reserve Banks of Philadelphia, Dallas, and Minneapolis, respectively

Mr. Axilrod, Staff Director and Secretary
Mr. Bernard, Assistant Secretary
Mrs. Steele, 1/ Deputy Assistant Secretary
Mr. Bradfield, General Counsel
Mr. Oltman, 1/ Deputy General Counsel
Mr. Kichline, Economist
Mr. Truman, Economist (International)

Messrs. Broaddus,1/ R. Davis,1/ Kohn,1/ Lindsey,1/ Prell,1/ Scheld,1/ and Ms. Tschinkel,1/ Associate Economists

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

1/ Entered meeting after action to ratify foreign currency transactions.

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Mr. Coyne, Assistant to the Board of Governors
Mr. Roberts, Assistant to the Chairman, Board of Governors
Mr. Promisel,1/ Senior Associate Director, Division of
International Finance, Board of Governors
Mr. Gemmill,1/ Staff Adviser, Division of International
Finance, Board of Governors
Mrs. Low,1/ Open Market Secretariat Assistant,
Board of Governors

Messrs. T. Davis,1/ Lang,1/ Ms. Munnell,1/ and Mr. Rolnick,1/
Senior Vice Presidents, Federal Reserve Banks of
Kansas City, Philadelphia, Boston, and Minneapolis,
respectively

Messrs. Burger,1/ Pearce,1/ and Scadding,1/ Vice Presidents,
Federal Reserve Banks of St. Louis, Dallas, and
San Francisco, respectively

Mr. Sniderman,1/ Assistant Vice President, Federal Reserve
Bank of Cleveland

Ms. Meulendyke,1/ Manager, Securities Department,
Federal Reserve Bank of New York

By unanimous vote, the minutes of actions taken at the meeting of
the Federal Open Market Committee held on August 20, 1985, were approved.

By unanimous vote, System open market transactions in foreign
currencies during the period August 20, 1985, through September 30, 1985,
were ratified.

By unanimous vote, System open market transactions in Government
securities and agency obligations during the period August 20, 1985, through
September 30, 1985, were ratified.

By unanimous vote, the Committee approved an increase from \$8.0
billion to \$10.0 billion in the limit on the System's overall open position
in all foreign currencies contained in paragraph 1D of the Authorization
for Foreign Currency Operations. This action was effective immediately.

1/ Entered meeting after action to ratify foreign currency transactions.

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With Mr. Black dissenting, the Federal Reserve Bank of New York was authorized and directed, until otherwise directed by the Committee, to execute transactions in the System Account in accordance with the following domestic policy directive:

The information reviewed at this meeting suggests that economic activity expanded in the third quarter at a moderately faster rate than in the first half of the year. In August, industrial production increased somewhat. Total retail sales rose considerably, boosted by a surge in auto sales. Housing starts, while increasing in August, were still no higher than their average level in the second quarter. Incoming information generally suggested a leveling of business capital spending. The merchandise trade deficit in July and August averaged somewhat less than in the second quarter as a drop in imports was partly offset by a slight decline in exports. Total nonfarm payroll employment rose somewhat more in August than in most other recent months. The civilian unemployment rate fell from 7.3 percent in July -- its level since February -- to 7.0 percent in August. Broad measures of prices and wages appear to be rising at rates close to or somewhat below those recorded earlier in the year.

Following the Committee's meeting on August 20, the trade-weighted value of the dollar against major foreign currencies appreciated through mid-September. The dollar subsequently declined sharply, especially after the announcement on September 22 by the Finance Ministers and Central Bank Governors of the G-5 countries that exchange rates have not fully reflected economic fundamentals.

M1 growth surged in August, reflecting exceptional strength in interest-bearing checkable deposits and relatively rapid expansion in other components; data for the first half of September suggest slower but still substantial expansion. Reflecting the surge in M1, M2 accelerated in August, and M3 also strengthened somewhat. Expansion in total domestic nonfinancial debt has remained relatively rapid. Most market interest rates have changed little on balance since the August meeting of the Committee.

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The Federal Open Market Committee seeks to foster monetary and financial conditions that will help to reduce inflation further, promote growth in output on a sustainable basis, and contribute to an improved pattern of international transactions. In furtherance of these objectives the Committee at the July meeting reaffirmed ranges for the year of 6 to 9 percent for M2 and 6 to 9-1/2 percent for M3. The associated range for total domestic nonfinancial debt was reaffirmed at 9 to 12 percent. With respect to M1, the base was moved forward to the second quarter of 1985 and a range was established at an annual growth rate of 3 to 8 percent. The range takes account of expectations of a return of velocity growth toward more usual patterns, following the sharp decline in velocity during the first half of the year, while also recognizing a higher degree of uncertainty regarding that behavior. The appropriateness of the new range will continue to be reexamined in the light of evidence with respect to economic and financial developments including developments in foreign exchange markets. More generally, the Committee agreed that growth in the aggregates may be in the upper parts of their ranges, depending on continuing developments with respect to velocity and provided that inflationary pressures remain subdued.

For 1986 the Committee agreed on tentative ranges of monetary growth, measured from the fourth quarter of 1985 to the fourth quarter of 1986, of 4 to 7 percent for M1, 6 to 9 percent for M2, and 6 to 9 percent for M3. The associated range for growth in total domestic nonfinancial debt was provisionally set at 8 to 11 percent for 1986. With respect to M1 particularly, the Committee recognized that uncertainties surrounding recent behavior of velocity would require careful reappraisal of the target range at the beginning of 1986. Moreover, in establishing ranges for next year, the Committee also recognized that account would need to be taken of experience with institutional and depositor behavior in response to the completion of deposit rate deregulation early in the year.

In the implementation of policy for the immediate future, the Committee seeks to maintain the degree of pressure on reserve positions sought in recent weeks. This action is expected to be consistent with growth in M2 and M3 over the period from September to December

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at annual rates of about 6 to 7 percent. A marked slowing of M1 growth over the period to an annual rate of around 6 to 7 percent is also anticipated; slower growth over the next three months would be acceptable in the context of satisfactory economic performance, given recent very rapid growth in M1. Somewhat greater or lesser reserve restraint would be acceptable depending on behavior of the aggregates, taking account of appraisals of the strength of the business expansion, developments in foreign exchange markets, progress against inflation, and conditions in domestic and international credit markets. The Chairman may call for Committee consultation if it appears to the Manager for Domestic Operations that reserve conditions during the period before the next meeting are likely to be associated with a federal funds rate persistently outside a range of 6 to 10 percent.

It was agreed that the next meeting of the Committee would be held on November 5, 1985.

The meeting adjourned.

Secretary

Secretary's Note: On October 24, 1985, the Committee members approved an increase of \$500 million, to a level of \$2.0 billion, in the intermeeting limit on changes in the System's overall open position in foreign currencies specified under paragraph 2A of the "Procedural Instructions with Respect to Foreign Currency Operations." The action was effective October 24, 1985, for the period ending November 5, 1985.

Votes for this action: Messrs. Volcker, Black, Guffey, Keehn, Martin, Melzer, Rice, Ms. Seger, and Mr. Timlen. Votes against this action: None. Absent and not voting: Messrs. Partee and Wallich (Messrs. Guffey, Melzer, and Timlen voted as alternates).