

Meeting of the Federal Open Market Committee

December 15-16, 1986

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 Monday, December 15, 1986, at 3:30 p.m. and continuing on Tuesday, December 16, 1986, at 9:15 a.m.

PRESENT: Mr. Volcker, Chairman
Mr. Corrigan, Vice Chairman
Mr. Angell
Mr. Guffey
Mr. Heller
Mrs. Horn
Mr. Johnson
Mr. Melzer
Mr. Morris
Ms. Seger

Messrs. Boehne, Boykin, Keehn, 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. Bernard, Assistant Secretary
Mr. Bradfield, General Counsel
Mr. Kichline, Economist
Mr. Truman, Economist (International)

Messrs. Balbach, J. Davis, R. Davis, T. Davis,
Kohn, Prell and Siegman, Associate Economists

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

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

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

Mr. Oltman, Executive Vice President, Federal Reserve Bank
of New York

Messrs. Broaddus, Lang, Scheld, Rosenblum, and Ms. Tschinkel,
Senior Vice Presidents, Federal Reserve Banks of
Richmond, Philadelphia, Chicago, Dallas, and
Atlanta, respectively

Messrs. Beebe, Fieleke, and Miller, Vice Presidents,
Federal Reserve Banks of San Francisco, Boston, and
Minneapolis, respectively

Mr. Guentner, Securities, 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 November 5, 1986, were approved.

By unanimous vote, System open market transactions in government
securities and federal agency obligations during the period November 5, 1986,
through December 15, 1986, were ratified.

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

The information reviewed at this meeting suggests
that economic activity continues to grow at a moderate
pace in the current quarter. Total nonfarm payroll
employment grew appreciably further in October and
November, and employment in manufacturing also rose
after declining on balance in previous months. The
civilian unemployment rate remained at 7.0 percent in
November for the third consecutive month. Industrial
production picked up considerably in November. Total
retail sales rose moderately last month after changing

little on balance over September and October. Housing starts have weakened and business capital spending generally appears to have remained sluggish. Preliminary data for the U.S. merchandise trade deficit in October suggest a moderate narrowing. Broad measures of prices have firmed somewhat in recent months due to developments in food and energy markets. Labor cost increases this year have remained moderate compared with other recent years.

Growth of M2 slowed substantially in November, while growth of M3 remained moderate. Expansion of these two aggregates for the year through November has been just below the upper end of their respective ranges established by the Committee for 1986. In November growth of M1 accelerated to a very rapid rate. Expansion in total domestic nonfinancial debt remains appreciably above the Committee's monitoring range for 1986. Short-term interest rates have risen somewhat since the November 5 meeting of the Committee, while long-term rates have declined on balance. In foreign exchange markets the trade-weighted value of the dollar against other G-10 currencies has declined moderately on balance since the November meeting.

The Federal Open Market Committee seeks monetary and financial conditions that will foster reasonable price stability over time, promote growth in output on a sustainable basis, and contribute to an improved pattern of international transactions. In furtherance of these objectives the Committee agreed at the July meeting to reaffirm the ranges established in February for growth of 6 to 9 percent for both M2 and M3, measured from the fourth quarter of 1985 to the fourth quarter of 1986. With respect to M1, the Committee recognized that, based on the experience of recent years, the behavior of that aggregate is subject to substantial uncertainties in relation to economic activity and prices, depending among other things on the responsiveness of M1 growth to changes in interest rates. In light of these uncertainties and of the substantial decline in velocity in the first half of the year, the Committee decided that growth of M1 in excess of the previously established 3 to 8 percent range for 1986 would be acceptable. Acceptable growth of M1 over the remainder of the year would depend on the behavior of

velocity, growth in the other monetary aggregates, developments in the economy and financial markets, and price pressures. Given its rapid growth in the early part of the year, the Committee recognized that the increase in total domestic nonfinancial debt in 1986 may exceed its monitoring range of 8 to 11 percent, but felt an increase in that range would provide an inappropriate benchmark for evaluating longer-term trends in that aggregate.

For 1987 the Committee agreed on tentative ranges of monetary growth, measured from the fourth quarter of 1986 to the fourth quarter of 1987, of 5-1/2 to 8-1/2 percent for M2 and M3. While a range of 3 to 8 percent for M1 in 1987 would appear appropriate in the light of most historical experience, the Committee recognized that the exceptional uncertainties surrounding the behavior of M1 velocity over the more recent period would require careful appraisal of the target range at the beginning of 1987. The associated range for growth in total domestic nonfinancial debt was provisionally set at 8 to 11 percent for 1987.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. This action is expected to be consistent with growth in M2 and M3 over the period from November to March at an annual rate of about 7 percent. Growth in M1 will continue to be appraised in the light of the behavior of M2 and M3 and the other factors cited below. Slightly greater reserve restraint or somewhat lesser reserve restraint would be acceptable depending on the behavior of the aggregates, taking into account 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 4 to 8 percent.

It was agreed that the next meeting of the Committee would be held on February 10-11, 1987.

The meeting adjourned.