

TRANSCRIPT

FEDERAL OPEN MARKET COMMITTEE MEETING

October 6, 1979

Prefatory Note

This transcript has been produced from the original raw transcript in the FOMC Secretariat's files. The Secretariat has lightly edited the original to facilitate the reader's understanding. Where one or more words were missed or garbled in the transcription, the notation "unintelligible" has been inserted. In some instances, words have been added in brackets to complete a speaker's thought or to correct an obvious transcription error or misstatement.

Errors undoubtedly remain. The raw transcript was not fully edited for accuracy at the time it was produced because it was intended only as an aid to the Secretariat in preparing the record of the Committee's policy actions. The edited transcript has not been reviewed by present or past members of the Committee.

Aside from the editing to facilitate the reader's understanding, the only deletions involve a very small amount of confidential information regarding foreign central banks, businesses, and persons that are identified or identifiable. Deleted passages are indicated by gaps in the text. All information deleted in this manner is exempt from disclosure under applicable provisions of the Freedom of Information Act.

Meeting of Federal Open Market Committee

October 6, 1979

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 Saturday, October 6, 1979, beginning at 10:10 a.m.

PRESENT: Mr. Volcker, Chairman
Mr. Balles
Mr. Black
Mr. Coldwell
Mr. Kimbrel
Mr. Mayo
Mr. Partee
Mr. Rice
Mr. Schultz
Mrs. Teeters
Mr. Wallich

Messrs. Guffey, Morris, Roos, Timlen, and Winn,
Alternate Members of the Federal Open Market
Committee

Messrs. Baughman and Eastburn, Presidents of
the Federal Reserve Banks of Dallas and
Philadelphia, respectively

Mr. Altmann, Secretary
Mr. Bernard, Assistant Secretary
Mr. Petersen, General Counsel
Mr. Axilrod, Economist
Mr. Holmes, Adviser for Market Operations

Messrs. Ettin, Kichline, and Truman, Associate
Economists

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

Mr. Allison, Secretary of the Board of
Governors

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Mr. Coyne, Assistant to the Board of
Governors

Mr. Beck, Senior Economist, Banking
Section, Division of Research and
Statistics, Board of Governors

Ms. Farar, Economist, Open Market Secre-
tariat, Board of Governors

Mr. Corrigan, Vice President, Federal
Reserve Bank of New York

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CHAIRMAN VOLCKER. Well, gentlemen, I think we might as well start. I hate to start without Emmett but he seems to have been incommunicado for 40 minutes now, so let's begin. Maybe we should take a minute to hear Mr. Kichline go over the latest business news. I realize you did that yesterday, Jim, but not everybody had the benefit of your comments yesterday. So, why don't you do that.

MR. KICHLINE. All right. I'll try to be brief. Economic activity in the third quarter appears to have expanded a little faster than we had anticipated earlier. We now believe that real GNP probably grew at an annual rate of around 1-1/2 percent, maybe a shade higher. Employment, production, and sales all seem to have been somewhat higher. The most recent news, of course, was on the employment situation in September. Total employment grew substantially and the unemployment rate dropped 0.2 percentage point to 5.8 percent. Industrial production now appears to have grown about 1/2 percent in September on the basis of the most recent labor market report and some physical product data on auto sales and steel production. As you know, housing starts were unchanged in August at 1.8 million. We have some additional information that suggests capital goods shipments in August were rather stronger than we had anticipated as well. On the inventory side, inventory still seemed to have been accumulated at a substantial pace in August, at least at the manufacturing level. And this is an area of growing concern given what we perceive to be substantial imbalances developing unless we get sustained growth in final sales or further downward adjustments in production.

While the recent data clearly suggest more strength than the staff had anticipated at the last meeting of the Committee, the fundamentals still seem to be running against sustained growth in coming quarters. Namely, I would point to declining real income, which we have now had since December of last year. At the present time we think that real growth in the fourth quarter is likely to decline at about a 3-1/2 percent annual rate, which is a bit bigger decline than we had estimated earlier. But over the whole projection period through 1980 we don't anticipate any significant change in the forecast we presented to the Committee in September. On the price side, the most recent information relates to production. The producer price index, as you know, increased at a 1.4 percent annual rate. It was particularly discouraging. There were widespread increases, with food and energy prices continuing to rise very rapidly.

CHAIRMAN VOLCKER. We might take just a minute to see if any of the Presidents in particular have comments they would like to make on the business scene from [a regional] perspective that would add to the statistical information that we've had on prices, production, or other fronts. Let's hear quickly.

MR. MORRIS. Well, I think we're seeing an amazing replay of 1974-75. We have declining final demand, with the economy cushioned by very large inventory accumulation that produces big demand for bank credit, resulting in growth in the aggregates. And we've been leaning against that growth by pushing up the federal funds rate. I gave a

talk to my directors on Tuesday in which I overlaid the 1974-75 period on the current period. I assumed March '79 was the peak in this period and compared that to the November '73 peak. The behavior, including the tracking of the federal funds rate, is amazingly similar. It seems to me that we have a very big inventory accumulation; and when the inventory accumulation does stop, I think the recession is likely to be bigger than we are projecting.

MR. BAUGHMAN. Did you see evidence of a credit crunch in that earlier period?

MR. MORRIS. Well, I don't have a measure of credit crunch but I do have measures of the funds rate and the rate of growth in the money supply, and the behavior of those is quite similar.

MR. BAUGHMAN. My recollection is that we had a very different situation with respect to credit availability but I was told just recently that a bank from Chicago was working diligently in an eastern area to round up business loans. We wouldn't have had that, I think, in 1975.

MR. MORRIS. Well, I think the money center banks are still very aggressively looking for loans. But if you go outside the money centers, the banks are very tight. At least they are in New England.

MR. PARTEE. Of course, the real estate situation is entirely different, with 1.8 million housing starts. That compares with what we had, say, in the summer of '74 when starts were down to a 1.1 million annual rate or thereabouts and there just wasn't any mortgage money.

MR. MORRIS. But the state and local sector is much weaker than it was in 1974-75.

MR. PARTEE. That's true.

MR. WALLICH. That is hardly speculative although it's a little speculative. In '74 it was virulent.

MR. COLDWELL. In '74 we had a constraint in terms of capacity that we haven't faced to a big degree.

MR. BALLE. To follow up on what Ernie said, I've had conversations in some depth with various directors over the last week and whether they're businessmen or bankers they report essentially the same story--that the present level of interest rates, in contrast to the situation generally in '74, is just not deterring borrowing in any way that they can see. I'm sure that's not true for everybody in the country; small businesses and farmers are in a big cash flow bind. But medium- and larger-size companies, according to the companies themselves as well as their bankers, just don't blink at this level of interest rates. They just go ahead and borrow anyway. I don't think we're approaching the credit crunch type of situation that we had in '74. I think that's one of the big differences.

MR. MAYO. We have plenty of tightness at 90 percent of our banks but they probably don't account for more than half of the business. And the other 10 percent can get money whenever they want.

MR. MORRIS. But bank credit was expanding pretty rapidly in the first half of '74.

CHAIRMAN VOLCKER. Any other quick comments?

MR. EASTBURN. Yes, Paul. A quick and informal [survey] of some people in our area confirms a bit what I think Frank [Morris] was saying. There's increasing concern about the inventory situation and the likelihood that the recession is going to be more severe than they had thought. This is on the part of retailers and of bankers who have some feeling that the strength in business loans is inventory-based and that it is going to collapse.

MR. TIMLEN. We had a businessmen's meeting in our Bank about a week ago and we had three or four industrialists as part of the group. Of the three or four, all were predicting a rather good year in 1980 with the exception of one that is a supplier to the automotive industry. It's generally the same kind of [story] we've been hearing for a long time. The industrialists were all vigorously defending their accomplishments in the area of productivity. They were saying that their own companies were doing very well in that regard and they thought the national statistics really related to the services field and government regulations. One of the people there was a mutual savings banker who was not very happy about the prospect for deposits in New York for the next quarter.

CHAIRMAN VOLCKER. If there are no other comments--. Bones did you want to comment?

MR. KIMBREL. I'd simply echo [Tom Timlen]. In the last week we had a series of business leaders in from Jacksonville, Atlanta, and New Orleans. They [exhibited] an enthusiastic lack of confidence in so many areas. But for their own individual businesses the only expression of any concern was from a convenience store operator with about 1500 outlets who suggested that one [sign] of a possible recession was the fact that they were having many more thefts--more stealing [of merchandise] as well as robberies. That was the only [indication] of recession they could see.

MR. MAYO. Sales at Sears Roebuck were ahead of last year for the first time in twelve months.

MR. PARTEE. Was a year ago bad, do you recall?

MR. MAYO. Well, Sears has gone through particular problems.

MR. PARTEE. It seems to me that they were in bad shape about a year ago.

MR. MAYO. It shouldn't be used as an example for the whole country.

MR. PARTEE. Wards had a very small change over a year ago.

MR. MAYO. Yes, but Penneys and Kmart are still doing fine.

CHAIRMAN VOLCKER. Well, let me say where I think we are even though Emmett is still absent. I appreciate your all standing by so

patiently over the past few days, but we've had a few complications putting this together, with some people out of town and so forth. Just in terms of the schedule for today, I think we have to assume that the Board of Governors is going to have to meet after we get finished. And depending upon what we decide, the presidents may want to meet, too, to discuss any reserve requirement changes and what kinds of problems that will create in the short run. [Unintelligible] and we may need to talk about straightening out mechanical problems that may arise [when we implement] any decisions we make. So we can play that by ear as we go along.

I don't know how long we're going to have to be here today. We will be here until we arrive at a consensus and proceed [from there]. I'm not sure when we would announce any decision that we make--whether we'd do it late today or Monday morning. Those seem to be the two practical alternatives with the Pope here rather blanketing the area [news] tomorrow and creating a little difficulty [for us] in terms of an orderly announcement.

Let me say that I think there are several dimensions to the current situation. We wouldn't be here today if we didn't have a problem with the state of the markets, whether international or domestic. They were pretty feverish last week--or beginning in the previous week, really. Beginning about 2 weeks ago and carrying over into the early part of what is still this week, the foreign exchange market was in a situation that was clearly not amenable for very long to such techniques as intervention. The markets have turned around some in the past few days, as you know. I think that is almost entirely explicable by the fact that at about the time I returned from Belgrade Treasury officials and others were making some statements that left hanging the possibility of some kind of a package, so the foreign exchange dealers have retreated to the sidelines.

MR. WALLICH. The reporters left the room when [Secretary] Miller said that Paul had gone home. They just rushed to the phones.

CHAIRMAN VOLCKER. That typically is the case these days. I arrived at the airport and there was a reporter accompanying me on the plane. I don't know when he got to a telephone; he couldn't until we got to London. I have thought that one way of managing the markets might be to ascend in an airplane and just circle, with a refueling [plane] and no known destination! [Laughter]

I don't think we can count on that [state of relative calm] for very long. In fact, as you know, while the markets have been standing still or even declining, the gold market has not exactly been in a calm situation. And the phone calls have begun to escalate, reflecting a kind of extreme nervousness in all directions. I think the rumors that were floating around in the market yesterday--first that I had resigned and then that I had died and then that I was mad at Governor Schultz--are symptomatic of the state of the market. [Market participants] are living with fragile expectations and inspired rumor and all the rest from day to day. I do think that the psychology in that sense is ready to crack open, depending upon what decisions they see coming out of here or elsewhere in a very short-term time horizon.

Now I turn to the economy and you know generally the situation there. We have had at least an Indian Summer, which I suppose raises some questions in peoples' minds as to whether the recession is all that imminent after all. There is an inventory problem potentially or actually without any question. I myself feel a little less--concerned isn't quite the right word. I think the risks of the economy dropping off--. [Secretary's note: Mr. Rice arrived at the meeting.] There you are! I'm sorry that somehow somebody didn't get the accurate word to you on the timing here. We really just started. I have described the state of the markets as in some sense as nervous as I have ever seen them.

In terms of the economy, I was about to say that my own concerns about the risks of the economy falling off the table, though they have not evaporated, have diminished a bit. The possibility of that occurring appears to be somewhat delayed at the least. My own judgment of this may change, but I think the risks certainly are a little less than they were before. That's a judgment that may not mean much if I don't tell you what I thought the risks were earlier. I thought they were significant. But [the possibility of a downturn] seems to me at least postponed.

On the price front, expectations have certainly gotten worse rather than better. Even though the price news is bad, it does not in my judgment as yet reflect a spreading of the whole inflationary force into areas outside of energy. We had a fluctuation in food [prices] last month, but that [component of the price index] goes up and down. If we look at the wage trend, so far as we know--with the exception of the General Motors settlement--we haven't had a real breakout yet. But we're dealing with a situation where that's an imminent danger on the one side as is the possibility of a recession on the other side. Mr. Schultz had an apt description the other day of where we are--and I certainly share the feeling--in saying that Scylla and Charybdis have now come together. There is clearly no risk-free course for us here; there are risks on both sides. The idea that we can absolutely thread the needle between the risks is probably a nice hope but it may be an illusion. At this stage you've got to place your bets one way or the other and move.

I certainly conclude from all of this that we can't walk away today without a program that is strong in fact and perceived as strong in terms of dealing with the situation. I would put that case into context. Ignoring some of the more feverish psychology for the moment, we are in an interim period of sorts where if some of what I think are quite reasonable--but never absolutely certain--projections develop in a favorable way we're not going to see that in fact in the statistics. The statistics are not going to be convincing to anybody for a period of some months. I'm thinking there particularly on the price front where, if the present trends continue and we don't have an excessive oil price increase from OPEC in December, energy prices shouldn't level off in any absolute terms but should come down from the enormous rates of increase recorded in recent months. And if other prices are held more or less in check, there is a chance that inflation will at least come down toward the single digit level--and if you want to get hopeful, within the single digit level--by the end of the year or early next year.

If one looks at the balance of payments side, I think most projections, given foreign growth and given the outlook for the domestic economy, suggest that both the trade position and the current account should look considerably better going into 1980. That's simply because, ex-oil, [the external sector] has been doing pretty well and should continue to do pretty well under these conditions. As we get into 1980 the burden of the increased price of oil imports in the price indices should be [diminishing]. So, we could get a substantially stronger looking picture then, but we're not going to know that until probably well into the first quarter. And, of course, current account figures for the whole first quarter aren't going to be out until the Spring. The trade figures come out on a monthly basis and they should reflect [the improvement] to some extent, although part of the projected strength is in non-trade areas of the balance of payments. The point is that there is a bridging or an interim period here before the best news one can [reasonably anticipate] is going to come about. And in the present mood of the markets, I think it's going to take some time before they're convinced. So we have to fit our programs into that interim period.

The other element, of course, is that we are not dealing with a stable psychological or stable expectational situation by any means. And on the inflation front we're probably losing ground. In an expectational sense, I think we certainly are, and that is being reflected in extremely volatile financial markets.

Let me give you a little background in terms of foreign components or elements of the package of anything that we might do here. I want to make a couple of comments that I really consider off the record. I don't know if we want to keep the recorder going or not. I'd prefer not to. Let me just say a few words about the attitudes of foreign countries as I've experienced them first hand. This is not particularly new, although the depths of the feelings... [Secretary's note: The recorder was turned off while the Chairman gave his assessment--based on discussions at recent international meetings--of the views of foreign officials regarding a coordinated package.]

That does not reflect entirely a feeling that a package is impossible, despite all I have said. I think it's clear that an international package is impossible without strong action by the Federal Reserve. But when you look at the components of a traditional package of that kind, there is a question of how impressive it is going to be psychologically. We could perhaps build up something like a \$10 billion further availability of marks through fairly obvious techniques--increasing the swap lines, selling the Germans some SDRs, and drawing on the IMF.

I think, but I'm not saying it's absolutely impossible--in a bind, I should say--if people really thought it would be effective in terms of market psychology. But after a lot of discussion, by general consensus the feeling was that that kind of a package isn't going to add all that much to an announcement at this point, as compared to the other possibility of indicating that resources are not really the problem, which I think is true in the technical sense. If the Germans wanted intervention, they'd provide the resources. And there may be some merit in keeping some of these possibilities dangling over the market for a period of time and perhaps announcing some of them as the period

evolves. That probably would be more effective than trying to wrap them all up in a package that may not be very impressive at the moment anyway.

The Treasury undoubtedly will be announcing a bond issue in the German market, I suspect in a matter of days. They have flexibility in the timing and they will do it when they think they will get some advantage from it. That's not a big deal in the sense that it has been amply leaked in Belgrade already both by the Germans and the Americans. But that will be coming along; I think we can just assume that that is [a given]. There are no specific swaps, SDRs, or IMF drawings [under consideration] for the reasons I suggested. There was no desire to solidify any of that at this point.

The possibility of gold sales has been canvassed up and down. That this is not a great question of philosophy is, I suppose, the way I would word it. This is a very practical question of what seems useful and what doesn't seem useful. The question has been debated up and down and I think it is essentially unsettled. There is a possibility [of gold sales], particularly if the gold market acts up again, but there has been no firm consensus reached on that point simply because in our mutual discussions some concern was expressed about whether they are effective or not effective over a period of time. They might be effective immediately. But if the gold sales have a nice effect immediately and we test it a little while later and the gold price goes up again, the question arises: Is it confidence inspiring or is it not? Or is it really better over a period of time just to leave the [gold] market alone? I think that question has to be left on that basis for the time being. It is indeed an open question and something that I think will depend upon the performance of the markets over a period of time--not just of the gold market, but of all markets. So, that is essentially the background we are dealing with in that area.

We will have cooperation, I think, from our foreign partners either on gold or on intervention to the degree that they feel that we have done something here; that is an essential part of setting the stage. We will get that kind of cooperation, I suppose, with the limitations of enthusiasm that are inherent in my earlier comments. I don't mean to suggest that that type of activity is "out" if we mutually think it is advantageous. On the contrary, it is "in" over a period of time with an appropriate background. But it is not "in" in the sense of announcing an international package of that type this weekend.

Now, when it comes to our action here, I think there are broadly two possibilities. One is taking measures of what might be thought of as the traditional type. That would include a discount rate move on the one side and so far as this Committee is concerned a significant increase in the federal funds rate--putting those moves together. The Board will be considering some reserve requirement changes later today. Let's assume that the package would include that. Also, we would go forward with whatever changes in the federal funds rate we thought appropriate, which would be evident in the market. Or maybe we would say something about that in the announcement of the discount rate change and the reserve requirement change. I think we ought to look at that possibility.

The other possibility is a change in the emphasis of our operations as outlined in the memorandum that was distributed, which I hope you've all had a chance to read. That involves managing Desk operations from week to week essentially, with a greater effort to bring about a reserve path that will in turn achieve a money supply target--which we have to discuss--recognizing that that would require a wider range for the federal funds rate and would involve a more active management of the discount rate. And of course the question of reserve requirements and the discount rate change at this point are relevant in that context too.

As I look at these two approaches there are advantages and disadvantages, obviously, to both of them. I must say that the thought of changing our method of operations germinated--in my mind at least--before the market psychology or nervousness reached the extreme stage it reached over the past week or so. My feeling was that by putting even more emphasis on meeting the money supply targets and changing operating techniques [in order to do so] and thereby changing psychology a bit, we might actually get more bang for the buck. By that I mean our having a more favorable impact on psychology and perhaps a more favorable impact on banks by introducing a little uncertainty per basis point of rise in money market rates than would be possible through the traditional method. I overstate it, but the traditional method of making small moves has in some sense, though not completely, run out of psychological gas. Every time the interest rate goes up by a small amount [bankers] say okay, we'll raise the prime rate. Whatever you do is inadequate--you, the Federal Reserve--and we'll go along. We have access to liquidity at a fairly fixed federal funds rate--the rate isn't going to change all that abruptly--and you're not having much impact on market thinking or on market confidence in your ability to keep the money supply under control. I am not saying that that reasoning is correct but I think it is the reasoning in the market psychologically.

So we run a risk, almost whatever we do, that [in response] to next week's changes they will say: "It's not quite enough; the interest rates should be a little higher. The Fed undershot again." And we won't get the psychological impact we are looking for. So there may be something to [be gained in] a change in the psychological atmosphere that in some sense will give us more bang for the buck, as I put it. It's possible. It's an easier political sale, and we are obviously moving into an area that is sensitive, to say the least. We do have a background of some Congressional thinking that puts great emphasis on the money supply targets. So, to the extent that we accept that emphasis one might argue that we will get more support. I think that it is a factor to be weighed, but there are those who would say: "The hell with all this theorizing about where the targets are; when Congress sees the interest rate effects, that won't make any difference." So it is not a black or white situation by any means but I think it is something we can take into account.

If we're lucky, this change [in our operating technique] will improve our chances of reaching our money supply targets on the one side. On the other side, it has some built-in pressure to move interest rates downward more promptly if the money supply begins running low. If the money supply were running low because the economy was falling off more rapidly, triggering a faster response on the down side clearly might be considered an advantage--and maybe an important

advantage. A context where the decline in interest rates is being related to weakness in the money supply should offer us some psychological and real protection in terms of financial market appraisals of why the interest rates are going down.

Now, there are disadvantages as well, and they are important. To take one that flows immediately out of the advantage that I just cited, some people may consider it a disadvantage that we get too locked into [responding to] fluctuations in the money supply. [That might lead to] a prompt decline in interest rates at a time, let's say, that would be unsettling internationally or might be misinterpreted domestically. So there is clearly an opposite side to that advantage. There is a feeling that we can get stuck. We are going to have to constrain the [funds] range whatever we do; it should be much wider under this approach but we certainly can constrain the fluctuation in an uncertain world. There is a danger that we could get stuck at the top of the range if the money supply turns out to be fairly strong; we'd be back basically to the kind of operation we are in now, bumping against [the upper limit of] a federal funds target, which at that point would be at a higher level than we otherwise really would have wanted. I suppose there are two dangers out of that. We may get a little more restraint than we bargained for; that is one possibility. Another is that we will defeat the psychological purpose if this puts us back into that kind of constraint.

There is a feeling that by responding to the particular situation we have now with a change in technique, we may get locked into a technique that isn't very suitable over the longer run, including into 1980. The technique might have implications for interest rates or other things that we wouldn't be happy about in other situations, yet it would be hard to reverse our ground. I think we also have to consider [the risk] of putting a lot more emphasis now on the money supply targets, knowing that there is no technique that's going to assure that we are going to [achieve] the money supply targets--either because of the inherent lags in the situation, the uncertainties of the money demand function and all the rest, or because we would resist any absolutely extreme movement in interest rates that might be necessary to keep [the money supply] within the target ranges. We could well end up exceeding the targets for the year, after making a hullabaloo about this change in technique. And we could run into a reaction that at that point would be adverse. So there are advantages, disadvantages, and risks on all sides of this equation.

I should report to you that obviously I discussed the whole problem on the international side and inevitably on the domestic side with the Administration. I think I can say flatly that they are ready for a strong program; they would have no disagreement with that conclusion at all. They shy away very strongly or have an uneasy feeling about a shift in technique at this point because of the uncertainties of the situation. There's a rather strong feeling, I think I should report, that that is the more risky course for a variety of reasons that I've touched upon: concern that the interest rate may move in a contrary way at some point in terms of the international situation; considerable concern about locking ourselves into a technique beyond this year that might not be suitable in light of all the circumstances; and concern that an immediate rise in the rate might be excessive depending, of course, upon where the federal

funds rate ceiling is put. But there's a fear on the other hand that if it is put too low we're in a box where we would be bumping against the ceiling all the time.

Finally a feeling that I think we have to consider too, if we do make this change, is that there is no apparent encore for the Federal Reserve; we will have in effect shot our bolt. Now, I don't think that's necessarily a minus, but it's another factor we might want to take into account. It has been clear all along but it's particularly clear at this point that we cannot by brute strength of monetary policy alone correct all the ills in the economy and in economic policy generally. I don't mean to infer that I think economic policy is bad. I think fiscal policy has given us all the support we could ask for right now and, in terms of general business analysis, one might even argue more support than would be absolutely desirable. I don't think we can [count on] the possibility of changing fiscal policy in this psychological situation. I don't believe it should be changed for that reason. But if we change techniques, I think in a broad way we have gone to the limits of what monetary policy can really expect to accomplish and we can't come back with something entirely different a month from now and another [change] two months from now or whenever.

Now, I can go with either of these broad approaches because I think, with regard to our immediate situation, that we can develop an [alternative] package of measures that is basically equivalent in terms of market impact or psychological impact or whatever we want to achieve immediately. I have told you what the instincts are elsewhere; I have also told you that [the Administration] is ready for a strong program. I think it's clear that the decision is one that is within our province and we have to make it today. We need a program that's as convincing as we can make it. In my view it's also very important that we have the widest possible consensus among us in this kind of situation where there is no good answer. I think we all do recognize that there is no good answer, but there is strength in diversity here, if you will. So, to the extent that we have a consensus, that in itself will help carry the program and help achieve what we want to achieve. I am prepared, within the broad parameters, to go with whichever way the consensus wants to go so long as the program is strong, and if we adopt a new approach so long as we are not locked into it indefinitely. If we adopt a new approach, I'd consider it something that we adopted that seems particularly suitable to the situation at this time. We'd obviously gain some experience either pro or con by adopting the new approach. And I would say that early next year or late this year in connection with considering the new [money and credit growth] targets for the next year we would have a thoroughgoing ground up decision as to whether we wanted to maintain this kind of approach, modify it, return to more traditional practices, or whatever. That should be a completely open decision. I was intending to have that discussion in any event at that time and I just don't want to prejudge the issue by whatever we consider suitable at the moment.

And finally I would say that I don't think we can adopt a mechanical approach on the reserve side. While there would be a clear change in emphasis if we decide upon [this new approach], inherent in it is that we simply are going to have to leave a lot of discretion in the actual operations to the Desk, to my benevolent oversight, and to

ex post review [by the Committee] with whatever frequency you would like, looking ahead on an interim basis. But I am not prepared to recommend or to accept a mechanical device that says nonborrowed reserves or the reserve base or total reserves or whatever, are going to meet x figure on a week-to-week basis come hell or high water regardless of what judgments are about the outlook or regardless of whether the interest rate is 17 percent or 6 percent. We are just not going to carry it to that extreme. But if we go in that direction, there is a real change in emphasis involved that would need to be reviewed carefully as we move along.

That is my analysis of the situation. If you have any reactions at a very general level now, let's have them. And then I think we ought to get into more detailed questions about the new approach. The traditional approach is obviously much more clear-cut. It is a quantitative question of where you want to go. Many of the questions overlap. The differences are not night and day, but I think we need the time for a little more exposition on what the new approach would entail.

MR. MAYO. Paul, in your review you made no mention of controls. I hear more rumors about those than you can shake a stick at these days.

CHAIRMAN VOLCKER. Bank credit controls or any kind of controls?

MR. MAYO. Various types.

CHAIRMAN VOLCKER. Well, let me just say a word on that. In this situation we get more talk about that, and there are certainly market rumors. I don't know that I hear such strong rumors that controls are a great possibility right now but there is a very large segment of market opinion that says if not now we are going to be driven to [impose them] later because the situation is out of control. My reaction--which on the basis of some earlier discussions I think is shared by some other Board members and by people in the Administration who at the very least would have to trigger the control mechanism when we're talking about domestic credit controls--is that of all the options one could think of theoretically, that is probably the most dangerous in terms of the business situation. That's because a control program that really bites at all might lead to [undesirable] reactions. For instance, grave questions might be raised about whether financing was available for some of the inventory that one would like to see financed. And all the anticipatory effects, with people trying to protect themselves, would [put the economy on] a very dangerous course at this particular juncture in the business cycle. The feeling is that there is some danger, on which people will put different [probabilities], of the economy having a most severe inventory reaction and indeed [that controls might] even inhibit planning for capital spending that we wouldn't want to inhibit.

Controls in the international dimension have not been discussed at all. I personally cannot conceive of controls in the international area. Forgetting about philosophy or long-term effects or anything else, I can't imagine--I speak for myself--how one would design them so they'd be effective. They would have so many leaks around them because the major types of flows that involve foreign held

dollars [have] leads and lags or what could be disguised as leads or lags. Such controls just don't have any prospect of effectiveness that would make them within the range of possibilities.

MR. COLDWELL. Paul, it seems to me that the situation we are faced with is pretty much as you outlined here. Maybe I could streamline this for my own thinking. I see our objectives as perhaps four-fold--centered around dampening [inflation] expectations, achieving some credit restraint that might flow from that, hopefully strengthening the dollar exchange rate, and--depending upon how one views this--a somewhat self-serving target of meeting our longer-range objectives and bringing growth in the monetary aggregates down. If those are our objectives and I lay heavy stress on the dampening of expectations, then it seems to me that the program has to be strong enough to impress the market. I have my doubts that the foreign market is going to be impressed for three reasons: (A) I don't think they are going to believe it; (B) I don't think they'll understand it in terms of our change [of technique]; and (C) I think they are so skeptical that they'd just say it's too little and, without some effort on the part of the Treasury or somebody else, there would be no direct impact on the gold price.

So it seems to me that we are designing something here to a considerable extent [for] our [domestic] situation, hoping there is a fallout internationally. The risks are large, of course, and [primarily] on the side that whatever recessionary tendencies are already there might be compounded, creating a [greater] decline. I suspect that risk involves 1980, not 1979. I think the risks are equally strong on the other side in that if we don't put out something fully credible, we face a potential blow-up [via] a speculative move in the metals commodities that spreads out from there--in effect a flight from dollars. So I'm prepared to move ahead on this because I think the latter risks are too high.

CHAIRMAN VOLCKER. I'm glad you mentioned the commodities issue. I don't know whether all the Presidents have caught up with this, though I presume they have. Beginning a little more than a week ago, late in the previous week when the gold market was gyrating, there was some very clear evidence that this psychology was getting into the metals markets in particular in a very forceful way and maybe in the grains market very temporarily. There were very sharp price increases in some metals markets which continued into Monday or Tuesday. They have relapsed along with the gold market and the exchange market fervor for the same reason and I'm sure they were related psychologically. But it's worth mentioning that we have this evidence of extreme sensitivity. And the price increase was what--20 percent in the copper market in 2 days or something like that?

MR. PARTEE. Lead went up 20 percent.

CHAIRMAN VOLCKER. Lead went up 20 percent, too. It was frankly a bit of scary psychology to say the least. That has also in some sense relapsed for the moment in this [general] atmosphere of nervous anticipation.

MR. PARTEE. I might make a general comment, Paul. I approach the situation a little differently than Phil does. And I don't pay as much attention to foreign and international aspects as

you do. The thought I would like to emphasize or underline is uncertainty. I think the staff forecast--which I believe is not that much different from the forecast of the Council [of Economic Advisers] or from those one sees in standard private market services--is quite plausible. We certainly do have a lack of final demand right now. We certainly do have a decline in real income and we are going to continue to have a decline in real income. And today, at least in Washington, the winter heating season is beginning. The drain on purchasing power from that is going to be much greater on a seasonally unadjusted basis over the coming six months or so. There will be less money available for everything. So it's fairly reasonable to think that there is going to be a recession trend rather promptly, one that develops and continues over the winter and into the spring. If that's so, why of course we are going to want to try to keep the monetary aggregates growing. And we will have a sudden shift in our problem, which will be overly slow growth rather than overly rapid growth in the aggregates. That's one scenario.

On the other hand, I was extremely bothered by the market developments of the last two weeks. I think the spreading of the gold [market psychology] into the more remote metals is very bothersome. Silver we understand and platinum we understand, but the spreading to copper, zinc, and lead is very bothersome. And not only grains but a number of other futures prices were moving [up], with no real justification for those moves. It leaves one with the thought that because of a run from currency--a desire to get into goods and out of money--we might have now a new development in our economic experience that would lead to a "last gasp" round of demand for goods, probably most intensively for inventory. That might last 2 or 3 months or it might last 4 or 5 months. It's very limited but it could last for a while. And then when the recession occurs, it will be much deeper because in addition to having to adjust to the lower level of final demand, people will have to liquidate inventory. They will move from inventory accumulation to decumulation and we will have a recession that is more like 1975 or perhaps worse than that. If that's the case, for the next few months or during the period in which there's this anxiety and concern about possibly moving from money into goods, it is very important to restrain the growth in the aggregates, and we could be talking about significantly higher interest rates.

With that uncertainty, it seems to me that our traditional method, which is to estimate the short-term market rates that will adjust the demand functions for various kinds of money on a lag structure, has [inherent in] it the danger that we are going to miss. [Either] we will miss an intensification in the demand for money and be behind the gun, as we have tended to be here over the last six months, or we will miss a decline in the demand for money and overstay and be behind the gun, as we traditionally have done [going] into recessions. It's an extremely dangerous, risky proposition to change our operating mode. We have tried it a couple of times. We had RPDs back in the early '70s and we had that experiment a few years ago. For one reason or another--and we know the reasons--they didn't work. But even though it is extremely risky, I think it's the less risky course than to stay with our traditional system. So my emphasis is on uncertainty and the need to be aware of the fact that we no longer can specify interest rates given this uncertainty, rather than our need to tighten up or anything like that at this time.

MR. MORRIS. I agree with Chuck. His analysis fit my views very closely. Despite my view that the recession is going to be sharp, I think we are in a situation where we have to be willing to do something dramatic today. It's not clear to me that a change in operating procedures is going to gain us much yardage on the foreign exchange market because many will not understand what we are doing.

MR. PARTEE. Unless they think it's more of a commitment.

MR. MORRIS. That means that we also have to have some traditional measures to go along with it that they will understand.

CHAIRMAN VOLCKER. No question.

MR. MORRIS. I think the Committee has to understand that we are talking about something that will give the Manager discretion; [I'd] give him at least 2 percentage points on the up side in the next few weeks. We have never done that--that's a dramatic change in our behavior--but that's what we are talking about. And I think our credibility will really suffer if we announce a change in procedure and then fail to have the guts to go through with it.

CHAIRMAN VOLCKER. If I may just interject, Frank, I agree with what you are saying and I think [the issue] has to be approached in that light. But presumably the guts will have a number on it--the degree of our guts on the up side.

MR. MORRIS. Well, that's right. But it's got to be a pretty big number.

CHAIRMAN VOLCKER. I understand.

MR. MORRIS. The other thing is that we are going to need to educate the market very soon on this. So, if we go ahead with this change to a new procedure, I think you ought to have a press conference today.

CHAIRMAN VOLCKER. Well, if we have a new procedure, I will have a press conference. Whether I have it today or Monday is an open question.

MR. MORRIS. [If you have it today], the markets will have the weekend to absorb this.

CHAIRMAN VOLCKER. Well, I don't know. We have a holiday on Monday and we may do the press conference Monday morning. You can assume that I will have a press conference if we go through [with this change].

MR. MORRIS. Are the bond markets closed? Okay.

MR. PARTEE. The stock market is open, but that's it.

MR. EASTBURN. Could I add one other point? I follow along with Frank on this. However, I think there is one [aspect of making a change] that is a disadvantage. I don't think this can be a short-run change in technique because it is going to require a certain amount of time for it to work out. I understand the point that you made about

meeting the special situation we have, but this is a basic change in technique. And we've learned before that it really does take time to know whether [a new technique] works or not. There's a credibility problem if we launch this and stop and go with it. So I really think we are committed to this if we go [forward].

CHAIRMAN VOLCKER. Well, I don't want to accept that. I don't think we can make that decision now. If we [change our operating technique], I do accept the fact that to some degree we have prejudiced the discussion we will have at the end of the year. We will have to have a reason then to move back to the traditional method. But I don't think we can really make that decision now, nor should we. Nor do I think this commits us that fully, though it prejudices to some degree what we would do next year.

MR. PARTEE. We'd run it for several months in any event.

CHAIRMAN VOLCKER. Oh yes. I think we are committed for several months.

MR. EASTBURN. I'm thinking partly in terms of the public impact that this will have. If the impression is conveyed that this is something we are just trying, I really don't think it will have the impact on credibility that we need to have.

CHAIRMAN VOLCKER. Maybe we lose some, but in this particular situation I don't think we lose the whole [impact] or anywhere near that. We may lose 10 to 20 percent of it.

Let me comment on a point that has come up a couple of times. I don't think we are talking about a program here just to support the dollar. I know [different] people place different emphases on that. The dollar is part of the total situation, but I think this is really all one ball of wax at this point. The psychology in the foreign markets is the same as the psychology at home; it is reflected in the metals markets. It is the inflationary psychology or whatever. So I don't think of this as a program specifically directed to the foreign side. If anything, it's specifically directed toward the domestic side, but it will have foreign repercussions. One of the interesting questions--it's very hard to express and I don't know the answer--is whether the new approach will carry a message of its own even in the international markets. I would be a little more optimistic [on that score] than some of the comments I just heard. There has been a great deal of discussion about the money supply and the feeling that so much of this psychology is related to the fact that the money supply is out of control. That's the comment we hear all the time. The virtue of a new approach, if it has one, is that we are accepting--with all its risks and dangers--more of a focus on the money supply. I think that is understandable at that kind of gross level.

I have a list here [of people who have indicated a desire to comment], so maybe I will [proceed] in an orderly way. John.

MR. BALLEES. I think there would be considerable agreement that the kinds of steps that were taken last November were viewed as bridging actions. They were effective but, of course, they can only be effective as long as some fundamental changes are being made that get around to solving the problem. One aspect of that, from the

standpoint of the Federal Reserve, is to do what is necessary to slow the growth of the aggregates and to begin to bring inflation under control. Other elements, as I look back on it--and I'm sorry that we [as a nation] haven't made more progress--would have been to do something more effective on the energy front and so on. I think there is a wide perception from the standpoint of the Fed's responsibilities and functions that there has simply been such excessive monetary growth in the last six months that we aren't making any progress on the inflation front. Fred's comment about Scylla and Charybdis coming together is a very apt analogy, I'm afraid. We've all been struggling with this problem in that if we know a recession is probably in prospect, we normally would want to ease [policy] somewhat. Some of us felt so strongly about that last spring that we dissented; the record will show that we thought [policy] ought to be easing. Since that time inflationary developments and inflation expectations have become even more dangerous.

One definite advantage that I see in moving to this new operating target of reserves is that it's likely to result in greater credibility in the marketplace [on the part of] a great many observers here and abroad that we will do something more effective than we've done, say, in the past 6 months in slowing down the rate of monetary growth. That [growth] in a way has been good in that it [may be] counter-cyclical but I think it has seriously damaged our ability to control inflation.

One thing that hasn't been said yet--perhaps it's so widely understood that it doesn't need to be said--is that the possibility of using the kinds of reserve targets that are set forth in this memo has been studied at great depth over a considerable number of years. We are not moving into this as if it were untested and unstudied; there's an enormous body of research, including staff papers and very good analytical delineations of the problems and so forth. So I don't think we are taking on something that's new and experimental in the sense that it hasn't been very thoroughly examined. When this subject came up four years ago under a predecessor subcommittee of the current subcommittee on the directive--and I served on that predecessor subcommittee--I was in favor of moving to a nonborrowed reserves target then. And that was not in a crisis atmosphere such as we have today. If anything, I think the argument for adding a reserves target, with a considerably wider range of possible movements in the federal funds rate to make it effective, is stronger now than it was then, particularly in view of the explosive inflationary psychology that we have today.

So, on balance, I would feel very comfortable in moving to the sort of approach that was set forth in the Axilrod-Sternlight paper. I fully agree with you that we shouldn't go by a strict mechanical formula. I agree completely that we're going to need to give you and the Desk a lot of discretion if we get into this. I, for one, think we would make a real impact on market expectations by announcing this new technique. Obviously, we'd have to follow through with some results, but I would strongly support the proposal for moving toward the sort of approach outlined in the paper by Steve and Peter.

CHAIRMAN VOLCKER. Bob Mayo. I'll get back on course.

MR. MAYO. Mr. Chairman, I would like to enthusiastically support the change in emphasis in our operations. I have felt for a long time that we were doing the best that we could, but I've changed my position on that under these circumstances of the most sensitive monetary situation that I can remember at any time in our history. It seems to me that we are dealing with an essentially psychological situation, both abroad and here at home. I'm not going to suggest that we do something dramatic just to do something dramatic. I share John Balles's feelings that this isn't something that is so unknown to us that we should register fear and trepidation and do it blindly. I think the RPD experiment, looking back over the history of it, failed because we were too timid on the federal funds ranges that we associated with it, and it killed itself.

So, I think now is the time for us to take the plunge, so to speak. I would do it for international reasons, too. I don't think it is just a question of fallout from what is good for domestic reasons. I have talked over recent years with a number of people throughout the world in their home offices about the role of money targets and so forth. And I've come to realize that for better or for worse these [targets] are there; there is an acceptance of the idea of a more monetarist approach than we have taken. It seems to me that this is the time to do something a little more [dramatic]. If I may be so crude, the patient has been constipated for a long time and Ex-lax will no longer work. I'm suggesting an enema or, if you want the full prescription, an enema plus some change in diet. Dr. Mayo is speaking, though I'm not one of the Mayo brothers, thank you.

Anyway, at this point I think we can capitalize psychologically on monetarist support throughout Europe in particular, as well as in the Congress of the United States and much of the journalistic fraternity today. That doesn't mean that I, Bob Mayo, agree with all the arguments of the monetarists, but I recognize that they are there and they are important. They can give us support in what is essentially a psychological situation. I would not worry about whether, in going with the new emphasis, we are taking a risk that we cannot reverse [our decision] if we have to go to something else later. This is not black and white. We could decide--to use an extreme example--that we don't want to say anything about a federal funds range in the directive today, but keep to ourselves the idea that the Desk should have plenty of leeway. If the market dictates--in the way it responds to what we're doing--that the federal funds rate should go temporarily to 15 percent, we'd let it go. I wouldn't worry about that. If sometime after 90 days--or it may take even longer--we find that this [new operating technique] has served its purpose, we can go back to including a federal funds range that is broad but nevertheless there, if we wish to. I think we have these options as we move along. A decision today to go to the technique described in Steve's and Peter's memo is not a decision for all time, either on the technique or obviously on the policy. We may wish to reverse it before we get locked in [at] too high [a rate], as Paul has said. If we believe in targets at all and believe that we have a responsibility to meet our targets, I think our best bet--not our riskiest--at this point is to take the bull by the horns and change our emphasis of operations.

I'm probably getting ahead of myself or ahead of the group, but I would combine this with some increase in reserve requirements,

particularly aimed at the larger banks where the tightness is not apparent. Our agricultural banks are tight as a drum. It's not needed there but it is needed for the bigger banks. And I would think that any discussion of the discount rate today would probably be premature; that would follow along with whatever the market is showing. But we should keep on the alert on a day-by-day basis to the way the market is responding to our shift in emphasis. And I would give considerable publicity to the change in emphasis. In my view this can be very important psychologically at home as well as abroad.

CHAIRMAN VOLCKER. Roger Guffey.

MR. GUFFEY. Thank you, Mr. Chairman. I believe almost everybody who has spoken up until now has said that they would endorse the change in operating procedures. I'd just like to raise a voice, not necessarily in opposition to it but at least to question it. First of all, let me say that I agree that there's a need for something to be done today and that it has to be rather dramatic. Hopefully, it would include the Treasury, but if that's not in the works then we have to move ahead. But if I understand what is being proposed--the change in operating technique--it seems to me a very high risk venture, particularly in view of the fact that it has never been tried. To be sure, it has been studied to death. Moreover, I happen to be somewhat sympathetic to this kind of operating technique. But we are in a time of crisis. For us to move to a new technique that has never been tried will be viewed by the markets, it seems to me, as our grasping at the last straw, so to speak. And if indeed it doesn't work to get the aggregates in better position by the end of this year I think we would have shot our last round and missed. I think that's putting the Federal Reserve as a system in a very, very precarious position.

Lastly, if I understand what is being proposed, I would say that the very same thing can be accomplished by using our present operating procedures simply by broadening the federal funds range and narrowing the aggregates ranges. We would have as much chance--or perhaps more chance because we have experience with it--of hitting the targets we're shooting at instead of starting to swim in new and untried waters. If we can get the public reaction that we're trying to get by operating with our present procedures, I would prefer to go that route rather than go into something that we know very little about. I happen to believe that we may be on the verge of moving into a recession but it isn't clear. And I think we do need some dramatic action. I would rather see a press announcement by you framed in the context of having a wider range for the federal funds rate, which certainly will be understood by the market though maybe not by the public. And it will probably be better understood by the market than our moving into a new operating procedure. That coupled together with a rather dramatic increase in the discount rate--and letting the fed funds rate move up to a fairly high level--would be a preferable action to me. However, I do recognize, as you mentioned earlier, that it's absolutely essential that we have a broad consensus [on whatever action we take today]. Accordingly, I will [not object] if a consensus forms on the other side.

CHAIRMAN VOLCKER. Mr. Timlen.

MR. TIMLEN. Mr. Chairman, it is clear to me that expectations of some strong action by this group this weekend are at a high level. I'm not sure that the Committee should always respond to expectations, but in the circumstances today the proposal of combining something new and different with strong traditional steps has real appeal to me. For some time we've been hearing complaints that the United States is not dealing with the fundamentals. And in my mind, the rapid growth in the aggregates that we've been seeing is thought of as one of those important fundamentals. I'd say it is very important that the announcement connect this new technique with an effort to control the rapid growth in the money supply. The total package must not be perceived, as some have been in the past, as a flash in the pan. I'm not sure how well this will be understood. As a result, I would endorse those people who have strongly recommended that we have an in-depth explanation of this technique and its relationship to coping with the aggregates growth. I also agree with the remarks that Roger just made on the importance of a strong consensus coming out of this meeting.

CHAIRMAN VOLCKER. Governor Wallich.

MR. WALLICH. I think the main argument in favor of the reserve strategy is that it allows us to take stronger action than we probably could by the other technique. We are much more constrained in the other technique by the appearance of very high interest rates. In the new strategy interest rates become almost a by-product of a more forceful pursuit of the aggregates. I think we need stronger action because of the resurgence in inflation and the behavior of the aggregates and the dollar. I realize that this may involve a higher cost in terms of the length and depth of a recession. But I try to look beyond that and ask myself where we would be late in 1980 if very little inflation has been wrung out of the system and we resume an upward price trend from a much higher base.

Now, I wouldn't say that the proposed new technique is superior if the same strength of action could be taken by the existing methods. That's because the existing methods have the advantage that we know the interest rate and we don't run the risk of the rate going in the wrong direction and creating dollar problems. But I think the issue is really how strong an action we can take. And it seems clear that an action via the reserve strategy is capable of greater power. I've leaned toward that strategy for a long time, but I must confess increasingly less as I saw the interest rate becoming more important from the point of view of the dollar. There is that risk of interest rate uncertainty involved in the new strategy. We would have to guard against interest rates going in the wrong direction.

MR. PARTEE. Which is what direction--up or down?

MR. WALLICH. It is quite clearly down. Upward we can control [through] money supply. We're aiming at a tight money supply, and that raises interest rates--or that is what we [are talking about]. But downward has a totally different implication. It involves a signal that we've switched policy and the markets are going to respond accordingly. Obviously, as we go into a recession there will be a time when interest rates will have to come down. They will probably come down by themselves if the time is right. And if it is feasible in terms of the exchange markets, then we should

[accommodate] that and the more the better. But we need to watch this strategy in terms of what it produces for interest rates and for the exchange market so that we don't get surprised by interest rate movements when they could be harmful.

CHAIRMAN VOLCKER. Let me just make a couple of comments. I'm not sure it's self-evident that in interest rate terms the new technique is stronger. It may or may not be, depending upon what happens to the money supply. I think that is inherent in the new technique. It also depends upon a judgment on how much traditional-type action we would take and I don't think at this stage of the discussion we know the answer to those [questions]. We'll never know the answer, no matter how long we talk, to what the money supply actually will do in coming months. And until we get further along in our conversation, we don't know how strong our traditional-type actions will be.

MR. MAYO. Paul, at some point I think we need to hear from your associates in New York as to how they would operate under this technique if we adopt it. I think that is part of--

CHAIRMAN VOLCKER. We'll get into that. I'm just getting general reactions now--and I think they should be rather general--of the type that we have had so far.

Let me just say, too, that on the issue of interest rates coming down there probably are going to be differences of opinion; there always are. But I don't think we can sit here today and say it would be a terrible thing if interest rates went up to 14 or 15 percent on the new technique, just taking some numbers that are used [in the staff paper]. If they come down off that peak to the neighborhood of where they are now, that may be inherent in the new technique if it's successful under present projections of the money supply. And I'm not sure it's terribly alarming--to me anyway--in the exchange market sense. It's a matter of judgment. But I don't think we can get ourselves into a position where no matter how high rates go at some point with the new technique, any decline from a new peak is in itself a disaster. It might be great. It might actually encourage the feeling that we're over the peak. I don't think we're in a situation where the interest rate differential vis a vis German interest rates--whether it is 5 percent or 7 percent--is an important market consideration. That implies a little more stable psychological atmosphere. Let me say it is overwhelmed by the psychology of the situation. Who is next here on the list? Ernie Baughman.

MR. BAUGHMAN. Mr. Chairman, I picked up on your earlier observation that we can get there either way--with some modification of our present technique or by shifting emphasis to reserves to a greater degree. I'm somewhat inclined to think that if we do announce that we have made a rather basic change in our mode of operation--in our intermediate if not ultimate operational target--that unless it obviously is a disaster fairly soon, it is something we are stuck with for some period of time. I don't have any strong feeling as to which way we try to get where it seems we want to go at the moment. We can do it through the route of a monetary aggregates directive under our present format, with a broad range for the federal funds rate, lifted, and with a continued focus on targets set in terms of monetary aggregates. Or we can go the route that is suggested in the wire of

putting greater emphasis essentially on intermediate targets or reserves. [Secretary's note: The memo entitled "Proposal for Reserve Aggregates as Guide to Open Market Operations," dated October 4, 1979 was wired to Reserve Bank Presidents.] But it seems to me that there's a good possibility that if we adopt that [latter approach] we will be read as de-emphasizing rather than additionally emphasizing the monetary aggregates as targets or objectives of policy.

MR. PARTEE. Those are the objectives.

CHAIRMAN VOLCKER. I don't think so, but that will come out in a later discussion, I think.

MR. BAUGHMAN. We will be read as accepting some reserve measure as the objective--a kind of M target in the financial sector before we get over to the real sector. As I say, I agree with your suggestion that we can get where we want to go by either route. It would seem to me that it might be appropriate to take [action] in two steps. The first step would be an announcement that we are substantially broadening the operating range as far as the federal funds rate is concerned and that we are committing ourselves to more effective control of the monetary aggregates by that process. It seems to me that that would get the necessary attention in the market, and operationally I don't really see that it's much different.

CHAIRMAN VOLCKER. Mr. Winn.

MR. WINN. Paul, during this past period, the rumors were everywhere. One of the ones that bothers me the worst is the feeling of an explosion on the wage front. For example, we see banks violating the guidelines pretty generally. Some of my most knowledgeable friends seem to be predicting 20 percent increases next year and that really frightens me. They all had solutions with respect to what we ought to be doing. But they never have as a solution that we should do nothing. So I've tried to [assess] what the risks and implications are of doing nothing in this area and that was rather frightening. Being sympathetic to what you're proposing, I wonder if we really have tried to look at the risks inherent in this. We've talked about the price on the international side and so forth, but what are some of the risks here? While we say we don't emphasize interest rates, the implication of this [proposal] is considerably higher rates. And if we think about that, what does that mean at least in the short run in terms of money flows? What does that mean in terms of those with prime plus 3 percent embedded in their costs? What does it mean to those institutions with short-term funding? What does it mean in terms of the commitments and lines of bank credit that will be accelerated? In other words, what are the risks on this side that we have to grapple with as well as the risks that we've talked about on the other side?

CHAIRMAN VOLCKER. I think some of those will come out later in a more detailed discussion. Mr. Rice.

MR. RICE. Mr. Chairman, I favor moving to the new operating technique--the change of emphasis--at this time. I believe our current approach has not been working and we need to change our style. But in changing our style in this case we probably also are changing our strategy at the same time. I believe it's more than just a matter

of operating technique, though I could be wrong. First of all, the psychological impact of a change in operating technique will be strong. I think it will be strong not only in domestic markets but also in foreign markets. In my view the foreign markets will read such an announcement as an expression of our determination to control the money supply, and that will have salutary effects.

It seems to me that up to now what we've been doing is pushing up interest rates, largely in response to market expectations, and we've been assuming in effect that we know what the appropriate level of interest rates should be. And when the market wants high interest rates, we end up supplying more reserves and the money supply increases. I think that if we moved to a technique where we decide what the money supply should be--and we operate directly on the reserve base to get as close to the level of aggregates that we want--we would stand a better chance of producing the kinds of results we would like to see. The good thing about moving to this operating technique is that, contrary to some of the views that have been expressed, we introduce new uncertainty into the market. I think that's a good thing. The new uncertainty will have the effect of cooling some of the speculative activity and perhaps have an impact on those demands for credit that are based purely on inflationary expectations and on the assumption that money will always be available at any level of interest rates that the Fed tries to establish. Probably the first reaction will be a sharp rise in short-term interest rates. But I do believe that the rise will probably be short-lived and that the period over which interest rates will remain high is much likely to be shorter than would be the case if we continue to follow our present approach of gradually ratcheting up interest rates in response to market pulls.

Obviously, there are high risks involved; these risks have been outlined. But in the current circumstances I think these risks are acceptable. And in any case the risks are less than we would be accepting if we continued to follow our present approach. I would, however, like to have it understood that the money supply targets--the aggregates targets that we set--are important here. They are very important for the success of the program. I would also like to have it understood that interest rates should be flexible downward as well as upward. Thank you.

CHAIRMAN VOLCKER. Mr. Black.

MR. BLACK. Mr. Chairman, Governor Rice has made many of the points that I wanted to make, but I'd just like to say that I feel better about what I've heard around this table than I've ever felt at any time since I've been attending these meetings. I think we are now on the road to formulating better monetary policy. I often think of our position as being analogous to that of a monopolist in the sense that we control the money supply. A monopolist has a choice of controlling either price or quantity but he can never control both. I believe we've been trying to control the quantity of money by setting the price and we have misjudged. We've juggled the price, in terms of the federal funds rate, one way or the other, and we've usually met with less than complete success in judging what quantity of money will be forthcoming from that. So, I think this gives us a much closer handle on the aggregates than we would have under any of these other approaches, although conceptually we certainly could do it by the old

method if we had a wide enough band on the federal funds rate. But I don't think we would know what federal funds rate we would have to choose in order to get the desired rate of growth in the aggregates.

Now, I do think there are some broad considerations--and we'll touch on some of these later--that we ought to address before we close today. The first is that the discount rate is going to play a very important role under this operating technique. If we have greater or less fluctuation in the level of borrowing, that's going to make it more or less difficult to hit our total reserve target. So I think we're going to have to be very careful in choosing the appropriate discount rate. It will not necessarily be what we thought was appropriate in the past.

My second point is that I think in your press conference you ought to state, among other things, that we would expect the federal funds rate, at least initially, to fluctuate more than it has in the past. You should also stress that there are various slippages in this mechanism; it is not a precise tool. I think you should also say why we have taken the action we have taken on the discount rate, because it will be important to explain why we've put it where we have.

Another point I would emphasize, as the staff did, is that we are going to need a pretty wide range on the federal funds rate; it may mean that we have to let it move up sharply--or we may not--in the beginning. I agree with Henry Wallich that we need to watch it, at least initially, on the down side. I'd be inclined to put a floor on the down side until we know what the market perception is on this [approach]. That's because falling interest rates very early in the game, even though we appear to be controlling the aggregates, might be counter-productive. But I would want to see that floor removed as soon as the aggregates come under control. If I've seemed hawkish to some of you in advocating that we push up the federal funds rate to bring the aggregates under control when I thought they were growing too rapidly I think you'll view me as very dovish if I see them growing less rapidly than I believe they should. We have to be prepared to let the funds rate go down.

Another point I would stress, which is in the material that was handed out by the staff, is that we have a problem in specifying the width of this band--whether it's for a day, a week, or a weekly average and whether we take into consideration the settlement date and that sort of thing. My guess is that Emmett Rice has diagnosed correctly what will happen to interest rates; they will go up initially as people rush to obtain funds because they perceive that the supply will not be as readily available. But I think also that rates are going to move back down, partly because of the elimination of some inflation expectations and also because I believe we are indeed slipping into recession, which would naturally cause them to drop.

Finally, as we get into the long run, there are a couple of items that we are going to have to think about. An example would be structural changes that we ought to consider making to improve our control mechanism. One such change might be lengthening the reserve period to maybe a month or we might want to drop the lag part, although I'm not persuaded on that. Certainly we would want to get rid of the graduated reserve requirements to the extent we could.

And, if we lose the Merrill case, I think we're going to be forced into this kind of targeting technique anyway. If we were to announce on the day of the meeting what in fact the federal funds band was, I think we could have some very disquieting effects in the market, whereas the announcement of a change in our money supply target would not really tell the market a great deal. Only the most sophisticated or lucky would be able to figure out the interest rate implications of that.

CHAIRMAN VOLCKER. Mr. Roos.

MR. ROOS. Well, Mr. Chairman, I assume that my credibility with you and my colleagues would be severely jeopardized if I came out flatly in opposition to this proposal! [Laughter] I also was told by my father to keep my mouth shut when things are going well. So all I'll say is briefly: God bless you for doing this! [Laughter]

MR. GUFFEY. I would say that when Bob Black and Emmett Rice agree, I would expect everybody else to be able to agree!

CHAIRMAN VOLCKER. There are one or two things that I didn't agree with here but that's okay. Do you want to take a little coffee break or not?

SEVERAL. Yes.

CHAIRMAN VOLCKER. Okay, we will return to a more detailed exposition unless somebody wants to say something at this point.

[Coffee break]

CHAIRMAN VOLCKER. Mr. Coldwell is developing a computer for forecasting the money supply, converting it into the reserve base, nonborrowed reserves, borrowings, and the federal funds rate! [Secretary's note: As the meeting was in the process of reconvening, Mr. Coldwell was demonstrating an electronic device of some kind.]

Let me try to describe the so-called new system, as I understand it, in an unprejudicial way. Out of this discussion will emerge some of the risks and dangers that have been referred to. To the extent possible, let's avoid detailed technical exegesis that will [keep] us here until Monday morning and not resolve the issues. I think there are unresolved issues that we are going to have to play by ear. The basic theory of this procedure is that the Committee would decide--in this case only through the end of the year--on some money supply targets. There are two extremes, I think, that are practical, though one of them may not be practical. On page 3 of this memorandum it says that if we met the midpoint of the present target we would have [September-to-December] movements of 1.3, 1.5, or 5.3 percent, depending upon which [aggregate] we are looking at. If we aimed basically for the top side of the targets or a bit inside them, we'd end up with [growth rates for M1, M2, and M3 for the fourth quarter of] 4.6, 7.5, and 7.3 percent. The 7.5 percent number leaves M2 at exactly the top of its range for the year.

Those happen to be, I say with all deference, the present projections of our projectors. I have about as much confidence in those projections as any projections, with all due respect to the

projectors. I don't have a great deal of confidence in them. But they happen to be the rates we have to achieve to come within the targets. That doesn't allow any significant leeway if indeed we are going to get within the target ranges, and that is one of the problems we're dealing with here. We have practically no leeway to go wrong if indeed we are going to be within the yearly targets we adopted [unintelligible].

Now, our concept of the process is that those money supply figures that were chosen would be converted into a reserve base number. The reserves for currency would be projected and that would be subtracted from the reserve base, leaving us with reserves against a deposit component of the money supply--and reserves against a few other things, too, which is one of the complications. Allowance would be made for the growth in the non-money supply components; allowance would be made for whatever we know about shifts of deposits among banks and all the rest; and we would trace out a reserve path presumably consistent with those money supply figures. We would compare that with what we thought was going to happen.

Suppose we happen to put a lot of weight on the current projection of the money supply and pick figures that would closely coincide with that. We would then provide, making some assumption on the level of borrowing that seemed to be consistent with the level of interest rates that presumably laid behind the projection of the money supply in the first place--we can't avoid interest rate assumptions the way these things are done--nonborrowed reserves along that path. If the money supply actually grew faster, borrowings would go up and presumably interest rates would go up; if the reverse happened, borrowings would go down and interest rates would go down.

We live in an uncertain world. And in view of fluctuating projections regarding the trend in the money supply, our first point of judgment would arise--let's say particularly in the present circumstance--because we might get some ease in the money market immediately if we did nothing but follow the path week by week. If we thought we were going to have trouble later because the projection [has money growth] going above [our targets], we would under-supply reserves in the current week to provide some assurance that we're going to cope with the fluctuation later and not have borrowings running ahead of what we had assumed. That would mean that total reserves were running ahead of what we had assumed and the money supply would be running ahead of what we'd assumed. Or in looking ahead, if we were expecting some great decline in the money supply, we might apply judgment and do the operation in the opposite direction. In view of the outlook, we might permit some easing prematurely from the mechanical application of the [amount of reserves called for in the path]. That is, we'd let borrowings drop sooner because we thought the money supply subsequently was going to come in below path. That's one area of judgment we get into right away.

As the borrowings fluctuate, they would themselves be reflected in interest rates. But rates also would be affected further by our subsequent decisions on the discount rate, in terms of whether to follow the trend of borrowings in either direction. In other words, if the borrowings rose, we could increase the discount rate to bring further pressure on reducing the money supply, the increase in borrowings itself being a sign that money growth was running above

where we wanted it to run. If it began running the other way, presumably borrowings would decline; then we'd have to make that additional judgment as to whether to reduce the discount rate in order to accelerate or facilitate a decline in interest rates. The rates at that time would also be reflecting the fact that the money supply was running low compared to where we wanted it to be.

It is firmly set, in my mind at least, that in this process the federal funds rate is going to be constrained but constrained over a substantially wider range than has been our practice. Now we have a range of about 1/2 or 1 percentage point in our directive, though typically we do not actually operate on that wide a range. We operate on a day-to-day basis with almost no range at all. Well, we let it fluctuate on unusual days, but basically we are operating in an environment where everybody in the market is looking out to see whether Peter Sternlight intervenes at 1/16th of a point or 1/8th of a point higher or lower than before. In practice, the kind of range we have is 1/8th percentage point, roughly. And the market is sensitive to changes in interest rates of that magnitude--at least when we are in the market and not on a Wednesday or something like that. Obviously, with this technique we are going to ignore changes of that magnitude; and we are going to ignore changes of some great multiple of those 1/8ths we've been concerned about in the past. Whether we ignore them when they reach 2 or 3 percentage points or let them go to whatever ceiling is put on the funds range is a matter of judgment, I guess. But we certainly are not talking about the type of operation in which we've engaged in the past where the market is sensitive in an extremely narrow range to where we operate.

When I talk about putting a constraint on the [funds rate range] on the top or the bottom, I'm not talking about a constraint that applies every hour of every day. The typical Wednesday situation would presumably run its course; we might get an exceedingly high rate of interest on a Wednesday or it might fall out of bed on a Wednesday, as it sometimes does. I think we'd let those kinds of fluctuations go outside of the kind of range we're talking about. I think we would attempt, probably not very successfully, to avoid telling the market if we hit the [constraint] in more normal circumstances or precisely what the range is. But they're going to be smelling around for it just as they do now and I don't know how successful we would be in avoiding that entirely. All I'm saying is that perhaps we can try to disguise the operations by doing them at a quarter point less or letting the rate go a quarter point or a half point above [the constraint] for a day or so. But the market is going to be feeling for where the top or the bottom of that range is if [the rate] goes persistently in one direction or another. And if it does, we can get in a situation, as I said earlier, where it's just going to lock itself against the upper level or the lower level and stay there.

We are working with a two-week lagged reserve requirement. Somebody mentioned that that probably isn't the most desirable [arrangement] in the world if we are operating on this kind of system. I think I would agree with that. But we have it, and that's not something we can change overnight. What it means in practice is that we're going to have lags with this system in affecting the money supply, as we have lags with the present system. We always know analytically that we're going to have lags; presumably with the new system we've shortened them somewhat. But we have a mechanical lag of

two weeks and on top of that a lag in the reaction of the banking system because we don't control borrowings from week to week. How much more pronounced effect on the money supply we will have in the type of period we are talking about here is one of the risks or dangers, I suppose. We should have more control, I think, when we look through the entire 3-month period. By December we ought to have a good deal more assurance that we're going to hit whatever December figure we have in mind. But we are talking about a quarterly figure and we are already into the quarter, so whatever we do now isn't going to have much effect on the October figure. Fortunately, the current projection for October, for what it's worth, is pretty moderate anyway but the month is basically gone, whatever technique we apply. We will probably have somewhat more effect on the November number with this technique and I would think significantly more in December. But there is no assurance that we're going to meet our target by using this technique--given the inevitable lags and given what I at least visualize as some constraint on [allowing fluctuations in] the funds rate--though maybe more than with the present technique. You know what the errors have been in the present technique. So we would not be adopting a technique here that provides us with certainty--more assurance but not certainty--that we are going to be able to sit here at the end of the year and say proudly that we aimed for a [particular] M1 number from September to December and we came out [there]. There is nothing in this technique that I see that permits that kind of precision, even though it should have somewhat more precision than what we now have.

I just want to emphasize that because of the comments that some people made about all the publicity we should give to this change in technique. There's an immediate advantage in the publicity; there is a disadvantage not very far down the road if people read this as a commitment and in fact we are not going to be able to live up to that commitment. That's without even injecting into the equation that we indeed might change our minds next month or the following month. We might say look, this technique is fine, but it may give us a 16 percent interest rate and we just don't want a 16 percent interest rate. Or the reverse. I think that's a policy judgment we cannot avoid during this period. So I feel there are limitations as to how much we can promise from this technique. I don't think that eliminates, but it diminishes, the sense of psychological satisfaction that one can provide.

I don't know what the current New York projections are for this period and I don't think it's important specifically. I know some other people in town have a much higher projection for money supply growth over the remainder of this year, given current interest rates. All I'm doing is emphasizing [the uncertainties] again. Nobody really knows what the money demand function will be over a period as short as this, which reflects upon the risks in the proposition.

Let me say just [one more thing] before I stop and then we ought to turn to the mechanics and try to clarify that as much as we can. Steve can say whatever he wants to say. When one thinks about being committed to this kind of process over a longer period of time, just put yourself back in the first half of last year. I don't know how many people feel in retrospect that we should have been very substantially easier in the first half of last year in terms of

interest rates. I personally think that would have been a disaster in retrospect and I thought so at the time. And we were not. But looking backwards I don't see how our present situation would be improved in any way by having followed religiously a money supply target during a period in which none of the money demand equations were working right. There was vast institutional change going on at the time, with money market funds, ATS, NOW accounts, a big surge in RPs, and all the rest. That's the [reason] I'm not willing to make a judgment at this point as to the long-term desirability of this technique through thick and thin and in all possible circumstances.

So, I would remind you that because of the particular circumstances I am thinking of using this technique for the [coming] 3- or 4-month period. This is a time when it may be particularly important to our credibility and to the economy and to psychology and everything else that we provide ourselves with greater assurance that we will get a handle on the money supply. I think it prejudices the discussion that we will have at the end of the year but it doesn't lock us in with respect to that discussion. There is a basic instability in the demand function for money in the kind of period that we are talking about. There is an instability in the relationship between reserves and deposits that is inherent in this system. And in a sense those kinds of risks get translated into the concerns [about interest rates that different members] have in varying degrees. I'm sure that interest rates will either go up too far or go down too far, depending upon one's preoccupation at particular periods of time. We can control that, to some degree, by setting these limits around [the funds rate], which I think are essential despite the fact that they have some disadvantages.

I would conclude in the end that this is not a black and white situation. We are not--at least I am not--proposing that we go to a purely mechanical reserve targeting approach. There are elements of judgment which I have described to some extent; there are uncertainties in the estimates that we are taking into account. We are not adopting an approach that says: Well, currency may be going twice as high as we projected during this period but in the long term that will wash out, so we will ignore it. We are proposing an approach where somebody--some human being--will sit down and say: For the period ahead I'm making a new estimate of currency and allowing an adjustment for its impact on the total reserve base and, therefore, on the nonborrowed reserves that are the immediate operating target. Somebody will be looking at CDs and if they are going up or down twice as fast as projected, he will be making a new projection of the nonborrowed reserve base to allow for the fact that CDs have moved contrary to our expectations in the original projections. We are allowing some human being to sit there and [judge] that the multiplier between reserves and deposits [used for the projections] is off and to make some adjustment for that in conducting operations in the next few weeks. There are all these elements of judgment that enter into the process. That, combined with the constraint on the federal funds rate, brings us to something of a hybrid. Inevitably, we are merely talking about where we are on the spectrum between a mechanical reserve targeting approach and what we have been doing.

MR. ROOS. Recognizing that, Mr. Chairman, rather than try to plug in numbers today and agree on detailed procedures--if, as I assume, we have a consensus on a change of approach--wouldn't it be

wise to ask the staff to work on that? Perhaps we could ask the Board staff as well as selected or interested staff representatives from some of the Reserve Banks to wrestle with the details of how to do this as well as the details of the specifications. That could be done between now and the time we would normally come here for our meeting in a couple of weeks. That might make sense rather than trying to work with these figures that we have seen for a very short time and that our research staffs, in most instances, have not even had an opportunity to react to. If you made this announcement on Monday and if there were a 10-day period for staff to try to put together more [precise] specifications and procedures, those could be circulated and we could discuss them at our regular FOMC meeting. Would that be more productive? Some of us are not professional economists and to sign off on specific numbers and specific details today--

CHAIRMAN VOLCKER. I will make two comments, Mr. Roos. I don't think it would be more productive because I hope the Committee as a whole, at this particular meeting at least, will not get into that detail. We will be in an absolute morass if we attempt to arrive at some judgment as to whether the staff has made all these translations correctly and on precisely how we should proceed. If we decide to go on this approach, I believe we are going to have to go on it with the Committee indicating only broad guidelines. There is enough judgment involved that we can get a good sense of how the Committee wants this process to operate in a very uncertain world. And even in a two-week perspective, I don't think we can attempt to have a technical resolution of all these detailed issues. There will be plenty of opportunity for that kind of [analysis] in the next few months and it would be relevant in terms of any further decision at the end of the year on whether or not to stay with this procedure.

But inherent in the situation today, and I'll just put it very simply, the Committee has to have faith that it can give some general guidance and that we--basically the staff here at the Board under Mr. Axilrod's direction--will translate that as best they can, within these general parameters, into operational numbers. And then, it has to have faith that Mr. Sternlight will use his best judgment in taking the figures that are produced here [in Washington] and deciding on precisely which day he will provide how many reserves to the market.

MR. ROOS. Well, I thought we were going to get into the numbers. I was off base there.

CHAIRMAN VOLCKER. Well, any way we go we have to get into the money supply number. If we're going to go this way, the Committee is going to have to make a decision on the federal funds constraint and what biases--if I can put it that way--we want to introduce into the operations, particularly in the next couple of weeks. A number of people have referred to a point on which I fully agree: After going through this hullabaloo, if we have made some miscalculation here and the federal funds rate drops by a percentage point, say, next week, we are in a hell of a fix. So, I assume we would want to bias it on the up side. However these calculations come out, we want to have some sense of what the Committee wants to do in that respect.

MR. ROOS. Couldn't your announcement say that over a mandatory period of a couple of weeks we are going to do this in an orderly, gradual, manner? Do we have to do it right from the beginning?

MR. COLDWELL. Yes.

MR. MAYO. No way.

MR. MORRIS. We are going to have to go through a learning procedure anyway. Even if we were to postpone it for a couple of weeks, we have a lot to learn and we might as well start learning now.

CHAIRMAN VOLCKER. I personally don't think that the nature of the problems we have are susceptible to sitting down around the table and saying: "Do we use this figure or do we not use this figure?" We can argue about that kind of thing if we are willing to adopt this experiment in a fairly rigid way for a period of a year. I, frankly, am not willing to take the risks of [operating totally on the basis of] some long-term equation or mechanical relationship that we know can be way off in a period of a month or in any particular week--or even in a 3-month period.

MS. TEETERS. But we don't want to keep the funds rate biased upward too long.

CHAIRMAN VOLCKER. No. Well, inherent in this technique, the Committee can keep it biased however it wants to keep it biased. We have to discuss that. But in the mechanics of the process that I described, let's say we biased it for the first two or three weeks, quite deliberately, and we were wrong. It turns out that in fact we didn't have to bias it to keep the money supply under control. But we biased it in that direction because we wanted to make extra sure that [the money supply] didn't rise. The result would be a slower growth in the money supply four, five, or six weeks down the pike than we otherwise would have gotten. Then, out of the mechanics of the system, unless we made a quite deliberate decision to bias it in the other direction, we'd have the expense of biasing it tight in the first place and biasing it easy down the road. Now, the Committee obviously can make a new decision at that point. The biasing is, I suppose, where the Committee thinks the major risks lie. Take [the current] money supply figure. It's already in the top of the range, so we'd be much more sensitive to missing it on the up side than to a little miss on the low side. Particularly initially, we would bias it in that direction, apart from the interest rate implications.

MR. ROOS. In your announcement Monday, will you announce any figures?

CHAIRMAN VOLCKER. No. We would announce that we want to be within the targets for the year.

MR. ROOS. Right, but not any more precise figures. What I'm worried about, for example--and I'm not trying to get specific--is the 8 percent monetary base figure referred to in this document. Our research staff said that if the people who watch this saw an 8 percent figure for monetary base growth, that would immediately destroy the credibility of the whole effort.

MR. WALLICH. I think that's purely an [incidental] number.

MR. PARTEE. They will, of course, be able to make a calculation if we say we're determined to be within the targets for the year. They will see how much more room there is for the remainder of the year for growth in the aggregates that we have been using as [our target] variables.

MR. BLACK. If we give them the adjusted figure for M1-- remember we cited the 1/2 to 4-1/2 percent--

MR. PARTEE. We might have to underline that.

MR. BLACK. We are going to have to clarify that one, I think.

MR. COLDWELL. Mr. Chairman, I wonder if we shouldn't at least make the initial decision if you are ready to go that far. Or if you want to discuss the specifications, which Mr. Axilrod can [expound on], we can go that route.

CHAIRMAN VOLCKER. Well, we can go that route. Maybe we ought to discuss specifications. But in my mind, at this point we've made no decision to go in this direction. I think that's a decision we should make at the end of the road, and citing some specifications may put some concreteness on this discussion in terms of whether we want to tolerate the risk. I just want to come back at the end to the question that Mr. Guffey put very well in stating the other case. There is a danger of a too high [funds] rate and there is a question of all this publicity and then falling short. There are these analytic difficulties: the instability in the demand function for money and the [multiplier] relationships that we work with. There is the problem that we may run into a situation where, in effect, our collective judgment tells us to do something different than what the aggregates are telling us to do. Do we want to get locked into a procedure that prejudices us so far toward worrying about the aggregates? Those are the questions that should be in our minds, questions we want to return to before making a final decision here. [We need to weigh that] against the knowledge that we can do something very comparable, to the best of our wisdom, by devising a package using the traditional technique--or the traditional technique as modified somewhat to accomplish the same immediate purpose. So that's the final question. But let's [proceed].

MR. COLDWELL. I was merely raising the question of whether you wanted to get the specifications of the traditional as well as the new procedure.

CHAIRMAN VOLCKER. Why don't we [discuss the specifications], unless somebody wants to ask more about the mechanics. That will come out to some degree in the discussion anyway.

MR. WALLICH. I'd like to understand a little better the role of the discount window and the discount rate in this procedure. If we bias the reserve path in one direction or another, that will influence the volume of borrowing. That will then influence interest rates, which in turn will affect borrowing by virtue of the spread between the discount rate and the funds rate. We could leave it to that

mechanism to control borrowing, we could leave it to the administration of the discount window to control it, or we could move the discount rate. It's not clear to me which way might be the best.

CHAIRMAN VOLCKER. Well, if we adopt this approach, that is one of the issues I had in mind when I suggested that the Reserve Bank Presidents might want to meet for further discussion this afternoon. One of the problems with this approach, it seems to me, is that the administration of the discount window is very confused at the moment. Inherent in the way we have been operating--to put it bluntly--there is no legitimate reason to borrow. Banks borrow because of the rate spread, but that's not really a legitimate reason. Now, that ignores computer breakdowns and that kind of thing. Except for accidental circumstances or late on a Wednesday--and here I'm talking about the larger banks--under our present guidelines there really isn't a legitimate reason for banks to borrow from the discount window, as I understand it.

I know I have had the experience in New York where the discount officer happily comes in to tell me that he called up bank x, which borrowed for the first time in six months, a few hundred million dollars. He asked them why they were borrowing. And the bank official cautiously says: "What the hell, I hadn't borrowed in a while and your rate looked pretty low." And the discount officer replies: "Well, you can't borrow for that reason." Now, if a Reserve Bank really enforces that kind of discipline, it doesn't get many borrowings. But it's obviously not enforced evenly. And I suspect there are no additional guidelines we can give the discount officers at the moment. We have to let events take their course. We have been doing it for years, and I suppose we can do it for a few more months. It will raise this question in the bankers' minds. I think we will have to develop a more coherent policy in a few months and it might be useful for the Presidents to think about these implications.

MR. AXILROD. Mr. Chairman, if I might add a point. If the Committee goes this route, I was planning to have a conference call with the discount window officers. My intent would not be to say anything about their administrative procedures but to explain that they might expect more volatile movements in borrowing than under existing procedures.

CHAIRMAN VOLCKER. Whatever they are.

MR. AXILROD. I wanted the discount officers to be aware that they shouldn't be shocked if one bank is in and another one is out, because the funds rate might exhibit more volatility.

CHAIRMAN VOLCKER. What I visualize happening--but it may not if we move the discount rate frequently enough--is that with the volatility in the funds rate, more and more banks will be tempted to borrow despite the presumed guideline against it. So the discipline that now exists will break down, and the same level of borrowings will mean something quite different than it means now. But it's very hard to measure that. How do we prevent that from happening?

MR. BLACK. They might arbitrage out some of the fluctuations we would otherwise have in the federal funds rate, too.

CHAIRMAN VOLCKER. No question that the federal funds rate will be influenced by the discount rate. It is now, but it will be more so.

MR. BLACK. It seems to me that the main [objective] ought to be to set the discount rate at a level--if we can figure out what that is--that would reduce the volatility of borrowing, which would enable us to get at total reserves more precisely. I think that would mean that we should try to keep the discount rate at a penalty rate most of the time. That, of course, has implications for our--

CHAIRMAN VOLCKER. I think that is the implication of this technique in the long run but not in the short run.

MR. EASTBURN. There is a question here of how the Reserve Banks should report all this to their boards of directors. I think some of the sharper directors will raise questions about what the role of the discount rate is and what their role is with respect to this new mechanism. We are going to need to consider this. My guess would be that we'd view this as a special program for a special period and that we'd probably want to handle it more through the administration of the window than to develop a whole new procedure to make the discount rate a flexible one.

CHAIRMAN VOLCKER. Well, I haven't thought about it a lot, but I presume that the discount rate would be more flexible but not so much more flexible [as to preclude] a variety of requests from various Banks in a timely fashion. So there wouldn't be any special problem. I think we are going to have a lot more requests for discount rate changes. But we'll need them to provide a menu of choices in the short run as to where we set the discount rate.

MR. MORRIS. You may remember, Paul, back in 1974 we were operating the discount window with a 4 percent spread between the funds rate and the discount rate.

CHAIRMAN VOLCKER. I think we can do that, too.

MR. COLDWELL. Sure, we can do that.

MR. MORRIS. Administration of the window can control--

CHAIRMAN VOLCKER. Oh, it can ultimately control it if we make that decision. Did you want to say something, Phil?

MR. COLDWELL. Well, Mr. Chairman, it seems to me that there are at least four major decisions the Committee needs to make if we are going to move to a reserve targeting procedure. I'm not saying that is the [decision]; as you said, you want to come back to that.

The first decision is what target we should aim at. That's [addressed in the memo in the footnote] at the bottom of page 3. My preference would be in between the two alternatives shown there. I don't like the idea of aiming at the upper half [because of] the potential for a miss and I question whether we can get as far down as the midpoint of the target. So I would suggest to the Committee that we might aim for 5 percent growth in M1 for the full year, which would

connote something around 3 percent for September to December and a quarterly average, if I calculated this right, at about 4-1/2 percent.

The second decision is how much bias to put in, and I think the borrowing is the key there. If we're going to bias it on the basis of the present borrowings it would be \$1.2 billion. I would allow a little more leeway, say, up to \$1.5 billion.

The next decision, as I read this paper, is what to do if CDs stray off path badly. That, I think we would have to play somewhat by ear but if they really take off, then I would adjust the nonborrowed path.

Finally, it seems to me, we have a fundamental question of where to constrain the federal funds rate. I would suggest to the Committee the possibility of a range of 11-1/2 to 14-1/2 percent.

CHAIRMAN VOLCKER. Let me comment. Let's take what you said about CDs as given without objection and reduce the variables by one. You suggested one particular way of biasing this and I would just note that in some sense it depends upon what you mean by bias. If you fill in a money supply figure of 3 percent from September through December against the projection of 4.6 percent, in concept you have already biased it toward higher interest rates. Then to specify borrowing above the current level in the context of this operating procedure would imply a double biasing, I suppose. Aiming for 3 percent would be biasing it in favor of higher interest rates and then you would take out a little more insurance by raising the borrowing level. I think mechanically that's the way it comes out.

MR. COLDWELL. And I am speaking in terms of the next 2 to 3 weeks with this sort of biased arrangement.

CHAIRMAN VOLCKER. Well, in the money supply sense you [can] call that a bias. That would be [a bias] for the quarter. I guess it's only a 2- to 3-week bias in the sense of higher interest rates.

MR. PARTEE. But if we put in 3 percent for the money supply for September to December, Phil, given the fact that we can't affect October--assume it comes in at 4-1/2 percent--that means we are putting in a November-December growth of about 2 percent. The demand function is still there and we can affect the supply, but it would mean that we would be moving toward a negative number for December. That's really a very tight bias.

MR. MORRIS. Well, if we follow Phil's formula, we do have a little room to miss on the up side. If we shoot for the--

MR. PARTEE. Well, the 4.6 percent [growth in M1 for September to December] is not at the very top. That gives us 5.3 percent for the year and the top of the M1 range is 6 percent.

CHAIRMAN VOLCKER. Growth reaches the top for M2.

MR. PARTEE. Well, the M2 is a little [above] and M3 is below. There has been a shift from the thrift institutions into the banks and that accounts for some of that.

CHAIRMAN VOLCKER. Well, these numbers are illustrative.

MS. TEETERS. What is the projection for October, Steve?

MR. AXILROD. For M1?

MS. TEETERS. Yes.

MR. AXILROD. 4.8.

MR. PARTEE. We already have to have a November-December averaging below October.

CHAIRMAN VOLCKER. I don't know whether this facilitates the discussions or not. Let's for the moment concentrate only on the money supply and the federal funds constraint. Those are enough variables to consider. And we'll consider any further bias later.

MR. BAUGHMAN. I find Governor Coldwell's suggestion fairly reasonable, all things considered.

MR. RICE. Mr. Chairman, I would like to see a wider range on the federal funds rate.

MR. COLDWELL. Wider, Emmett?

MR. RICE. Yes, wider on both the low and the high sides. I would like to see something like 9 percent on the low side and 15 to 16 percent on the high side.

MR. WALLICH. What we would do if it went to 9 percent-- intervene in the [exchange] market in very large amounts to offset the effects?

MR. RICE. Yes.

MR. WALLICH. And probably be defeated.

MR. RICE. Why would we probably be defeated?

MR. WALLICH. Because it's not the effect of the interest rate as such. That doesn't play a big role in the short run. The exchange market would be the symbol but all over the world they would be saying the new procedure really is a form of easing.

MR. RICE. I really don't see how they could say that.

MR. COLDWELL. Well, I don't think we need to set this for all time. It seems to me that a fed funds rate constraint of 11-1/2 to 14-1/2 percent for 2 or 3 weeks--

CHAIRMAN VOLCKER. We can come back to the question of scheduling the next meeting. My own instinct at this point is to delay what would have been the regular meeting for a week just to provide another week's experience. It seems awfully quick to come back. We'd be coming back in less than 2 weeks.

MR. ALTMANN. Yes, a week from Tuesday.

CHAIRMAN VOLCKER. My own thought is why not delay it a week so we would have another week.

MR. TIMLEN. We have another event associated with the next meeting--the annual meeting of the retirement committee. That meeting is about the Federal Reserve's retirement system and it brings all the Presidents here. Then they would have to come back again the next week for the FOMC meeting.

CHAIRMAN VOLCKER. Maybe we can even change that.

MR. TIMLEN. We'd just need to know in order to change our schedules.

MR. COLDWELL. Well, it wouldn't be too bad just to have an informal discussion at the time of the next scheduled meeting, even if you decided you didn't want to have a regular FOMC meeting.

CHAIRMAN VOLCKER. We may not even be having a regular meeting then.

MR. BAUGHMAN. Is it presumed, Mr. Chairman, that we would release to the public the same items of information as we do now?

CHAIRMAN VOLCKER. Do you mean in terms of the actual directive? I see two things that would be in the directive. One is the money supply target, however expressed, from now to the end of the year. And the other is the federal funds constraint.

MR. MAYO. But with the usual lag. This would not be in your press release Monday or today.

CHAIRMAN VOLCKER. No.

MR. COLDWELL. We do get caught with that, don't we? That's because we would have to release this--

CHAIRMAN VOLCKER. Let's worry about that later. I don't see that we have to release it before 30 days, but we will decide that subsequently.

MS. TEETERS. I think Phil's target [proposal] is too strict. In a sense, he's choking [the money supply]. And that seems to me ridiculous, given the underlying state of the economy as we see it. I think if we aimed to be within the upper part of the range [for the year]--aimed for 4.6 percent [for September to December]--we'd tend to offset the dangers of putting this economy into an actual tailspin. It's all right to control the money supply, but we don't have to cut it off completely, Phil, which is what your proposal would do for the last two months of the year.

MR. PARTEE. I must say that I agree with Nancy. If this is the nature of the detail, then I can't agree to it.

CHAIRMAN VOLCKER. I think the thing to do at the moment is just to concentrate on the money supply.

MR. PARTEE. Well, if you want to go around the table, I would view the figures in the right-hand column [at the bottom of page 3] as quite appropriate objectives. I would be prepared to bias the initial funds rate range. Oh I forgot, you don't want [us to address] the funds rate yet.

CHAIRMAN VOLCKER. Well, we have to sometime; let's discuss the whole bias issue. We can [talk about] both the funds rate range and the money supply.

MR. PARTEE. I would leave the money supply [range unchanged] and bias it with the funds rate range in the initial go-around. Then we can review the funds rate range depending on progress. I would point out that with that projection for the first month [of the quarter] being above the 4.6 percent--and September deposits have determined reserves for the first 2 weeks of October--we already have a bias in the money supply for the initial two weeks of operation.

CHAIRMAN VOLCKER. Well, I'll let that go. I won't get into that technical point of whether we bias the operation--since the reserves of the forthcoming week are already in the bag--during that week.

MR. PARTEE. Yes, sure we do.

CHAIRMAN VOLCKER. No, I think the answer is that we [start with higher] borrowings that first week. We start, even though we know we can't affect the level of reserves that week.

MR. BLACK. We can affect deposits in that week, even though we are addressing the reserve needs of two weeks hence.

CHAIRMAN VOLCKER. We might affect deposits in that week.

MR. BLACK. And that's really what we are after, so I don't really think [money supply growth] is in the bag for October, Chuck.

MR. COLDWELL. I don't either.

MR. PARTEE. I don't think we are going to affect it much.

MR. BLACK. I agree that this is not going to affect it a lot, but conceptually it isn't in the bag yet.

CHAIRMAN VOLCKER. Well, it's a matter of degree. We have two proposals: one for 3 percent M1 growth and one for 4.6 percent.

MR. MAYO. I would like to throw a third one on the table. I'd make it 4 percent. I think we need to shade it, but I don't want to shade it as much as Phil suggested.

MR. BLACK. I'm getting confused here. Are you talking about the September--

MR. MAYO. [Growth for] September to December.

MR. BLACK. Okay.

MR. BALLE. Mr. Chairman, could I ask a technical question of the staff regarding the right-hand part of the table on page 3? You say, Steve, that the right-hand panel shows the fourth-quarter growth rate consistent with a yearly increase in the upper half of the long-term range. I didn't have a chance to do the arithmetic on this. Do you mean right at the upper end of the range or somewhere within the upper half of the range?

MR. AXILROD. The growth rate shown there produces a rate [for M1] for the year of 5.3 percent. The range for the year, suitably adjusted, is 3 to 6 percent. So, that 5.3 percent is about halfway between the 4.5 percent middle of the range and the 6 percent upper end of it.

CHAIRMAN VOLCKER. Just compare the third from the right column on the bottom table with the column at the left on the top table. The target ranges are given at the top of page 3 and the growth for the year is given at the bottom of page 3.

MR. STERNLIGHT. Mr. Chairman, those of us who have the Axilrod-Sternlight memo in wire form have a different pagination.

MR. COLDWELL. It's on a different page.

CHAIRMAN VOLCKER. Well, there is a target range for M1, M2, and M3. Just write them down along side the growth for the year in the upper half of the target ranges. They are: 3 to 6 percent for M1; 5 to 8 percent for M2; and 6 to 9 percent for M3. So [growth for the year] is right at the top of the range for M2 and somewhat below the top, but in the upper half, of the ranges for M1 and M3.

MR. BLACK. Mr. Chairman, do you want the growth rates [we prefer] stated in terms of the growth for the year or not?

CHAIRMAN VOLCKER. From September through December.

MR. COLDWELL. September to December.

MR. PARTEE. That's going to be the operational period.

MS. TEETERS. I would support the 4.6 percent.

MR. AXILROD. There's going to be variability. It's possible to get different September-to-December growth rates for the same quarterly average, as I'm sure the Committee realizes, depending on when in the quarter the growth occurs and all that.

CHAIRMAN VOLCKER. The operational one is September to December, even though that doesn't assure precisely that quarterly average.

MR. AXILROD. Or you could use the quarterly average and have varying growth rates for September to December, whichever you want.

MR. MAYO. Steve, 4 percent for September to December would give us a 5 percent growth rate for the year, right?

MR. AXILROD. I would have to translate it into the quarterly average.

MR. BLACK. The quarterly average would hold it to around that, I think.

MR. AXILROD. The Committee's target is for Q4 1978 to Q4 1979. If we had a quarterly average rate of 5.9 percent [for the fourth quarter] the rate [for the targeted period] would be 5.3 percent. To the degree that you lower the [rate desired for the remaining] months to what you were suggesting--and depending on when exactly in the quarter that slower growth occurred--it would affect that quarterly average. If it occurred early in the quarter, the quarterly average would go down more than if it occurred all in December, say.

MR. MAYO. Well, that's why you are emphasizing September to December because that would at least bypass a variable.

MR. AXILROD. This shows the slowing that's going to occur. The slowing is in process, but the effect on the quarterly average is delayed because we are going into the quarter with such a high rate.

MR. COLDWELL. And we already have 5 percent for the first three quarters. Am I right?

MR. AXILROD. Yes.

MR. MAYO. Yes.

MR. COLDWELL. So with 5.3 percent, M1 growth would actually be going up in the fourth quarter?

MR. AXILROD. We are coming off a 9-1/2 percent rate in the third quarter.

CHAIRMAN VOLCKER. We are starting the fourth quarter high, so it's very hard to get that down.

MR. BLACK. It seems to me that we can target better on what we want the growth for the year to be than on September to December.

MR. MAYO. Well, that's true.

MS. TEETERS. Oh, I don't agree.

MR. BLACK. Well, I know it has to be translated into [the rate for the September-to-December period] for purposes of the operating technique, but it's hard--unless you know what the pattern is apt to be between September and December--

MS. TEETERS. That's what we are doing. We would be determining a pattern.

MR. MAYO. Well, I agree with Bob.

CHAIRMAN VOLCKER. I think the only number we can concentrate on operationally is the one for September through December, given the

figures that have been shown here in the memo. We can make a precise arithmetic computation at lunch if we want to, I'm sure. Obviously, the lower that figure is, the more it takes a little off the annual growth rate.

MR. BLACK. My point, Mr. Chairman is that the staff started with the numbers on the left-hand side, 4-1/2, 6-1/2, and 7-1/2 percent, or 5.3, 8, and 8 percent. And then they went back and produced a September-to-December figure. It's very difficult for us to produce the figures here that would be compatible with what we might want for this.

CHAIRMAN VOLCKER. Just interpolate.

MR. MAYO. It seems to me we are better off, Mr. Chairman, to aim for a growth rate for the year and let the staff work it out.

MR. BLACK. That's essentially what I am saying.

CHAIRMAN VOLCKER. I don't think that's right because a very small change in the growth rate for the year has a very big effect on the growth rate for the September-to-December period. And it's that latter period that we are dealing with here.

MS. TEETERS. Really, we have only 2 months that we can influence.

CHAIRMAN VOLCKER. You just have to interpolate. If you went all the way down to 1.3 percent [for September to December] you would be at 4.5 percent [for the year]. So if you want to aim half way between [the two figures shown], the annual growth is going to be exactly half way between 4.5 and 5.3 percent.

MR. PARTEE. But [the choice] has tremendous interest rate implications.

MS TEETERS. Yes.

MR. RICE. Mr. Chairman, I would support 4.6 percent.

MR. MORRIS. I would propose 4 percent for M1 and 7 percent for M2 in order to give us a little margin for error.

MR. MAYO. Yes.

MR. BALLE. That's fine with me.

MS. TEETERS. We have some margin [with the 4.6 percent].

MR. COLDWELL. We haven't got much margin.

MS. TEETERS. It's 0.7 on the yearly average.

MR. WALLICH. We need to do two things, in my judgment. One is to set a money supply target that causes the funds rate to rise but not excessively. The other is to set a range that won't allow the funds rate to fall excessively. And to me it looks as if something like 4 percent on the money supply would probably do that.

CHAIRMAN VOLCKER. Let me note that we have other instruments for biasing at the start, including the discount rate that the Board is going to have to decide upon here. If we raise the discount rate substantially, we are going to get an upward movement in the funds rate in the short run.

MR. COLDWELL. And the impact of the reserve requirement change can do the same thing.

MR. SCHULTZ. I'm going to vote for the 4.6 percent.

CHAIRMAN VOLCKER. Given a moment of hesitancy here let me make a suggestion, at least tentatively. Nothing is solid. I just want to move on. Let's assume 4.6 percent for the moment, or 4.5 if you want a round number. There is obviously a good deal of concern that that is too high and a good deal of concern about what will happen in the short run. We can accept that. But in the interest of getting [the full] picture, if tentatively we say 4.6 percent, there is a lot of interest both in biasing [the outcome in] the short run and in biasing the possible errors in the direction of not exceeding 4.6 percent because that indeed is getting pretty close to the upper end of the annual target. So let's proceed on that basis for a moment and go to the federal funds range.

MS. TEETERS. Well, what are you going to do with the discount rate, take it to 12 percent?

CHAIRMAN VOLCKER. Well, I think that's obvious.

MS. TEETERS. If we take it to 12 percent and we want the federal funds rate around the discount rate, that means the funds rate should be approximately 12 percent.

CHAIRMAN VOLCKER. I didn't want to get into that question. I would assume that if we take the discount rate to 12 percent--unless we have a reverse bias in terms of the borrowings--that the federal funds rate is going to go up in the neighborhood of 1 percentage point under normal relationships.

MR. PARTEE. That's 13 percent.

CHAIRMAN VOLCKER. Now, whether any relationship is normal in this period, who knows? But I think that's the best guess one could make and that would introduce the bias in the short run.

MS. TEETERS. But to talk about a funds rate range, it seems to me we have to have in mind where we are going to put the discount rate.

CHAIRMAN VOLCKER. I agree. These things are very hard to [separate].

MR. RICE. Mr. Chairman, do we have to move on the discount rate immediately?

CHAIRMAN VOLCKER. Well, we have to discuss that. Obviously, all these things have to be decided. But for myself, when I look at this potential package, I think there is enough risk of confusion in

the announcement that an increase in the discount rate of 1 percentage point would be highly salutary in terms of our immediate objective. Intellectually, though, you can argue the other point. I just don't know whether we want to take the risk in the initial announcement of a possible interpretation that we don't really mean it. That's the problem that I see.

MR. MORRIS. The increase has to be at least one percentage point.

CHAIRMAN VOLCKER. Well, maybe it's easier if we [discuss] all the [aspects]. Let me tell you what the Board has been discussing on reserve requirements. What I would presume the Board members will agree upon is a packaging together of all managed liabilities, with all its difficulties. That would include CDs, federal funds for non-members, repurchase agreements, Eurodollar takings--this is all very difficult technical business. One proposal is to make a basket of all those liabilities, establish a base date in September, and then [impose] a marginal reserve requirement of some size--some size meaning in a range of 5 to 10 percent--on any increase in the basket. We've discussed also [imposing a reserve requirement] on total outstanding managed liabilities.

For purposes of discussion, and to get the whole picture out, assume a target of 4.5 or 4.6 percent for the money supply number. Assume the increase in the discount rate, which itself biases this initially and has the announcement effect as well. Also assume Phil Coldwell's initial federal funds constraint and a moderate assumption on the borrowings for 2 or 3 weeks of the nature he suggested, which involves very little change from the current level of borrowings.

MR. PARTEE. Was his suggestion \$1 billion?

MR. COLDWELL. I said \$1.5 billion; it's \$1.2 billion now.

CHAIRMAN VOLCKER. Let's say \$1.2 billion to \$1.5 billion. I would feel quite differently, frankly, about that borrowing level without a discount rate change. I think we would probably lose too much without the discount rate change. Without the discount rate change I'd put in a much bigger bias on the borrowing side initially, in effect, to force the discount rate change very quickly. But the more I think about it, the other way of doing it--announcing a discount rate change with the package--seems much safer. With that kind of initial discount rate change, I think we can be relatively moderate in biasing on the borrowing. It wouldn't immediately force another discount rate change. So, that's somewhat of a "family" [of potential actions].

MR. TIMLEN. You are staying with the suggestion of an 11-1/2 to 14-1/2 percent funds rate range, right?

CHAIRMAN VOLCKER. Yes, for purposes of discussion.

MR. MAYO. If we have a discount rate change to 12 percent, why would we want an 11-1/2 percent lower constraint on the federal funds rate?

CHAIRMAN VOLCKER. Well, in those circumstances, I think the probability of going to 11-1/2 percent is negligible.

MR. MAYO. Sure.

MR. COLDWELL. Yes.

MS. TEETERS. But I think we want a fairly wide range.

MR. MAYO. How symmetrical do we want to make it at this point? I grant that 12 is close to 11, closer to 11-1/2--

CHAIRMAN VOLCKER. Phil probably figured it out. The 11-1/2 to 14-1/2 would probably make the range symmetrical around the best guess of where the actual funds rate might go in the short run.

MR. COLDWELL. It's a 13 percent midpoint.

CHAIRMAN VOLCKER. Let me say again that if we adopt this technique, I don't think we can be at all sure where the fed funds rate will go in the very short run.

MR. WALLICH. It doesn't matter all that much.

CHAIRMAN VOLCKER. And it doesn't matter all that much.

MR. WALLICH. It would disavow us.

CHAIRMAN VOLCKER. No.

MS. TEETERS. It matters to you, Henry, if it goes down.

MR. WALLICH. Yes.

MS. TEETERS. It doesn't matter to me if it goes down.

MR. WALLICH. It doesn't matter very much within a range that is set like this one here.

CHAIRMAN VOLCKER. Well, that's an important point--not so much for a decision today, but looking toward the future.

MR. SCHULTZ. Well, looking to the future, I may want to let [the funds rate] be more responsive, because in my mind that's one of the advantages of this system. The technique fits the times; our situation is more volatile. So, that's one of the reasons I like this. I would vote yes, for the time being, on the package that you presented.

MR. WALLICH. The rates that really would matter would be the other short-term rates; the funds rate matters much less. The other short-term rates, I think, would move up in relation to the discount rate and the money supply constraint. If the funds rate stays at the lower end of the band for a long time, then that would pull the other rates down.

MR. PARTEE. My only concern is whether that [range] is too constraining on the funds rate.

MR. BALLEES. I agree.

MR. MAYO. I agree, too.

MR. PARTEE. I can see a real possibility that it will hit 14-1/2 percent and if we seem to lock on it, it will then establish that as the rate.

MR. MORRIS. If we are in that situation, the Chairman can have a telephone conference and we can discuss whether we want to stay locked in or not.

MR. BALLEES. The staff paper did recommend a range of 3 to 5 points didn't it, Steve?

MR. AXILROD. Yes. I don't know about Peter--he can speak for himself--but I feel very strongly that if we are in any way going to be held responsible for this operating technique working out, a very wide federal funds rate range is necessary.

CHAIRMAN VOLCKER. Well, we have a real conflict here in terms of the way we want to place our risks. I must say that pretty consistently in my own thinking I come down on the side of not wanting to let this federal funds rate go out of sight by accident in the initial stages. Now, that's a matter of judgment. And the general tenor of the plan, of course, is to take whatever punishment--if that's what it is--quickly and get it over with so rates can come down and that's an offset. For once let's get ahead of the market expectation in a sense and get in a position to [move rates] down, which is the other side of the coin. But we are going into unknown territory and there is a limit as to where my own sangfroid gives out here.

MS. TEETERS. May I suggest a 4 percentage point spread of 11-1/2 to 15-1/2 percent with consultation if it goes over 14-1/2?

MR. BALLEES. I'd support that. That's good.

MR. BLACK. I'd rather see it wider.

MR. COLDWELL. I think we ought to have some sensitivity to a 16 percent federal funds rate.

CHAIRMAN VOLCKER. Understand that even with this kind of constraint, on an individual day it might well be [outside the range].

SEVERAL. Oh, sure.

MR. COLDWELL. We are talking about a weekly average.

CHAIRMAN VOLCKER. Let me ask a question. Are we very closely in the ball park here?

SEVERAL. Yes.

CHAIRMAN VOLCKER. Why not stop for lunch?

MR. ROOS. I second that!

CHAIRMAN VOLCKER. I don't mean wander away for lunch. Let's take 10 minutes and come back to the table.

SPEAKER(?). Where is lunch?

SPEAKER(?). Next door.

[Lunch recess]

CHAIRMAN VOLCKER. Let's try to reach some consensus on what the proposal should be like if we do it [under the old method]. And if we have a consensus on both of those, we could just vote up or down on which approach we like better, with as many people feeling comfortable about [our decision] as humanly possible. I think you can assume there will be a discount rate of 12 percent I should say.

MR. SCHULTZ. 12 percent?

CHAIRMAN VOLCKER. A 1 percentage point increase. Under those circumstances, let me modify my proposal slightly. We work with a 4.6 or 4.5 percent target for M1, recognizing that people would rather see M1 growth come in somewhat lower, certainly, than higher. But that to us is a satisfactory target. In an uncertain world, all other things equal, the money market nice and equitable, expectations changing nicely, things settling down, it's possible we would feel better if it came in below than if we were embarrassed by it being too high. We have a discount rate of 12 percent. We have the reserve requirement change, which I think will be 8 percent, on a basket of managed liabilities. That is about equivalent to an added cost of 1 percent on those [liabilities]. That's the effect that has, mechanically. I don't know what that does to the prime rate, but [the added cost to banks] is just marginal. If the banks want to be mean-- I've got to speak to the ABA--they raise the prime rate and say that's our marginal cost of funds. If they want to be reasonable, they don't because that cost is only going to apply to a very small amount at the margin. I would be inclined to tell them at the ABA that they shouldn't reach forever on the interest rate. That sounds like a good idea.

In and of itself, I think [all] that means some increase in the federal funds rate. How much of an increase? Although this scenario only puts the discount rate at about or slightly above the current federal funds rate, it nonetheless, all other things equal, puts some upward pressure on the federal funds rate. In terms of the range, Phil suggested 11-1/2 to 14-1/2 percent. As I told you, it makes me nervous to think of [the rate] going up and getting locked in at a higher level. But if you want to put the upper end higher, I reserve the right to consult if the funds rate were to begin getting up that high. We could have that understanding. I am not talking about for a day; I think it would be fine if it went there for a day or a bit beyond.

MR. BALLEES. Excuse me, Paul, are you talking about 11-1/2 to 15-1/2 percent?

CHAIRMAN VOLCKER. Yes. That's what would appear in the formal record, whether or not we consulted later. Then in starting off, I would suggest a mild further bias. I think the discount rate

in a sense is a bias to start with, at least to get the federal funds rate up. And there's a bias in the sense that these projections, if they mean anything, are based upon a lower level of interest rates. So by getting the interest rate up we've biased it some already. I would suggest a mild further bias--for about 2 weeks maybe--and I could express that in one of two ways. We just take the operating flexibility depending upon how things develop. It could be expressed as a slightly higher level of borrowings, as we discussed before. But even that I don't think is necessarily essential, if as things developed it appeared that the federal funds rate in fact was settling down around 13 percent plus or minus. In other words, I'm saying let's bias it enough, if we have to, to get that kind of federal funds rate originally if it doesn't go up there by itself. Or, if it goes beyond that by itself, we probably don't need any bias in the borrowing component. Now, that's just going to be a matter of judgment in this early period. Peter is looking quizzical and wondering how he can make all these judgments every day. And he might miss. Inherent in this operating procedure is the possibility that the rate might be much higher or lower.

MR. PARTEE. The borrowing is a starting point, I think.

CHAIRMAN VOLCKER. We would be biased toward a slightly higher level of borrowing unless we found the funds rate going to 14, 15 percent. If that appeared to be happening, we just wouldn't bias it at that point. That should be consistent with all these relationships, though it would never work out in practice on a weekly basis. Doing nothing else should bring the federal funds rate to around 13 percent, but who knows what will happen in this jumpy market.

MR. AXILROD. Mr. Chairman, if I may [ask a question]. I assume that means, in giving Peter some estimate of the nonborrowed [reserve objective], he might start with a level of borrowing that is somewhat higher than the \$1.1 to \$1.3 billion it has been running on average in the past 3 or 4 weeks. So initially in constructing the path for nonborrowed reserves that seems consistent with the money growth path the Committee sets, we would reduce the total by having a level of borrowing that is somewhat higher [than it has been recently].

CHAIRMAN VOLCKER. I think that would be the initial assumption. But if the funds rate goes up well beyond the 13 percent area, and if we still had time in the week, I think you would reverse the bias.

MR. MAYO. Just to pin it down, are you thinking of \$1.5 billion?

MR. AXILROD. Well, in a way I'm a little puzzled because our knowledge of the relationships comes through a whole span of rates. As we get to very high rates, it may be that banks' willingness to borrow becomes stronger. If their willingness to borrow is about the way it has been, I would be thinking about \$1.5 billion. But the banks may become more willing to borrow and we may have to think of a higher level of borrowing for the same federal funds rate.

CHAIRMAN VOLCKER. Don't forget, there is estimating in this procedure. We don't know from day to day what the level of borrowing is going to be for the week, particularly when there's so much of it on the last day. So what we are looking at is some guess of what the borrowing is going to be for the week. Peter might be sitting there without all that much borrowing initially in the week with the federal funds rate very high but his projection could show that there are going to be huge excess reserves accumulated by Wednesday and that the federal funds rate should come way down on Wednesday. What I'm saying is that if he's in that situation, even though we don't have much reported borrowing at that stage, if the fed funds rate is way high in the range we don't bias it so much.

MR. STERNLIGHT. My guess, for what it's worth at this point, is that pushing borrowing to a billion and a half dollars might tend to push the funds rate higher, but that's just my feeling.

CHAIRMAN VOLCKER. Higher than 13 percent?

MR. COLDWELL. There is a possibility it might go the other way, though.

CHAIRMAN VOLCKER. Yes, it might go the other way, in which case we would retain the bias. None of this is going to be cleared up until the end of the statement week; that's the nature of it. I think you ought to have a better estimate than usual of what the borrowings will be this week because you know what the total reserves are going to be, given that they are based on deposits two weeks earlier. But you still [don't know] the distribution of reserves in the banking system or what excess reserves are going to be.

MR. AXILROD. Well, we know what the borrowings are going to be. We can tell that. It's a question of what rates are going to fall out of those borrowings.

CHAIRMAN VOLCKER. Well, you can't even tell what the borrowings are going to be because you don't know what excess reserves are going to be.

MR. AXILROD. That's right; we know what free reserves are going to be.

MR. STERNLIGHT. Another tricky little thing, if we are going to start something [different] as of right now, is that we are within a statement week. The statement week has just two days left as well as a partial holiday, which is usually associated with lousing up the estimates. So there may not be very much of--

CHAIRMAN VOLCKER. Oh, I don't know what we do in these two days.

MR. STERNLIGHT. Play it by ear.

CHAIRMAN VOLCKER. Play it by ear the first two days. And one of those two days is a Wednesday, so--

MR. MAYO. Would you expect to get action from us and our boards of directors on Monday?

CHAIRMAN VOLCKER. Well, we have a request for a [discount rate] increase of 1 percentage point, so the Board can act. And I still don't know whether we are going to be making this announcement this afternoon or not. If we are, I don't know what you can do [about contacting your directors] on Saturday, anyway. If we are not going to announce until Monday, I still don't know what you can do because I don't know whether we want to--

SPEAKER(?). We can get them on Sunday.

MR. MAYO. We could probably get some of them, but with it being a long weekend in Chicago--

MR. COLDWELL. It's not a good idea if you are going to wait until Monday.

MR. PARTEE. Since you've already got the [request on the discount] rate.

MR. BALLE. Mr. Chairman, may I make a strong plea that you allow the rest of us to get in on this [discount rate action]? Some of our directors in San Francisco were [pushing] strongly for [an increase such as] this in our last telephone meeting a week ago. I asked them to hold off until we could--I did not say it in these words but it's what I really had in mind--get a coordinated package. Is there any reason that you see as compelling to announce it Monday morning rather than in just a few hours? We can get our directors together on Monday morning and I think it would look better if all the Reserve Banks did [the discount rate increase] at the same time.

MR. PARTEE. The foreign exchange markets are open.

MR. MORRIS. We can't wait.

CHAIRMAN VOLCKER. Let's come back to that at the end; let's finish this meeting. Is that broadly agreeable as an alternative package?

MR. EASTBURN. Paul, I missed the aggregates figures that you proposed. Are they the same as you had before?

CHAIRMAN VOLCKER. The aggregates are the ones on the right-hand side of page 3, recognizing that we'd rather miss on the low side than the high side.

MR. PARTEE. A little on the low side.

MR. COLDWELL. No, I don't agree with you.

CHAIRMAN VOLCKER. The alternative, it seems to me--though we could fiddle around with the percentages--would be basically the same. We'd do the same reserve requirement change. We'd do the same with the discount rate. And then we'd move the federal funds rate basically to 13 percent, and put a 12-1/2 to 13-1/2 percent range on it, say. We could operate a bit more flexibly than we have before to the extent that that's possible, borrowing a little from what we're talking about in the new technique. But we'd have a much tighter

constraint [on the funds rate] relative to what we just talked about on the new technique.

MR. COLDWELL. Reserve requirements?

CHAIRMAN VOLCKER. Yes, the reserve requirement [change would be the same]. I think that's essentially it. I don't think I left anything out here [relating to the provision of] reserves.

MR. COLDWELL. Targets?

CHAIRMAN VOLCKER. I think the same. We've got to have a money supply target, which I presume would be the same. However, any of those [targets] could be altered.

MR. ALTMANN. Are they the same as under the existing directive?

CHAIRMAN VOLCKER. No, the same as in package number 1. So it's a longer time horizon [for the money supply target] than we would ordinarily have. And if that objective is stated another way, it would have to be interpreted that if [money growth] were running ahead of this track, we would use the upper part of the 12-1/2 to 13-1/2 percent range we are talking about. And if it's running below, we'd use the lower part of the range. I say again that I think the difference largely comes down to the constraint we are putting on the fed funds rate. That course of action would be very much preferred by our friends elsewhere in the city, in terms of the general framework. I don't think it makes a lot of difference, actually, as we modified the other approach. I don't want to make a federal case out of this, but it's nevertheless true. I've just tried to state here what I think is more or less the equivalent in immediate market impact. I suppose you could say that we should be a little tougher in the conventional package to [equalize] the psychological effects that we'd get from the talk about the reserve target.

MR. BLACK. I think that's clearly true.

CHAIRMAN VOLCKER. Remember that one of the dangers of the approach we have been talking about is that we may miss the target anyway, and we are a little less vulnerable to that with the conventional approach. The problem wouldn't disappear if we missed the targets either way. But without going through the rigmarole of a new dedication to [achieving] them we are a little less vulnerable. Maybe I ought to put that federal funds rate that I talked about a little higher to make the [two alternatives] fully equivalent, say, 1/2 point or 1/4 point higher. We could talk about that.

These are basically the two propositions we have before us. What I want to know is if there is a strong preference--it doesn't have to be unanimous--for one of them. Let's first take our famous preference [poll]. Let me say the second one would be a little tighter on the federal funds rate than I suggested earlier--[by moving it] at least to 13 percent or a little over 13 percent to make the psychological impact equivalent. How many would prefer the traditional approach? This is a matter of preference.

MR. BAUGHMAN. Voting members or all of us?

CHAIRMAN VOLCKER. Well, we will take everyone now. Raise your hand if you prefer the present method. Does everybody else prefer the other or--?

MR. EASTBURN. How many was it?

MR. ALTMANN. Three or four--I'm not sure.

CHAIRMAN VOLCKER. Hold up your hands a little higher, even if you don't feel strongly.

MR. ROOS. These are those who feel we should continue as with everything we said this morning?

MR. COLDWELL. It's just continue the regular procedure.

MR. ALTMANN. It's five.

CHAIRMAN VOLCKER. All right. How many would prefer the other alternative? Is that everybody else?

MR. ALTMANN. Twelve.

CHAIRMAN VOLCKER. There is quite clearly a great majority who want the new technique. Now let me ask the question slightly differently. How many feel strongly about this? I doubt that anybody thinks it's a matter of life or death but I just want to see how strong the sentiment is.

SPEAKER(?). I think it's big.

CHAIRMAN VOLCKER. Who has a strong preference for moving in the new direction?

MR. ALTMANN. 1,2,3,4,5,6,7,8.

CHAIRMAN VOLCKER. You're in that camp, Nancy?

MS. TEETERS. I feel queasy about it.

MR. PARTEE. Well, some preference.

MR. MAYO. Your feeling is semi-strong, Nancy.

CHAIRMAN VOLCKER. Now, let's look at the voting members. Who has a strong preference?

MR. ALTMANN. Seven, again not counting you.

CHAIRMAN VOLCKER. Did you count Nancy in or out?

MR. ALTMANN. No, I didn't count Nancy.

MS. TEETERS. I'm in.

MR. ALTMANN. Eight.

SPEAKER(?). Out of 11.

CHAIRMAN VOLCKER. Well, I guess that's strong enough that we ought to go with it.

MR. PARTEE. I don't know how much difference it will really come down to. I think we have a better intellectual agreement.

CHAIRMAN VOLCKER. I will just give you my interpretation of a non-mechanical [application], as I put it from the beginning, of the new technique. The difference isn't all that dramatic. There will be more emphasis on [the new technique] in the press announcement because it will be, in effect, a warning that the federal funds rate is going to be permitted to fluctuate over a wider range. Of course, we can say that in either announcement, but it will be said a little more strongly [with the announcement of the new operating method].

MR. SCHULTZ. I think we are going to get a bigger psychological impact than you think we're going to get.

MR. BLACK. I do, too.

MR. MAYO. Paul, one of the problems with the alternative is that we either adopt a wide range or start with a funds rate that's already above where it is now. In other words, if it's at a little less than 12 percent now, and we put our range at 12-1/2 to 14 percent or whatever you suggested, that raises another difficulty. Maybe it's mechanical. But from a realistic standpoint we almost have to widen the range on the alternative.

CHAIRMAN VOLCKER. Oh, I said we would have to widen the ranges on the alternative [technique].

MR. MAYO. Almost to the full 4 points, if we are going to sell it.

CHAIRMAN VOLCKER. Let me, for my [information], put it the other way. I just want to get a sense of this. Suppose we used the conventional approach; the range might be stated formally as 1 percentage point in width. But suppose I also said that in practice right now, as we usually say, we are going to aim for 13-1/4 percent and we are not going to move that from day to day or week to week unless there's a strong indication from the aggregates. I mean literally it's what we do now. How many people would find that acceptable or would prefer that? Maybe nobody, but I just want to get a feel of that.

MR. WALLICH. You mean announce that rate?

CHAIRMAN VOLCKER. No, do it just the way we do now. The market would be looking at Peter's actions over the next 3 days to find out that he was intervening at 13-3/8 percent on the up side and 13 percent on the down side.

MR. MAYO. Ugh! We lose any--I hate to use the word--drama.

CHAIRMAN VOLCKER. That's interesting. Is everybody saying that they don't like that?

MR. WALLICH. I still think it's the safer thing to do.

MS. TEETERS. I don't, Henry, because all we'd be doing is tightening with no possibilities of [the rate] coming down again.

MR. MAYO. It would look as if we are just chug, chugging, more [of the same]. It lacks the announcement effect of the other approach.

MR. COLDWELL. You get your announcement effect out of the reserve requirement [change].

CHAIRMAN VOLCKER. We have a tentative directive written, which is quite general as you can imagine. [That is being distributed to you now.] We can vote on the directive.

MR. BLACK. Is this just in favor of the approach or does it have the specifications tied to--

CHAIRMAN VOLCKER. Specifications, too.

MR. COLDWELL. Well, I'm not going to dissent against what the Board and Federal Open Market Committee think they ought to do if the majority is clearly in favor of package 1. I must admit that I think the M1 target is too high.

MR. BLACK. I concur, Mr. Chairman. I certainly would like to see it shaved down a bit because I think it is very important that we come within the ranges. And remember, we just announced 1-1/2 to 4-1/2 percent as the target on M1 and we are going to have to tell people that it's really 3 to 6 percent.

CHAIRMAN VOLCKER. The announcement will say that.

MR. WALLICH. I share that view. I would like 4 percent rather than 4.5 percent.

MR. BALLE. I would, too.

MR. MAYO. I would, too.

MS. TEETERS. I wouldn't.

MR. COLDWELL. Well, why don't we take a vote on the 4 against the 4-1/2?

CHAIRMAN VOLCKER. Well, I'd be reluctant to fine-tune too much here. That is why I suggest 4-1/2 percent, recognizing that if market developments permit and if there are opportunities to get [M1 growth] somewhat below that without pressing the limits of our funds ranges, we ought to take them.

MR. AXILROD. Mr. Chairman, I could save the Committee some trouble in reading [this draft directive] by pointing out that page 1 is a repeat of the existing long-run target [directive language]. Page 2 is the new operational paragraph that is proposed.

MR. MAYO. Mr. Chairman, would it be too much of a straddle to say that we were going to aim for a 4 to 4-1/2 percent range [for M1] for September-December?

CHAIRMAN VOLCKER. Let me just suggest this. Why don't we put in the directive at this point that we now estimate the ATS and NOW account effect at about 1-1/2 percent, which would make the equivalent range for M1 3 to 6 percent. I'm going to have to say that in the press conference, anyway.

MR. MAYO. Well, my point isn't just to straddle more, but to cite an intention within a half point range. It seems to me that we've been range conscious on all of our aggregates so there's no harm in saying we are aiming in a range of 4 to 4-1/2 percent for September to December.

CHAIRMAN VOLCKER. We could do that. Whatever way, this is not specifically in the directive is it?

MR. MAYO. No.

MR. COLDWELL. It will be in the minutes.

CHAIRMAN VOLCKER. It will be in the minutes.

MR. BLACK. You mean the statement of policy actions?

MR. ALTMANN. The policy record.

MR. COLDWELL. Policy record.

CHAIRMAN VOLCKER. That's the release that comes out about a month [after the meeting]?

MR. ALTMANN. That's right.

MR. KIMBREL. I hate to keep asking, but is the funds range 11-1/2 to 15-1/2 percent, as Nancy suggested?

CHAIRMAN VOLCKER. It's 11-1/2 to 15-1/2 as Nancy suggested, with a clear warning to you that you may get a call for a consultation if the rate gets up there.

MR. COLDWELL. The way she stated it was that a consultation clearly would be called at 14-1/2 percent, wasn't it?

MR. MAYO. That's right.

MR. PARTEE. I just wanted to point out that this last paragraph I think has a little range implied for M1--and for the other aggregates--and the range is centered around 4-1/2.

CHAIRMAN VOLCKER. Why? Oh, because of the "around" 4-1/2?

MR. COLDWELL. Well, if we are going to center a range, then I certainly would rather center it around 4 rather than 4-1/2 percent.

MR. PARTEE. But this is the exact statement of what Paul suggested. It seems to me that at the press conference what he'd be saying is that we are determined to hold these aggregates within the targets previously announced. My point simply is that if we happen to come out at 5 percent for September-December we wouldn't be outside

the target range. I think 4-1/2 percent does imply a [bit of a] range. Now for safety, we'd rather be on the lower side of 4-1/2 percent.

MR. BLACK. There isn't any safety on M2, Chuck.

MR. PARTEE. Again, it seems to me that you can trade that M2 off against M3.

MR. BLACK. It may well come in less than that anyway with disintermediation.

CHAIRMAN VOLCKER. I think we are dancing on a pin a little bit here.

MR. MAYO. Yes, I accept Chuck's point. I think it's well taken.

MR. PARTEE. Yes. We're going to have an awfully hard time--

CHAIRMAN VOLCKER. We are going to be awfully delighted if we come in any place within these ranges.

MR. ROOS. Mr. Chairman, is this communication, this [directive], going to be kept within this group as far as publicity--?

MR. PARTEE. Except for the press conference.

MR. ROOS. There are aspects that I think could cause some trouble with the analysis. I'm talking about the wire and the [decision].

CHAIRMAN VOLCKER. By all means, that is kept strictly confidential.

MR. KIMBREL. Mr. Chairman, we seem to be getting close together and I sure would hate to have my friend Mr. Roos cast my vote [as my alternate] but I have to leave and I just want to vote.

CHAIRMAN VOLCKER. I think we are ready to vote. We are voting specifically on this directive. Those blanks are to be filled in with 11-1/2 to 15-1/2 and I think we write in the sentence there about consultation when the funds rate is "in the upper part of the range" or something vague like "toward the top."

MR. PARTEE. Toward the top.

CHAIRMAN VOLCKER. Toward the top. And I think what we mean by that is something like 14-1/2 percent. We are talking about 4-1/2 percent "permitted," if you will. Obvious we'd rather have less, if things develop so that we can do it without putting untoward pressure on market rates. And what we are saying clearly is that if this money demand function collapses we'd be delighted to come in below 4-1/2 percent. It is not going to collapse before we meet again.

MR. MORRIS. For security reasons you'd prefer not to get the other Reserve Banks in on the discount rate?

CHAIRMAN VOLCKER. Well, let's just get this vote over with. I believe you understand this slight bias in the way we play that. We are thinking of a federal funds rate ideally in the 13 percent plus range, initially. That would be a highly satisfactory response, but we don't have any close control over it--it could be more or less--and that would affect our biasing decisions. I think we are ready for a vote.

MR. ALTMANN. All right.

Chairman Volcker	Yes
President Balles	Yes
President Black	Yes
Governor Coldwell	Yes
President Kimbrel	Yes
President Mayo	Yes
Governor Partee	Yes
Governor Rice	Yes
Governor Schultz	Yes
Governor Teeters	Yes
First Vice President Timlen	Yes
Governor Wallich	Yes

CHAIRMAN VOLCKER. Well, I very much appreciate this discussion. I think it was important. We do have a press release prepared by Joe Coyne. I would like to insert in the press release--and I just want to ask your advice on it--that the Committee voted unanimously on this.

MR. MAYO. I think you should.

END OF MEETING