TRANSCRIPT

FEDERAL OPEN MARKET COMMITTEE MEETING

August 16, 1977

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.

Staff Statements Appended to the Transcript

Mr. Sternlight, Deputy Manager for Domestic Operations

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Meeting of Federal Open Market Committee

August 16, 1977

A meeting of the Federal Open Market Committee was held in the offices of the Board of Governors of the Federal Reserve System in Washington, D.C., on Tuesday, August 16, 1977, beginning at 9:00 a.m.

PRESENT: Mr. Burns, Chairman
Mr. Volcker, Vice Chairman
Mr. Coldwell
Mr. Gardner
Mr. Guffey
Mr. Jackson
Mr. Lilly
Mr. Mayo
Mr. Morris
Mr. Partee
Mr. Roos
Mr. Wallich

Messrs. Balles, Baughman, Eastburn, and Winn, Alternate Members of the Federal Open Market Committee

Mr. Kimbrel, President of the Federal Reserve Bank of Atlanta

Mr. Altmann, Deputy Secretary
Mr. Bernard, Assistant Secretary
Mr. O'Connell, General Counsel
Mr. Axilrod, Economist
Messrs. R. Davis, T. Davis, Eisenmenger, Kichline, Reynolds, Scheld, Truman, and Zeisel, Associate Economists

Mr. Pardee, Deputy Manager for Foreign Operations
Mr. Sternlight, Deputy Manager for Domestic Operations

Mr. Hudson, Assistant to the Chairman, Board of Governors
Messrs. Coyne and Keir, Assistants to the Board of Governors
Mrs. Farar, Economist, Open Market Secretariat, Board of Governors
Miss Klaput, Open Market Secretariat, Board of Governors

Messrs. Rankin and Van Nice, First Vice Presidents, Federal Reserve Banks of Richmond and Minneapolis, respectively
Mr. J. Davis, Senior Vice President, Federal Reserve Bank of Cleveland
Messrs. Brandt, Broaddus, Burns, Hoskins, Keran, and Karnosky, Vice Presidents, Federal Reserve Banks of Atlanta, Richmond, Dallas, Philadelphia, San Francisco, and St. Louis, respectively
Mr. Kareken, Economic Adviser, Federal Reserve Bank of Minneapolis
Mr. John Hill, Senior Economist, Federal Reserve Bank of New York

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CHAIRMAN BURNS. The agenda indicates an executive session, but that session will be postponed until we have concluded our monetary policy meeting. Is there, gentlemen, a move to approve the minutes [of the July 19, 1977, meeting], if that be the inclination of the Committee?

SPEAKER(?). So moved.

SPEAKER(?). Seconded.

CHAIRMAN BURNS. The motion has been made and seconded. No objections heard. I take it the minutes are approved. We will now hear from Mr. Pardee on foreign currency operations.

MR. PARDEE. [Secretary's note: This statement was not found in Committee records.]

CHAIRMAN BURNS. Thank you very much. I take it [that], while foreign exchange markets start boiling, our rhetoric also becomes more interesting, more exciting.

MR. PARTEE. You bought $77 million--is that what it amounts to in the market? You got rid of the $35 [million].

MR. PARDEE. Yes, 35 plus 43.

MR. PARTEE. How much had you sold earlier?

MR. PARDEE. Oh, well, in the total operation, it had been somewhat over $100 million between June and July. And $88 million reported last month.

MR. PARTEE. But you haven’t quite recouped your position, I suppose.

MR. PARDEE. I’m building up balances very gradually, dollar averaging as the dollar rate rises. Buying marks at times when the dollar is rising particular sharply, again on the idea of avoiding disorderly conditions.

CHAIRMAN BURNS. Any questions or comments? Yes, Mr. Wallich.

MR. WALLICH. In your report for the period, you mentioned that various currencies tried to avoid getting into the lower part of the snake [intended exchange rate band] and also, I guess, wanted to avoid being at the top, and so they intervened. Is that now the standard procedure? That they will not wait and operate in their own currencies, which I understand is the rule of the snake?

MR. PARDEE. Yes, I think the central banks have found that, as we did in the fixed-rate world, that the last place you want to be is at the upper limit with no flexibility whatsoever, just taking in taking in currencies or handing them out. And that to maintain the flexibility of intervention, it's better to start somewhat earlier, and the central banks in the EC snake group do intervene in dollars at their own discretion and with the approval of the group prior to reaching the outer limit. And the practice in recent months has been to avoid getting to the outer limit if they can. That's when the big speculative pressures, one-way pressures, are likely to emerge.

MR. WALLICH. Is there any evidence they're thinking of using their own currencies within the limits? I realize that there are accounting difficulties.

MR. PARDEE. They have from time to time, but not in transactions outside the fund, the pooling arrangement. There are all kinds of bonds that are being issued, and so forth, and currencies come into their hands. We have the odd situation where the Bank of France is now operating much more in German marks, and at one stage they were buying dollars and selling marks, trying to position the franc somewhere in between the dollar and the mark as the two currencies were moving. So there's a lot more flexibility on the part of the central banks both in and out of the snake, in dollars and other currencies.

MR. JACKSON. Is the morning telephone call in Europe still in action? If so, how did it work out?

MR. PARDEE. Morning telephone--

MR. JACKSON. As I remember, the central banks were exchanging a morning conference call.

MR. PARDEE. Yes, well they have consultation calls three times a day. And that's working out fine. We, of course, receive a call--from the so-called captain of the day, after they finish their day--and get the full information. We ourselves make an early morning call, around 7, and several other [calls] during the course of the morning, and pick up the same sort of information. Now that they know that we are hooked in on the system, it's working very well.

MR. PARTEE. I think that's full exchange.

MR. PARDEE. Not full exchange, but much more than there used to be. There are still some elements, particularly on some of the more delicate intervention operations, which are passed at a higher level. But we get the information we need.

CHAIRMAN BURNS. Any other questions or comments? Very well, a motion to approve the transactions conducted by the foreign Desk would now be in order.

SPEAKER(?). So moved.

SPEAKER(?). Seconded.

CHAIRMAN BURNS. The motion has been made and presumably seconded. I hear no objection, and therefore we pass to your recommendations, if any, Mr. Pardee.

MR. PARDEE. No recommendations.

CHAIRMAN BURNS. Well, it's a good day. All right, let's pass quickly before recommendations emerge. Mr. Kichline, we're ready for your economic report.

MR. KICHLINE. [Secretary's note: This statement was not found in Committee records.]

CHAIRMAN BURNS. I wonder how many of you may have read this morning's editorial in the *Wall Street Journal*. Well, we can't very well discuss that.

SPEAKER(?). Unless you want to read it to us.

VICE CHAIRMAN VOLCKER. We might have a better discussion.

CHAIRMAN BURNS. Mr. Kichline has reviewed very competently the recent run of economic statistics, and these are summarized in the Greenbook and in the Supplement. I think it would be especially valuable if members of the Committee who have contacts with businessmen, and bankers, and citizens generally, in their own area, would comment on businessmen's current attitudes with regard to the economy. What are their concerns, are they experiencing improving profits, are they anticipating a continuance of the economic expansion, are they uncertain about the trend of economic events? I think a discussion or anything that members of the Committee may contribute along those lines--I, for one, would find it especially valuable. I think I have in the back of my head the statistics pretty well summed up, and not much is to be gained by going through those again. Yes, Governor Lilly.

MR. LILLY. Well, Willis Winn and I, last week, had a meeting in Cleveland with a very representative cross section of the industrial world, and we gained some insights there as to what their thinking was, and I'd like to hear [Mr. Winn] summarize it. Unless you were--

MR. WINN. Was I the recording secretary? Maybe I missed my role in this setup. I'm not sure that I'm summarizing our meeting, Dave, but I have been impressed that the press sometimes influences the thinking of businessmen [more] than their own appraisal of what's happened to them. I was interested particularly--when we were sort of probing with the steel people, and they said, "Well, business is quite good but profits aren't. But the order rate and the tonnage and other factors are really quite good." Now I don't know how much of this is due to the fact that the ore people are out on strike and it's thought that the coal people will be out on strike, but they have--

CHAIRMAN BURNS. But the steel companies had a poor second quarter.

MR. WINN. Earningswise--

CHAIRMAN BURNS. Earningswise, exactly.

MR. WINN. But the volume is surprisingly good.

CHAIRMAN BURNS. Well, what good is volume if you don't make a profit?

MR. WINN. Well, they hope to turn it around, of course. But if you don't have volume either, then you've really got problems.

MR. LILLY. That's the worst condition--no volume.

MR. WINN. When you sort of probe--you can't rent warehouse space, for example, across the country. And part of this is this inventory increase, but there haven't been any warehouses built for the last three years or so. And my guess is that, if sales continue to grow, you're going to see a big move in this direction.

Second, there are five major buildings downtown in Cleveland that will be going on the board here in the next six to eight months. There are talks of office construction across this country in various spots. And apartment [construction] is just on the horizon. But very little available space. And with some change in rents and other factors, I think you're going to see a rather major move in the construction of multifamily homes. [To] pick up on what's happening in terms of the housing factor, I can't see growing from this level, but probably it will hold on this sort of basis. But I--

MR. PARTEE. You said five new office buildings in Cleveland?

MR. WINN. Yes. One of them is a state building; Standard Oil; the two banks; and a private development.

MR. JACKSON. Any of these speculative? Or just institutional?

MR. WINN. Just one. And so this is really a major change in the construction outlook, in this sense of the term. They are all cautious when they talk to you in one sense of the term, but you probe about their own business and it is surprisingly good.

MR. LILLY. There's a great concern about the loss [on the] capital gains tax. There is a great concern about inflation and the loneliness of the Fed and it's position. They're very bullish as to the rate of capital investment expenditures.

MR. WINN. All of them are well fixed financially. They've really protected themselves against the squeeze, so you're going to get the expansion without going back into the financial market. Their positions will take care of it.

CHAIRMAN BURNS. Mr. Kichline, you didn't comment--or I perhaps wasn't listening carefully enough--on the trend of corporate profits.

MR. KICHLINE. No, I did not. You're talking about the recent past, or our forecast, or both?

CHAIRMAN BURNS. Both.

MR. KICHLINE. Profits in the latter half of 1976 were revised down significantly with the recent revision in the GNP and national income accounts data. The first quarter is very weak. The implicit profits currently contained in the GNP data, which we'll receive next week for the second quarter, indicate an increase of around 7 percent or so. We think it's likely to be a bit stronger than that.

For our forecast, I must say that we were much more optimistic about profit performance several months ago than we are today. [The difference] stems in part from a little bit weaker performance on real output as we go through this period. But importantly, it stems from a look at unit labor costs, which in our forecasts had been edging up over the past several months. And in general, corporate profits now in the forecast are sufficient to retain their share of GNP or gross corporate product but do little more than that. So, historically, they have not fully recovered and are not up to levels that we had seen back in ’72, ’73. So I would say that it’s not a terribly bearish performance, but it certainly isn’t good, particularly if you take a longer sweep of history and look at the performance of profits at a much higher level in relative terms in the ’50s and part of the ’60s.

CHAIRMAN BURNS. Thank you. Yes, Mr. Jackson.

MR. JACKSON. The people with whom I’ve discussed the situation within the last three weeks have come back to a surprising concern about inflation. This appears to be the number one issue in the minds of most people that I’ve visited. They think business conditions are good, they think underlying demand is good. They think the biggest single risk event that would destroy future growth is a sufficient resurgence of inflation [unintelligible] that would destroy confidence [unintelligible]. And in the minds of the people I’ve talked to, that’s been surprisingly number one and very strong, much stronger in their views than I’ve heard before.

CHAIRMAN BURNS. Thank you. Mr. Mayo, please.

MR. MAYO. I don’t want to dwell too much on this, because basically, the comments we have had out of our directors are, I think, quite consistent with the staff projections. And so it gives support, I would say on the “feel” side, to what you might say is a more statistical approach. We have some softness in the Midwest in farm machinery and some other heavy equipment. We still have a drought situation right around Des Moines, with the corn crop being basically a failure in about seven counties in Iowa.

But the rest of Iowa and the rest of the Midwest in our area is rejoicing that even subsoil moisture is beginning to build up again, and the drought is behind them. They have record crops expected in Iowa and Illinois in soybeans and corn--[for those crops] they are the two leading states in the country.

The farmers, of course, are feeling poor because the prices are so low, but this is the market economy at work. It has its effect on bank credit. They are against price supports [in] principle, but they are looking forward to the benefits of new legislation that will give them two bucks for their corn instead of $1.85.

CHAIRMAN BURNS. Thank you, Mr. Mayo. Mr. Rankin, please.

MR. RANKIN. Thank you, Mr. Chairman. At our board meeting last Thursday [for] the Fifth District, most of our directors characterized retail sales as moderately strong. Construction of single-family housing is apparently continuing at a high level throughout the District. There are some indications that it will pick up in multiunit construction.

Their comments regarding prospects for business capital spending during the second half, however, were less optimistic. There is little evidence of any sizable increase in outlays for new or expanded facilities. One director stated flatly that there is simply too much uncertainty regarding energy and regulatory policy to permit major new undertakings. And on the financial side, while consumer mortgage lending is expanding at a healthy pace, business loan demand was characterized as still flat. And interestingly, the president of one of our larger banks reported that he knew of loans that were being made below prime.

CHAIRMAN BURNS. Thank you, Mr. Rankin. Mr. Balles, please.

MR. BALLES. Well, by and large, as I reviewed the comments of the directors at our various Branches, I get a mixed picture, which is not unusual. But I think it may be more mixed now than I have seen in a while. My general impression is that business confidence is not quite as good as the business statistics. There are elements of caution and concern that we've known about for some time, of course, about the inflation outlook, about the full implications of the energy program. And you get into companies that are in the public utility, the energy field, and they are quite upset about developments and the uncertainties.

The strengths that we see on the West Coast are in such fields as aerospace, housing construction, retail sales. And, as an indirect indicator, loan demand in the so-called middle market seems to be very strong across a broad front. All kinds of loans in the medium- and small-sized banks. The weak parts of the economy in the West would be many segments of agriculture because of our terrible drought conditions. Some slowing down in the pulp, paper, and container business. As a leading indicator, according to one director, a number of lumber mills on the West Coast are in trouble because of very high, rising labor costs. In fact, we got a report last week that four lumber mills in Oregon are shutting down because of this. As I say, it's kind of a spotty picture, and a little more of a contrast type of situation than I would normally expect at this stage of the business upswing.

CHAIRMAN BURNS. Thank you, Mr. Balles.

MR. JACKSON. May I ask a question about the lumber situation? My impression is that lumber prices are closer to their peaks. They're very high, yet you talk about mills unable to operate in a relatively efficient market like that. I'm surprised.

MR. BALLES. Well, they've had some whopping big wage settlements going along with the rising prices.

MR. JACKSON. Is this slopped over from British Columbia, where they have those massive settlements?

MR. BALLES. I gather that's true.

CHAIRMAN BURNS. Mr. Wallich now, please.

MR. WALLICH. I'd like to throw out a hypothesis about the investment and profits picture. I have long been puzzled: Why would capacity pressures [that are] clearly ahead--[firms] having invested less than the growth of the labor force seems to imply--[why are] we not getting any additional investment? Now, when one ties that together with a poor profit performance, then the following may not be an unlikely course of events. The present level of profits doesn't permit adequate investment, even though the capacity needs may be quite visible in many industries. What is happening then is, we're moving up closer on capacity until those pressures are really of the kind where prices begin to rise, [unintelligible] and then at that point, profits will become sufficient to justify the investment that should have been made a year or a year and a half earlier.

CHAIRMAN BURNS. In other words, we need a little more inflation?

MR. WALLICH. That is what I think is the likely course of events. There'll be price pressure upward that will get us investment at the delayed point--better late than never, but under conditions that will be somewhat inflationary. Well, that is a reasonable hypothesis. There is still ahead an element of strength in the economy from that source. At present we seem to see more weak spots in the economy than strong. I think it's partly just perhaps characteristic of shifting from a 7 percent rate of growth, such as we had in the first half, to 5-1/2, and later 5, and 4-1/2. There are bound to be more weak spots as one gets down to a little above the level of long-term growth. So, in all, it looks to me as if a somewhat choppy period [is] ahead but with this expectation that eventually profits and plant and equipment spending will come around.

CHAIRMAN BURNS. Thank you, Mr. Wallich. Mr. Morris now, please.

MR. MORRIS. Mr. Chairman, I think I have some differences [with] the point of view of staff and the point of view of Mr. Winn. It seems to me that animal spirits in the [Keynesian] sense are pretty well [hid]. Governor Wallich's analysis is correct. But I think, in addition to that, you have the psychological factor of all these uncertainties generating an unwillingness to make commitments. I think it's reflected in behavior in the stock market, for example. And it's reflected, I think, in the commitments figures for new capital investment, which is really while we have an upward trend. I think it's an upward trend that is not going to be of sufficient strength in the next six months to offset the slackening that I see in the consumption sector and the housing sector.

It's a surprising thing--although my own staff happens to agree with the Board's staff in their projections--I tend to think [unintelligible]. I was surprised that the ray of data coming in [during] the past month did not lead to a more significant change in the projection. Because it seems to me that the probabilities are now that--and this may be bad--the projections for this quarter and the next are going to prove to be substantially too high, and that the first half of 1978 is likely to be substantially stronger. And [it] could well be that this will be a better path, as far as maintaining control over inflation, than the path we've projected.

Well, I feel very strongly that the weight of the evidence--no growth in new orders for durable goods, flattened retail sales for several months, substantial decline in basic commodity prices--right across the board [in] the indicators that tend to lead the economy, there is a base of weakness that I don't think is compatible with the modest slowdown in near-money growth rates. We would have to see quite a basic change coming up pretty quickly in these factors to justify the projection. My intuitive feeling is that we're going to be revising these numbers down.

MR. KICHLINE. Well, as I indicated at the end, when we put this projection together, we did not have the retail sales data. It's not so much July which shows an increase, which we had been anticipating, but it's from a considerably lower level than had been indicated earlier because of the downward revision in June. So taking that, I think we've looked at this quite carefully, and we also had anticipated a bit stronger increase in industrial production in July than turned out to be the case. So that's been after this projection was prepared and went to press.

For the current quarter, our thinking now would be somewhere in terms of 4/10 percent to 5/10 percent less real growth than we've indicated. So we get a little below 5 perhaps. And I think our view of the longer run does indeed differ, in the sense that we think there is a prospect of good performance for the fourth quarter. But you're quite correct about this quarter, and given the information we have, we would weaken the projection.

MR. COLDWELL. Would you care to comment on President Morris's pattern question that he talked about?

MR. KICHLINE. Well, I think it's quite possible. I think, really, the best bet now is not to have a repeat of 1976. I'm not sure it's in the cards. I'd be reluctant to go that far, and as I read what President Morris said, it's essentially what we're talking about, but a much stronger performance going into the early part of 1978.

Some other data that we didn't have at the time this Greenbook went to press dealt with some early indications of capital appropriations from the Conference Board. And their survey is not fully tabulated for the second quarter, but it has sort of a year's lead time. And it does show capital appropriations rising significantly, and I think that bodes well for '78. I think the mix on the investment side is sort of positive, but it's at the same time very hard to stake out a sizable increase. We do have good growth in business fixed investment. It's just hard at this time to see the evidence to justify substantially larger rates of increase in investment than we have in our projections.

MR. MORRIS. When you say significant, what percentage rates of increase over the first quarter do they think about?

MR. KICHLINE. From first [quarter] the first [quarter] in business fixed investment?

MR. MORRIS. I was thinking from the first quarter to the second quarter.

MR. KICHLINE. Excuse me; all right. The number they have is about 7 percent for totals. In the first quarter, it was down 2.6 percent, and if you take out petroleum refiners in the first quarter, capital appropriations rose about 1 percent. And in the second quarter, if you take out petroleum, the increase is indicated to be about 17 percent. I would indicate, that's the Alaska pipeline and associated facilities. These numbers are supposedly confidential, I believe September 1 or 2, and it's an early reading, but it is up, and it's after a very strong fourth quarter, which was about a 31 percent increase, in the fourth quarter of '76. So there seems to be a lot going on in this area that perhaps could come on stream as we get into '78. We're counting on that.

CHAIRMAN BURNS. All right, thank you, Mr. Morris. Mr. Baughman, please.

MR. BAUGHMAN. Mr. Chairman, I hesitate to generalize from one of the strong areas of the country, but all the indications we see, of course, are suggestive of a continued, rather heavy flow of funds into new investment and continued expansion in activity. And even our retail firms represented on the board--we have three of them at the present time--who had been speaking rather bearishly about a month ago, have recently felt obliged to acknowledge that things have developed much better than they had expected during the past month and that they are now viewing the future with a little more optimism.

We are seeing some commitments for large projects, and, of course, they are all energy oriented. We are also seeing indications that present capacity, in chemicals based on petroleum and natural gas products, particularly, is coming under pressure. And it has seemed to me that the sort of thing that's showing up in Cleveland is likely to show up in center after center around the country

But at a minimum, the staff projection will probably pretty well characterize what develops. I would think, in so far as it may prove to be wide of the mark, it's likely to be low rather than high, both in terms of the dollar measures and the deflated measures of economic activity. I would think that managements will find that a fair amount of their existing plant may have been obsolete prematurely, in part as a result of the much more expensive fuel prices. And I think it quite understandable that that could be a disconcerting thing in terms of the timing of a decision to make additional investment. But, on balance, it seems to me that it's going to call for more investment than otherwise would take place and that we will see this coming along.

Now having said all this, there is the further disconcerting aspect of the picture as you look around and see the management of a fair number of firms apparently concluding that the most profitable investment available to them is buying up their own shares. That, it seems to me, you have to weigh on the negative side of the balance sheet when you're trying to arrive at a judgment as to how businessmen are looking at the future. My inclination would be--and I'm repeating--to feel, overall, the staff projection is a good one, but insofar as it proves wide of the mark, it will probably be on the low side rather than the high side.

I had a little difficulty on a specific item. And this is certainly a small detail--the rather large swing they show in private final purchases from fourth quarter this year to first quarter next year and then back to the second quarter. This apparently is heavily weighted with an expected swing in inventories. The basis of that particular aspect of the projection, I don't comprehend.

MR. KICHLINE. That stems largely from the projection for imports, which, if you note in this projection is bouncing around a good deal [and is] related to the staff's expectation with regard to oil imports particularly. In the fourth quarter, it is anticipated that there will be a substantial stockpiling of imported oil, which drives up imports and gets carried into inventories, which go up and [then] run off in the first quarter.

And the rationale for that is that the imposition of the well-head tax on January 1 coincides with the Administration's plan to eliminate the so-called entitlements program, which provides something like 75 cents a barrel to imported or foreign oil. And that will disappear January 1 according to plan. And hence it is assumed that there will be a substantial buildup in the fourth quarter. Something similar was going on in the second quarter of this year in our interpretation of the data, where oil inventories rose substantially [in] anticipation of the OPEC price increase as well as [because of] the initial announcement effect of the Administration's well-head tax and the removal of the entitlement program. So it's essentially a wash over this time period and has no lasting influence.

MR. BAUGHMAN. Thank you.

CHAIRMAN BURNS. All right, thank you, Mr. Baughman. Mr. Kimbrel now, please.

MR. KIMBREL. Mr. Chairman, [we see] a good deal of concern in the farm area at the moment because of the extended drought and difficulties of the corn crop and the possibilities of some financing of the farmers against the difficulties of the production of corn. However, many of the others are coming along very well--peanuts, soybeans, citrus operators, and vegetable people have not done badly at all.

The businessmen are still possessed of a good deal of uncertainty related to a few things that have been commented on here: energy, tax, environmental concerns, and certainly inflation. But against all of that we still detect a rather optimistic outlook for most of these businessmen. Even in the construction area, two of the large regional construction companies recently suggested that they were intentionally adding extra margins of profit simply because they had all the work they wanted to take on anytime soon. It was simply, if they took anymore work, they were going to make certain that they made an extra profit on it. Construction, sure, the housing is still very strong. Particularly on the west coast of Florida, it's almost incredible what's happening in the residential construction area and the prices that are attached to it. Industrial or commercial construction, federal building yes, but utilities, Coca Cola, Bell. Contrary to the difficulties of paper on the West Coast, new paper and pulp plants are being built in Alabama. New hotel in New Orleans. So certainly it's not doom and gloom there at the moment.

CHAIRMAN BURNS. Thank you, Mr. Kimbrel. Mr. Partee, please.

MR. PARTEE. Well, Mr. Chairman, I think I agree with Frank Morris that we're likely to have a quarter or two here of considerably less rapid growth in the economy, for much the same reasons that he gives. I think that retail sales are showing signs of sluggishness. You can't really anticipate that durable goods spending by consumers, which has been extraordinarily high, will rise. It's more likely to fall in the period to come. Consumer credit has been rising at a rapid rate, and historically, you follow periods of rapid growth in consumer credit with periods of lesser growth as you get an adjustment in people's appreciation of their debt service burden and what they can take on. And so I think, as far as the consumer surveys are concerned, it's been pretty well demonstrated that what a consumer survey represents is what people feel like now rather than what they will be doing in the future. They have not been very good forecasters of the behavior at any time that I've been aware of in recent years. So I think maybe we'll have this quarter, certainly, perhaps two quarters, Frank, of considerably slow growth. And less than the staff is projecting but more like 3 percent to 4 percent annual rate of growth.

However, I don't feel badly about the business situation because I think that underlying this is the prospect of continued gains in 1978. I don't really see any evidence that recovery is going to come to an end anytime soon. I'm very impressed by Willis's comments about building in the commercial area. I think that's about to take hold. There's been a lot of indication on that in Washington, too, by the way. Washington has got quite a bit of building that's in the works, both office building and shopping center construction. And I think capital spending is going to be moving up. I don't think profits are as bad as they've been suggested to be in earlier comments here, and I don't think there is the prospect that business will be responding as they see more certainty that markets will take up the product that they might be able to produce with new plants. So capital spending will be on the run.

The stock market is a puzzle to me, because that certainly does seem to suggest that '78 wouldn't be a good year, at least not a booming year, and very possibly a beginning of a recession. But I think there that we have to make an adjustment for perceptions that the capital gains tax may be changed. You mentioned that Dave and I think it's a very important thing. Anybody who has got a profit of size in a stock position, in order to play it safe, is likely to want to realize some or all of that profit in a year in which capital gains taxes are still being treated in the conventional way. And anybody who anticipates there may a push on that, that is, to [raise] the capital gains tax later this year, is going to want to move in advance of that news so that he can beat the market. And so the whole market will move in advance of a real prospect that that might occur. And I think that, by itself, is a pretty substantial reason for explaining the performance of the market in the last several months, when it's been moving pretty steadily downward. So that's a level-adjustment type thing and it doesn't really indicate anything about future profits prospects or future business activity prospects; it's simply a stock adjustment in a capital value to reflect something that may happen in the future.

So as I say, Mr. Chairman, I think that there aren't serious imbalances in the economy, except perhaps a little overspending by consumers. We will have capital spending picking up as time goes on. I think government purchases, federal and state and local, which have been rather weak for the last two years, are going to be a source of considerably greater strength in the period to come. And so even though we do have in prospect a quarter or two of lesser real growth, I still think that the business recovery is alive and well and will be continued in '78 and that we ought to think in terms of that continued expansion as we try to develop policy prescriptions.

CHAIRMAN BURNS. Thank you, Mr. Partee. Mr. Roos now, please.

MR. ROOS. Mr. Chairman, I find myself, as a non-economist, somewhat confused. In looking back over the year and a half that I've had the privilege of attending these meetings, and listening to inputs such as we're presently providing, that year and a half in terms of business conditions has been a strong period. We've had basically good business, we've had strong output nationally.

And yet, I think with the exception, perhaps, of one or two meetings, as we go around the table, so many of us have attempted to express concerns and doubts and rather pessimistic attitudes toward what is in our minds; we imagine [things] of a negative nature to be lurking just around the corner. And one of the things that confuses me is what seems to be somewhat of an absence of a real definition of what we would consider to be a healthy economy. I mean, we speak in relative terms so often. And if we feel that a slowdown in output from a 7 percent rate of growth to 5-1/2 is something that is really bad, that [it] should be a cause for alarm, then perhaps we have a right to feel some concern about where we're going.

CHAIRMAN BURNS. I don't think anyone has expressed such a view.

MR. ROOS. Well, sir, am I correct to assume that if our economy does better than what it has over the average of 10 or 15 years, that we're really apparently in a fairly comfortable condition? I mean, what I'm getting to, and then I'll hush up, sir, is that I think that the public generally, that the business community, tends to be overly pessimistic about what is occurring and what has occurred. I think that perhaps this is due partially to what Phil Jackson referred to, which is an almost unanimous attitude in our part of the country, that regardless of what happens, this inflationary potential is of great concern to everybody.

But I wonder whether there isn't an absence, both within our own group here as well as within the leadership in the nation, of people with credibility who are expressing or stressing the positive instead of the negative. I feel that what is happening is not a subject of justifiable concern economically, in the interpretation of the economy. I can be terribly wrong in this, I'm not a professional. But I think everybody tends to look negatively on what may be happening instead of considering that, in historical perspective, the performance is and has been pretty good.

CHAIRMAN BURNS. Thank you, Mr. Roos. Mr. Coldwell now, please.

MR. COLDWELL. Mr. Chairman, that's an interesting act to follow because Governor Partee has covered what I was going to say in rather considerable detail, and I don't see any point in repeating it. Except my final answer is that I'm quite happy with a slowdown in the economy in the fall of this year. In the spring and early winter of this year, as you may recall, I predicted such a thing, and I'm kind of delighted that it's occurring because I can't really see a 7 percent continuation without real pressures on the economy. So if we're getting a slowdown from 7-1/2 to 4-1/2 or something like that, I'm just delighted that it's occurring as long as we don't accumulate the baggage. I think you've got the strength of government spending which is going to come along. And maybe we'll get some clarification in the tax matters if this Administration ever gets its act put together, and if so, I think we've got a good possibility of some strength in 1978. That's the horizon I'm looking at, not this second or third or fourth quarter of '77.

MR. PARTEE. I agree with Governor Coldwell, by the way. I should have said that I don't think it's a bad thing--the profile that's developing.

MR. MORRIS. No, I feel the same way.

MR. COLDWELL. What I was trying to get Mr. Kichline to say earlier is, the pattern might even be a better one for long-range growth in this economy--to have a little slowdown in the fall of this year.

CHAIRMAN BURNS. Thank you, Mr. Coldwell. Mr. Volcker now, please.

VICE CHAIRMAN VOLCKER. Mr. Chairman, I think I found the staff analysis quite persuasive this morning, as I guess most people did in a qualitative sense, in terms of the continuing momentum of the recovery. When my staff puts the numbers together, just following up in these comments that were just made, they get a slower rate of growth in the second half of this year, closer to 4-1/2 percent than the 5-1/2 percent, but I take it that there's no major disagreement. I don't see at this stage, nor does my staff, that we can sit here very content that it's going to take off again in '78. I think that remains to be seen. Our actual projections have a little further slowdown in '78.

I'm not sure where the strength comes from in '78. I think it's just too early to say, except from the kind of analysis that Governor Wallich had. And I think there's a great deal to that. When I assess the business mood, while I haven't gotten fresh input in recent weeks, the input has generally been recently along the lines that Presidents Morris and Balles have already commented on in terms of uncertainty--more uncertainty than the production trends seem to justify--which I do think can be traced largely to the profits performance and a feeling that there's a certain amount of pressure on prices now. There is ample capacity available, they can't raise their prices yet nearly as fast as they would like to, but they hope it's coming some day. They haven't seen it, and they feel a little discouraged about their ability to raise prices, which isn't a very happy situation from my standpoint.

My feeling about the inflation side, in terms of business attitudes, I'm afraid, has been more one of resignation than real concern. They certainly see it there. They don't see us--not the Federal Reserve but the United States--dealing with inflation very effectively--they don't see themselves dealing with it very effectively. They see wage demands coming up, and the level of resistance to those wage demands seems to me to be very low. I have three business directors, as everybody does. Mine have just had three wage settlements, averaging about 10 percent. They're all nationwide employers, and I must say I fail to detect the great sense of concern in any of those three directors over the size of the wage increase they just awarded. They think it's in the swing of things, that's the kind of wage increase you have these days. If you don't pay it without too much protest, you're not doing right by your own company because you may have a strike, and that's going to be much worse than paying the same wage increase that they expect all their competitors to be paying.

And this kind of attitude and momentum, which I think we see in the cost figures and indirectly in the profits figures, it seems to me, continues to present the major challenge for monetary policy. Some day we're going to run into a collision. We keep reducing the growth rate targets [for the monetary aggregates], and if [money growth does come in within those] growth rate targets and there hasn't been any decline in the momentum of cost increase, some day we're going to have a problem, and I don't see yet how this works itself out. Add to that Governor Wallich's concerns, which I share to a degree. I don't know whether he expressed them as concerns; I think they are a concern in the inflationary context.

We have a problem down the road. That's not being very helpful in terms of our immediate decision. I share the general feeling that we're going to have some slowdown, but the momentum is pretty good. And some slowdown is not a matter of great concern at the moment. This underlying inflationary cost momentum does concern me.

CHAIRMAN BURNS. Thank you, Mr. Volcker. Mr. Eastburn now, please.

MR. EASTBURN. Well, I would second those last words Paul gave us. A couple meetings ago I reported on the sentiment of businessmen in our area, which of course is not the most vigorous area in the country, and it's one of concern and remains one of concern. I think [their sentiment] is more pessimistic than the statistics would suggest is warranted, but I think that Phil Jackson is entirely correct that inflation is a primary concern to businessmen.

Along that line, one question I would have about the staff's projection is that the assumption about money growth clearly, I think, is under what we're likely to have, at least what we seem to be having now. And I presume that would be a factor on the other side--when we make revisions on the basis of current events, you would make some further revisions, I presume, for a faster rate of money growth.

MR. KICHLINE. Well, the way we go about this is to tie it to the Bluebook path B, and we have incorporated from quarter two [1977] to quarter two '78, 5-1/4 percent [growth in] M1. So implicit in the forecast this time is, I think--Steve, is it something like 4 percent in the next three quarters?

MR. AXILROD. Yes.

MR. KICHLINE. So what we have as the offset to that, of course, is higher interest rates. So we have higher interest rates this time than last time, and it comes out that way. So we tie it really to the longer-run target and do not allow for a judgmental feel as to what may happen on the high side of the range or the low side.

MR. EASTBURN. I see.

CHAIRMAN BURNS. Well, thank you, Mr. Eastburn. Anyone else like to speak or speak once again? Well, if not, just to break the monotony, I'd like to say a few words. There's little doubt in my own mind that the expansion that we've been experiencing will continue for some time. I share Mr. Volcker's doubts as to whether the slowdown that is likely to occur in the second half of this year will or will not be followed by a re-acceleration of the economy. I think it would be premature to express a judgment on that with any confidence.

I think that this economic expansion has been well balanced from the viewpoint of inventory control; inventory adjustments have been prompt. We've been going through such an adjustment now in the nondurable goods area. I do see some signs of potential trouble ahead. This year, unit costs of production have crept up on selling prices, and profit margins have narrowed. And if that trend were to continue, while the expansion that we are having would still have some life in it, the forces would be building up that would bring the expansion to a close. And that is something that we ought to be watching with very great care. We don't pay nearly enough attention here within the Board and possibly within the Banks to the behavior of profits. And historically, when unit costs of production begin creeping up on selling prices, within a year or two a downturn has occurred. And therefore, the distribution of income, something we don't like to talk about, is a matter to watch closely.

Secondly, here I have a quarrel with our staff, and it's a long-standing quarrel that I must try to resolve. I can't agree with Mr. Kichline's judgment that the debt capacity of consumers remains favorable. I don't think that is true. That's not the evidence as I read it, but I have to sit down with Mr. Kichline and members of his staff and go through the evidence. I hope to convince them that they are wrong, but they're not easily convinced, nor should they be. I think that there are some signs of speculation in real estate, farm real estate, and in home buying generated by an effort of individuals to somehow protect themselves against inflation in the future. I think if this continues, it may become very troublesome. On the other hand, I do see business capital investment expanding, and early investment indicators, I think, point rather unanimously to a continuation of an upward trend--and I think a strengthening in the upward trend--of business capital investment. And therefore, I have considerable confidence that the expansion will continue for some time.

But I'm not ready to speak about any long run, and I would very much hesitate to make a projection through the year 1978. Our staff estimates it because we require it. I don't have to make it, and I'm not going to, and I'm not going to because my vision is much too cloudy. And that is a counsel that I would urge on my colleagues. Now I do attach significance to the behavior of the stock market. It's been in the doldrums much too long. And I think the behavior of profits is one factor in the indifferent or declining behavior of the stock market. I think that there is at least, as I sense it, very great uncertainty about economic policy in the business and financial community. Now that has not been commented on at this table to any extent, and I may be getting an eccentric sampling of opinion. But that is what I hear from businessmen and financial executives repeatedly, and I must say in all honesty I share that opinion. Well, that's all that I can contribute at this point. Mr. Winn.

MR. WINN. A question and a comment, Mr. Chairman. We're finishing the third year of an automobile boom which has characteristically run in the threes. Now I don't know whether the change in the financing and the possibility that next year is the last year of the large car may help sustain that to a fourth year. But if you go back in history, at the end of the three years of successive increase--I don't know, Bob, whether you have any feeling on the automobile market, but their inventories are in pretty good shape.

MR. MAYO. Yes, they are. Down to 60 days.

MR. WINN. Yes.

MR. PARTEE. Was '75 an up year?

MR. WINN. Yep. [unintelligible] term '75 to '77 is the end of the three-year cycle.

A comment on the [stock] market, Mr. Chairman. You've had the first boom in the early '70s; it was an individual boom. The second one was an institutional market. I have a feeling that now you've got an insider market--that explains part of this sloppiness and a very great--

CHAIRMAN BURNS. What does that mean, precisely?

MR. WINN. My guess is that a very much larger proportion of trading is done by people that used to be on the floor and have gone upstairs and are trading among themselves. The market itself is in very much disarray [as an] organization and you've got strange--I don't know all the answers to this, and the market is concerned about it, but they're not willing to spend the money to find out. A large part of the margin credit, I suspect, is insiders tied into the option setup, and that's a more explosive thing than I think any of us realize, what's involved in this leveraging. But a greater proportion of the trading is done by what I would call the professional trader rather than the individual or the institution.

MR. MAYO. Well, statistical studies to date apparently do not support the position that the options market on calls has done anything to depress the general market. My elbow is still uneasy about this. There is a counterculture, if you want to distinguish it that formally, developing now with the evolution of puts, that will counterbalance the calls, and the market will be better again. But this is getting into real mystique. I don't think anyone really knows what he's talking about. And the effect of the options market, either puts or calls, it's very minor, except psychologically, and I would support what Willis said on the insider facet of the market.

I think you are correct, Mr. Chairman, in your evaluation of the almost smothering uncertainty among businessmen or among investors, many of whom, of course, are businessmen. We also know that that is a characteristic of the [stock] market, that it goes in sheep-like fashion. I think I would give quite a bit of support to Chuck's point, though, on the further uncertainty on the capital gains side, even though much of the market is institutional, where capital gains are only a secondary factor.

As long as I have the floor, one other observation on the real estate speculation. We see definite signs, Mr. Chairman, as far as farm real estate's concerned, that the wild, and I use the word advisedly, wild increases in farm real estate prices that have taken place in the last two years are leveling off. They're still increasing, but the low prices for corn and beans are catching up with us.

CHAIRMAN BURNS. Thank you. Mr. Jackson, please.

MR. JACKSON. I don't know that I'd share that judgment about the threat of the capital gains tax. It appears that the stock market has had a type of segregated action: The so-called high-growth, high-multiple corporation has had an agonizing readjustment in future expectations of their growth, or the profits that might be achieved in the market as a result of their growth, and they have come down in price; on the [other hand], many of the other small corporations that have not had as much influence on the S&P 500 and the Dow Jones have had pretty good experience.

If I had to guess, I would guess that your major institutional buyers, bank trust departments, pension funds, and things of that sort have been a major factor in the reduction of the share price of these major growth companies, whereas individuals have been more inclined to go with the smaller companies. Individuals, in turn, have probably had a net increase in values, which wouldn't sustain the belief that there was any likelihood that there would be a depressed [market] as a result of the loss of capital gains.

I would guess that some of this has got to be the continued shift of expectations by professional managers of major portfolios, and their expectation for profit through the stock market, and their shift to fixed-income securities--which I think would be supported by the stable long-term interest rates we've been seeing and continue to expect--and the high cash flow the life insurance companies and the pension funds have experienced and their predilection to stay in fixed-income securities to a large extent.

MR. PARTEE. Well, there are a lot of things going on in the market, of course, Phil. I was just referring to a new incremental factor. Now there [are] certainly many individuals that have got sizable profits in stocks like IBM, Xerox, and, you know, the high flyers of yesteryear, even though they're down from their peaks. I wouldn't think that the gains would be nearly as sharp in small companies because they've had an indifferent performance for quite a few years. But at the same time, I agree with you that the professional, the institutional investor, is tending to grow more into fixed[-income] securities so that there isn't anybody there really to buy up the individual sales in the growth stocks except the companies themselves, which may buy their [own] stocks because of the fact, as Ernie said, it's the best place they can put their money.

MR. MAYO. The current fad of indexing hasn't been mentioned here, which I think supports the same analysis that's been given, as an additional factor, with people saying, I give up, I cannot--no investment manager can give me a consistent record of beating the S&P 500. Let me get an index fund that will buy the S&P 500. And they rush out of the big ones into the little ones in order to balance their portfolio, in quotes. Now this is an important marginal factor.

MR. MORRIS. I agree with you on that, Bob, and I think there's a lot of what they call closet indexing going on. The managers not admitting that they're indexing, but they're acting as if they were indexing, out of the same sort of desperation that made this fad go as far as it has. The actual number of overt index funds is still very small. But closet indexing is very big.

MR. BAUGHMAN. Why should indexing have a negative effect on the overall level of stock prices? That's what they're saying.

MR. MAYO. Well, I was thinking of the Dow Jones [industrial average] in particular. The general market has performed better in the last year than the Dow Jones has. And our thrift plan has performed better than the Dow Jones has.

MR. MORRIS. The depressing prices of the growth stocks have overweighed in most professional portfolios, so, in order to get closer to the index, they are selling growth stocks and buying others.

MR. BAUGHMAN. If I was to take $10 out of one and put it into something else, why should that change the level of the market?

MR. MORRIS. Because the major indexes are weighted very heavily by the growth stock, much more so than the general market. The general market has done better than the growth stocks.

MR. GARDNER. Gentlemen, I want to ask a question of staff and make one point. Last year, we were in the midst [of the] bicentennial and a presidential election, and the country's bicentennial [celebrations were] dispersed. I don't know how much travel occurred. Resort travel, vacation business is a very large industry in this country, and I want to ask the staff, since I don't worship at the idol of seasonal adjustment, I continue to be impressed with where we are in the calendar and I just want to ask the staff what indications they've had of Americans traveling, going to resorts, vacationing.

We're concerned a little bit about the diminution in retail sales. This is a very normal year in my opinion; there's nothing terribly exciting going on. The economic factors, while they're not what we would like--let's look at the average man and what his plans are for his summertime. Jim, have we had any look at how much Americans are traveling or are away from home on vacation, spending money in resort places, rather than in their normal residences?

CHAIRMAN BURNS. Any advice you may be able to give us on that point--

MR. KICHLINE. Well, I just went to the local beach, so it's not a good guide. And you're just back from vacation, so I presume it's sort of hazardous for me to venture out with an answer.

MR. GARDNER. Well, having followed long lines of campers and recreational vehicles, and having been totally astounded by the traffic in rural Maine seaports, yes.

MR. KICHLINE. We have [some] selected data on hotel occupancy and figures from the airline industry, but unfortunately I am just not familiar with those currently, and Jerry, too, is not up to date. So I'm afraid we can't provide a reasonable answer to question at this time. But we can prepare a memo for you on that.

MR. MORRIS. We find New England resorts have been doing very well.

MR. BALLES. I think the Redbook comments would support that for our area.

VICE CHAIRMAN VOLCKER. I understand from one of my directors, a chairman of an oil company, gasoline consumption is actually down this summer.

SPEAKER(?). [Unintelligible].

VICE CHAIRMAN VOLCKER. Year-to-year decline.

MR. GARDNER. Not what [President] Carter says. The Administration is very concerned, of course, that Americans have not stopped driving and have--

VICE CHAIRMAN VOLCKER. But there's some other indications of this, too, that travel is down this summer from last summer. One of our directors is an airline director and travels--

MR. ROOS. Mr. Chairman, we have a director who is a high executive in Holiday Inn, and this came up at our meeting last week, and I regret that I don't recall the precise statistic, but the hotel and motel and travel industry has had--last year was up considerably in terms of volume from previous years--this man's a walking encyclopedia, and he can give us enough--but they have had a strong year in the industry basically.

MR. MAYO. Very strong in central Michigan, northern Michigan.

MR. GARDNER. Well, thank you. This may not be worth a memorandum, Jim.

The point I wanted to make is that, in my career in lending, banking, it seemed to me that there are two sides to this question of profit. [Unintelligible], one significant way to increase profits of course, is to make capital investment. And we know that capital investment has lagged, has been a disappointment to us. Prices can be raised, sure, if profits are inadequate, but most of my manufacturing customers were continually on a process of applying capital to the business of reducing their cost. And so, if we find American industry less likely or disposed to make major capital investment for all the good reasons and uncertainties that we're aware of, we're not getting the benefit from the profit side that one might expect and have to rely too much on pressure on prices.

MR. JACKSON. May I ask to what extent our industrial capacity in this country presently differs from the industrial capacity of other major industrial countries throughout the world? It is the question of, we're closer to the top than they are, and therefore future demands worldwide might be supplied [unintelligible]?

MR. KICHLINE. I have the impression that in a number of the major countries, capacity utilization rates are somewhat below those of the U.S., and world supplies in many of the basic commodities are in quite a strong position, but I'd like to defer to Ted Truman.

MR. TRUMAN. Well, I don't have the information with me.

MR. JACKSON. Just in general, your impression.

MR. TRUMAN. Well, my general impression--

CHAIRMAN BURNS. Does an answer exist to the question?

MR. TRUMAN. The Wharton School puts out global capacity utilization indices--

CHAIRMAN BURNS. Oh my heavens--

MR. TRUMAN. --but the last figures that I saw were only through the last quarter of last year. At that time, if my memory is correct, capacity utilization figures in this country were somewhat higher than abroad, but [the figures are] not up to date. The only other figures you can use [are] figures on how we perform relative to previous peaks in the other major industrial countries. In that case again--in which we need more updated information--we have gone further compared to relative previous peaks in industrial production than the other industrial countries.

In fact, only one other has reached the previous peak, and on that crude measure, it's fair, I think, to generalize.

CHAIRMAN BURNS. I don't think we can even answer that question reliably for the United States. And the Wharton index is worthless for the purpose of answering either for the United States or foreign countries. And we just have to make up our minds. There's a great deal that we would like to know and that, in view of our responsibilities, we probably ought to know, but we simply don't know. And we travel in darkness much of the time, and that's the way the world has been, and it will remain that way for some time. And this is a statistical no man's land, really.

MR. JACKSON. It strikes me as that is the essential question to Governor Wallich's potential hypothesis, as to what extent will pressures from capacity utilization in this country and capital expansion be ameliorated by the capacity of other industrial nations if they increased their [exports] to the U.S., which would not enable prices in the U.S. to rise to respond to the need you describe.

MR. WALLICH. Of course, other countries [are] probably further away from capacity pressures than we are here. As far as our own situation is concerned, if we were to go, just in a model sense, to full employment overnight, we would not have the capacity to employ the labor force. I think that's quite clear. The Council of Economic Advisers is doing a study now--sounds somewhat ominous to me--they want to compute the optimum path by which you might move quickly to high-capacity utilization and then slow down so as to move at that continued level of capacity utilization as more capacity comes on stream. That means accelerate fast now and then taper off, a proposal that one would--you or I---view with considerable alarm.

Well, tying this to the [foreign] situation, I think if anything, the international situation has weakened. The Germans are now ready to accept 4 percent GNP growth as about the most they're going to do instead of the 5 they have been talking about, and that they [unintelligible]. The Japanese seem to be of a mind to do somewhat more. But overall, the sense of a settling down that I get from our discussion here is not going to fit very happily into the international situation.

MR. COLDWELL. I had an industrialist spring a new idea on me, at least new to me, in terms of why he wasn't building a plant. He said, "I don't need to build a plant because if my demand overruns me, I've got several plants abroad that are at a much lower capacity utilization, and I could import to the United States if I run into capacity problems."

CHAIRMAN BURNS. It's interesting.

MR. LILLY. You have a good proxy for this capacity abroad, in the sense, when you look at all the people that are asking for import quotas, you get a pretty good sense as to who is faced with a [capacity] overhang abroad, to wit, the steel industry being number one, and the TV people being number two.

CHAIRMAN BURNS. Well, gentlemen, unless there is a desire to continue the economic discussion--you know, our staff has to write a report, and I think, let's have a show of hands, simply to help the staff write its report. It's a function that we, I think, should keep in mind. The staff might have difficulty, on the basis of the discussion so far, in writing a report that would be sufficiently illuminating. Let's have a show of hands of members of the Committee who expect the expansion to continue through 1977.

MR. PARTEE. Expansion to continue.

SPEAKER(?). At what rate.

MR. PARTEE. At any rate.

CHAIRMAN BURNS. At any rate--okay, let's have a show of hands of those who expect the expansion in the second half of this year to be significantly lower than in the first half of the year.

MR. LILLY. Now what are our alternatives going to be?

MR. COLDWELL. [Unintelligible].

MR. LILLY. Lower.

CHAIRMAN BURNS. Significantly lower.

MR. MAYO. 2 percent.

MR. COLDWELL. Less than the staff forecast?

MR. PARTEE. Significantly lower.

MR. JACKSON. Significantly lower.

MR. ALTMANN. Eleven, Mr. Chairman.

CHAIRMAN BURNS. Well, now--

MR. ALTMANN. That's counting all--

CHAIRMAN BURNS. You're not going to put these numbers in the report--

MR. ALTMANN. No.

CHAIRMAN BURNS. After all, adjectives serve a function. Now, let's have a show of hands of all those who are reasonably confident that the expansion will continue through 1978.

VICE CHAIRMAN VOLCKER. What's the definition of reasonably?

MR. GARDNER. I'm listening to the adjectives.

MR. LILLY. I'd like to see all the questions.

CHAIRMAN BURNS. Okay, let's have a show of hands of all those who expect business capital investment to rise at a faster rate than it has hitherto during the next 12 months or so.

MR. PARTEE. Faster rate.

VICE CHAIRMAN VOLCKER. There's a pretty fast rate in the first quarter--

CHAIRMAN BURNS. At a faster rate than the past--

MR. PARTEE. Over the past year.

VICE CHAIRMAN VOLCKER. Over the past year.

MR. LILLY. I expect it to continue.

MR. ALTMANN. All but one.

CHAIRMAN BURNS. Well--

MR. WALLICH. Mr. Chairman, I think your questions have produced a set of answers that may not be fully reflective of what's been going on here as conversation.

CHAIRMAN BURNS. You see, I wanted to supplement what has gone on in conversation, and I could just see the reports each month--which I read word-for-word, more than once--and I could see the initial report before you see it. And in the absence of the questions that I've just put to the Committee, I think we would convey to the general public a very distorted picture of the underlying thinking of members of this Committee. Don't fear that there'll be a lack of balance; and if there should be, after all of the purifying and sanitizing that goes on, you'll have an ample opportunity to set Mr. Altmann and his staff straight. Any further protest on my procedure? Let's move on to Mr. Sternlight's report on domestic open market operations.

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

MR. COLDWELL. Has the market moved to an expectation of a discount rate change?

MR. STERNLIGHT. There's been a good deal of talk of the discount rate change and a fairly widespread expectation of a move of at least 1/4 [point], with some people beginning to talk of a change of as much as 1/2.

MR. PARTEE. Would you say that the market is adjusted to a 6 percent funds rate, or is that process still going on?

MR. STERNLIGHT. I find it a little bit hard to answer. The market has moved less than I would ordinarily expect it [if it were] to accompany the move up to a 6 percent funds rate. In that sense I wondered, as this process has gone on, whether that adjustment has fully taken place, and yet when I couple this with the fact that the dealers remain in a net short position and have even deepened their short position, I come to conclude that perhaps the adjustment has pretty well occurred even to a 6 percent funds rate.

MR. PARTEE. Once they think the move is complete, why, they would tend to restore [unintelligible]--or at least cover their position.

MR. STERNLIGHT. I think they'd tend to move toward covering some of that short position.

MR. PARTEE. What was the bill rate yesterday in the auction?

MR. STERNLIGHT. 5.67.

MR. PARTEE. 5.67.

MR. COLDWELL. What's the 90-day futures market for bills looking like?

MR. STERNLIGHT. I don't have a figure in my head on that, but it's tended to pretty well just be a measure of the difference between the three- and six-months bills.

MR. BALLES. Out to June '78, I think it's almost 7 percent now.

MR. AXILROD. If you go out for this three-month bill on the second quarter, it's on average about 6.8 percent; I was averaging. And in the third quarter '78, its 7.1 percent, which is about the 7 Mr. Balles has mentioned.

MR. COLDWELL. Given the dealers' net short positions, do you find any congestion in the market?

MR. STERNLIGHT. Any congestion in the--

MR. COLDWELL. In the bond sales?

MR. STERNLIGHT. No, the Treasury's sales went very well, and dealers took down about the normal proportion they would usually take down--roughly half, a little less than half in this case, and they rather quickly sold out of that.

MR. COLDWELL. What about corporates?

MR. STERNLIGHT. Corporate bonds--the calendar's been moderate, and the issues have gone fairly well, with little evidence of congestion.

CHAIRMAN BURNS. Didn't the federal funds rate go above 6 yesterday?

MR. STERNLIGHT. The effective rate on the day was just about 6--6.01. Some of the trading was above 6, and late in the day the trading was largely at 6-1/8.

CHAIRMAN BURNS. All right, any other question or comment? Yes, Mr. Winn.

MR. WINN. Peter, do we have any feeling as to what the foreign sellers were doing with the proceeds of sales of bills?

MR. STERNLIGHT. Well, yesterday we had some very heavy foreign account selling of bills. Much of that was in order to purchase coupon issues. Yesterday was the delivery date for the Treasury's new issues. There had been some sizable foreign-account takedowns of these new issues, and that was a big chunk of the foreign sales.

CHAIRMAN BURNS. Mr. Eastburn.

MR. EASTBURN. Governor Coldwell asked my question, but just to make sure I understand it--Peter, is it fair to say that there would not be much adjustment in the market if the discount rate went up 1/2 percentage point?

MR. STERNLIGHT. I would think that the market has fully discounted 1/4 percentage point. I don't think they have fully discounted 1/2 percentage point. I think there would be some adjustment.

MR. EASTBURN. Some adjustment, but not a great deal.

CHAIRMAN BURNS. Any other questions?

MR. COLDWELL. I move we ratify the suggested action.

MR. MAYO. Second the motion.

CHAIRMAN BURNS. Well, the motion has been made to ratify the actions of the Desk, and I take it there's no objection. We might as well break for coffee now.

[Coffee break]

CHAIRMAN BURNS. Well, let's move on to your comments, Mr. Axilrod.

MR. AXILROD. [Secretary's note: This statement was not found in Committee records.]

CHAIRMAN BURNS. A rather incisive set of comments. Any questions? Yes, Mr. Coldwell.

MR. COLDWELL. Mr. Axilrod, did I hear you say that the model had stopped overpredicting for the third quarter?

MR. AXILROD. Yes, in the third quarter. That's on the assumption that the rate of growth in M1 in the third quarter is about 8-1/2 percent.

MR. PARTEE. That's the first quarter, but it has no reflection--

MR. AXILROD. Well, in the second quarter it's very small. It sort of phases down. In fact, I had written out during the second and third quarters because it was very small in the second quarter, but I wanted to be absolutely precise and write in the third quarter. But it's sort of phasing down [unintelligible].

MR. COLDWELL. My question was, how will you know? The third quarter isn't over yet. Well, even if there is no growth, it's going to be very difficult to avoid a very large growth rate in the third quarter. But essentially the second quarter has a very small overprediction, 3/10 percent on the level.

MR. WALLICH. Does this overpredict on what basis?

MR. AXILROD. Given the GNP and the actual interest rates.

MR. WALLICH. Does that involve a shortfall for some previous period, and--

MR. AXILROD. Oh yes, there has been a consistent shortfall. The percentage error--by the fourth quarter of '76, it was almost 12 percent off, that is, it had overpredicted--its predicted M1 is 12 percent higher than we actually attained. And by the first quarter, it was up to 13.3, and then by the second quarter it phased down to 13.6, and by the third quarter, it seems roughly to be the same, 13.6.

MR. WALLICH. In other words, it stabilized, but has not made up--

MR. AXILROD. Oh, no, no, nowhere near, and we're assuming--actually, in all projections we present to the Committee--we are assuming further shortfalls. We are nowhere near staying with this model. We assume further shortfalls.

MR. MAYO. When you say prediction of M1 by the model, this is over what period? How do you define the word prediction?

MR. AXILROD. Well, this quarter--

MR. MAYO. Where we are, or over what period?

MR. AXILROD. Well, this shortfall I'm measuring is from around the third quarter of '74, where we started--

MR. MAYO. I see.

MR. AXILROD. --going off. It's been rather consistently going off since then.

MR. ROOS. Mr. Chairman, may I ask a question? Don't we have the ability to control the growth of M1, especially if we are willing to let fed funds rates and interest rates rise? Do we predict these things, or do we control them?

MR. AXILROD. Well, I think, President Roos, that the Committee could, if it wished, control within plus or minus 1 percentage point, or 1-1/2, something like that, over a year or so, the rate of growth in M1 if it were willing to see whatever interest rate behavior developed, to see whatever M2 and M3 behavior developed as a result, and to take whatever economic consequences were in process. In that sense, it's controllable.

MR. COLDWELL. Does your model tell you what would have happened, for instance, to the funds rate had you tried to hold M1 on target?

MR. AXILROD. In this period, oh sure. Yes, you would have to work backward, but it's essentially the bill rate that's in the equation. But the model is still saying that, for the money supply growth, it's the Committee's target. You would have a substantially higher Treasury bill rate than you see in the Bluebook. That is the data that we are presenting to the Committee, assuming shortfalls in terms of the model.

MR. COLDWELL. May I ask one other question, Steve? You made a comment here about the implicit velocity of M1 in the fourth quarter of the year, that it would have to be [growing] 4 to 8 percent--

MR. AXILROD. 6 to 8.

MR. COLDWELL. --6 to 8 percent, and that is grounded on an assumption of what?

MR. AXILROD. That assumes that if the Committee would obtain a 4 percent rate of growth in M1 in the fourth, first and second quarters, which would be consistent with obtaining the midpoint of that 4 to 6-1/2 percent, then on average the velocity would be about 7 percent, given the staff's GNP forecast for that period.

MR. COLDWELL. The assumption also includes the GNP forecast.

MR. AXILROD. Yes indeed. And if that, of course, is lower, then you would have much less demand for money and much less pressure on interest rates.

VICE CHAIRMAN VOLCKER. It's true that would have followed a low-velocity quarter, the current quarter.

MR. AXILROD. Yes, that's right. When interest rates were up.

VICE CHAIRMAN VOLCKER. And the average for the year would be lessened.

CHAIRMAN BURNS. Any other questions? Yes, Mr. Wallich.

MR. WALLICH. What are the prospects for significant disintermediation for the thrifts and for bank time and savings deposits.

MR. AXILROD. Well, we've been surprised two ways by the behavior of thrift flows. We were surprised that they were relatively low in April and May. We were surprised that they were relatively high in June and July. Now our data for August is suggesting, at least for banks, another slowdown in flows. You may want to keep that background in mind when I give you our appraisal: We would expect a slowdown to around a 7 percent rate of growth in flows of thrift institutions in the first half of 1978, and to about a percentage point or so more than that at commercial banks in time deposits other than large CDs, without any action on Regulation Q ceilings and with a bill rate, say, on the order of 7 percent or perhaps a little higher. This would rather clearly, I think, begin to exert pressure on the mortgage market and on loan terms and conditions at banks.

As I mentioned, this doesn't assume any change in Regulation Q. As of now, there is no leeway left for banks to adjust the ceiling rates and maintain a spread over market rates in savings deposits or in shorter-term time deposits. There is a little leeway left for thrifts, and in the four-year-and-over maturity area, there's leeway for both banks and thrift institutions. So I think it's within a percentage point or so, in terms of bill rates, of real pressure on institutions.

MR. PARTEE. This 7 percent inflow to the thrifts--compared to what? It's been coming in around 12.

MR. AXILROD. In the second quarter, it was running around 11, and recently it picked up, and so we are projecting a third quarter--with some little slowdown from the recent pickup--on the order of 13 percent. This would be a sharp drop. It would be a material reduction from where you are now because of this bill rate moving up. That's our assumption.

MR. JACKSON. As I recall, in the fourth quarter of '76 it was up in the 18 range.

MR. AXILROD. It was very high.

CHAIRMAN BURNS. Mr. Guffey, please.

MR. GUFFEY. Yes, Mr. Chairman. Steve, do you have any information of what's happening to these wild-card renewals, and are they in your projections for the rest of 1977?

MR. AXILROD. Well, we've taken account of them. We don't have any information that there are substantial difficulties, and of course they are in the over-four-year area, where we still have rather considerable room, and we don't expect those [to make] for much of a problem.

MR. COLDWELL. Mr. Chairman, a question. Maybe it's better directed to Peter. Where is the commercial paper rate after this series of moves to 6 percent?

MR. STERNLIGHT. Well, that has moved up not quite as much as federal funds. I think they're in about the 5-5/8, 3/4 area now. It perhaps hasn't made a full adjustment to the 6 percent federal funds rate.

MR. COLDWELL. If there were no change in formula, would this make the change in Citibank prime?

MR. STERNLIGHT. I think it would, within about another two weeks.

VICE CHAIRMAN VOLCKER. Wait a minute. In three weeks.

MR. STERNLIGHT. Three weeks.

VICE CHAIRMAN VOLCKER. It's got to run through the full moving average.

MR. STERNLIGHT. Because of a three-week moving average.

MR. BAUGHMAN. Mr. Chairman, [this is a] rather detailed [point], I guess--I noticed in the recent report of weekly reporting banks that deposits of foreign banks in U.S. banks are up about $1.6 billion, $1.7 billion from a year ago. Now, is it correct that those deposits run into the money stock numbers?

MR. AXILROD. That's correct.

MR. BAUGHMAN. And is there any basis for expecting that kind of growth in that type of deposit to continue, or that what we have seen in the past year is a temporary phenomenon?

MR. AXILROD. Well, there was an increase in two weeks in July, and we believe that will be coming out. That was a temporary increase and not one we expect to continue. In fact, we expect it to be coming out, and the fragmentary data we have, I am told, suggest that it is coming out, and I am not exactly sure of my number, but I think that increase, if you have taken that out of M1 for July, would have reduced that growth rate on the order of 2 to 3 percentage points. We had for years kept track, [in] the series that we put in the Bluebook for M1, "less foreign deposits" in our money stock, and it showed every once in a while [that] it would affect the monthly growth rate a little bit, but it didn't prove significantly different to keep track of it continuously.

MR. COLDWELL. Is there any likelihood that that would be affected by a change in relative interest rates?

MR. AXILROD. We were not able to come up with any explanation that was satisfactory of why those foreign deposits went up in that middle week of July and stayed up in the next week.

MR. COLDWELL. At least I'm not aware of a satisfactory explanation.

CHAIRMAN BURNS. Yes, Mr. Mayo.

MR. MAYO. Mr. Chairman, I am bothered here about something else in terms of our yardsticks. We have again an illustration in July of a huge increase, way beyond what we expected. Some people may say, well there's the Fed with its seasonal adjustment factors again, and yet it's pretty obvious, in answer to that, that, well, forget seasonal adjustment, we are up 7 percent in M1 from a year ago, that washes out the seasonal adjustment factor. Which brings me back to a concern that we are dealing here in a real world where interest rates are not seasonally adjusted, thank heaven, where we are talking about flow of funds in the market that isn't seasonally adjusted. We appraised the stock market without any attempt, again thank heaven, to put in a seasonal adjustment. I'm just wondering if, in sorting out some of our own analysis, we are failing to be able to appraise except on a year-to-year basis. The difference between the unadjusted figures and this margin, which you have mentioned so many times, Mr. Chairman, of the fragility of our seasonal adjustment factors. I guess what I am saying is maybe too philosophical to be considered seriously at this meeting but--

CHAIRMAN BURNS. Don't underestimate us.

MR. MAYO. Well, what I am saying is, I am trying to maybe even take refuge in looking more at unadjusted numbers than we had before, and not that I lack any confidence in staff to do the best job they can in seasonal adjustment, but it may be that we are dealing in an area were the unadjusted numbers over a period time can be analyzed quite constructively along with the others. Now, I hesitate to say this because we've got too many numbers already. But maybe we need a substitution of numbers, not an addition of numbers. End of speech.

CHAIRMAN BURNS. You are indeed suggesting a revolution. I don't think we want a substitution, but I do think we want and need at least a partial addition. I find it very disconcerting--when, at times, I ask one or another member of our economic staff [about] the recent behavior of unadjusted figures, that seems to shock the individual to whom I put the question. He no longer knows the world of unadjusted figures. He knows the world in terms of seasonally adjusted figures. I think we have all gotten into the habit of living with seasonally adjusted figures, and we are overdoing it. I would like to see, well, at least now or then, unadjusted figures and try to arrive at some rough judgment as to the quality of the seasonal correction, its stability, its degree of fragility. I have a great deal of sympathy for your suggestion except for the--I don't know whether you meant it seriously--the substitute.

MR. MAYO. No, I mean let's get rid of some other numbers--it sounds like a budget director--let's get rid of some other numbers that maybe aren't as valuable. I don't mean a literal substitution of unadjusted for adjusted. That would be a mistake. We are entitled to our best evaluation of the seasonal.

But if I may take one more minute of the Committee's time. Thirty years ago I was in charge of doing the revenue estimating base in the Treasury. We had to get our base figures from Commerce. Obviously you do your revenue estimates not as seasonally adjusted figures; you do them unadjusted. The Department of Commerce was able to give us unadjusted figures on everything except farm and nonfarm entrepreneurial income, where they had to go to great lengths to create unadjusted figures for us to use in the Treasury. The absurdity of that has stayed with me to this day and, I guess, colors what I have to say. End of second speech.

MR. AXILROD. President Mayo, I think there might be a misunderstanding of how we make the projections. The projections for the period between Committee meetings--well, we have a variety of projections, and models, and what have you. But the basic judgmental projection--sometimes that's adjusted on the basis of the model results--but the basic judgmental projection is made from unadjusted weekly data.

MR. MAYO. Oh, I understand that, Steve.

MR. AXILROD. And, in judging whether the data coming in are above or below paths that seem consistent with what the Committee finally adopts for an intermeeting period, that judgment is based on the unadjusted data that's coming in. And the seasonal factor is a constant, and that's just the transformation that transforms it into a level that is more consistent with past behavior and is more familiar to the Committee and to the public. But, essentially, tracking of the path and our development of what we propose to the Committee are based on an evaluation of expectations with regard to unadjusted data in the period.

MR. MAYO. Well, I understand that, and I guess I'm just asking for a further sharing of that base so that the Committee judgment as well as staff judgment has a greater input on the unadjusted figure.

MR. BALLES. Mr. Chairman, if I could piggyback on Bob's comments here. I think he has a very useful idea, as a matter of fact. He has referred to some of his experiences as budget director. I recall a time when I was responsible for establishing and maintaining a tracking and monitoring system for all kinds of loan and deposit components of a major commercial bank. And one way that the top management insisted that this be done is that--all these charts where we had the seasonally adjusted data, we have right smack on that same chart the actuals. It was of no consolation to know that deposits were rising at a seasonally adjusted basis but actually going down--that was an actual decline in funds irrespective of what the seasonal trend showed, and it meant a real need to raise money. That's a key discipline--to match, just for example, Bob, on the same chart, your unadjusted and seasonally adjusted figures. It gives it a hard-base reality, and that's one technique that we might use.

CHAIRMAN BURNS. Well, I think Mr. Mayo's comment on seasonal adjustments is very useful, and at the risk of complicating life, let me point out another, perhaps even more serious, difficulty. And this time I will be using seasonally adjusted figures, and this difficulty will extend equally well, I'm sure, to figures that have not been adjusted for seasonal variations.

I've had the staff recompute M1, that is, make computations on the rate of growth of M1 using a modified, and yet I think reasonable, definition of M1. And the modification of our standard definition was as follows. First, we included the NOW account. Second, we included the demand deposits of mutual savings banks. Third, we excluded demand deposits due to foreign commercial banks and foreign official institutions. Fourth, we included business savings deposits. And fifth, we've included governmental savings deposits.

Now, in my judgment, M1 redefined in this fashion is a better measure of transactions balances than the one that we have been relying on thus far. But whether or not you accept that judgment, I think it is somewhat startling to compare the figures given by the M1 that we rely upon and the redefined M1 which I have just described. For example, in the first quarter of 1976, our standard M1 rate of growth was 2.9 percent--Steve, is this based on quarterly averages or end-of-quarter figures?

MR. AXILROD. Yes, its quarterly average, I believe.

MR. PARTEE. '76 or '77?

CHAIRMAN BURNS. No, '76--2.9, and the redefined M1 is 9.2. You are living in a different world. Now let me take the first quarter of 1977. The current M1 is 4.2, and the redefined M1 is 8.9. Again, a very different world. Now, for the second quarter this year, the difference is very much smaller: 8.4 for the current M1, and 8.7 for the redefined M1. But very large differences appear in other quarters, and the differences for individual months are really enormous.

Now this is not too surprising. I had the calculation made because I was quite sure the differences would be large. What it does mean is that the knowledge we at times assume we have concerning the growth of the money supply, or the relation between the money supply and economic activity, or the relation between the growth of the money supply and the inflation rate is very precarious, very fragile. And I'm not quite sure what the implication of all this is. One implication may be that we ought not to be apologetic about paying a little more attention to interest rates than we do. That is not a necessary inference from anything that I have said; it's one possible implication.

MR. WALLICH. Excuse me, Mr. Chairman, do we have data on what happens to the calculation of velocity using the money stock as you redefined it here?

CHAIRMAN BURNS. Well, I don't have these calculations, but the velocity figures would be cut back very sharply.

MR. WALLICH. So that the miracle of the inconsistencies in that area might be reduced by this redefinition.

CHAIRMAN BURNS. Oh, no question about it.

MR. PARTEE. But it's mainly just a question of adding in some of the items into which substitution has occurred.

CHAIRMAN BURNS. That's exactly--

MR. PARTEE. You're taking 100 percent of that. People wouldn't have thought you ought to take 100 percent because there were probably also some diversions in the market into those points?

CHAIRMAN BURNS. Well, whatever you do in this area I think will have an arbitrary element. Take demand deposits. Demand deposits can be active or stagnant, and sometimes they'll be the one, sometimes the other. And these are difficulties that are inherent in the kind of complex monetary system that we have and human behavior being what it is.

Well, Mr. Mayo's comments and perhaps also the comments that I've just made ought to make us feel very humble as we go about our task.

MR. PARTEE. Might I ask, Mr. Chairman, what did M1 do on an unadjusted basis in July? Do you know, Steve?

MR. AXILROD. I don't have that.

CHAIRMAN BURNS. That was a nasty question.

MR. PARTEE. I thought for sure he would have the figures.

MR. MAYO. I bet it went up a great deal. But the question of--

MR. PARTEE. I think it did, too--

MR. AXILROD. It either went up more than expected or went down less.

MR. MAYO. My comment is not meant that you can explain all of the difference in M1 in that one month. It's probably only a small amount. It's a question of being unable to sort out the apples and oranges. We get a bale of fruit--a box of fruit; here I'm getting all mixed up with my metaphors.

CHAIRMAN BURNS. Well, gentlemen, any other general observations? If not, we'd better turn to our monetary policy discussion, looking toward a new domestic policy directive to the New York Desk. I think that it would be useful if--this remark is addressed totally to the Bank Presidents at the table and their alternates--it would be useful if our Bank Presidents would comment on the desirability as they see it--speaking for themselves rather than for their directors--of an increase in the discount rate. Whether such an increase would be desirable, and if so, would it be desirable immediately or possibly two or three weeks down the road, when certain adjustments in interest rates as yet uncompleted in the marketplace would have taken place. Your views on that subject would be helpful to the [Federal Reserve] Board.

Now, as far as the Bluebook is concerned, I look rather favorably on alternative B in the Bluebook, on page 6, except, you see, the lower limit of M1 is 2. Well, why should it be 2? Why shouldn't it be 0 or even negative 2? And likewise, the lower limit of M2 could be lowered. This may be a time when, in view of what has just happened to M1, we should be willing to lower the lower limit of M1 very substantially. Well, that is one suggestion the members of the Committee may want to consider. Who wants to speak first? Mr. Coldwell.

MR. COLDWELL. Mr. Chairman, you have just destroyed my whole thesis--what I was just planning to spring on you--of lowering the lower end of the M1 and M2 ranges.

CHAIRMAN BURNS. Well, I haven't destroyed it. I haven't destroyed your thesis.

MR. COLDWELL. I approached it a little different.

CHAIRMAN BURNS. I've reinforced your thesis, reading your mind as I am capable of doing--

MR. COLDWELL. Yes, I understand. Well, let me make a couple of comments first. From my perspective, the planning horizon for policy using the aggregates must be down the road apiece, and I look for early '78 as my target area, in that the job of the Committee today and over the next couple of periods is to position itself for what it expects is coming up.

Now, if there is anything to this monetary aggregates target business we are going through, and the long-run target growth, I think we have to keep the growth [with]in those target ranges we have set for ourselves. And thus I would hope we would widen the range on the downside as we did in the longer-run target the Chairman presented to Congress recently, leaving room for restraint if further excessive growth develops but leaving ourselves some room to accommodate this lower range.

I had suggested in my jotted notes here that we might go down to a 1 to 6 frame [for M1] [and] in the 3-1/2 to 8-1/2 range [for M2], but I would be willing to go to zero on the M1. I would not want to see a negative figure. As far as the funds--

CHAIRMAN BURNS. Let me just stop you there to ask a question. I would not want to publish a negative figure. I would welcome a negative figure if it just developed naturally.

MR. COLDWELL. I'm talking about publications.

CHAIRMAN BURNS. Well, that's what I wanted to clarify.

MR. COLDWELL. On the federal funds rate, I am disturbed about this concentration and limitation on the range. And I would hope if we are going to look at these widened ranges of M1 and M2 that we would also widen the range on the federal funds rate, and I would suggest to the Committee a 5-1/2 to 6-1/2 rate, which centers upon where the Desk is supposedly now, at 6 percent.

One other comment, Mr. Chairman, to the general paragraphs of the directive--

CHAIRMAN BURNS. May I just say I don't think that that recommendation is consistent with your recommendation on lowering the limits for M1. The reason for lowering the lower limit [on money] is not to tap lower interest rates very quickly. But if you permit the lower limit [of the federal funds rate] to go down to 5-1/2, you may be forced to do that--

MR. COLDWELL. But only if [M1] goes down below the lower limit, if we put it at 0 or into the negative range, then I would think we would.

CHAIRMAN BURNS. I think you are weakening your recommendation with regard to M1. Now going the other way, widening, I don't see any inconsistency there, but I think I see an inconsistency--

MR. COLDWELL. I don't think it's inconsistent, and perhaps more philosophically I'd rather have the full percentage [point] range.

In the general paragraphs on line number 8, Mr. Chairman--in the past we have published these figures in our policy directive concerning local retail sales.

CHAIRMAN BURNS. Where are you?

MR. COLDWELL. Line item 8 of the general paragraph. I think it would be desirable for us to cover our tracks here to say "total retail sales according to advance estimates grew somewhat."

CHAIRMAN BURNS. Why do you think that is unsatisfactory? The retail sales which rose somewhat are retail sales expressed in nominal dollars, I believe. Is that correct?

MR. PARTEE. Yes.

CHAIRMAN BURNS. Well, then, I'm not ready to say that when you have retail sales in July going up five-tenths, to 1 percent, and therefore [up at a] 6 percent annual rate, I'm not ready to say the total [real] retail sales rose at all.

MR. COLDWELL. Well, it's certainly uncomfortable the way it's stated because of the change that we had this past month in the revision. I looked back at prior figures, or statements and policy records, and we are trapped in this advance-estimate approach.

CHAIRMAN BURNS. Well, I think that this is something our staff ought to watch a little more. Now one of the great difficulties with a period of inflation is that it confuses everyone. Confuses businessmen with regard to their profits, confuses economists with regard to their readings of the economy. It confuses the general public because we keep on shifting back and forth. One minute we are talking about changes in dollar figures and another minute we are talking about changes in physical magnitudes. And we all do that. I know I do, but we ought to mend our ways.

MR. COLDWELL. I would suggest, Mr. Chairman, that we leave it to the staff to amend this.

CHAIRMAN BURNS. Right. I think it's a useful correction.

MR. COLDWELL. May I have one other moment, because while you directed the question to the Presidents, and I will not comment concerning my opinion on the discount rate, I do think it would be of some help to not only consider the discount rate but, in this period of seasonal expansion of required reserves, to consider the possibility of a structural adjustment of reserve requirements.

CHAIRMAN BURNS. Well, I--

MR. COLDWELL. I'm not prepared to make that a recommendation.

MR. PARTEE. Look at it over the next several months.

MR. COLDWELL. Yes, over the next several months.

CHAIRMAN BURNS. I think that members of this Committee should feel prepared at all times to comment on whatever is on their mind. But I do want to point out that we are engaged in a congressional enterprise at present and that sensitive legislation involving reserve requirements is now being considered on Capitol Hill. Therefore, let us keep that dimension in mind as we consider desirable changes in reserve requirements.

MR. COLDWELL. That's all I have.

CHAIRMAN BURNS. Thank you, Mr. Coldwell. Mr. Eastburn now, please.

MR. EASTBURN. Thank you, Mr. Chairman. I begin with a view that the economy is stronger than the sentiment would suggest and also with the uncomfortable feeling that we may someday look back on the current period as being a mistake, so far as monetary policy is concerned. We have a second and third quarter with M1 growing more than 8 percent. If you were to assume a fourth quarter at the same rate, this would create money growth in 1977 that would be the second fastest since 1970.

The question, of course, is what to do. I think two observations that have been recently made are helpful. One is the observation that, although we've been consistently and persistently lowering our targets, that the actual growth rates have actually increased. Second was the observation made last time that it's important to make sure that we do in the short-term what we want to accomplish in the long-term. And it seems to me that this is a good test of that principle.

This leads me to a position that at least the aggregates of alternative C would be desirable. I like very much your proposition of lowering the lower limit [of M1] to 0. I also would lower the upper limit to about 4 to give a range of something like 0 to 4. I am concerned, of course, with what this would mean for the federal funds rate, and I would approach that somewhat cautiously and opt for the ranges that are specified for alternative B, 5-3/4 to 6-1/4, with very close consultation between the Desk and the Committee.

As far as the discount rate is concerned, I think it is time to raise the rate. I'm prepared to recommend to my board of directors an increase of 1/2. I think that, from what Peter said, the market has almost adjusted to that. It hasn't quite adjusted to it. I think maybe the additional amount might have a good announcement effect at this particular time, given the kind of growth rates that we've been having in the money supply.

CHAIRMAN BURNS. Do you have any observation on the timing?

MR. EASTBURN. I would do it right away.

CHAIRMAN BURNS. You would do it immediately.

MR. EASTBURN. Yes.

CHAIRMAN BURNS. Rather than wait a week, or two, or three.

MR. EASTBURN. Yes.

CHAIRMAN BURNS. All right, thank you. Mr. Morris.

MR. MORRIS. Mr. Chairman, I am quite pleased with our performance during the past month. I think that the move we made in the funds rate was needed to maintain our credibility in the marketplace, in light of the big bulge in the aggregates. I think we could take some pleasure from the performance of the bond markets. The reaction in the long-term market has been practically nil, and in fact the long-term rates are just about where they were, when the funds rate was at 4-3/4 in March.

CHAIRMAN BURNS. That's correct. Yes, there was no reaction to the move we made in late April, and there's been virtually no reaction to the move we've made during the past month. Why should we take pleasure in that? I do, myself, but I sometimes get very uncomfortable with myself, because what's the purpose of an increase in interest rates? What is this exercise all about, you see. When we release forces tending to make for an increase in interest rates, why should we take pleasure when these forces do not extend to the long-term market.

MR. MORRIS. Well, because I think that the fact that long-term rates have been stable is an expression on the part of the bond investor that the Federal Reserve is exercising a reasonable degree of control over the money supply, and that therefore a long-term commitment makes some sense at the current level of rates.

CHAIRMAN BURNS. Well, I say that all the time, and I believe it, and yet I feel a little uneasy because the purpose is to slow down the rate of growth of the money supply. And do you succeed in slowing down the rate of growth of the money supply if long-term rates do not rise? So, I feel a little uncomfortable with myself and with my own rhetoric, and therefore, with your rhetoric, which is so similar to mine.

MR. MORRIS. I think you can slow down the rate of growth in money supply without pushing long-term rates up. The long-term rates are to a large extent a function of expectations.

MR. MAYO. Mr. Chairman, isn't it that we're looking to a slowdown in the rate of inflation as the net result of our policy? The net slowdown in the rate of money supply growth is secondary. It seems to me that this is very important, what Frank has said, because we're saying the real interest rate component of long-term interest rates is indeed rising, but the inflationary premium inherent in those rates is declining.

VICE CHAIRMAN VOLCKER. It's pretty hard to argue that we've had a burst of 18 percent or whatever in the money supply, and because we acted against this, the net result is a decline in inflationary expectations. Maybe so, but--

MR. MAYO. But again, the 18 percent has to be looked at in terms of our inflation rate. I consider this a ship that passes in the night, the 18 percent.

VICE CHAIRMAN VOLCKER. Okay, you're just looking at what actually is the--

MR. MORRIS. Well, what I would argue, Paul, is that, if we had not responded to the extent that we did in the face of an 18 percent rise in [money], the reaction in the long-term bond market would have been very different.

Well, to go on, Mr. Chairman, I think that I would support alternative B, which is essentially a stand-pat policy for the next four weeks, [as] a pretty good one. I think it takes time for the monetary aggregates to respond to a change in interest rate policy. I don't think that we have yet seen the effect of the upward adjustment in our short-term rates, and I think you won't see that until September-October.

CHAIRMAN BURNS. Any views on the discount rate?

MR. MORRIS. My inclination would be to go easy on the discount rate at the moment, for two reasons. I think it could well be, in view of my feeling about the deceleration in the economy, that we might have to move short-term rates lower before the end of the year. I would like to see some confirmation in the next month or so of some resolution of what I see as the conflict between the real economy and the monetary economy right now. In other words, we've got, in the real economy, a deceleration of the rate of advance; and in the monetary economy, you've got an acceleration in the rate of advance. And these two are going to be reconciled either in terms of a stronger economy or a decline in the demand for money.

And for that reason I would be inclined to go slow on raising the rate until this reconciliation happens, because I think the timing of a rise in the discount rate at a time when we're going to see more and more talk in the press about a deceleration in the economy could lead some unsophisticated observers to see a causal relationship between an increase in the discount rate and a slowdown in the economy. I would like to see a little more evidence of which way we're going before we raise the rate, and we can live--we've learned to administer the discount window with a differential between the discount rate and the market rate in the past.

MR. JACKSON. May I ask what you mean by that. You mean that you change your criteria for loans?

MR. MORRIS. By administration I mean that we can avoid an excessive use of the window by a bank in order to pick up the differential.

MR. JACKSON. In what way could you avoid it?

MR. MORRIS. By kicking them out of the window after a certain amount of time.

MR. JACKSON. Why? On what basis would you justify such action?

VICE CHAIRMAN VOLCKER. We do anyway.

SPEAKER(?). [Unintelligible] Regulation A.

MR. MORRIS. Our policy is that the discount window is not a permanent source of capital.

CHAIRMAN BURNS. Well, the purpose of the discount window is not to enable a bank to arbitrage.

MR. JACKSON. But I got the distinct impression you changed your policy in view of a change in monetary attitude on our part. Is that what you're saying?

MR. MORRIS. I don't understand what you mean, Phil.

MR. JACKSON. I got the distinct impression that you were tougher on the banks and wouldn't allow them to get credit--on some of the banks--as a consequence of your changed attitude about monetary policy.

MR. MORRIS. No, I think the wider the spread you have between the discount rate and the federal funds rate, if you have the gap where the discount rate is lower, obviously it's going to be very attractive to banks to come and use the window. And therefore, in that kind of a context, we'd have to administer the window a little more rigorously than you otherwise would. I'm saying that I'd be willing to do that for another month or so until I can see which way--until I can see some resolution of the conflict between the real world and the monetary world.

MR. COLDWELL. I think Philip's got a point there.

MR. JACKSON. But do we adjust the concept of the discount window to suit our whims or is that a constant criterion that we use at the moment.

CHAIRMAN BURNS. I don't think Mr. Morris was saying that. I think all that Mr. Morris meant to say was that if bankers are tempted to, as some of them will be, to borrow at the discount window because the discount rate is low relative to this or that market rate, this is something that Mr. Morris's Bank will be aware of, will watch, and this is something that in every period when such a discrepancy arises, the Federal Reserve Banks around the country do more or less well and more or less systematically. I think that's what Mr. Morris meant to say--

MR. COLDWELL. They do it on a standard of administration which would very seldom change.

CHAIRMAN BURNS. But I didn't interpret Mr. Morris to say that the standard would change--

MR. COLDWELL. That's what I think Philip was saying.

MR. JACKSON. That's what I would want to get clear, that we weren't changing our standards.

MR. MORRIS. No, but it's just that the larger the gap between the funds rate and the discount rate, the more administration you have to do.

MR. COLDWELL. The more attractive it is to borrow.

MR. MORRIS. I'm not saying the standards are different. For obviously, when the discount rate is above the funds rate you don't have to do any administering at all. I think that this doesn't mean that we can't live for another month with the present discount rate, that's all, even though the gap is 3/4.

MR. COLDWELL. You get more borrowing then.

MR. PARTEE. You would expect borrowing to go up then.

MR. MORRIS. Sure.

MR. GARDNER. I understand exactly what Frank is saying. Inflection in the voice, examiners coming in early.

MR. PARTEE. [Unintelligible].

MR. GARDNER. The discount window is administered pretty expertly.

CHAIRMAN BURNS. Well, all right. Now we pass to you, Mr. Kimbrel.

MR. KIMBREL. Mr. Chairman, operating, I guess, from a personal hunch that maybe the economy is moving along somewhat stronger than it would appear in some segments--

CHAIRMAN BURNS. Yes.

MR. KIMBREL. --I believe we are reasonably agreed that our fundamental task here is to try to bring the money growth back into the target range, and if that should [require] almost no growth in the aggregates in the near term, that translates with me as at least [a] slightly less accommodative posture. So I find comfort in the numbers you have assigned to M1.

I guess I would not like to see the federal funds rate slip below the 6 percent range since they have accomplished that. I would hope that maybe we could stay somewhere in that area for the near term. Also, to see that range widened if we possibly could. I've been uncomfortable with such a narrow range for some time. Maybe even if we [lowered] the bottom [limit] of 5-3/4, I'd like to see [us raise the top limit] up to 6-3/4 if we could, to begin to widen that, not with the idea we would move immediately above the 6 percent, but certainly [strengthen] the inclination not to slip below that until we're somewhat more comfortable in what is happening with the money numbers.

As to the discount rate, our directors for some time have been under the impression that, with the inflation and with the growth, a change would be appropriate. I would personally prefer to see a smaller move, 1/4 [point], but maybe the numbers now are such that the market is reasonably conditioned, and if we could not move again another 1/4 point within a month to six weeks, I would prefer to have a 1/2 percentage point and do it reasonably early.

CHAIRMAN BURNS. By reasonably early--

MR. KIMBREL. Friday of this week.

CHAIRMAN BURNS. We'll now hear from you, Mr. Baughman.

MR. BAUGHMAN. Mr. Chairman, I think it's already been mentioned that we have been in the process of writing a record of monetary policy which will be described as having been procyclical and that we do need to be moderating that as rapidly as possible. There was also a fair amount of conversation this morning about the lack of optimism or confidence on the part of businessmen. I think the process of moderating the rapid growth in monetary [aggregates] will tend to shore up and reinforce the confidence of businessmen in the economic situation.

With respect to monetary policy prescription, I have usually felt constrained from picking one measure from one alternative and another from another alternative in the staff's representations, but today I don't feel so constrained. So I'd be inclined to take the federal funds rate from alternative B and the aggregate measures from alternative C. I'd be inclined not to widen the ranges of either the aggregates or the federal funds rate. It seems to me that that would move us in the direction we want to go, although I would not have a serious objection to a lowering of the minimum in the two aggregates.

With respect to the discount rate, I've begun to see just within the past week some borrowing for--pretty clearly--rate purposes by banks who normally would get their funds from the money market. So my inclination would be, within this monetary prescription, probably to stick to the 6 percent funds rate for a week or two, and at that point then--I'm thinking about two weeks--it would be desirable to move the discount rate up by a 1/2 point. This would kind of separate the discount rate from a policy move and make it a move in response to market conditions. I think the 6 percent funds rate will in another week or so have come through clearly as a policy move, and that will have been settled. I would not be averse to seeing the discount rate move, say, in one week, but it seems to me it would be a little better if we had two weeks' experience behind us with a 6 percent funds rate. That's all I have, Mr. Chairman.

CHAIRMAN BURNS. Thank you, Mr. Baughman. Gentlemen, I really have been listening very attentively to what each of you has been saying, but at the same time, I've been engaging in some arithmetical calculations that are of some interest, I think. I commented on the difference earlier between the rates of growth of M1 as we now compute M1 and the rate of growth based on a revised concept of M1. Now, with very minor exceptions, for some 15 months the revised M1, month by month, showed a higher rate of growth than the standard M1. In April, the two were identical, and in the last three months, the revised M1 shows a lower rate of growth than the standard M1.

Assuming the arithmetic here is right, this would suggest to me that money has moved out of temporary savings balances into transactions balances, either to carry out payments on transactions that have already been made or to provide checking deposit money for transactions to be made in the near future. In any event, the figures are much lower. Let me just read the figures for May, June, July. The first figure is the standard [M1], and the second figure is the revised M1: 0.7 for May and then 0.4; 4.5, l.8; 18.3, 12.2. Well, that's my interruption for you to use or not use and interpret as you see fit.

Mr. Rankin, please. Mr. Rankin, we're very glad to welcome you to this table today.

MR. RANKIN. Thank you, Mr. Chairman. Well, I'll just briefly say we could accept the specifications of alternative B, but in view of the July experience, we certainly would not be concerned if growth in the aggregates came in as much as 1 or 2 percentage points below the lower limits of the alternative B tolerance range. In other words, 0 to 6 [for M1] is fine with us.

CHAIRMAN BURNS. Any view on the discount rate?

MR. RANKIN. Well sir, I would not want to speak for Bob Black, but I might speak personally. I guess it would be a tough decision, and looking at what's occurred in the funds rate since April, the cumulative rise, it has been up about 1-1/4 percentage points. One could be inclined, I guess, to kind of hold steady for a while in order to get a better line on the impact of the actions that we've already taken. But I would think, if evidence isn't forthcoming within the next 10 days or two weeks, the time to increase the discount rate had arrived.

CHAIRMAN BURNS. Thank you, Mr. Rankin. Mr. Partee now, please.

MR. PARTEE. Well, Mr. Chairman, I have mixed emotions today. I'm troubled by the increase in various defined aggregates because I think that I am rather in agreement with what Dave Eastburn said, that we're in the process working on a record that's going to show growth well above our limits in the narrow money supply, and perhaps even in M2, which has been pretty strong over this most recent period. We had a surge in April, and then May and June looked nice and quiet. And we had a surge again in July, that's the second [unintelligible]--whatever Bob Mayo's analogy is. And [it] looks as if August and September are going to be quiet. But the result of it is that you get a second quarter that's large and a third quarter that's large. And so I'm troubled by it.

Now your alternative definition [of M1] I think tends to show that we've had pretty accommodative growth throughout the period rather than that we had slowing more recently, [which is] why we get an adjusted money supply that is up quite sharply over the last 15 months or so. So I'm worried about it. I don't know, maybe we shouldn't have an M1 target, but we do, and the market makes quite a bit of it, and we make quite a bit of it and the need to reduce it over time, and so forth; and so there is a credibility question here. And there also is a possibility--if we use it as an index of monetary growth, imperfect as it is--that we're going to have excessive monetary growth in this period.

On the other hand, I would note to the Committee that we've had a considerable increase in short-term interest rates. If you look at chart 3 in the Bluebook, you can see that the funds rate was very stable at about 4-5/8 in the early months of this year. It rose 3/4 [point] abruptly in late April and May to the 5-3/8 range, and now it's risen abruptly another 5/8 [point] in the last day or two, to 6 percent. So we've had an increase of almost 1-1/2 [percentage points], and it takes us into new high ground on this particular economic recovery.

We have a bill rate that, it seems to me, if it has just a little more adjustment in it, Peter, is increasingly threatening flows to the intermediaries, and we haven't quite seen what that would be. I have a perception that the market may not yet quite have adjusted to the 6 percent funds rate, which is going to be a signal to the market, as Governor Jackson just pointed out to me, quite clearly--if not now, [then] on Friday--when the publication of the Record of Policy Actions will include the telegram and will show that the Committee adjusted its target to a high of 6 percent if there continued to be strong growth in the aggregates. So that 6 percent is certainly going to be established in the market's mind and there may be some further adjustment in rates to that.

I think it's probably true, since I agree with Frank that GNP is not going to go up so fast in the second half of this year. But the demand for money will be a little less than the staff probably is projecting in this period. And so I think we won't have the pressures that I would anticipate if we use the staff's projection of the second half GNP. And therefore, I would rather like to see us pause for a bit and observe the situation.

So I like the funds rate centered on 6 percent, say 5-3/4 to 6-1/4. I think that we should be tolerant of a shortfall in money growth, either in M1 or M2, if we should get one, and I would have chosen as my ranges, 0 to 5 for M1 and 3 to 8 for M2. It [would] keep a fairly high upper end, open the range a little bit, and indicate, I think clearly, that we would have some tolerance. And, unless we get unusual growth or unusual shrinkage in the monetary numbers, [it would] emphasize the stand-pat character for a few weeks here while we see what happens in the market and let the forces regroup. I would also shift to a money market directive this time.

CHAIRMAN BURNS. Thank you, Mr. Partee. I'm going to interrupt the flow of thought once again by reporting on what I can extract from these figures. You're going to get very strong support, Mr. Mayo. The table I have before me starts in 1976. Let's go back to April 1976; the rate of monetary growth in April was higher than in the preceding month and the following month. Now next we go to July 1976; the rate of growth in July was higher than the preceding month or in the following month. Next we go to October; the rate of growth in October was higher than in the preceding month or in the following month.

Next we go to January 1977, and the rate of growth in the preceding month was higher, not lower; the rate of growth in the following month was lower. So this pattern is only partially repeated. Next we go to April 1977, and the rate of growth in the preceding month was lower; the rate of growth in the following month was also lower. Next we go to July, and the rate of growth in the preceding month was lower, and presumably our staff will testify to the rate of growth in August being lower.

So you have here something approaching a repetitive movement, a quarterly seasonal pattern, except for one partial deviation. In six observations, 5-1/2 [observations] were consistent with the hypothesis of a seasonal in these seasonally adjusted figures, and half an observation was inconsistent with that interpretation. Well, I'm making life no easier for any of us--yes, Mr. Wallich.

MR. WALLICH. I think our question is whether we want to make a strong effort to get back on track. We've made, to all appearances, a poor record of these two very high quarters, and the question is whether we should make that effort at the cost of high interest rates and substantially lower growth of the aggregates. Now I'm going to argue against this in light of both the technical factors and the state of the economy, the international situation. Let me say why. I think these adjusted numbers as you've described them, Mr. Chairman, seem, in good part, to differ from the standard M1 numbers by the very factors that we've always had in mind as causing changes in velocity. So here we've expressed, I think very helpfully, what we used to call the change in velocity.

CHAIRMAN BURNS. Exactly right.

MR. WALLICH. It's really a difference in M1 that tells us that M1 has been higher, which is plausible because we've had these high increases in velocity that we've found hard to explain. Well, given that, now I look at where we are with respect to past long-term ranges, and it's my impression that we are not all that far outside, even though we've done poorly and will have done poorly in the light of the second and third quarters of this year.

Going back to the ranges announced [for] the second quarter of '76 and continuing since then, M1 is [mostly] high, but fractionally with respect to the range based on the second quarter of '76. In fact, we are inside the range--making a reasonable prediction for M1 for the end of this quarter. For M2, one can say somewhat similar things. We are high, but not disastrously high in this long sweep of our ranges. Sins that they are, sins that look bad mostly with respect to the last, the third and second quarter, and to the relatively low increases we've had just before this.

So my sense of urgency to get back on track is somewhat diminished by that. My sense of urgency is further diminished by the thought that we've had these shocks clearly from the monetary side. And the old rule of thumb says that when you're shocked from the monetary side, stay with interest rates, ignore the aggregates. We're not prepared to ignore them, but I think there is, in terms of that rule of thumb, a message here because we've had monetary shocks and not shocks in the real sector. We look at the real sector. The economy is not very strong. It's shifting gears downward. If we had a very booming economy, I think there might be a better case for trying to get back on track with the aggregates. It's not clear to me that our economy could even stand a concerted effort to get on track. Interest rates have risen very substantially, as Governor Partee has pointed out, and maybe enough [unintelligible].

I would just add that, from the international point of view, we've heard that the rise in interest rates has done a good deal in getting the dollar back up. I think we could get to a point where the rise in interest rates here might present problems for other countries in terms of their own monetary policy. They are weakening; Germany still is. And rising interest rates here would make it somewhat more difficult for other countries to assume easier policies that they might want to continue.

So I come down to a very moderate set of numbers. I would like a wider funds range, as I always do--5-1/2 to 6-1/2. On M1, I'd go with the alternative C in order to give it a little more leeway on the downside, 1-1/2 to 5-1/2; M2, 4 to 8; and an aggregates directive.

VICE CHAIRMAN VOLCKER. What are the monetary shocks you were referring to?

MR. WALLICH. A sudden change in the demand for money, which seems to be what we've had--it went up very suddenly, and that shock did not come with money [holding] constant [and] the real sector moving. It was the demand for money moving.

CHAIRMAN BURNS. All right, thank you, Mr. Wallich. Mr. Volcker now, please.

VICE CHAIRMAN VOLCKER. I must say, Mr. Chairman, if one gets your periodic reports from examining your tables, and listens to Mr. Mayo, and looks at the difference between A, B, and C of 1/2 percent on the aggregates, and looks at what's been happening in ranges of errors of 15 percent, and the estimates are close to it, one has a little sense of futility in picking between A, B, and C. I ended up, just to cut through all that, exactly where Mr. Partee did. I think it's right to be tolerant of low growth in the M1 and low growth in M2, and I've written down exactly the same figures he cited, 0 to 5 and 3 to 8, to express that I think our much longer-term problem, as I alluded to earlier, is how we're going to reconcile getting these aggregates down over a period of time with the inflationary momentum built into the economy and how we achieve that without a real shock to the economy. I don't think we really face that this month.

I think I join practically everybody else who's talked here in pushing interest rates up at the moment in an effort to further assure we get the aggregates down. But I wouldn't be allergic, I think, if the aggregates continue to outrun the kind of range that I just cited. I don't think that's impossible, seeing some further increase here after a little pause. I don't think I would be that sensitive to a further increase in rates, particularly against the background--I feel a little bit of the schizophrenia that you expressed--but I still think, when we can get by with it without setting too much of an impact on long-term rates, I feel a little more comfortable on balance. So I would be prepared to see some further increase in rates after a little pause.

If the aggregates are exceeding this kind of number with a couple of more weeks experience, and I don't know if we can be sure that it's not--how you express that in terms of a funds rate, I don't know. I could live with the range that's under B and that you cited. I had thought in terms of 5-3/4 to 6-1/2, with a kind of a 6 percent asymmetrical midpoint expressing what I just expressed verbally, perhaps a little better. But I could live with it either way. My principle point is, if the aggregates really show further signs of exceeding where we want to go, I don't think we should be unwilling to make some--at least modest--further increase in interest rates despite the amount we've already gone.

On the discount rate, I have not thought it was appropriate until now to increase it. I do, at this point, think the time has come, given the degree of divergence that exists between the market rate that we, in effect, have manipulated and the existing discount rate. As a matter of general policy, it's not compelling in any particular instance. I don't like the idea of having to engage in the kind of partly semantic, partly real, I guess, discussion that Governor Jackson had with President Morris. I would rather keep the discount rate, all things equal, somewhere near the market rate so you don't run into that kind of a problem. To the extent it has a signaling [effect] now, I'd be willing to accept it in terms of our deliberate effort to increase rates here against the background of a very large increase in aggregates. I think that President Eastburn already expressed the thought that I have in mind here, that some mild signaling effect, I don't think it would be much, is not all together undesirable.

I appreciate-- and I think this is the one difficulty--that if a change in the discount rate appeared to trigger change in other administered rates, we may be in a less satisfactory position in some context than we would otherwise be. I think, on balance, Mr. Kimbrel has the timing about right on this, and maybe even Thursday's the afternoon, all things considered, partly against the danger that the longer you leave it unchanged--if we don't change to market rates--we're in an unsatisfactory gap situation. If the economy is slowing down, it looks increasingly awkward to raise the discount rate, and we're left with an unsatisfactory technical situation, it seems to me, in terms of the amount of the gap.

CHAIRMAN BURNS. That last I don't see. If the economy slowed down and we became concerned about the degree of retardation of the expansion that was occurring, then presumably market rates would be moving down.

VICE CHAIRMAN VOLCKER. I agree. If it slowed down that much. If we became concerned over the degree of retardation, I agree with you. If it just kind of slowed down to the point we weren't concerned, we wanted to keep the level of market rates, I think this is a fine judgment--

CHAIRMAN BURNS. Not only a fine judgment, but it's a [unintelligible] very, very difficult to, given specific facts, very difficult to--

VICE CHAIRMAN VOLCKER. I don't think this is an overwhelming case one way or the other here. But I think the presumption is, you keep the discount rate closer in line with market rates than it is at present unless you have a pretty strong reason not to. And I'm not sure we have that stronger reason at the moment.

MR. PARTEE. Paul, may I clarify. Now you said you would have a funds rate range of up to 6-1/2. That would technically mean that you would raise the funds rate conceivably from its present 6 to as high as 6-1/2 with a monetary growth of 5 percent in M1 and an 8 percent in M2. That is to say, you gave as your example, where the instructions were not consistent, which would call for a wire or a telephone meeting or something, but then you incorporated that within your funds rate range. Did you mean to do that?

VICE CHAIRMAN VOLCKER. Well, I think technically you might be right. I don't think we should be very eager to change the funds rate, and I wouldn't conceivably go into 6-1/2 until it got above that 5 and 8, for a week or two anyway.

CHAIRMAN BURNS. That's not the rule under which we function.

MR. PARTEE. That's not the rule, I think. Exactly.

MR. COLDWELL. Let me clarify as far as the rates are concerned. You would go up to a 1/2 percent[age point] increase or 1/4?

VICE CHAIRMAN VOLCKER. I'm still debating that in my mind. I think I probably feel a 1/2. But I don't feel very strongly about that.

CHAIRMAN BURNS. Well, I thank you, Mr. Volcker. Mr. Winn now, please.

MR. WINN. Mr. Chairman, I have been studying the new math here, too, this morning, and I must confess the relationship between the funds rate and ranges we have been given either have no meaning or we are in a strange posture. Because should we pick the 0 to 6 as our range for M1--that's a median point of 3, which as I understand it would really call for a [6-3/4 to 7-1/4 percent funds rate] range. It's just that if you got a 4 median, then you've got a 6. A 3-1/2 gives you 6-1/2, and then a 3 median would give you 7 as the midpoint of the range, generally.

MR. PARTEE. Funds rate.

MR. WINN. So if we are going to be consistent at all, maybe we shouldn't be, but it seems to me that the relationship between the funds rate we are talking about and the quantities we are talking about are inconsistent with the first presentation we had here this morning.

MR. AXILROD. Well, President Winn, we made the effort, as you noted, to present what we think are consistent--

MR. WINN. I understand.

MR. AXILROD. Whether they turned out to be consistent in the real world--

MR. WINN. I understand.

MR. BAUGHMAN. But we never follow a consistent pattern.

MR. AXILROD. And the reason there are only half-point [funds rate] differentials is because of the short run. Whatever M1 is going to be, we don't think there's hardly anything we can do to prevent it from being that in the short run, and all you can do is affect it a little bit with the variation in the funds rate.

MR. WINN. Yes. Well, that's a probably an accurate one. But I wanted to show what our consistency would be--the 0 to 6 with a midpoint of 3 would give you a much higher funds rate direction than we are showing here. My own feeling would be, stay with the B numbers and quantities, spread the fed funds rate range to 5-1/2 to 6-1/2, with the realization that we would be outside before we made our moves.

I would take advantage of the market acceptance of what we've done and be prepared to move the discount rate by a half [point]. I think we shouldn't reward our sharp-pencil friends who are taking advantage of us at the moment, not extensively, but I'm not sure this is the way we ought to pass out the rewards. And I would like to see that [discount] rate moved first before we did much to tamper with the funds rate above the 6 area, and see if we get any impact from the first move. If we're wrong, I'm prepared to move it down.

I think it shows great flexibility in the quantities we get. We've been very successful [with] the upward range, with a relatively [strong] market confidence being shown in it, and I'd be prepared to push that if necessary with the discount rate moving first. And I'm like Mr. Kimbrel--I would have done it last week rather than this week, but that's neither here nor there.

MR. PARTEE. A half, did you say?

MR. WINN. A half, that's right. And you've still got a differential there of 1/4 point. You don't really have any market impact, except for a psychological impact showing that we're resolved to continue our fighting in this direction. And I'd be prepared to move that first before I'd move the funds rate above 6, because I do think we need time to see that the impact has worked its way through. But I'd keep the funds range there if we need it, and if we go out of control again, I think you know the confidence that we built up can be lost just as quickly.

CHAIRMAN BURNS. All right, thank you, Mr. Winn. Mr. Guffey now, please.

MR. GUFFEY. Thank you, Mr. Chairman. Sir, I think many of the expressions that have already been made around the table with respect to the longer-run performance of this Committee in controlling monetary policy--in the sense that the [growth rates of the] aggregates are continuing to be very high--as Mr. Volcker has expressed [it], there has to be a time when we face up to that. But I guess I would hope that we wouldn't do it all at one time simply because we are following one month [of] very high aggregates growth. There is a need, it seems to me, to let the market digest what we have done because we've taken a fairly major step in the market, and the funds rate particularly.

And as a result, looking ahead, [I can see the] proposal to move the B alternative to a 0 to 5 range for M1; a 3 to 8 for M2; with a further prescription that the funds rate be broadened, but only on the up side, to 5-3/4 to 6-1/2 with an asymmetrical midpoint of 6; and a money market conditions directive hopefully to get the lower growth of the aggregates in the upcoming period, therefore maintaining a 6 percent funds rate. But if, indeed, we start getting a 5 or above figure in M1, I would be quite happy to see the funds rate move on up to the 6-1/4 to 6-1/2 area. I don't think that we can have two or three months strung together with very high aggregates growth without this Committee acting or reacting.

With respect to the discount rate, I would like to see the discount rate increased 1/2 percent[age point] as of tomorrow [Wednesday] afternoon, Thursday afternoon, or Friday. This would be simply a validation of what would be published on Friday, that we are indeed at 6 percent, that we are then 3/4 of a percent out of line with the funds rate and some other shorter market rates. And I would oppose going 1/4 [point] now and maybe 1/4 a month from now, as has been suggested around the table. I think we ought to take a bite at it and do it all at one time, simply with the public statement that we are only following the rates and the movements already taken place.

But also I give support to further consideration of a reduction in the reserve requirements at an appropriate time later this year.

CHAIRMAN BURNS. Thank you, Mr. Guffey. Mr. Balles, please, now.

MR. BALLES. Mr. Chairman, just going back to the economy for a moment, my own views correspond pretty closely to those of the staff. But I'm not really concerned about a slowdown to, say, 5 percent real growth for the second half of the year following this extraordinary rate of almost 7 percent for the first half because, I think all of us would probably agree, that was unsustainable. Five percent is not at all bad when one looks at the long-term historical record.

I am concerned about the inflationary psychology in the market today. You made reference to the *Wall Street Journal* today. I'd like to make reference to the lead article on the front page as to the inflation outlook, particularly seen by various parts of the government forecasting fraternity. The general thought is that we will have at least 6 percent, if not a bit higher, going into 1978. I'd also like to allude to what I thought was a very important comment that you made in your testimony on monetary policy, to the effect that, while we have reduced growth ranges in the aggregates moderately, in a slow way, the actual growth rates have in fact gone up somewhat. And unless we begin to take action here to play this game a different kind of way, I expect we will see a continuation of that. My own feeling, as one objective we ought to have, is to try to diminish inflationary expectations and also prevent long-term rates from rising significantly, even if have to have a further increase in short-term rates.

I'm still concerned with the longevity of the current expansion and the extent to which a healthy pace of business capital spending; a healthy pace of capital spending by state and local governments; and a good, ongoing rate of housing construction [will continue]--all of which have somewhat tempered long-term rates. In the sense that we can keep long-term rates from rising based on inflationary expectations, I think we will have made a real contribution to stretching out this expansion.

Getting down to what might be an appropriate thing to do at the moment, I think there's already been an upset, and I share the concern about overshooting our targets, whether it's over the past year or the present quarter. And as I look back on the record, I think we do have something of a history of overshooting targets materially when interest rates are rising because of a natural and understandable reluctance to push up the funds rate in the short run in small, prompt bites to keep the aggregates within our ranges. And as a result, the aggregates move up by an even bigger amount over a longer range.

So in terms of the choices facing us today, I recommend starting off the aggregates with the range in alternative C, although I would certainly accept your proposal [to] consider a lower limit on M1 and M2 than [is in] alternative C. As far as the federal funds rate is concerned, I would not go as far as the alternative [C] proposal, which was 6-1/4 to 6-3/4, but I would come out, I think, for the proposed range of 5-3/4 to 6-3/4, centered on 6-1/4, not with a thought that we move up there immediately, but move up there gradually until there is solid evidence that we in fact are getting these aggregates under control. The danger continues to be an outcome which would not offset the surges in April and again in July and thus end up for a longer period outside of our ranges both on M1 and M2, which we have been over the past year and the past quarter.

With regard to the discount rate, I am on the side of those that think a good solid case can be made for action, and I would prefer to see it done sooner rather than later, like this coming Thursday--that's when I would have to make recommendations on [it]. I think closing the gap partway between the funds rate and discount rate would certainly be an appropriate signal to the market that we are going to reinforce the actions we've taken in the open market with actions at the discount window to give some public signal of our attempt to keep the aggregates in the target ranges--not overshooting.

I think the timing is quite crucial now because we are in a little interlude here when we just had a settlement date yesterday, as I understand it, for the recent Treasury financing, and it won't be too long in the future before we get another Treasury financing. So this would be a good time to move. As to whether it ought to be 1/4 or 1/2 [point], I'm still kind of debating that point, but I could go with either one.

CHAIRMAN BURNS. Very good. Thank you, Mr. Balles. Mr. Roos now, please.

MR. ROOS. Mr. Chairman, I would subscribe almost verbatim to the rationale expressed by John Balles, and specifically I would prefer an M1 range of 0 to 4 percent growth; M2, 4 to 8; and fed funds range, broaden to 5-3/4 to 6-3/4.

I think that anyone who views the inflationary trend as just a temporary monetary shock or something that's been very short lived--on page 5 of the Bluebook, it shows us that, for several years, there has been a continuing trend toward an acceleration of growth of the monetary aggregates: past 12 months, M1, 7.1; past 6 months, 8.3; past month, 18.3. That is certainly a disturbing trend, and I am very fearful that it isn't going to be long until people who watch these things will feel that they have reason to expect a return of severe inflationary tendencies as a result of the growth of the aggregates. So I lean toward the greatest degree of restraint possible, even if it means an increase in interest rates.

In terms of the discount rate, I would subscribe to a 1/2 point increase just as quickly as it could be done.

CHAIRMAN BURNS. Thank you, Mr. Roos. Mr. Jackson now, please.

MR. JACKSON. I think the issue of rates of growth for our economy for the next six months or year are pretty clear. I think the recent rates of growth we have had are unsustainable. At the same time, I think that, unfortunately, we've overlooked the result that our rates of unemployment are still unacceptable politically or socially. And it's going to take rates of [economic] growth above 4 percent to make any net change in that percentage of unemployment, particularly given the prospects for the rates of growth in the labor force.

So I think the target is rather clearly before us all, that rates above 4 percent are going to be the objective, whether they are achieved or not. Now what are the most likely [circumstances] that would cause us to fail to reach that objective? I think the most likely cause of failure, given the rest of the economy, is a collapse of sentiment and optimism on the part of our society. And there again, I think the most likely cause of such a collapse would be inflation and its ramifications, or the expectation of it.

Now that sounds very simplistic to say, but I think it equates to our purposes because, unfortunately, many of our people have become four o'clock Thursday disciples. And we have a large number of people in this country--particularly those that make decisions for plant and equipment expansion and those aspects of this economy that we are required to see expand to reach our expectations--we see many of these people have become mechanical monetarists by watching money supplies, and things like that, in a very superficial way. I don't think they understand it, but they look at it. And sometimes people react based on what they see rather than what they expect.

For that reason, I do think that we are going to have to be alert to significant deviations from our long-term targets in monetary aggregates more than underlying circumstances would have otherwise reasonably dictated. And I think that that will be the best tool that we can utilize to assure the type of expansion in our society that would be socially, politically acceptable to us and to the rest of the world.

And when it comes to equate that right now to current action, I would advocate that we would have a 0 to 6 M1, a 3 to 8 M2. I don't share Governor Partee's judgment that going to a money market directive is appropriate at this time, with this wide range. Meaning [that the monetary aggregates directive] accomplishes the same result but clearly provides for the alternative that, if we do get continued sustained growth in monetary aggregates over the 30 days ahead of us--and we're two weeks into it now--then we would not hesitate to go ahead and move even within that range.

As to the federal funds rate, I would personally favor the skewed situation of 5-3/4 to 6-1/2, using the 6 percent [as midpoint]. I do think that, given what we know for the first two weeks, and given this type of broad sentiment of the Committee for accepting the lower rate of growth, going below 5-3/4 would probably be a mistake. At the same time, if we do see strong expansion in the money supply even within the next 30 days, I think the most constructive thing this group could do for the sustained confidence of our people to go forward with our economy would be 6-1/2, if that's what it takes. And so I would be prepared to do it.

CHAIRMAN BURNS. Thank you, Mr. Jackson. Mr. Gardner now, please.

MR. GARDNER. We're running late. I will try not to be long. I was not around here when you got your reports of an 18 percent growth in M1. I was quite surprised when I heard about it. And it bothers me because it is an out-of-phase blip. We've spent a lot of time trying to explain our April surge, but we can't find many good reasons for the July surge, and that makes me a little uncomfortable. I think you took the right course. I think your telephonic meeting was proper; I'm glad to see that you climbed that next ridge. I would also say that, without that 18 percent change, the sensitivity that many of you have expressed about the economy ahead and the reasonable satisfaction that our growth rate, though declining, will be all right, are two points in some conflict.

Therefore I come to the conclusion that the alternative B is a good idea, that the lower limit could be 0 on M1 and 3 on M2, and that the federal funds rate might well be 5-3/4 to 6-1/2. But I want to point out that--Governor Partee said it first--if you've got a 5 percent upper limit on M1, you are probably going to be very, very quickly faced with going to the 6-1/2 federal funds rate. So that's why I prefer the 0 to 6 [on M1]. I think the skewed [federal funds] rate makes pretty good sense, because the Desk has only 25 basis points to deal with at the moment, starting from where we are today in the range that's listed in alternative B.

So in substance, what worries me most is the July surge, and I haven't yet grappled enough with the new math to understand or allay my fears. So I would follow that course. And as to the directive, I think the aggregates directive would be probably a better solution.

CHAIRMAN BURNS. Thank you, Mr. Gardner. We still haven't heard from Mr. Mayo.

MR. MAYO. Mr. Chairman, first a vote of enthusiastic support for the new concept of transaction M1, M1.5, or whatever we want to give it as a nickname. I would hope that this is the beginning of a serious effort of this Committee to study carefully the implications of a reconstructed [M1] that would indeed lead to a redefinition. Perhaps it would be a redefinition for range-setting purposes in your congressional testimony.

Having said that, my arguments for my position have already been stated. I will merely state the conclusions. [For the federal funds rate], 5-3/4 to 6-1/2; I agree with what Steve just said. And I guess, come to think of it, I agree of what he just said on M1 and M2--0 to 6 and 3 to 9. I would not like to see us make changes triggered by about a 5 percent increase in M1. I think that would be unfortunate. I believe in the asymmetrical philosophy on the federal funds rate of 6 percent being the center. I feel we should have a monetary aggregates directive here because I am ready to see a little more increase in fed funds, and I think the intention is properly focused on the behavior of the aggregates right how. Some of that focus is out of my control, but I think much of it is there.

I want to give a word of support to Phil Coldwell's statement on reserve requirements. For the factor that you do mention, I would reserve judgment until friends under the dome at the other end of Pennsylvania Avenue go home for vacation. Regardless of what happens to legislative proposals, [and] unless I'm wrong in my estimate of when the seasonal demand is over, I think we will still have time to take some action, and it will be less controversial. And appropriate.

I would do the discount rate change immediately. I think it would be essentially a confirming action. I think Roger has put it very well in his statement. If we wait more than past the end of this week, I think it would be misinterpreted as somehow a sign of further tightening rather than a confirming action. My recommendation to my board a week ago was a quarter [point]. I have seen what has happened in the interim. I expect if this were to come up again this week, my recommendation would be a half [point]. But I think doing it immediately is more important than whether it is a quarter or a half.

CHAIRMAN BURNS. Thank you, Mr. Mayo. Mr. Lilly now, please.

MR. LILLY. While I was very interested in your new M1, I only wish that you had included in there the nondeposit source of funds, which I think really belong in M1. That's where all the corporate treasurers are squirreling away money today that they have raised from long-term borrowings, and it's overnight money--it's a great deal more ready to be spent than savings accounts.

As far as the program presented is concerned, I favor, not terribly strongly, the 0 to 5 [for M1], the 3 to 8 [for M2], and a 5-3/4 to 6-1/4 [federal funds rate] with the money market directive. The reason for that--I think 157 basis points since April and 62 basis points [in] July deserves some stopping and waiting.

CHAIRMAN BURNS. Thank you very much. Mr. Van Nice, please.

MR. VAN NICE. Mr. Chairman, I think at this point of the meeting, anything that I would have to say is going to be quite redundant. It's all been said. I came here prepared to report alternative C across the board, both aggregates and the funds rate, so we can give confidence for reasons that have already been stated--namely to get back on target.

My confidence has been shaken a little bit by several developments that have come up here. First of all, the hypothetical new M1 is somewhat comforting to me at least in the last three months. Secondly, the suggestion that the downward shift in money demand is perhaps [attenuated] if not actually stopped. The third concern is that it seems that either our seasonal adjustments are wrong or every three months, by happenstance, we get a bulge in the M1 money supply. And fourth, there seems to be some doubt as to the virtue of consistency between the federal funds rate and the monetary aggregates.

Nevertheless, I still vote for alternative C, although I would be willing to see the lower [limits] of both monetary ranges, M1 and M2, lowered somewhat. And in line with Mr. Kimbrel's suggestion, I think that I would like to see the federal funds range widened somewhat, perhaps dropped as low as 5-3/4, with an upper end of 6-3/4.

On the discount rate, if Mark Willes were here, I know he would recommend at least a 1/4 percent[age point] increase. I think that he might go along with a 1/2 percent[age point] increase at this time. As has been said, the market is already adjusted to the expected increase. On the economy, we are somewhat more optimistic in the Ninth District than is the staff. And--although as an old discount officer I strongly dispute the idea that we change our criteria according to the phase of the business cycle--I must admit that it's a good deal easier to administer the discount window when the discount rate is close to the fed funds rate. And in order to discourage the temptation for arbitrage, I would be in favor of raising the discount rate at least 1/4 percent[age point], perhaps 1/2 percent[age point], and I would do it immediately.

CHAIRMAN BURNS. Well, I appreciate, really, what you say about the discount rate, but let me remind you that the discount rate went to 8 percent in 1974 at a time when the prime rate was 12, and the commercial paper rate 12-1/2, and the federal funds rate a little higher than 13. Let me remind you that the 8 percent discount rate was the highest in our nation's history. Let me remind you that the next highest, if my memory is correct, occurred in 1920, when Governor Harding was the head of the Federal Reserve System. Let me remind you, finally, that he lost his head soon after the rate moved to 7 percent. Now this is just a recital of some more or less connected historical facts.

MR. MAYO. Are you speaking of 12 heads? May we remind you that Chairman Burns didn't lose his head when it went to 8 percent.

CHAIRMAN BURNS. Well, the discount rate is a headache. Some central banks have tried to get rid of that headache by adjusting the discount rate mechanically to market interest rates. We debated that, and we have felt on balance that we would be giving up an instrument of policy that is useful at certain times.

Gentlemen, we have to reach a decision. The discussion that we have had today ought to make all of us feel humble with regard to the task before us. There are differences among us. They are not really very large. No one of us can justly claim that he's glimpsed more than a part of the truth. And no one of us can claim that he's glimpsed more than a part of the future. There is a considerable sentiment for a 0 to 5 or 0 to 6 percent rate of growth for M1. There is a preponderance of sentiment in favor of a 3 to 8 range, I think, for M2. As for the federal funds rate, there is an equal division within the Committee between a range of 5-3/4 and 6-1/4 and 5-3/4 and 6-1/2. I would advise the [Committee] that we not go above 6-1/4 at this time, and if the rate of growth of the money supply comes in at the high end, I think you have found that I'm not tardy in advising the Committee by telegram as to further action.

We have made a significant move, as Governor Lilly summed up quite accurately and succinctly. The economy is not so obviously strong that a further move of 1/2 percent[age point] should be lightly contemplated or readily contemplated. I would advise that we stay with 5-3/4 to 6-1/4, bearing in mind that, if the rate of growth reaches the limits of our monetary aggregates target ranges, we can confer once again and decide if the sentiment of the Committee is to go higher.

MR. JACKSON. May I suggest, Mr. Chairman, that we use the 5-3/4 to 6-1/4 and then the 0 to 5 [for M1], [which has a] slightly lower midpoint [than 0 to 6], which I think would accomplish the two positions.

CHAIRMAN BURNS. It is consistent. Well, let me suggest, then, a 0 to 5 range for M1 and a 3 to 8 range for M2, and a 5-3/4 to 6-1/4 range for the federal funds rate. Now as to the directive, I think there is a narrow range [for federal funds, which] logically would suggest a money market directive. On the other hand, if we are willing to use that range, and I think that is the sentiment of the Committee, a monetary aggregates directive--in spite of the smallness of the range--would be indicated. And I sense, having listened to all of you, that that is probably the sentiment of majority of this Committee. Yes, Mr. Guffey.

MR. GUFFEY. Mr. Chairman, does that mean that, if you go with the monetary aggregates [directive and] you get [M1] growth that is projected to be 2-1/2 [percent] or greater, then you are going to use that other 1/4 percent [of the federal funds rate]?

CHAIRMAN BURNS. You see, the difference between the two is that you move much more slowly to utilize the full range with a money market directive than with a monetary aggregates directive. Is that a correct explanation, Mr. Sternlight?

MR. STERNLIGHT. Correct.

MR. GUFFEY. With the money market conditions directive, you would be projecting 5 [percent] plus [in the growth of M1] before you would actually start making a move from the 6 [percent federal funds rate] under this prescription. Is that correct? That is the appropriate--

MR. STERNLIGHT. I think you'd want to be projecting 5 before--

MR. GUFFEY. In other words, [reaching M1 growth] in the upper range before you would start making a move, and that's what I would prefer. If you are going to do it the other way, and that is, if you are projecting say 3 or 3-1/2 you start making a move towards your 6-1/4, I don't think I'd go along...

MR. PARTEE. I think its 3-1/2; [that is], 1-1/2 to 3-1/2 would be a zone of indifference, [and at] 3-1/2 to 5 you would begin to move.

CHAIRMAN BURNS. I would think so.

MR. STERNLIGHT. I would appreciate clarification--if you widen the ranges for the Ms by dropping the bottom, are we to consider them again to have symmetric midpoints or asymmetric midpoints? It would make a bit of difference in the rapidity with which we move.

CHAIRMAN BURNS. Why not take the symmetrical midpoints?

MR. PARTEE. That's what I think. I would use the money market directive, Mr. Chairman. Because we are taking aggregates that are deliberately low in their range compared with what our staff is projecting.

VICE CHAIRMAN VOLCKER. The logic says--in the box we are in with all this precedence--I think the money market directive expresses the intent of Roger and myself, I guess, even though I don't like its cosmetics. I'd rather have a sluggishly behaved aggregates directive.

CHAIRMAN BURNS. Gentlemen, let's have a show of hands. Those who would prefer a money market directive.

MR. ALTMANN. Five, Mr. Chairman.

CHAIRMAN BURNS. Those who would prefer a monetary aggregates directive.

MR. ALTMANN. Six, Mr. Chairman.

CHAIRMAN BURNS. Well, gentlemen, if I may, I would suggest we vote on the following: a monetary aggregates directive; an M1 growth range of 0 to 5; an M2 growth range of 3 to 8; and a federal funds rate range of 5-3/4 to 6-1/4, with the understanding that if we get into a high growth rate area, that the Chairman, as I believe he has done consistently, will continue to do his duty. Any--

MR. COLDWELL. Do you define this to mean above 5 percent for M1?

CHAIRMAN BURNS. Well, I don't want to be that precise, because the figures are never that precise, you see, but I don't think I have been tardy with any frequency at either end. And I don't want to be tied down any more rigidly, or have the Desk tied down to the tenth of a decimal.

MR. COLDWELL. I would prefer 6-1/2 [percent for the upper limit of the federal funds rate], Mr. Chairman. My count of the Committee would indicate that there was a majority in favor of that, but I guess you will find that out in a little bit.

CHAIRMAN BURNS. Well let me, let me. I don't think really we ought to be getting into the habit of dissenting on minutiae. I don't think it serves a constructive purpose. Let me have a show of hands, that is to say, I thought that the adjustment from 0 to 5 [for M1] was designed to accomplish what 5-3/4 to 6-1/2 [for the federal funds rate] would accomplish. I'm willing to continue this discussion, but I would counsel my colleagues to dissent only on matters of principle and not on minutiae. I don't think it helps.

VICE CHAIRMAN VOLCKER. I expressed a preference for 5-3/4 to 6-1/2, but I am perfectly satisfied with where we are, Mr. Chairman.

MR. GARDNER. My 6-1/2 was related to the 0 to 6, and I'm willing to go back [to] 6-1/4 at 0 to 5.

MR. MAYO. So was mine.

CHAIRMAN BURNS. Would you want me to test sentiment any further, or--apparently not, so let's call the roll.

MR. ALTMANN.

Chairman Burns	Yes
Vice Chairman Volcker	Yes
Governor Coldwell	Yes
Governor Gardner	Yes
President Guffey	Yes
Governor Jackson	Yes
Governor Lilly	Yes
President Mayo	Yes
President Morris	Yes
Governor Partee	Yes
President Roos	Yes
Governor Wallich	Yes

Unanimous, Mr. Chairman.

CHAIRMAN BURNS. Well now, we will finally break for luncheon, and then we have an--yes, we have to decide--let me find out about members of the Committee. Any of you have to get away very early? Would 2:30 leave us enough room for luncheon, or would you prefer 2:45?

MR. JACKSON. If we say 2:30, we will start at 2:45.

CHAIRMAN BURNS. We will reassemble at 2:30 then.

[Lunch recess]

[Executive session]

CHAIRMAN BURNS. Gentlemen, this is a meeting of the Committee in executive session. And we have a Freedom of Information [Act] [FOIA] item which Mr. O'Connell will describe to the Committee. Actually, he has prepared a memorandum which sets forth the facts, I think, quite fully. But I will call on Mr. O'Connell to summarize the question that is before us and give us his own best thought on the subject from a legal point of view, certainly. And any policy guidance that Mr. O'Connell may wish to give us would also be proper. Do you want to proceed Tom?

MR. O'CONNELL. Thank you, Mr. Chairman. The Chairman has put his finger on a very critical point, namely that I believe there is at stake here a policy question that will be discussed by you as members of the Committee. The legal issue can be framed very simply. The memorandum sets forth the occurrence that has brought the matter to the table today, namely, a request under the Freedom of Information Act by an editor of the *New York Times* seeking access to the Committee's 1972 Memoranda of Discussion. The request was initially denied, pursuant to the rules of the Committee, by the Secretary during the appeal period.

An appeal was filed by Mr. Herbers. That appeal was answered by Mr. Coldwell as the alternate for this purpose under the Committee's rules. His letter, as indicated in the attachment to the memorandum, came very close to a denial, and in a sense, of course, it was a denial, but [it] was couched in such words as to offer to Mr. Herbers the possibility that, having been advised of the Chairman's direction, this matter [would] be brought before the Committee. The Committee would give further consideration, looking for some possible altering of action to that reflected in the denial letter. That's the purpose of its being here today.

The issue is access under FOIA to the Memorandum of Discussion. The alternatives presented in [my] memorandum are quite straightforward. They are four in number, the fourth having an extension to it that I think bears some note. The first of these, as presented in the memo, indicates access to the world at large. It would constitute the Committee's action in releasing the '72 Memoranda of Discussion in a published form so that all media, all public, have simultaneous access, subject to deletions that would be made for sensitive foreign entries. This would, of course, offer the benefit that it wouldn't appear that we were favoring one arm or one single element of the media such as the *New York Times*.

The second alternative would be to give reading, or physical, access to the *New York Times* for whatever purpose they have in mind but not make a public release. The point I made earlier--this would be subject to the criticism that we have apparently favored one element of the media over another. But it also has the benefit that there wouldn't be wide publication of the fact that we had released the Memorandum [of Discussion] earlier than our standard five years. You know, the Committee has administered a rule of a five-year lag before release [of] the Memorandum.

The third alternative is probably the most generous--to use the term--of the alternatives, namely, the Committee could decide to release the 1972 Memoranda as well as all others now being held. That would be up through 1975 in collected form, and, as the Committee knows, there are three further Memoranda--the first three months of 1976--that have yet to be put in final release form, or a form as the other memos, but [that] could be done; all of those could be released prematurely of the five-year period, if the Committee [so] decided. This has the advantage, from a regulatory point of view, that it would obviate repeated demands for one year or another of the Memoranda. It has the disadvantage, of course, that, subject to the Committee's judgment, the closer you get to 1975 and '76, you are perhaps releasing entries, deliberations, and discussions of the Committee of a highly sensitive nature, causing the problem that gave rise to the five-year lag in the first place. My mentioning the five-year lag and the problems connected with it are not to be read as an argument for or against the five-year lag. I'm merely making factual observations that I think are of service to the Committee in its consideration of the matter.

With respect to alternative four, I note that there is an extension of that, and it's an extension of thought. If the Committee were, under alternative four, to decline to give any more than Governor Coldwell's letter now gives, namely, a denial of access at this time, and affirm that action, we could assume perhaps that Mr. Herbers would--his principal, the *New York Times*, would--litigate the matter, as [it] has a right to do under the Freedom of Information Act. At this time we have no evidence that such would take place. There is a suggestion, as a matter of fact, from conversations with Mr. Herbers, that they have no intention of suing, but the world being what it is, it's possible that an affirmation of denial by the Committee might trigger a contrary view.

If litigation were instituted under the Freedom of Information Act, the Committee has 30 days within which to respond to any complaint filed--to reply or otherwise plead. In that period, it is suggested in [my] memorandum that the Committee could have the issue involved again brought to its attention. If the Committee, to avoid further litigation, wished to alter its position then taken, there would be time, I believe, to proffer the Memoranda in question to the requesting party with a simultaneous suggestion that the lawsuit be dismissed and the entire matter compromised. This is, as I say, an extension of the denial. We could anticipate this might take place.

Mr. Chairman, those are the alternatives. You will note, I believe, [that] my memorandum doesn't come down on a legal recommendation, simply because I believe it is a policy consideration. I've pointed out the pros and cons of each in the memorandum, and I'd be glad to respond. I should say that Mr. Siciliano, from the Legal Division, whose name appears on the memorandum, works with the Freedom of Information Act and is present with your proper permission for purposes of this discussion. I think that's all I have at this time, Mr. Chairman.

CHAIRMAN BURNS. Thank you, Mr. O'Connell. I think before we start discussing the question, I want to make a few general comments. First of all, you may be interested in knowing that during the markup of the recent Federal Reserve Reform Act by the House Banking Committee, a suggestion was made by Congressman Hannaford to the effect that we return to the Memorandum of Discussion, which we had abandoned, and that a statute be adopted by the Congress which would protect this Committee from access to such a document or such Memoranda under the Freedom of Information Act. In other words, the statute or statutes would require that we return to the Memorandum of Discussion, that we release it after an interval of five years, and that this power be ours, all other statutes to the contrary notwithstanding.

Now, I wasn't present at the time of the markup. This was a new proposal. It had not been discussed previously among members of the [House] committee or with us, and the committee decided to postpone deliberations of it until members of the committee had had an opportunity to learn the Federal Reserve's view and crystallize their own thinking. I thought you ought to know about that, and I do not mean to suggest that we discuss this now. It isn't necessary to discuss it now. On the contrary, my suggestion is that we definitely not discuss it now. But I do [think] that it is [an] interesting proposal. If we had had the feeling of protection that we could go along as we had, we would not have, as a Committee, abandoned the Memorandum of Discussion. We did it only as a reaction to the judicial proceeding that has been started. So I think, before too long, we ought to discuss the Hannaford proposal.

My second suggestion to the Committee would be that we deal exclusively today with the *New York Times* proposal and not get into the question [of] whether there should be a release of Committee deliberations in years other than 1972; that we confine our discussion to the year 1972. In making that suggestion, I realize perfectly well that what we decide to do with regard to 1972 may have some implications to some degree with regard to later years. But I'm trying to be practical, and that is, I think that if we try to discuss not only the release of 1972 Memoranda, but also the Memoranda for later years, I think we'll have a very long and drawn-out discussion, and perhaps we want to do a little more deliberating. And we could return to that a month from now if the Committee so desires. But my suggestion would be that we confine ourselves to the request of the *New York Times* which relates solely to 1972.

Now I want to make two additional comments with regard to the request of the *New York Times*. I think we should recognize very explicitly that the five-year rule which the Committee adopted was not adopted in a moment of whim. It was not adopted capriciously. The rule may or may not be a good rule. It may or may not have been a good rule at the time it was adopted. It may or may not be a good rule today. But it was a rule adopted after thorough deliberation on the part of this Committee. That's point one, to keep carefully in mind.

Second, the rules adopted by this Committee are not adopted for all time. These rules are subject to change. But in considering a change in the rule, I think we ought to recognize very explicitly that a political dimension attaches to the request by the *New York Times*. And unless we recognize that and try to think clearly about that, we may not reach the sort of decision to which we always aspire, namely, a decision that is impartial, that is objective, that is not subject to political use or political abuse. That's all I want to say on the subject at this time. And I probably will have more to say later on. But now, perhaps, before we turn to a discussion, it might be desirable to put questions to Mr. O'Connell or possibly to me in so far as I'm capable of dealing with them. Mr. Kimbrel, you had a question, I believe.

MR. KIMBREL. Simply, Mr. Chairman, to the background environment in which this question comes. Is it one of openness and fairness or is it with some ulterior motive, or do you detect any--I guess a reading of the background from which it springs.

CHAIRMAN BURNS. Well, there is very little uncertainty about that. The request came originally--Joe, do you want to recite the history of that request, and then what the *New York Times* fellow did?

MR. COYNE. The request originally came from the New York financial desk. The editors there thought it would be a good idea to find out what the status of the 1972 minutes was. He had in mind the article [that] appeared in *Fortune*. So he asked the Washington bureau [of the *New York Times*]--that simple--to find out what the status of the minutes was. The reporter that was assigned to it was Bob Hershey. He drafted the letter; first he called us to find out what the procedures were. We told him what the procedure was, so he drafted the letter, which this gentlemen, Herbers, signed only because of his position as an editor at the Washington bureau.

The response went back. The request was denied originally. Hershey happened to be on vacation at the time, and when he returned, he found the denial there. He, at the time, was getting ready to transfer to London, where he is now. He was under pressure to do some kind of a column for the *Times*; this last week he happened to run into [former Federal Reserve] Governor Holland at church one Sunday and asked him about it, and then filed his appeal. He subsequently wrote a column on the subject, which did appear in the *Times* about a month or so ago, early July, and the *Times* seemed up to this point to have lost interest ever since that story appeared. But as Mr. O'Connell pointed out, although they indicated to me that they didn't want to pursue it any further, anything that happens could affect their decision. So it seemed to be just a perfectly legitimate inquiry which was satisfied.

MR. BALLES. Ball is in their court?

MR. COYNE. Not at the moment. I think that Governor Coldwell's letter has possibly held everything in abeyance.

MR. O'CONNELL. May I say from a perfectly legal point of view, it is in their court. They could move into court, reading that letter, if they wished, as a denial. I think it was couched so they would defer action, I think, awaiting further word from this Committee.

MR. MAYO. But if it is a dead issue, if they have no desire to revive it, is there anything that is scheduled to happen, or is it in their court--if they decide not to pursue the matter, will it just die?

MR. O'CONNELL. Well, if I may, Mr. Chairman, I'd suggest [that] the language of the second denial, or the appeal denial, would constitute a ground for them, reasonably anticipating some further word perhaps from the Committee. It's quite possible it would die if another word was never said. But I think the language of that letter suggests that this Committee would be deliberating it further.

MR. COLDWELL. I'd like to make a comment, Mr. Chairman, since I guess I'm the one who kind of moved this toward the Committee. When this was raised as to a question of denial, I had qualms about denying [release of] a five-year old document. But I didn't [see] that I had the authority to overrule the Committee's decision of a five-year rule. I talked to the Chairman and with Tom about it rather extensively, and then we drafted a letter of denial, and if I understand correctly, Mr. Siciliano, you talked with the Justice Department about the denial position.

MR. SICILIANO. That is correct.

MR. COLDWELL. And I wonder if you would mind acquainting the rest of the Committee with what Justice said to you.

MR. SICILIANO. The reason that we speak to the Justice Department is that there is a regulation under which the Department [of Justice] indicates that it will not defend an agency under a Freedom of Information Act suit unless, prior to [the agency's] taking final action, [the Department] has been consulted with respect to the agency action.

I called the appropriate individuals in the Justice Department before the final documents were presented to Governor Coldwell about continuing the denial recommendation. He basically indicated that while he agrees with our position that at least substantially all of the Memoranda are technically exempt under the Act, he feels that the Department cannot go along with the denial because denial would be inconsistent with the Department policy which dictates that an agency should release information unless disclosure would be harmful to some legitimate interest protected by the act. The Justice Department's view is that since the documents are approximately five years old, that no substantial harm would result [from] disclosure.

MR. COLDWELL. Well, this comment from Justice reinforced my hesitancy about a flat denial, and I suggested to the Chairman that we might want to raise this matter with the Committee because, at least interpreting Justice's position, it would seem that they're viewing a flat denial as being somewhat arbitrary in this five-year lag period.

MR. O'CONNELL. May I say, Mr. Chairman, that the consequence of an adverse position by the Department doesn't impact on the Committee's legal status to proceed exactly as the letter indicates. It merely means that the Department would not appear as our counsel should a suit be brought, at least if they kept their position as now stated. The Committee would have its own representation by counsel, and we would go forth with the defense if that suit was brought here.

MR. COLDWELL. But the fact would be well apparent in court that Justice was not there to defend us.

MR. O'CONNELL. Oh yes.

MR. GARDNER. Tom, when was the five-year rule adopted?

MR. O'CONNELL. Governor, I'd have to defer perhaps to Mr. Altmann. I'm not sure when this was.

MR. COLDWELL. 1970 [maybe].

MR. O'CONNELL. It was, I believe, in the early '70s, but I'm not sure of the exact date.

MR. COLDWELL. Very close to that anyway.

CHAIRMAN BURNS. I don't know the answer.

MR. O'CONNELL. I can find that out.

CHAIRMAN BURNS. Well, we don't need to find out. I mean it's been adopted some years ago.

MR. PARTEE. Some years ago.

MR. GARDNER. Prior to the five-year rule, what was the Board's procedure?

MR. PARTEE. Well, I think what we did was put out a number of them at one time.

MR. ALTMANN. That's right.

MR. PARTEE. And it had been a six-year lag, but that made it a five-year lag. And that they've communicated with you sensibly on the various things that could be deleted and so [forth].

VICE CHAIRMAN VOLCKER. I just would have guessed that it went back still earlier, that maybe it was just a change--six years to five.

MR. ALTMANN. I thought so. I would have guessed ’67, [because] they could be released to ’62, I think.

CHAIRMAN BURNS. I would have guessed that it was done before 1970.

MR. GUFFEY. Mr. Chairman, just a procedural question. Does this become moot as of January 1, 1978--do we release all of the ’72 minutes?

MR. O’CONNELL. Under the present schedule.

MR. GUFFEY. In other words, the December minutes of 1972, they’re only really four years old, is that correct?

MR. O’CONNELL. The December of ’72 are less than five [years old], but the difference between now--yes, about 4-1/2.

CHAIRMAN BURNS. It would be exactly five by then.

MR. O’CONNELL. Then it will. As of this date, it’s short of five, the December.

MR. COLDWELL. As of right now, seven months of minutes are five years old.

MR. O’CONNELL. That’s correct.

VICE CHAIRMAN VOLCKER. If you get technical about this, what is the Committee’s policy? Does it say generally after five years, or does it say January after?

CHAIRMAN BURNS. To the best of my knowledge, we’ve done it on a strictly uniform basis.

VICE CHAIRMAN VOLCKER. We’ve always done it in January.

CHAIRMAN BURNS. To the best of my knowledge.

MR. PARTEE. Shortly after the next coming year.

MR. O’CONNELL. The Chairman is correct. It’s been done on a collected basis. The entire year’s Memoranda have been gathered together--[with] the procedural aspect taking about a month--[the entire year is] thus [released in] January of the succeeding year following the five-year period.

MR. GUFFEY. Then the January minutes of 1972 are 5-1/2 years old now?

MR. O’CONNELL. By calendar date, that’s correct.

MR. GUFFEY. Is it not possible then to release part of the 1972 minutes and still comply with the five-year lag?

CHAIRMAN BURNS. The rule is not merely the language of the rule, but how the rule has been observed in practice for a good many years now. I think that's a fair interpretation.

MR. KIMBREL. Mr. Chairman, I guess that was pretty much the thrust of my original question. Is our relationship in this such that these people are just eager beaver to have them August 15, or are they willing to sit down and counsel a little bit with Mr. Coyne and wait for January or something--could ease off---or is there some real point they're trying to make. I guess what I'm saying is, if we want to maintain our orderly process of releasing them in January and that means something to us, can we sit down with them and say, "Well, you're going to get them in January--can you wait?"

MR. COYNE. I could be wrong, but I don't think the *Times* will take any further action.

MR. KIMBREL. That's what I guess I would--

MR. COYNE. Not likely.

MR. PARTEE. The letter said they'll get them in January.

MR. MAYO. Mr. Chairman, the ball, then, is in their court. Governor Coldwell said that he didn't have the authority unilaterally to take action without submitting it to this Committee. But does anyone know that this Committee is presently discussing this or that action is being taken? Does the *New York Times* know this?

MR. COLDWELL. The last paragraph of my letter says that--"However, in light of the possibility that the Committee decision on the question of near-term release, the requested Memoranda . . ."

CHAIRMAN BURNS. I think that Mr. Coldwell's letter must be followed up by another letter which will indicate this Committee's decision on the request.

MR. GARDNER. Mr. Broida discussed this matter with me when he first denied the request. The reason is, I'm another alternate for a Freedom of Information [Act] appeal. I formed an opinion at that time, a very firm opinion--after Roger discussing months, whether May [is] five years, or up from May, or for April--and the more I thought about it, the more I became convinced in my own mind that this Committee met as a body in 1972 with a general understanding that their Memoranda of Discussion would not be released and that therefore did not anticipate either the Freedom of Information Act or that the Memoranda of Discussion would be brought forward to be used for whatever purpose by media and otherwise except on a standard basis. And I think it's a disservice to the Committee, and I don't know how many of us were on that Committee. I know I wasn't in 1972. And I believe it's a disservice to that Committee to change our rule, and accordingly I'm going to vote for alternative four, Mr. O'Connell, if that's the one that you think I'm talking about.

MR. O'CONNELL. May I raise the procedural issue of the need for a formal vote? I think that a lack of a vote, or rather a consensus, might avoid an entry of an action vote on this matter, etcetera. Mr. Chairman, I'll defer to you on that.

CHAIRMAN BURNS. I think that Mr. O'Connell's legal opinion is perfect. I think it's a wise pronouncement, and I think we ought to strive for a consensus rather than engage in formal voting on this issue.

MR. LILLY. I have to take the opposite side from Steve. I feel very strongly that we are making a great deal out of nothing. There's nothing in the Memoranda, as I understand it, that is damaging to anybody; it's all old history. And [denial] just [attributes to] us the same attitude that we're accused of--being overly secretive for no real purpose. I would be very much in favor of giving permission. We're going to look very strange in court without the Justice Department representing us.

CHAIRMAN BURNS. As I understand Mr. O'Connell, he's indicated that if we do deny the request by the *New York Times* and if the *New York Times* should proceed to take judicial action, something that is quite uncertain at the present time, then at such a time we could reconsider. In other words, we might deny today. The *New York Times* might or might not go forward with a lawsuit. The informal indications are that there will be no lawsuit, but that may turn out to be a--

MR. LILLY. Why wouldn't--in other words, if we're forced right up against it, we might yield.

MR. PARTEE. Out of court.

MR. LILLY. Out of court. But why do we take that position? What is there damaging about releasing this now?

MR. MORRIS. Mr. Chairman, I think I see one thing that's damaging. I think on the basis of the memorandum that I read before I came to the meeting, I would have shared your position, but in light of this Hannaford amendment, it seems to me that if we voluntarily change our practice, that weakens our case for getting something like the Hannaford [proposal].

MR. LILLY. We have already changed our facts. We are defending a practice that we no longer follow.

CHAIRMAN BURNS. No, no we haven't changed the five-year rule.

MR. LILLY. No, but we no longer keep this kind of Memorandum, we no longer do that.

CHAIRMAN BURNS. I know, but the Hannaford amendment provides us with an opportunity to return to the Memorandum of Discussion if we so wished.

MR. O'CONNELL. And under that amendment, Governor, as the Chairman has indicated, there would be a provision, we hope, that precludes a suit under FOIA or demand--

MR. LILLY. I don't understand the purpose of the Hannaford amendment other than that it would provide more detail for some future historian.

CHAIRMAN BURNS. Well that is the purpose, and it's a purpose that this Committee in the past regarded very favorably.

MR. COLDWELL. Except, Mr. Chairman, I believe there's another element to the Hannaford amendment. That is that the minutes of the Committee will be made available promptly to the committee in Congress.

CHAIRMAN BURNS. Well, now, Mr. Hannaford has ideas in addition to the Memorandum. He not only has an idea with regard to the Memorandum of Discussion, he has all sorts of ideas, and undoubtedly, if we wanted to go forward with Mr. Hannaford's suggestion with regard to the Memorandum of Discussion, I think we might--I'd be surprised if we would not succeed in having him confine himself to that one suggestion. But that might or might not be the case. The fact that he has more than one idea merely means he's like the rest of us. He's got all kinds of ideas in his head.

MR. MAYO. We're not sure, sir, that the *Times* is even still worrying about this. We had a terribly lengthy meeting this morning. Wouldn't we have every reason in the world to say that we didn't get around to any decision on this. I just wonder what purpose we serve by being so totally conscientious that we act on this and get right back to them, when they might have let the whole matter drop.

MR. COLDWELL. The letter says that this will be raised at the meeting today.

MR. O'CONNELL. May I suggest, Mr. Chairman, that between the two positions is the possibility that Joe Coyne might be directed, subject to the Committee's judgment, to informally be in touch with them and visit with Mr. Herbers to indicate that a discussion by the Committee indicated a consensus to affirm the action announced in the Governor's letter, and that perhaps some future discussion would bring about a different result, but that was the general consensus now. It might then reveal what the attitude of the *New York Times* is, which would impel some further action by the Committee, and might put it at rest. It's an interim suggestion, Mr. Chairman.

MR. MAYO. I think that's a sound position, Mr. Chairman. I would also raise two points on the Hannaford amendment. First--just a political judgment, it probably isn't worth the price that you're paying for it--but such an amendment wouldn't get anywhere or would be twisted around in a way that a few of our friends in different parts of the Congress from Wisconsin have made it apparent that they were upset that we discontinued the Memorandum of Discussion and would like to have the names mentioned and so forth, particularly going back to five years for historical purposes. As we know, the people in question wrote to all of the, as far as I had heard, living ex-members of the Board of Governors and Bank Presidents to solicit their opinion on this subject, and as far as I know they failed to get any great resounding vote of confidence in the need for the Memorandum of Discussion.

So, on both of those grounds, I feel that the Hannaford amendment discussion here may not be productive of something that would be helpful to this Committee. Therefore, I would lend complete support to what Tom and Governor Gardner have suggested. Quite apart from my personal feelings that, as to the merits of [alternative] one versus [alternative] three, we can discuss that some other time.

MR. JACKSON. May I ask a question? First, I believe you characterize this as being politically inspired--partisan politically inspired. I'm not sure I understand what you mean by that.

CHAIRMAN BURNS. I don't think there's much of a mystery about this *New York Times* request. And the political dimension to me is perfectly obvious. The fact that you raised the question means that it's not obvious to you, and the same may be true of other members of the Committee, and perhaps, therefore, I ought to say a word about that to make at least my own meaning clear.

I believe that every now and then each of us reads one or another newspaper or listens to discussions over TV. And our journalists, our news commentators, finding a need to write or finding a need to talk, and there not being sufficient news on hand, have chosen to devote some of their energy to the question of whether the present Chairman of the Federal Reserve Board will or will not be reappointed by President Carter. So this question now and then is discussed by members of the press. That's point number one.

Point number two, there has been some speculation on the part of some journalists, some members of the Congress, some members of our general citizenry to the effect that in 1972, the Federal Open Market Committee, having as its Chairman a certain individual, was inclined to do what it could to promote the reelection of a certain gentlemen [named] Richard M. Nixon as President. So the political dimension here is, I think quite obvious--to get hold of the Memorandum of Discussion, to go through it and see whether that Memorandum of Discussion validates or repudiates that speculation. That is a political dimension. That was made quite clear in the article that, what's the fellow's name, Hershey--

MR. COYNE. Hershey.

CHAIRMAN BURNS. --[that] this *New York Times* fellow wrote for the *New York Times*. The article proved to be a completed dud. But it might not have been. But the political dimension goes further. Let me speak in a purely personal vein, since the political dimension happens to apply to the Committee as a whole, but primarily to me personally.

As far as I'm concerned personally, my cast of mind being what it is, I don't like to live with problems, I like to solve them, and to the extent that this is troublesome to anybody of suspicious--get the thing out, and there's nothing in that record that would concern me for one moment. Now, obviously any record can be interpreted one way or interpreted another way. Well, that's life, and that's the way books are read and articles are read.

But, you see, continuing in a personal vein, if the Committee decided to release these 1972 minutes, [let me say] why, quite apart from other reasons, I think it shouldn't be done. This could be interpreted as an effort on the part of the Chairman of that Committee to have that document in the open so that Mr. Carter and his henchmen in the White House will see that the Chairman's record in 1972 was an honorable record. I don't have to prove my personal honor. Now, whether I'm interested in what Mr. Carter wants to do about the Chairmanship, and what the Chairman himself wants to see happen, are things that no one in this room knows anything about. And no one is going to know until the time comes. But I would hate to see personally any such actions by the Committee interpreted as an attempt by the Chairman to throw this document into the public arena so that everyone would see that he has honorable credentials. I'm not looking for that and I don't think it's a good thing for this Committee to lend itself to what is so obviously, at least to me, a half-hearted political effort on the part of this or that individual in the *New York Times*. Well, that's the political dimension as I see it.

MR. JACKSON. Given that--and I appreciate your explanation because I wasn't aware of all the details you mentioned--but given that, should we not then consider whether or not the possibility of releasing all of the unreleased Memoranda could diminish any allegations that that was the motivation that you mentioned. In lieu of just the one you mentioned was under public discussion, release all of them.

CHAIRMAN BURNS. Well, this is something the Committee may or may not want to do. I think it's something we ought to deliberate on very closely. I would hate to see this Committee really change its rules in the kind of political environment that exists. Now, let's assume for the moment that the present Chairman seeks reappointment. That's an assumption. Let's make that assumption. Let's assume, next, that President Carter is concerned about the record in 1972. That's quite an assumption. There is not one ounce of evidence to indicate that. President Carter, if he wanted access to the Memoranda for 1972, if such a request came, I'd say we ought to telephone members of the Committee immediately with my recommendation that the President of the United States should have access, of course he should.

Now next, as far as the appointment of the next Chairman of the Federal Reserve is concerned, that is something that the President can do today, and that is something he may not do by February 1st. After all, he hasn't yet appointed the new director of the Federal Bureau of Investigation. And therefore, if the 1972 document were of interest to the President, let us say, and for the regular performance of his duties, he could have it immediately. Oh, and he'll certainly have it on January 1st.

MR. COLDWELL. Mr. Chairman, may I make a comment. What you've been saying is quite interesting in a theoretical vein to me, but the reason I brought this, and asked you to bring it, to the Committee has not yet been touched. And that is that times have changed, and we now have a Freedom of Information [Act] which requires the appeals officer of this Committee, whoever he may be, to rule on whether a particular document should be made available to the public. His ruling is to be not capricious or arbitrary but is to be grounded on good reasons for withholding from the public. I find myself in difficulty establishing good reasons to withhold this document after 5-1/2 years, except for the sheer decision of the Committee, which I think was an arbitrary decision in the first place--it could have been three years, it could have been six years.

CHAIRMAN BURNS. But it was a decision not reached capriciously, and if that rule is going to be changed, the next question is whether we have the right political environment for changing that decision right now. And as for your decision, you made your decision, you turned it down, which was within your power, and you referred it to this Committee--or rather, I referred it to the Committee, not you, following your suggestion, which I thought was a very proper one.

MR. PARTEE. I would say, I also am concerned about the arbitrariness of this. But let me be pragmatic, which I think Larry was trying to be earlier. If we can avoid a court suit in which we have to defend the arbitrary five years, we can avoid it. I don't really care how we avoid it. And so, if a discussion with the *New York Times* should lead to an indication that they would press this, fine. If they want to press it in court, I think the Committee has a fair amount to lose because this is exceedingly arbitrary. There is no telling what might flow from it in terms of court decisions.

MR. MORRIS. I want to say, shouldn't we wait until we find out whether they're going to sue?

MR. PARTEE. Well, that's what I said, that's the pragmatic way.

MR. MAYO. If there is reasonable doubt, let's find out first.

VICE CHAIRMAN VOLCKER. Well, this is a kind of delicate negotiation. It seems to me the worst of all positions is to let them take it to court and then we cave. If they take it to court, it seems to me we probably ought to fight it and see what happens, because we don't want the key to the kingdom being taken in case to court.

MR. ROOS. Why don't we do what Tom suggested, Mr. Chairman, and give Joe another shot at feeling them out, in effect. Seeing whether he can get any clear indication of whether or not they intend to take it to court before we make a decision in a vacuum.

MR. GARDNER. I think, more likely, that will inspire them to take it to court. Gentlemen, I want to make these points. When I considered this matter first with Mr. Broida, I did not consider it in the context of what the Chairman has just described. I thought about it a good deal. I want to also try to reinforce the point I made. Those of us who sit at this Board are fully experienced in the tyranny of a recorded meeting. And our meeting discussions are inhibited. Now during those FOMC meetings in '72, '73, '74, and '75, you had no such experience. You knew perhaps that your Memorandum of Discussion would be prepared and released five years later.

We sit here with a green light. I don't see it this morning--it inhibits us as a Board of Governors. We're fully subject to the [Government in the] Sunshine [Act], and my experience with the discussions that take place--and I have not reviewed those five years of minutes that will eventually become available--lead me to believe that the proper course of action is not to do a disservice to those who sat on those Committees over those years and spoke their minds with only the condition that they knew their thoughts might be fully disclosed five years later, and [so we should not] suddenly rush into court or rush into the *New York Times* with five years of FOMC discussion. Now--

MR. LILLY. Does five months' difference make--is it all that much difference?

CHAIRMAN BURNS. Yes, but that five months applies to the other way too. Why can't they have patience for another five months. Why? But they are going to get it by January, why can't they be patient? Why should we deviate from a rule that we've established, in a political environment that could lead to mischief as far as interpretation of this [Committee's] action is concerned.

MR. LILLY. In the first place, I think, I'll pick up Phil's remarks. I think times have changed since four years [and] seven months ago. We've had two very significant pieces of legislation that both say this is no longer appropriate, this keeping things for five years.

CHAIRMAN BURNS. Well, now, but your statement is inaccurate.

MR. LILLY. Well, we have [the] Sunshine in [the] Government [Act] and we have the Freedom of Information Act.

CHAIRMAN BURNS. Under the Freedom of Information Act, we've had one court decision, and according to that court decision, what the *New York Times* is entitled to is a fragmented document.

MR. LILLY. It is my understanding that the legal opinion now is that if we went to court, we would not have a good chance of winning this case.

CHAIRMAN BURNS. Well, I have not heard that legal opinion.

MR. LILLY. Is that correct, Tom?

MR. O'CONNELL. I believe that the Department's position could be fairly interpreted as saying that, Mr. Chairman.

CHAIRMAN BURNS. Well, I thought the Department's position was a matter of policy rather than a matter of law.

MR. O'CONNELL. Well, Steve can confirm this or not. I think in the discussion that took place, the Department took the position that it was likely that we would not succeed before a court of law, and it was [for] that reason they indicated they would not defend the position. Am I correct--

MR. SICILIANO. Well, I think to clarify, the Department's position was based on a number of rather bad experiences they had in litigation. The Department accepts our view [that] we have communicated to them, that the Memoranda are substantially exempt under the technical reading of the statute. I think our chances of succeeding in litigation to an acceptable degree are substantially impaired if we go into court without the Department. It's the court [that] will have to determine which portions of the Memoranda are reasonably segregable and therefore must be disclosed, and in doing that, it will have the Department's actions in mind.

MR. O'CONNELL. It also, Mr. Chairman, in due respect, has one decision on this matter out of District, and that's Judge Waddy, who, by his last order, required that the entire Memorandum be turned over to a Plaintiff, it being implicit in that order that he couldn't find that we're in [a] defensible position, by saying that we couldn't reasonably segregate that. His order is read that way, we compromised that, reached a settlement, and never had to follow that order. His last issue said, "Turn over the entire Memorandum, I will not go along with your segregation of facts," which ended up looking like Swiss cheese as we gave it to the plaintiff.

MR. PARTEE. And that's really quite recently--

MR. O'CONNELL. That was what--

MR. PARTEE. Quite recently--

MR. O'CONNELL. Yes, that was '75.

MR. GARDNER. In case my remarks are misunderstood, I want to add this addendum. We are fully complying with Sunshine and Freedom of Information at this Board, but we know what the rules are, and we're living under those rules. And my position is based on the fact that the FOMC didn't know it was living under those rules five years ago. Or three years ago. Or two years ago. I'm not trying to avoid the effect of Sunshine or Freedom of Information, I'm simply pointing out that we're now dealing with a post-operative situation, a situation that occurred when the FOMC had no idea they were subject to those rules.

MR. PARTEE. Well, Steve, if I might, the FOMC in 1972 did not know there would be five years for sure before the Memorandum of Discussion was released. We had discussions in that period. The Chairman remembers that, and we didn't know whether five years or, well, three years; the decision was made to take five and try it awhile. There was a sense of movement, I think.

CHAIRMAN BURNS. Well, that I can't say. My own recollection may easily be imperfect. I believe that the five-year rule was in effect at the time I joined the System. The Memorandum of Discussion was discussed from time to time informally within the System; the only formal discussion that I can recall on the part of this Committee of the Memorandum of Discussion in [regard to] the five-year rule arose out of the lawsuit that came from this outfit in Georgetown.

MR. O'CONNELL. The Merrill suit.

MR. JACKSON. May I ask a question. We've recently had some congressional requests for Reserve Bank minutes and forecasts. Is it our counsel's judgment that a congressional request for these memoranda will be properly and successfully refused?

MR. O'CONNELL. No, sir, it is not. There is a specific provision in the Freedom of Information Act, Governor, that exempts Congress from that act, the provisions of the Freedom of Information Act, so that neither the law nor exemptions apply to any of the requests from Congress.

MR. JACKSON. Considering our very unhappy recent experience, is it your judgment that it's possible the *Times* could ask certain well-known members of Congress to request these for their own judgment if they were refused by us? I'm not trying to urge them to do so, far from it. I'm trying to uncover the realistic alternatives that might arise on how to [unintelligible] on our part. We seem to have had so many other people effectively communicating with the Congress their wishes and desires.

CHAIRMAN BURNS. Now, I think there can only be one answer to your question--of course that could happen. But I think that this comment of yours [should] be placed in context. We have outstanding three requests from Mr. Reuss, which as yet have not been granted. One request is that the 28 items that were deleted from the--28 out of some 500 or 600 deletions--28 items that Mr. Reuss, out of some 900, wanted us to disclose. And that request has not yet been granted.

Number two, Mr. Reuss has made a request that the minutes of District Bank boards for three additional years be made available to him. That request has not yet been granted. Number three, Mr. Reuss has requested that [Federal Reserve] Board minutes for the past six years or thereabouts be made available to him, and that request has not yet been granted. Not only that, but a letter will go to Mr. Reuss indicating that these are matters that cause great difficulty and that I want to go over these problems with him once again.

Now my point is that we've not acceded very lightly, at least as far as I'm concerned--protecting the System to the best of my ability and drawing on the advice of my colleagues constantly; and we're not going to accede quickly or easily. In other words, if we acceded to such a congressional request--pure fishing expedition--the next thing may be a request for all interoffice memoranda, the next would be for all incoming and outgoing correspondence with regard to the Board, with regard to the Banks, and therefore, Mr. Reuss who has abused the documents that were sent him, the minutes for the first three years, is not going to get additional documents quickly or easily. I wanted to bring out these facts in relation to your specific comment. Well, gentlemen, any additional view on this?

VICE CHAIRMAN VOLCKER. Well, I don't know how we bring this to a conclusion, Mr. Chairman.

CHAIRMAN BURNS. Well, we have to seek the consensus.

VICE CHAIRMAN VOLCKER. Well, we seem to have been going off into different directions. My own feeling, I think, is pretty close to that expressed by Mr. Lilly, that it's so close to five years that we can both defend the general five-year policy and release them in the next few months sometime--at the mutual convenience of the *New York Times*. But I think we have to take very seriously your own feeling and argument. I would think the interpretation could be put the other way, that we were trying to cover up something. But I can understand the interpretation you put on, and I'm not prepared to say we should push and release the thing if you feel strongly the other way.

CHAIRMAN BURNS. I will answer that, the other interpretation could be put on it, but as far as that other interpretation is concerned, that other interpretation involves two individuals primarily, the President and myself. And I've already covered the President's part. I'm not going to cover my own. Now, as far as my feelings are concerned, from a purely personal viewpoint, I would want to get this out of the way and let's stop the nonsense. But I think for us to permit ourselves to be driven by the winds of political controversy, for us to depart from a rule simply because of a whim on the part of this or that newspaperman, for us to change a rule in the kind of political setting that exists would be extremely unwise.

MR. JACKSON. Frankly, Mr. Chairman, I think my personal conclusion is that we should not release the document currently. However, I think we should give serious thought to not only releasing 1972 but all the other unreleased Memoranda in January 1978.

CHAIRMAN BURNS. Well, I think we ought to consider that, but I do think that there is some great force in Governor Gardner's observation. And we ought not to abandon a long standing rule lightly just because there happens to be an environment right now for disclosure of this, disclosure of that. The present environment, I think, is going to change. Because some damage is being done by the kind of suspicion that is being generated, so that people no longer trust one another the way they used to. And I think we've reached a point in our political society where there'll be a revulsion of feeling against excessive disclosure. And after all, you know, as far as we're concerned, we disclose all of our doings, but with certain lags that we think serve the purpose of uninhibited discussion and that do not affect markets to the disadvantage of this or that group in the economy. Well, gentlemen, this is your decision and--

MR. LILLY. Could I ask one thing more. I would be concerned if we looked like we were trying to put this information out on a defensive basis. However, the record is very clear that we are very reluctant to put this information out and it's only after [unintelligible]. I don't think anybody could accuse us of rushing out there with the minutes to prove--

CHAIRMAN BURNS. Well, let's not make pronouncements about anybody accusing us or not accusing us. We live in a political world where anything at all might happen in the way of accusations.

MR. COLDWELL. Mr. Chairman, I think the final gun has to come down on this as to whether you need to release this information under the Freedom of Information Act request. We may not like the request. We may think that it is politically motivated, but nevertheless it is a request under a law of Congress, and if we're going to stand pat, then I think we run a risk of being overturned in court. If we are overturned in court, we run greater risks.

CHAIRMAN BURNS. Well, there is first the uncertainty about being sued. Second, if we were to turn this down, there is the possibility of changing our view after legal proceedings are started, and that is something that is done all the time in the practical world. There is, third, the possibility of fighting this in a court of law. And the real question before us is what we decide to do today. We're not going to act on the Hannaford amendment. I think that's clear. I think it would be unwise to act on minutes or Memoranda of Discussion for years other than 1972. I think we have been focusing primarily, and I think correctly, on the request for the 1972 Memoranda. Now let's have a show of hands now whether we want to grant the *New York Times* request or not.

MR. WALLICH. I wonder if I could ask that to put that in a somewhat different context than yes or no, because there are things in between. You mentioned one just now yourself. That is, wait and see whether we're sued, and then decide whether to settle.

CHAIRMAN BURNS. We have to follow up the letter that Mr. Coldwell sent, and we have to indicate whether this Committee--you see, Mr. Coldwell's letter referred to the request being submitted to this Committee for action. And therefore we have to inform the *New York Times* whether this Committee is granting the request for the 1972 Memoranda or is denying it. In other words, whether it is confirming Mr. Coldwell's decision or is granting the request.

MR. PARTEE. The consensus of the Committee is that we should not depart from the rule.

CHAIRMAN BURNS. Well, that's up to the Committee.

MR. MAYO. Well, it's alternative four we're voting on here.

CHAIRMAN BURNS. Well, I hope we don't vote. I think we ought to arrive at a consensus.

MR. MAYO. It's alternative four on which we're expressing ourselves.

MR. O'CONNELL. Mr. Chairman, may I be presumptuous to suggest one further alternative, and I think you would want me to mention [it]. Governor Coldwell's letter mentioned the fact that, under the law, the seeking party is entitled to have reasonable segregable facts but that it was the judgment of the writer, Governor Coldwell, that if such were undertaken and were done, he would be given such a useless wheel-spinning document that it wouldn't serve his purpose.

Mr. Chairman, there is an administrative burden involved in this; the staff, though, could accomplish this in a reasonable period of time. Is it possible that you and the Committee would want to advise the *New York Times* that we are willing to undertake a segregation of facts and present to you segregated facts, in the possibility the *Times* would say, forget the whole thing, we don't want segregated facts; which would be short of being confronted and a denial. [The *Times*] is entitled to that by law. We might re-offer this as a reasonable next step and have [them] be the part who say no, forget it, let's call it quits, we're finished.

MR. COLDWELL. Well, we already offered that to him, Tom. In fact, we recognize in the letter that he was entitled to it.

MR. O'CONNELL. But we reached, really, if I may Governor, the judgment that that letter reaches the decision, and thus we've decided not to do this.

MR. LILLY. We said that any segregated portion of the Memoranda would be [so] fragmented as to be unintelligible and virtually useless to use.

MR. COLDWELL. That's all we said.

MR. O'CONNELL. We had a plaintiff in the Merrill suit who was told the same thing and didn't believe us and pushed us for it and finally accepted it in settlement. So it's possible that, but for the purpose of the *Times*, who want to do an article, presumably our description was correct. I bring that up, Mr. Chairman, only as a--

MR. PARTEE. I think 72 facts should not be worth very much.

VICE CHAIRMAN VOLCKER. Does that letter say that he will get it in January? Does it pin it down to January?

MR. COLDWELL. No, it says--now, let's see: "I would note that, pursuant to the Committee to stay with scheduled public release, the Memoranda of 1972 will be available to you in January 1978." He is already advised on that.

CHAIRMAN BURNS. Well, he could be advised more specifically. It will be available January 1, so that they can spend New Year's Day--we might give it to them New Year's Eve, let them celebrate New Year's Eve.

MR. MAYO. If they want to use it for political mischief, Mr. Chairman, January would be an ideal time for them to have it anyway.

CHAIRMAN BURNS. Well, I don't really know whether they want to use it for political mischief or not. All that I know is that this fellow Hershey, who did want to use it for what I interpret--and I think that Joe will join me in that interpretation--has mischief of some sort, political or otherwise.

MR. JACKSON. It appears to me, Mr. Chairman, that it's my personal judgment that our best course of action would be to deny this request but at the same time advise that we will release all Memoranda in January unpublished as to now.

CHAIRMAN BURNS. Well, but, I think--

MR. JACKSON. Because I think that does two things: Number one, that does eliminate any inference that we are protecting this situation for improper purposes. But at the same time, I think it pushes this organization to the type of posture where our alleged secrecy, [unintelligible], of manipulating the strings of the world, is exploded and done away with once and for all.

CHAIRMAN BURNS. Well, it's a possible course of action, but I doubt that we ought to, at this late hour, reach any such decision without the most careful deliberation and without taking into account and appraising the Hannaford possibility. Now this may well be a decision that, after we spend a morning or a day on this whole question, a month from now perhaps, we may want to reach that decision. I, for one, I don't feel ready to reach the decision to release all of those and to throw away--I wouldn't want to throw away so quickly the Hannaford possibility.

If that Hannaford possibility had been open to us at the time when we were debating the desirability of continuing or dropping the Memorandum of Discussion, I have little doubt as to how the Committee would have acted at that time. Some of us were--I remember you, Mr. Baughman, were very eloquent on the desirability of getting rid of it. But I didn't gauge the sentiment of the Committee as a whole being that at the time, and I think certainly the majority of the Committee would have voted for the retention of the Memorandum of Discussion if we had the Hannaford protection at that time.

MR. PARTEE. If we could count on it. Things have changed so much since we made that decision, and now I would [not] put that much confidence in it.

CHAIRMAN BURNS. Well, I think that's fair.

MR. MORRIS. Well, Mr. Chairman, I think we are probably ready for some kind of consensus.

CHAIRMAN BURNS. Some kind of what?

MR. MORRIS. Consensus motion. I think several of us have to catch airplanes.

CHAIRMAN BURNS. Well, will someone make a motion, whatever it may be, and we'll--

MR. GARDNER. I made a motion earlier. I will revise that and say I urge the Committee to adopt a consensus that's generally consistent with [alternative] four--

CHAIRMAN BURNS. Well, without voting formally, can we have a show of hands indicating whether or not such a consensus exists.

MR. PARTEE. Generally consistent with what?

VICE CHAIRMAN VOLCKER. [Alternative] four.

CHAIRMAN BURNS. Members of the Committee only, yes

MR. ALTMANN. Seven. There are only 11 members present, Mr. Chairman.

CHAIRMAN BURNS. Well, I think I have to interpret that as a clear majority. I have to interpret that as the closest consensus that we could get out of this meeting. Let me just check; those who are opposed to Mr. Gardner's motion will raise their hands.

MR. ALTMANN. Three, Mr. Chairman

CHAIRMAN BURNS. Three, well--

MR. WALLICH. This is without prejudice to further consideration.

MR. PARTEE. I'm sure not going to vote on that side if they sue us.

MR. COLDWELL. May I presume then, Mr. Chairman, that either you or I will write a letter to Mr. [Herbers]?

CHAIRMAN BURNS. Well, I think I should write that letter. Anything else to come up?

MR. GARDNER. Yes, but you don't want to bring it up--agricultural credit, farm credit, use of the discount window.

END OF MEETING