FEDERAL RESERVE press release

For Use at 4:30 p.m. December 24, 1992

The Federal Reserve Board and the Federal Open Market Committee today released the attached record of policy actions taken by the Federal Open Market Committee at its meeting on November 17, 1992.

The record for each meeting of the Committee is made available a few days after the next regularly scheduled meeting and subsequently is published in the Federal Reserve Bulletin and the Board's Annual Report. The summary description of economic and financial conditions contained in each record is based solely on the information that was available to the Committee at the time of the meeting.

Attachment

RECORD OF POLICY ACTIONS OF THE FEDERAL OPEN MARKET COMMITTEE

Meeting Held on November 17, 1992

1. Domestic policy directive

The information reviewed at this meeting suggested that economic activity had been expanding at a moderate pace. Consumer spending had picked up somewhat, business purchases of capital equipment continued to rise at a brisk pace, and housing demand had increased moderately since midyear. At the same time, part of these demands were being met through higher imports, and recent gains in industrial production and employment had been limited. Incoming data on wages and prices had been mixed but suggested on balance a continuing trend toward lower inflation.

Total nonfarm payroll employment rose slightly in October after declining in August and September. Substantial job gains were recorded in the services industries, especially in health services and the cyclically sensitive business services, and employment in construction rebounded from a September decline. In manufacturing, the number of jobs declined further in October, although total hours worked were unchanged as the drop in employment was offset by an increase in overtime. Government employment continued to contract, reflecting the end of a federally funded summer jobs program and early retirements by postal workers. Initial claims fell somewhat during October, and the civilian unemployment rate edged down to 7.4 percent.

Industrial production rose somewhat further in October following a modest increase in the third quarter. Much of the October gain reflected a sharp rise in light truck assemblies, but there was another sizable advance in the manufacture of office and computing equipment. Elsewhere, the production of consumer goods other than motor vehicles and parts had changed little in recent months, and the output of defense and space equipment remained on a downward trend in October. Utilization of industrial capacity edged higher in October but was still near its 1991 low.

Retail sales increased appreciably in September and October, led by a substantial rise in sales at automotive dealers. Sales at general merchandisers, apparel outlets, furniture and appliance stores, and building materials and supplies centers also were up noticeably over the two months. Housing starts rose significantly in August and then edged up further in September to their highest level since March. Sales of new homes had increased on balance over recent months, and the inventory of new homes for sale in September had reached its lowest level since 1983.

Real outlays for producers' durable equipment posted another strong increase in the third quarter. A sharp advance in outlays for computing equipment outweighed a dropoff in aircraft purchases from an unsustainably high level in the second quarter. Purchases of items other than aircraft and computing equipment rose at a rapid rate in the third quarter, and recent data on orders for such goods pointed to additional growth in the near term. Expenditures for nonresidential construction, which had fluctuated within a narrow range earlier in the year, dropped sharply in the third quarter. Office construction registered the largest decline, but other commercial and industrial building also fell considerably.

Business inventories rose only slightly in September, but over the third quarter as a whole stocks grew at the same rate as in the second quarter. In manufacturing, stocks were drawn down in September, retracing a sizable portion of the runup that had occurred in August. In most manufacturing industries, inventory-to-shipments ratios in September were at or near the bottom of their recent ranges. Wholesale inventories rose modestly in the third quarter, and the stocks-to-sales ratio in September was at the low end of the range posted over the past year. At the retail level, inventories rebounded in September from an August decline, leaving the inventory-to-sales ratio for the retail sector unchanged from the second quarter.

The nominal U.S. merchandise trade deficit widened sharply in August; for July and August combined, the deficit was somewhat larger than its average rate in the second quarter. The value of exports was little changed from the second quarter, but the value of imports increased appreciably. Most of the increase in imports was in capital goods, especially computers, and consumer goods. Recent indicators suggested that economic activity in the major foreign industrial countries had remained sluggish in the third quarter. A recovery seemed to have gotten under way in Canada, but the economies of most European countries and Japan evidenced little if any forward impetus, and the downturn that began in western Germany in the second quarter appeared to have persisted into the third quarter.

Producer prices of finished goods edged up in October, reflecing a slight increase in food prices and a further sharp advance in prices of energy products. Excluding the finished food and energy components, producer prices declined slightly, and for the twelve-month period ended in October, this measure of prices increased considerably less than it had in the comparable year-earlier period. At the consumer level, prices of nonfood, non-energy goods and services advanced more rapidly in October than in other any month since March. Over the twelve months ended in October, however, the rise in this index of consumer prices was considerably smaller than that recorded in the year-earlier period. Increases in labor costs, measured by the total hourly compensation of private industry workers, slowed further in the third quarter, and both the wage and benefits components of this index had increased substantially less over the four quarters that ended in September than in the preceding four quarters.

At its meeting on October 6, the Committee adopted a directive that called for maintaining the existing degree of pressure on reserve positions and that included a marked bias toward possible easing during the intermeeting period. Accordingly, the directive indicated that in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might be acceptable or slightly lesser reserve restraint would be acceptable during the intermeeting period. The contemplated reserve conditions were expected to be consistent with growth in M2 and M3 at annual rates of about 2 percent and 1 percent respectively over the three-month period from September through December.

Open market operations during the intermeeting period were directed toward maintaining the existing degree of pressure on reserve positions. The emergence of more favorable indications regarding the performance of the economy and the continued more rapid expansion of money and credit were seen as obviating the need to implement an easing in reserve conditions that had been contemplated as a strong possibility under the directive issued at the October 6 meeting. Several small technical decreases were made during the intermeeting period to expected levels of adjustment plus seasonal borrowing to reflect the usual pattern of diminishing needs for seasonal credit. Actual borrowing averaged close to expected levels over the three reserve maintenance periods completed since the October meeting. Early in the intermeeting period, the federal funds rate exhibited some of the firmness that had prevailed over most of the previous period, but subsequently it averaged close to expected levels.

Most other interest rates increased appreciably over the intermeeting period. At the beginning of the period, rates generally incorporated an expected near-term easing of monetary policy. Subsequently, when an easing move was not forthcoming and when concerns about fiscal stimulus increased amid some signs of firmer economic activity and increasing money and credit demands, market interest rates rose for all maturities. The largest increases were in intermediate maturities, which were especially affected by expectations of additional federal borrowing and of a stronger economy that would stimulate rising private credit demands over the next few years. Expectations of firmer economic growth also boosted stock prices appreciably over the period.

With interest rates rising in the United States and falling abroad, the trade-weighted value of the dollar in terms of the other G-10 currencies rose very substantially over the intermeeting period. Declines in interest rates in foreign countries were widespread, reflecting signs of greater economic weakness as well as actual or prospective easing in monetary policies abroad. The dollar was particularly robust against European currencies but advanced only moderately against the yen.

M2 growth strengthened somewhat in October from its pace in the two previous months. The acceleration of M2 growth reflected more rapid expansion of its transaction components that appeared to be associated in part with the lagged effect of earlier declines in market interest rates and opportunity costs and the heavy pace of mortgage refinancing activity. M3 grew more slowly in October partly owing to reduced needs for managed liabilities in conjunction with somewhat weaker expansion in bank credit. Through October, both broad aggregates were estimated to have grown at rates a little below the lower ends of the ranges established for the year by the Committee.

The staff projection prepared for this meeting suggested a continuing expansion in economic activity. Growth was expected to pick up gradually over 1993 to a rate that, although quite moderate by past cyclical standards, would be sufficient to reduce the margins of unemployed labor and captial resources. The recent backup in long-term interest rates and the appreciation of the dollar in foreign exchange markets would exert some restraining influence over the next several quarters. Continuing cautiousness on the part of consumers facing uncertain job and income prospects would tend to hold down gains in consumption for some period ahead. But, as further progress was made in improving household balance sheets and employment growth gradually resumed, consumer spending would strengthen. Additional gains in outlays for business equipment were expected over coming quarters as firms sought to meet increasing demand for goods and to respond to competitive pressures by modernizing product lines and achieving labor-cost savings. The projection pointed to sluggish export demand in light of sustained economic weakness abroad. While recognizing the possibility of a stimulative fiscal initiative in 1993, the staff retained for this forecast the assumption employed in several previous forecasts that fiscal policy would remain mildly restrictive owing in large part to a substantial decline in defense spending. The persisting slack in resource utilization over the forecast horizon was expected to be associated with additional progress in reducing inflation.

In the Committee's discussion of current and prospective economic developments, the members indicated that they were encouraged by the somewhat more positive tone in the latest economic reports and by the signs of improving business and consumer confidence. The expansion appeared to have gathered somewhat more upward momentum than many had anticipated earlier, though a number of members commented that relatively slow economic growth was likely to persist over the nearer term. The outlook beyond the next quarter or two was subject to considerable uncertainty and indeed to both upside and downside risks. The advent of a new Administration and a new Congress early next year made fiscal policy especially hard to predict. Members observed that indications of some improvement in overall domestic demands, should they persist, might well generate considerable strengthening in production activity as businesses attempted to maintain or build up their currently lean inventories. On the other hand, the recent appreciation of the dollar and the signs of growing weakness in major foreign economies could have adverse implications for demands for goods produced in the United States. On balance, moderate but sustained growth in overall economic activity was seen as a likely prospect, though the gains probably would be uneven both in terms of their timing and the sectors of the economy that would be affected. Against this background, the members generally continued to view further progress toward price stability as a reasonable expectation and an important element in enabling the expansion to be sustained.

In their review of developments in key sectors of the economy, the members generally agreed that while the evidence of a strengthening business expansion was still quite limited and much of it was still anecdotal, there were growing indications of improving business and consumer confidence. Some members cautioned that changing attitudes alone could not be relied on as harbingers of a more satisfactory economic performance, as experience in recent years made clear, but the improved financial condition of many business firms, households, and lending institutions provided a further basis for optimism. A good deal of progress already had been made toward reducing debt burdens, and the retarding effects of balance sheet adjustments on current spending seemed likely to lessen over the forecast horizon. Moreover, despite many lingering problems, the general health of the banking industry had improved markedly and there were spreading reports of greater efforts by banks to find credit-worthy borrowers. At the same time, the members saw signs that demands for bank loans might be picking up a bit from very depressed levels.

The latest data on retail sales and anecdotal reports from many parts of the country suggested some improvement in consumer spending. There were widespread reports of increasing optimism among retailers regarding the outlook for sales during the holiday season. Sales of automobiles and trucks appeared to be rising. The members nonetheless generally continued to view the outlook for consumer spending with considerable caution. Consumers remained concerned about job prospects against the background of continuing downsizing and restructuring activities by many business firms. Ongoing efforts to reduce debt burdens also seemed to be exerting a retarding effect on consumer spending. Against this background, the upturn in consumer confidence indicated by a recent survey could prove to be relatively fragile and short-lived. On balance, a strengthening trend in consumer spending, though to a relatively moderate pace by past business recovery standards, was still expected to provide major support for a sustained economic expansion.

Since the stimulus from the consumer sector coincided with relatively lean inventories, its effects might well be reinforced for a time by business efforts to build their inventories. Business spending for equipment also appeared likely to remain fairly robust, given a moderate expansion in sales and the improving financial condition of many businesses. The housing sector was viewed as another potential, though limited, source of stimulus over the forecast horizon. There were reports of improving home sales and home construction activity in many parts of the country, including some otherwise depressed areas, and many business contacts also were seeing better demand for construction materials and home furnishings. On the negative side, nonresidential construction remained weak across much of the nation, and further reductions in construction activity were likely as major projects were completed. However, nonresidential construction was being maintained or even trending higher in a few areas and appeared to have bottomed out in others. The rise in natural gas prices had spurred drilling activity in recent months, but some members commented that the outlook for significant further gains in that industry was not promising.

Many of the members stressed that the external sector constituted a major source of downside risk for the economy. The economic prospects for major foreign economies appeared to have deteriorated recently, and given the appreciation of the dollar, net exports might well worsen further over the next several quarters. The possible failure of ongoing trade negotiations would further dampen the outlook for U.S. trade. For the present, anecdotal reports from around the country on export sales were mixed, with such sales still well maintained in some industries and areas but slowing in others.

The outlook for fiscal policy constituted a major source of uncertainty; while the enactment of some fiscal policy measures now appeared to be increasingly likely, there was no reliable way to predict their overall size, specific provisions, or the timing of their effects. For now, the downtrend in federal government purchases of goods and services constituted a sizable negative in the forecast of aggregate demands. In particular, the cutbacks in defense expenditures were having a major effect on local economies in several parts of the country. Any new fiscal initiatives might well contain some stimulative elements designed to provide a boost to a relatively slow economic expansion. However, the delays usually encountered in enacting such legislation together with the subsequent lags before much of the effects was felt in the economy implied continued fiscal drag during the quarters immediately ahead; moreover, the propensity for financial markets to raise interest rates in anticipation of fiscal policy stimulus might also damp spending for some period. Some members saw a risk that much of the fiscal stimulus would be felt at a time when economic activity might already be gaining considerable momentum.

Turning to the outlook for inflation, members commented that despite a disappointing report on consumer prices for October, the disinflationary trend still appeared to be well established. In the view of most members, the outlook for relatively subdued pressures on resources over the forecast horizon together with the slow growth over an extended period in broad measures of money augured well for further progress toward price stability. Members were continuing to observe strong competitive pressures in local markets, and business contacts were still emphasizing the stout resistance that they encountered when they tried to raise prices to widen profit margins or to pass along rising costs. Most businessmen currently saw and anticipated little or no inflation in their own industries. Consumers also remained highly price conscious. At the same time, however, there seemed to be a widespread view in the business community and among consumers that at some point the rate of inflation was likely to rise appreciably from its recent level, and such expectations tended to have adverse repercussions in long-term debt markets and to create tensions in wage negotiations and other price-setting activities. Members noted that current inflationary expectations had been built up over a period of many years and an extended period of reduced inflation probably would be required before they disappeared.

At this meeting, the Committee had a preliminary discussion of the ranges for monetary growth in 1993 that it had established on a tentative basis at the meeting on June 30-July 1, 1992. The ranges in question had been set at 2-1/2 to 6-1/2 percent for M2 and 1 to 5 percent for M3 and were unchanged from those adopted for 1992. While there had been considerable sentiment at midyear in favor of lowering the ranges, a majority of the members had concluded then that uncertainties about the prospective relationship between the monetary aggregates and nominal spending argued for caution in making any changes. The information since midyear had confirmed the persistence of sizable increases in the velocity of M2 and M3. A recent staff study had provided some reasons for this unusual behavior, and staff analysis pointed to a strong probability that velocity would rise again next year.

During the discussion, the members generally agreed that developments since mid-1992 had reinforced the case for some reduction in the 1993 range for M2, and they indicated that they probably would support proposals for a lower range. Such a reduction would be a technical adjustment intended to take account of the atypical strength in velocity. Some noted that a lower range also would be seen as underscoring the desire of the Committee to avoid any pickup in inflation should the expansion gain momentum and indeed as promoting further progress move toward price stability, thereby establishing a sounder basis for sustained growth in the economy at its highest potential. The ranges would be voted on in February prior to their scheduled announcement to Congress, and by that time more information would be available to gauge the prospective behavior of M2 during 1993.

In the Committee's discussion of policy for the intermeeting period ahead, a majority of the members indicated a preference for maintaining unchanged conditions in reserve markets, but several others believed that some easing would be a more appropriate policy. Members who supported a steady policy course emphasized the growing if still tentative indications of a strengthening economy--including the pickup in money and credit growth--and the apparent upturn in business and consumer confidence. Some also cited the increased prospects of fiscal policy measures that were likely to provide some net stimulus to the economy over the intermediate term. Members who preferred to ease monetary policy at this time referred to what they viewed as an unsatisfactory outlook for economic activity, and some stressed the desirability of taking prompt action to promote sustained growth in the broader monetary aggregates within the Committee's ranges. Members who favored an immediate easing also endorsed coupling such a policy move with a reduction at this time in the tentative M2 range for 1993 in order to emphasize the Committee's commitment to noninflationary economic growth.

In the course of the discussion, the members took account of a staff analysis that suggested some moderation in the growth of M2 over the remainder of the year, assuming unchanged conditions in reserve markets. While M2 growth on a quarterly average basis was expected to be stronger in the current quarter than in the previous two quarters, expansion for the year as a whole was still projected to fall a little below the Committee's annual range. Some members commented that an important policy objective would be to prevent M2 growth from faltering--such a development might parallel a similar pause in the economy--as it had earlier in the current expansion. On the other hand, some members noted the persisting increases in M2 velocity. They remarked that the level of short-term interest rates together with the very rapid expansion in M1 and reserves pointed to an adequate availability of liquidity in the economy and thus suggested that current monetary policy already was appropriately stimulative and properly positioned to support the projected strengthening in economic activity. Indeed, in one view continued rapid expansion in the narrrow measures of money and reserves, if allowed to continue, would be a matter of increasing concern with respect to the longer-run implications for inflation.

In the Committee's discussion of possible adjustments to policy during the intermeeting period, many of the members expressed a preference for a directive that did not bias potential adjustments in either direction. In this view, the expansion was on a reasonably solid footing, the risks to the expansion were now fairly evenly balanced, and a steady policy course should be maintained in the absence of unanticipated developments with significant implications for the economic outlook. Other members, while encouraged by recent economic developments, wanted to bias the directive toward ease, though without the strong presumption of some potential easing that had been associated with the previous directive. They observed that the economy was still expanding at a relatively subdued pace, inflation was on a downward track, and given the earlier tendency for the recovery to weaken, they believed that the Committee should react relatively promptly to indications, including any downturn in money growth, that the economy might again be falling short of a moderate growth path. Most of the members who preferred to ease immediately indicated that they could accept an unchanged directive that was biased towards ease, and such a directive also was acceptable to many members who favored a symmetrical directive.

At the conclusion of the Committee's discussion, all but three of the members indicated their acceptance of a directive that called for maintaining the existing degree of pressure on reserve positions and that would include some bias toward possible easing during the intermeeting period. Two of the members expressed a strong preference for a symmetric directive with regard to possible intermeeting policy adjustments, while another was firmly persuaded of the desirability of an immediate increase in reserve availability to strengthen the growth of M2. Accordingly, in the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, the Committee decided that slightly greater monetary restraint might be acceptable or slightly lesser monetary restraint would be acceptable during the intermeeting period. The reserve conditions contemplated at this meeting were expected to be consistent with growth in M2 and M3 at annual rates of about 3-1/2 and 1 percent respectively over the three-month period from September through December.

At the conclusion of the meeting, the following domestic policy directive was issued to the Federal Reserve Bank of New York:

The information reviewed at this meeting suggests that economic activity has been expanding at a moderate pace. Total nonfarm payroll employment was up slightly in October after declining in the previous two months, and the civilian unemployment rate edged down to 7.4 percent. Industrial production rose somewhat in October. Retail sales increased considerably in September and October. There was some strengthening in residential construction activity over the summer months. Outlays for business equipment have continued to increase, and recent data on orders for nondefense capital goods point to further growth in the near term; expenditures for nonresidential construction have remained weak. The nominal U.S. merchandise trade deficit widened somewhat in July-August from its average rate in the second quarter. Recent data on wages and prices have been mixed but suggest on balance a continuing trend toward lower inflation.

Most interest rates have increased appreciably since the Committee meeting on October 6. In foreign exchange markets, the trade-weighted value of the dollar in terms of the other G-10 currencies rose very substantially over the intermeeting period.

M2 has expanded at a moderate pace since mid-summer, with all of its growth stemming from its M1 component, while M3 grew slowly. Through October, both aggregates were estimated to have grown at rates a little below the lower ends of the ranges established by the Committee for the year.

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. In furtherance of these objectives, the Committee at its meeting on June 30-July 1 reaffirmed the ranges it had established in February for growth of M2 and M3 of 2-1/2 to 6-1/2 percent and 1 to 5 percent respectively, measured from the fourth quarter of 1991 to the fourth quarter of 1992. The Committee anticipated that developments contributing to unusual velocity increases could persist in the second half of the year. The monitoring range for growth of total domestic nonfinancial debt also was maintained at 4-1/2 to 8-1/2 percent for the year. For 1993, the Committee on a tentative basis set the same ranges as in 1992 for growth of the monetary aggregates and debt, measured from the fourth quarter of 1992 to the fourth quarter of 1993. The behavior of the monetary aggregates will continue to be evaluated in the light of progress toward price level stability, movements in their velocities, and developments in the economy and financial markets.

In the implementation of policy for the immediate future, the Committee seeks to maintain the existing degree of pressure on reserve positions. In the context of the Committee's long-run objectives for price stability and sustainable economic growth, and giving careful consideration to economic, financial, and monetary developments, slightly greater reserve restraint might or slightly lesser reserve restraint would be acceptable in the intermeeting period. The contemplated reserve conditions are expected to be consistent with growth of M2 and M3 over the period from September through December at annual rates of about 3-1/2 and 1 percent, respectively.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Kelley, Lindsey, Mullins, Ms. Phillips, and Mr. Syron.
Votes against this action: Messrs. Jordan, LaWare, and Melzer.

Mr. Jordan dissented because he preferred taking immediate action to increase the availability of bank reserves sufficiently to raise M2 growth to a pace more consistent with the Committee's annual range. Because desirable M2 expansion in line with the Committee's objectives would be likely to fall within a lower range next year, he would announce concurrently a reduction in the 1993 range to make clear that near-term action to increase M2 expansion was not an abandonment of the long-term objective of non-inflationary monetary growth.

Messrs. LaWare and Melzer dissented because they did not want to bias the directive toward possible easing during the intermeeting period. In their view, recent developments pointed to a strengthening economy, and they favored a steady policy that was not predisposed to react to near-term weakness in economic or monetary data. More time was needed to evaluate the effects of prior monetary policy actions, and they were concerned that the adoption of a more stimulative policy over the near term might well-establish a basis for greater inflation later. Mr. Melzer was concerned that rapid growth in total bank reserves, the monetary base, and M1 over the last two years might already have laid a foundation for accelerating nominal GDP growth and a reversal of the disinflationary trend. In addition, he noted that policy errors can easily be made at this stage of the business cycle. In an economic expansion, efforts to resist increases in the federal funds rate through large reserve injections eventually lead to higher inflation and higher nominal interest rates.

2. Authorization for Domestic Open Market Operations

The Committee approved a temporary increase of $3 billion, to a level of $11 billion, in the limit on changes between Committee meetings in System Account holdings of U.S. government and federal agency securities. The increase amended paragraph 1(a) of the Authorization for Domestic Open Market Operations and was effective for the intermeeting period ending with the close of business on December 22, 1992.

Votes for this action: Messrs. Greenspan, Corrigan, Angell, Hoenig, Jordan, Kelley, LaWare, Lindsey, Melzer, Mullins, Ms. Phillips, and Mr. Syron.
Votes against this action: None.

The Manager of the System Open Market Account advised the Committee that the current leeway of $8 billion for changes in System Account holdings might not be sufficient to accommodate the potentially large need to add reserves over the intermeeting period ahead to meet an anticipated seasonal bulge in the demand for currency and required reserves.