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STRICTLY CONFIDENTIAL (FR)
CLASS II - FOMC

TO: Federal Open Market Committee DATE: June 29, 1994
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Enclosed are the Greenbook and information prepared at
the Federal Reserve Bank of Boston.

Enclosures

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First District - Boston
Special District Report
Academic Level

Professors Samuelson and Houthakker were available for comment this month. Professor Houthakker expressed some concern about the recent movements in the value of the dollar. However, he does not believe that U.S. monetary policy should be altered to support the dollar. If the Fed is concerned about the recent decline, he advocates concerted, sterilized intervention with the other G-7 countries.

Professor Houthakker believes the decline in the dollar's value does not warrant an increase in U.S. interest rates because excess capacity still exists in the domestic labor market. The remaining labor market slack is sufficient to inhibit any wage inflation for the foreseeable future. Given this excess capacity, Professor Houthakker sees current monetary policy producing a soft landing later rather than sooner. Although he agrees with this policy, he feels the current level of underutilized capacity requires that the Fed be careful of raising interest rates too far, too soon.

Professor Samuelson also expressed some concern over the value of the dollar, but saw no justification for changing

domestic monetary policy to support the exchange rate. He believes that U.S. monetary policy should be determined solely by domestic conditions, specifically the strength of the economy and signs of inflation. The Fed should tighten because it feels the economy is going to overshoot capacity, not because it fears the dollar has fallen too far recently.

Professor Samuelson sees the economy approaching capacity; labor markets are beginning to tighten and some prices are beginning to increase. But he feels further evidence of continued strong growth is required to warrant another increase in the federal funds rate. Professor Samuelson also believes the Fed should avoid a reputation as "tight and tightening" and work for a reputation as "doing the right thing" at the right time. As a result, his proposal for current policy is to stand pat until new information revises the current consensus forecast for the economy; if the first half strength is sustained, then some further tightening will be necessary.