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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

DIVISION OF MONETARY AFFAIRS

Date: December 13, 1994

To: Federal Open Market Committee

From: Donald Kohn DLK

Subject: Topics for Committee Discussion

In the attached letter, President Stern suggests several special topics that the Committee might want to discuss at upcoming meetings. Chairman Greenspan believes that the idea of covering special topics merits serious consideration, and asked me to forward President Stern's letter to the Committee to solicit views about such a procedure and about what topics might be addressed. Not every topic would necessarily require a full and separate Committee discussion; some might be addressed in the course of regular staff briefings, others by special memoranda or studies without formal Committee discussion. As in the past, some special topics might involve cooperative efforts by Board and Bank staff.

A topic not raised in the letter is that of explicit inflation targets. At the last meeting, a number of you expressed a desire to discuss this approach, and Senator Mack has said he will hold hearings on it early next year. I have asked Dave Lindsey to write a memorandum outlining the issues involved with inflation targets.

Please send me your thoughts about expanding FOMC meetings to consider more special topics, how they might best be addressed, and about the subjects that might be covered.

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GARY H. STERN
PRESIDENT

November 29, 1994

The Honorable Alan Greenspan
Chairman
Board of Governors of the
Federal Reserve System
Washington, D.C. 20551

Dear Alan:

As I mentioned after the last FOMC meeting, there are several policy issues which I believe the Committee should discuss in the not-too-distant future. They are listed immediately below:

1. Should monetary policy respond to cyclical fluctuations in inflation, or should it care only about the trend rate? Can we distinguish between changes in trend as opposed to cyclical swings?

2. How useful are measures of capacity utilization in signaling cyclical or secular changes in inflation?

3. Is expansion in the monetary aggregates still a good indicator of long-run inflation? If so, which aggregate?

4. Do the benefits justify reducing inflation below 3 percent per year, as opposed to stabilizing it at that rate if possible?

5. Do changes in the prices of indexed bonds issued in Britain help estimate changes in inflationary expectations?

We have been considering these issues with varying degrees of intensity here in Minneapolis for some time, and I have become convinced that they merit Committee attention. Obviously, scheduling would be up to you; I see no alternative but to extend the meetings if we are to get into these matters.

I would be more than happy to elaborate on these suggestions at your convenience. Let me know if you see value in a serious review of these issues.

Sincerely,

Gary

Gary H. Stern