Monetary policy in 1989: balancing the risks

By Bryon Higgins and Dodd W. Snodgrass

Admittedly, the balance we are seeking is a delicate one.

—Chairman Greenspan in Congressional testimony on July 20, 1989.

The American economy entered 1989 with considerable momentum and an upward trend in inflation. The primary challenge for monetary policy in 1989 was to arrest the upward trend in inflation without precipitating an economic downturn.

To meet this challenge, the Federal Reserve had to balance the risks between higher inflation and recession. The published record of policy actions indicates clearly that the Federal Open Market Committee (FOMC) believed accelerating inflation was the primary threat early in the year to the long-run health of the American economy.[1] Monetary policy responded by further restraining the growth of money and credit. As evidence accumulated through the summer and fall that overall economic growth was moderating, the policy record indicates the FOMC believed the balance of risks had shifted away from inflation toward an economic downturn. In response, the FOMC relaxed the degree of monetary restraint. The easing of policy was gradual, however, because inflation remained unacceptably high. Preventing further acceleration of inflation was nonetheless a major stride toward the FOMC's long-run goal of price stability. Looking ahead to 1990, the Committee anticipates further progress toward price stability.

The FOMC took account of a wide variety of information in assessing the appropriate course for monetary policy in 1989. In directing open market operations by the Desk at the Federal Reserve Bank of New York, the FOMC considers several factors in determining whether the degree of pressure on reserve positions, and indirectly the degree of monetary restraint, should be changed. In 1989, these factors included indicators on the strength of the economy and inflation, as well as monetary and

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financial developments. Understanding monetary policy in 1989 thus requires understanding how FOMC members assessed these factors throughout the year.

I. January through April: Countering the Risk of Higher Inflation

> *Nearly all the members [of the FOMC] believed that the risks remained on the side of greater inflation and that the Federal Reserve would need to stay especially alert to inflationary developments.*
>
> —Record of Policy Actions of the February 1989 FOMC meeting.

Economic activity and inflation

The momentum from robust economic growth in 1988 carried into the early months of 1989. Fueling the demand for goods and services was the continuing export boom caused by the decline in the foreign exchange value of the dollar, which started in the first quarter of 1985. By early 1989, the lower dollar had made U.S. products very competitive on world markets. Moreover, demand for U.S. exports was heightened by strong growth of the economies of most major trading partners abroad. To meet this and other demands, U.S. firms expanded capacity by increased spending on plant and equipment, especially in the manufacturing sector. Despite declines in government spending, homebuilding, and in the growth of household spending for consumer goods, therefore, economic activity continued to expand at a fairly brisk pace in the early months of 1989 (Chart 1).

Continued economic expansion put increased pressure on productive resources. Rapid employment growth led to a drop in the unemployment rate to 5 percent in March, the lowest level since December 1973 and near a level that could lead to heightened pressure on wages (Chart 2). Job gains were widespread, including substantial gains in manufacturing employment. Capacity utilization rates in the manufacturing sector rose to the highest level in a decade. This and other information led FOMC members to fear that, in the absence of some further monetary restraint, pressure on already strained production resources would induce more inflation.

Direct evidence on inflation was not reassuring. Producer and consumer prices had risen sharply, in part reflecting higher prices for food and energy. Most broad measures of labor compensation suggested an upward trend in wage inflation (Chart 3). Moreover, staff projections prepared for the FOMC suggested that wage and price inflation would be higher in 1989 than in 1988.

Against this background, most FOMC members expected intensified inflationary pressures to persist. For example, in conjunction with setting monetary growth targets, FOMC members and other Reserve Bank presidents must submit projections for economic growth and inflation biannually. The central tendency of the projections presented to Congress in February suggested that consumer price inflation in 1989 would be 4½ to 5 percent, up from 4.3 percent in 1988. Inflation was expected to accelerate even though output in the nonfarm economy in 1989 was expected to grow at a moderate rate of 2½ to 3 percent. After allowing for drought effects, this range implied considerably slower growth than in 1988.

Monetary and financial developments

In the absence of monetary restraint, the acceleration of inflation could have been worse than projected. Accordingly, the FOMC lowered the target ranges for growth of money and the monitoring range for the growth of credit. The monetary policy report to Congress in February explained the lowering of the growth ranges for money and credit as signaling a commitment by

CHART 1
Output and employment

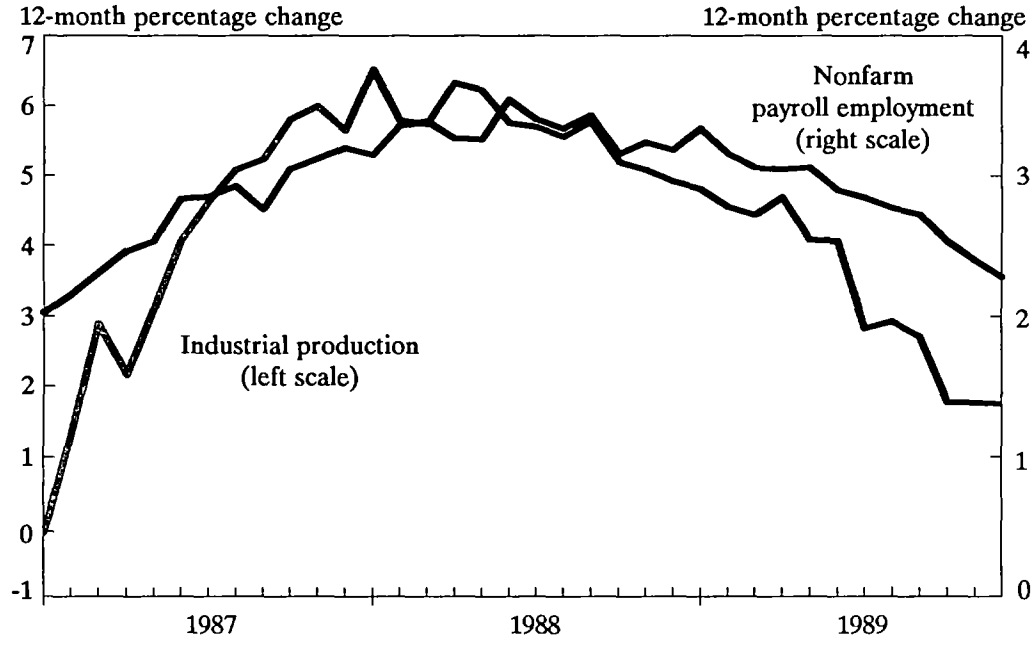


CHART 2
Pressure on resources

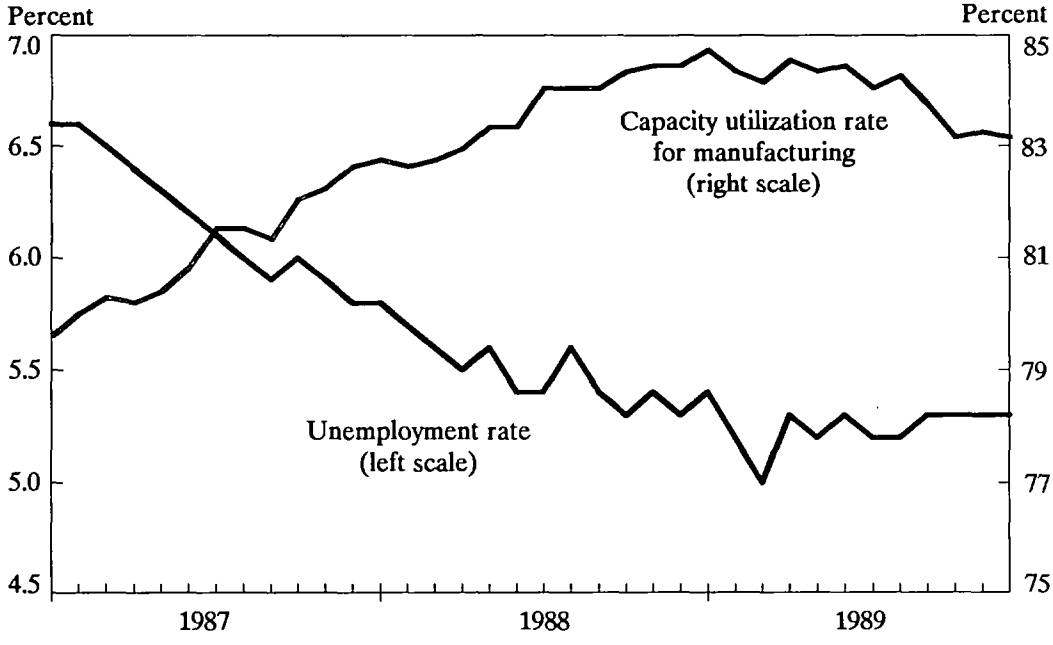
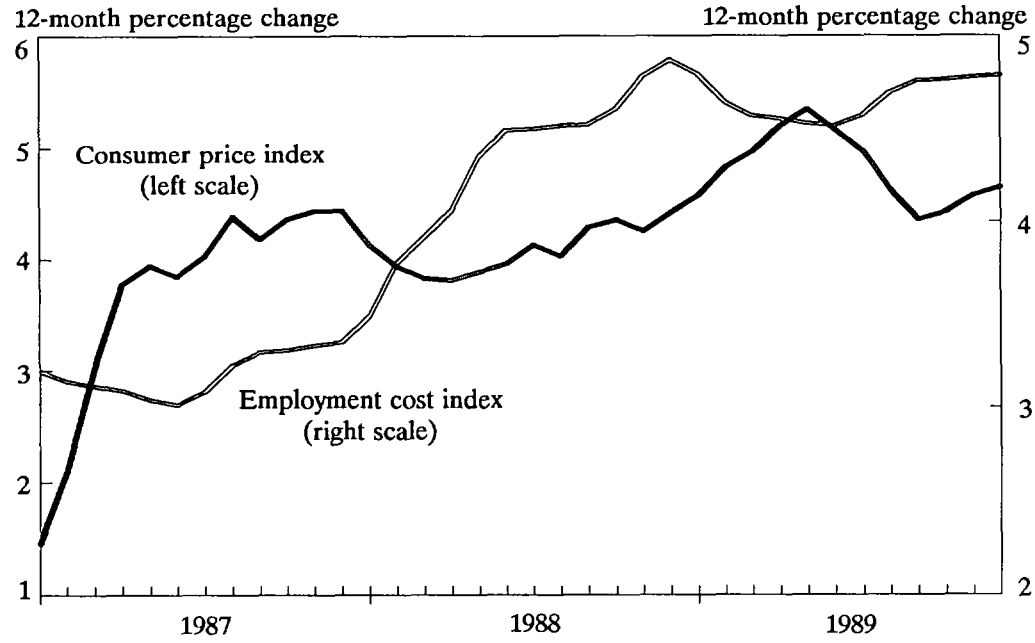


CHART 3
Wage and price inflation



the Federal Reserve to contain inflationary pressures.

Monetary growth was indeed subdued early in the year. After growing 5.2 percent in 1988, M2 grew at a rate of only 1.9 percent in the first four months of 1989. This slow growth was due in part to the upward trend in market interest rates that began in the spring of 1988. Because banks and thrifts slowly adjust rates on NOW accounts and other liquid deposits included in M2, the yields on such accounts become progressively less attractive as market interest rates increase. But such other factors as the S&L crisis and unexpectedly large tax payments also contributed early in the year to keeping M2 growth below its target range and M3 growth near the lower limit of its range (Charts 4 and 5). The weak growth of the monetary aggregates was thought by some FOMC members to portend lower inflation over time.

Strength of the dollar in foreign exchange markets was also cited as a factor that would help contain inflation. The dollar rose sharply early in the year, in part because higher U.S. interest rates made dollar-denominated assets more appealing to international investors. A strong dollar would help control inflationary pressures by keeping import prices down and by relieving pressure on productive resources, albeit at the cost of slower progress in reducing the trade deficit.

Monetary policy actions

At its meeting in December 1988, the FOMC agreed that an immediate step toward tighter policy would be followed by a further tightening after yearend unless economic and financial conditions changed unexpectedly. When they did not, the degree of reserve pressure was increased in early January, leading to an increase in the federal funds rate to a little over 9 percent.

The FOMC agreed at its February meeting

CHART 4

M2 growth range and actual M2

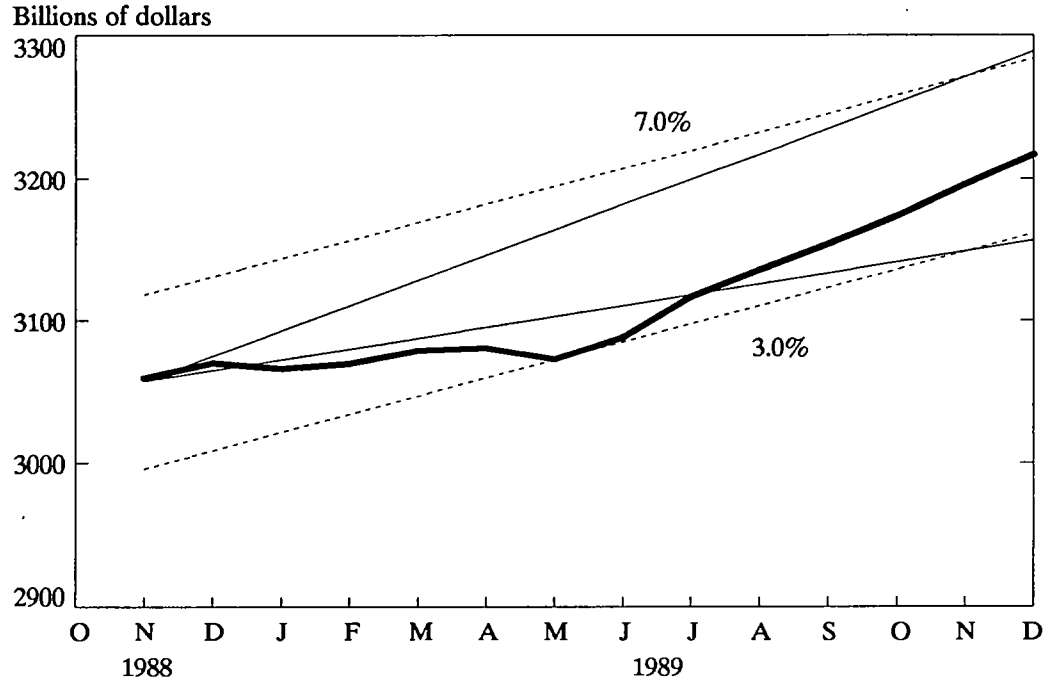
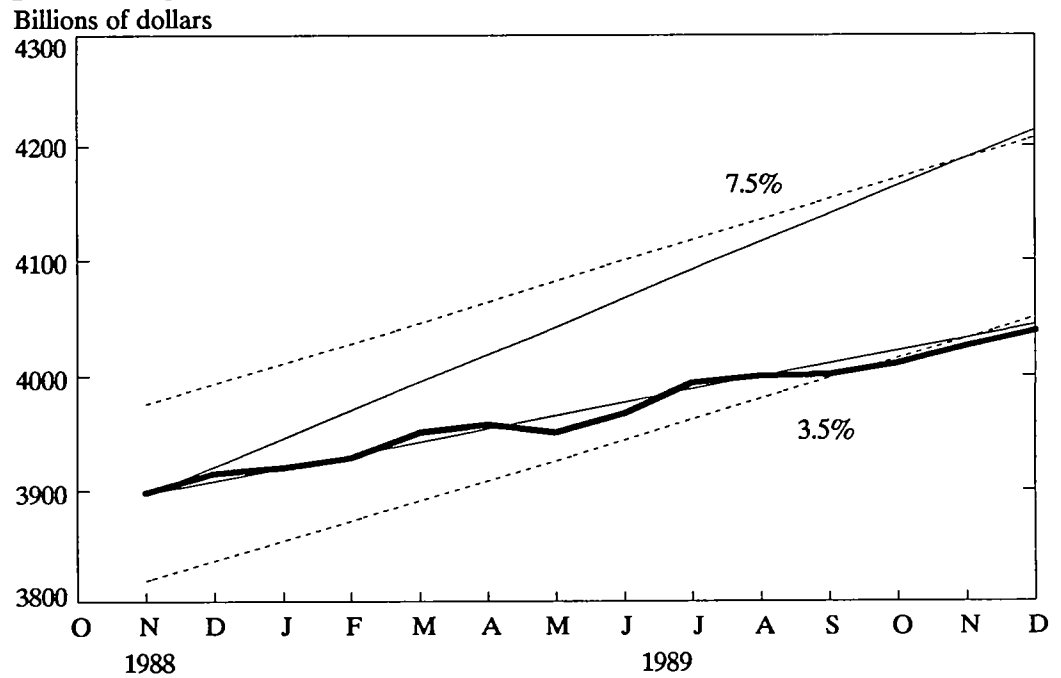


CHART 5

M3 growth range and actual M3



that policy would be tightened promptly if incoming information tended to confirm expectations of growing inflationary pressures. Soon after such confirmation in the form of sharply higher producer prices reported for January, the open market desk further increased the pressure on reserves in mid-February. This tightening was reinforced when the Board of Governors on February 24 approved requests by the Board of Directors of ten Reserve Banks, for an increase in the discount rate from 6½ percent to 7 percent. The federal funds rate rose further to a little above 9¾ percent in early March.

The cumulative effect of these monetary policy actions was an appreciable rise in interest rates. The federal funds rate rose a little more than 1¼ percentage points (Chart 6). Short-term market interest rates rose somewhat less, in part because some firming of monetary policy had been widely anticipated and was therefore already incorporated in rates. Yields on most private short-term debt instruments, including bank CDs, rose about three-fourths percentage point from early December to early March. The increased cost of funds led banks to increase their prime lending rate in two steps from 10½ percent to 11½ percent. Long-term interest rates increased much less (Chart 7). The yield on Aaa corporate bonds, for example, rose only about one-fourth percentage point.

By the time of the March FOMC meeting, preliminary evidence had suggested that economic growth was slowing to a more sustainable, noninflationary pace. Industrial production was unchanged in February following several months of sizable gains, and growth in consumer spending had moderated. Committee members felt, however, it was too soon to conclude that the slowdown in economic growth would continue. Although continued strength of the dollar and moderate growth of the monetary aggregates might lower inflation in the months ahead, there was no substantial information suggesting inflationary pressures were yet abating. To the contrary, monthly indicators suggested some pickup in inflation, in part due to spurts in food and energy prices. However, the full effect of earlier tightening had not been felt. Accordingly, the FOMC decided not to tighten policy immediately. The inflation risk was nonetheless judged to be sufficient to justify a directive skewed toward the possibility of further tightening before the next meeting in May.

II. May through December: Assessing the Risk of Recession

> . . . *what we seek to avoid is an unnecessary and destructive recession.*
>
> —Chairman Greenspan in Congressional testimony on July 20, 1989.

Economic activity and inflation

The momentum of the economy appeared to have moderated by the spring of 1989. Retail sales were flat in several areas of the country, and homebuilding activity had declined sharply. Continued strength of the dollar and slower growth in major foreign industrial economies had led to slower improvement in the trade deficit, thus reducing demand for U.S. products. Despite a rebound in government spending and continued strong spending for capital goods, the balance of evidence suggested a less robust economy.

More decisive evidence of weaker economic growth emerged in the summer and fall. A further rise in the exchange value of the dollar was accompanied by preliminary evidence that improvement in the trade balance was slowing, and previous declines in mortgage interest rates had failed to reverse the downward trend in homebuilding. Although incentives by auto producers led to a spurt in car purchases, consumer spending on other goods and services remained sluggish. And growth in business spending on plant and equipment had slowed from the pace

CHART 6
Short-term interest rates

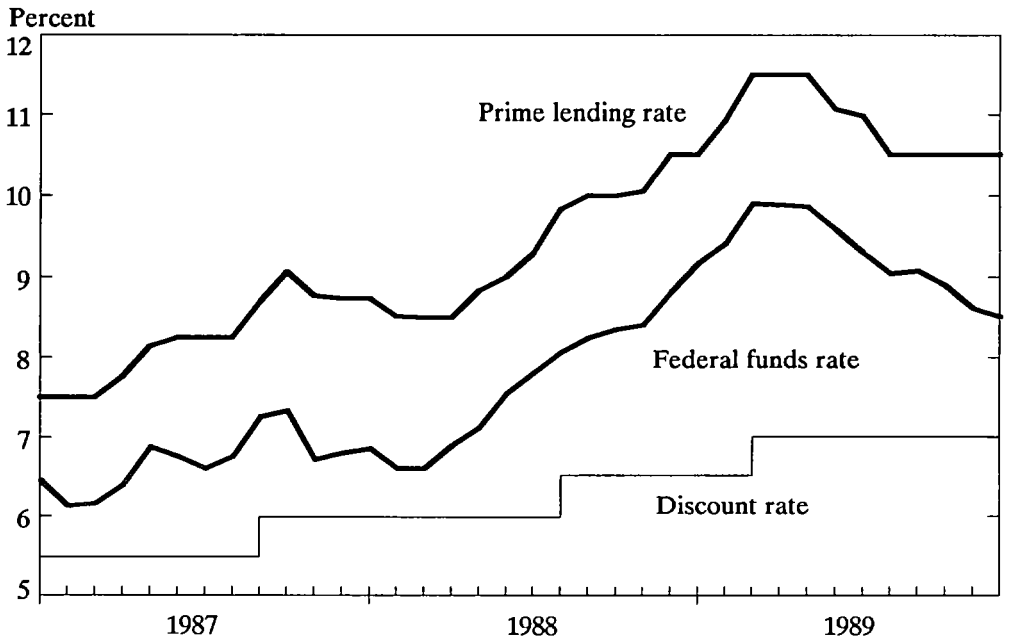
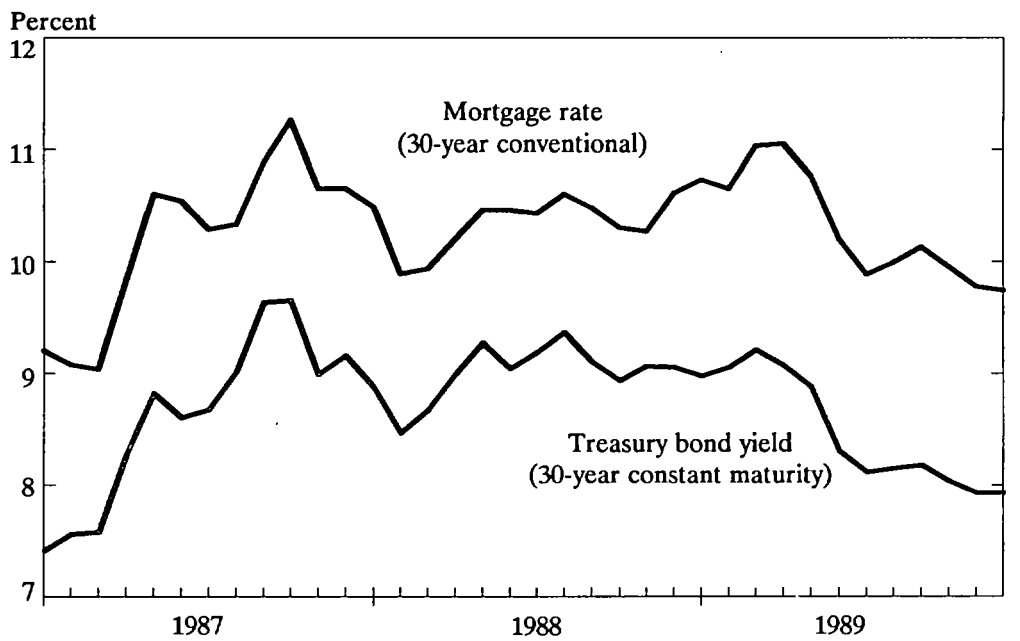


CHART 7
Long-term interest rates



earlier in the year. The manufacturing sector exhibited particular weakness. Manufacturing output, as measured by the manufacturing component of the industrial production index, had leveled out after advancing sharply in late 1988 and early 1989. Moreover, the survey of purchasing managers suggested that manufacturing output was contracting due to weakness in new orders for durable goods.

More subdued economic expansion progressively relieved pressure on productive resources. Employment growth slowed substantially, as jobs in the manufacturing sector dwindled. As a result, the overall unemployment rate edged up to about 5¼ percent. Capacity utilization rates in manufacturing also declined, especially at firms producing goods at earlier stages of processing. The resulting easing of pressure on productive resources contributed to a majority view of FOMC members by October that the risks to expansion were more heavily weighted toward an unexpected weakening in the economy rather than toward greater inflationary pressures.

Direct evidence on prices and wages tended to confirm that inflationary pressures were abating. Although fluctuating from month to month, increases in producer prices were substantially lower on balance than early in the year. Increases in food and energy prices elevated consumer prices for a while, but consumer price inflation excluding the volatile food and energy components trended downward gradually beginning in May. Broad measures of labor compensation showed that wage inflation had ceased to accelerate. Moreover, industrial commodity prices had leveled out, and the dollar remained strong on foreign exchange markets, leading the Committee to anticipate that inflationary pressures would subside further in the months ahead.

FOMC members nonetheless continued to expect that inflation would be somewhat higher than in 1988. At the midyear review of monetary policy in July, the central tendency of projections by FOMC members was for consumer price inflation of 5 to 5½ percent in 1989. This inflation projection was somewhat higher than at the February meeting, even though FOMC members now foresaw a more pronounced slowing of overall economic growth in 1989 to 2½ percent or less, implying less than 2 percent growth of nonfarm output.

Monetary and financial developments

In light of the somewhat changed outlook for economic growth and inflation, the Committee at its July meeting also reviewed the 1989 ranges of growth for money and credit established in February. Despite more rapid monetary growth since mid-May, M2 remained about one percentage point below its range and M3 remained near the lower bound of its range. However, a staff analysis suggested that more rapid monetary expansion was likely to persist. Recent declines in market interest rates, which were not expected to be matched by reduction in deposit rates, would enhance the attractiveness of holding M2 and M3 deposits. Moreover, the outflow of deposits from S&Ls was expected to have less effect on monetary growth for the remainder of the year. The staff analysis indicated the resulting acceleration of monetary expansion would yield M2 and M3 growth rates for the year as a whole that were well within the current ranges. Accordingly, the FOMC decided the existing ranges continued to be broadly consistent with its overall objective of reducing inflation over time.

This assessment proved to be accurate for M2 only. Growth of M2 finished the year within its target ranges. The higher M2 growth evident in late spring continued for the remainder of the year. As expected, lower interest rates and the absence of temporary depressing factors led to a sustained rebound in M2 growth from the sluggish rates early in the year. This rebound left M2 near the middle of its range by yearend. M3

did not fully recoup slow growth since July, leaving it below the lower limit of its target level for the rest of the year. Growth of M3 was boosted less by lower interest rates and may have been held down more by the shrinking of S&Ls associated with efforts to meet higher capital standards. Although not rebounding appreciably in the summer and fall, M3 growth nonetheless finished the year only slightly below the lower limit of its range.

The dollar remained strong in foreign exchange markets throughout the remainder of the year. Although the strong dollar helped keep inflation in check, further increases in the exchange value of the dollar would also impede progress in reducing the trade deficit. Persistent strength of the dollar gave rise to direct intervention in foreign exchange markets by several central banks, including the Federal Reserve. Intervening in exchange markets by selling dollars, it was thought, would foster exchange market stability by preventing a further rise in the value of the dollar. Although the Treasury Department is primarily responsible for the nation's international economic policy, the Federal Reserve consults with the Treasury on exchange market developments and actually carries out intervention when it is decided that doing so would help achieve international policy objectives. Such a situation arose in May and June. As the dollar advanced to the highest level against some key currencies in over two years, U.S. authorities sold a total of $11.7 billion during this period in exchange for Japanese yen and German marks (Cross 1989). These operations were undertaken in coordination with other central banks that sought to prevent further depreciation of their currencies.

Interest rate developments could not fully explain why the dollar continued to rise. The increase in the foreign exchange value of the dollar early in the year had been due at least in part to rising U.S. interest rates. But beginning in April, the amount by which U.S. rates exceeded foreign rates began to narrow. Interest rates in several major foreign countries began to rise as inflationary pressures in those countries mounted. Just as the strength of the dollar held down U.S. inflation, so the resulting weakness of the deutsche mark and the yen contributed to higher inflation in Germany and Japan. In response to the heightened inflation threat, the Bundesbank and the Bank of Japan tightened monetary policy by raising official lending rates. The dollar nonetheless remained strong in part because political uncertainties in Germany and Japan, together with turmoil in China, led investors to seek a safe haven in dollar assets.

In contrast to foreign interest rates, U.S. interest rates began to decline in the spring. As evidence accumulated that economic growth was slowing and inflation was not accelerating further, both short-term and long-term market interest rates receded from peaks reached in March. Market participants came increasingly to believe that the Federal Reserve would not need to tighten credit conditions further in order to control inflation. Moreover, the strength of the dollar lent support to bond prices by reducing foreign investors' concern that the real return on U.S. investments would be eroded by dollar depreciation. As a result, from late March to late May, most short-term market interest rates fell about three-fourths percentage point and most long-term interest rates fell nearly one-half percentage point. The prime rate was reduced to 10½ percent in late July. These declines were not a result of monetary policy actions. The Federal Reserve held policy constant over the period, with the federal funds rate remaining near 9¾ percent.

Monetary policy actions

No changes in policy were made immediately after the May FOMC meeting. The Committee adopted a symmetrical directive, however, rather than a directive skewed toward further

possible tightening, as had been typical earlier in the year. FOMC members expressed particular concern about sluggish monetary growth thus far in 1989, especially in light of the slowdown in economic growth that was becoming evident. Although weekly data in the latter part of May suggested some revival of monetary growth, both M2 and M3 declined for the month as a whole. Accordingly, policy was eased slightly in early June, leading to a decline in the federal funds rate to about 9½ percent.

The FOMC at its meeting in early July agreed to another slight easing of policy. In reviewing the economic outlook, Committee members noted recent evidence of weakness in housing and consumer goods. However, there were few signs of the kinds of imbalances that could lead to an economic downturn. Even though wage inflation apparently had leveled out, cost pressures remained intense and overall inflation, unacceptably high. Moreover, the extended period of slow monetary growth, the sustained strength of the dollar, and reduced growth in business activity were thought to bode well for lower inflation in the future. On balance, the Committee judged the risks of a sustained acceleration in inflation to be more limited than they had earlier in the year. Many members nonetheless stressed the importance of acting cautiously lest the actions be misinterpreted as a lessening in resolve to lower inflation. Accordingly, the degree of reserve pressure was lessened only marginally. Later in July, the degree of pressure was reduced slightly further. The combined effect was to lower the federal funds rate to about 9 percent by early August.

No further easing of policy was undertaken at the August FOMC meeting. The decision to maintain a steady policy course was based mainly on a reduced risk of recession. Incoming economic data suggested a somewhat stronger economy than at the time of the July meeting. Consumer demand in particular was estimated to be more robust. Moreover, monetary growth had accelerated in July to the point that M2 was within its target range, a development that the Committee clearly thought desirable at the July meeting. Indeed, the easing of policy in June and July had contributed to the rebound in monetary growth by reducing the opportunity cost of holding deposits. The conditions that led to earlier easing of pressure on reserve positions had thus by August become less compelling, despite evidence that inflationary pressures were abating. Producer prices had fallen for two consecutive months, and consumer prices had risen less than earlier in the year. On balance, FOMC members agreed an unchanged policy was justified by improved prospects for moderate economic expansion consistent with progress over time in achieving price stability. The commitment to such progress was underscored by substituting the phrase "progress toward price stability" for the phrase "indications of inflationary pressures" as a factor in the directive governing policy actions.[2]

Despite the decision not to ease policy immediately, the FOMC adopted a directive biased toward possible easing until the next meeting. In this limited sense, most FOMC members still viewed the risks as being primarily on the side of unacceptably weak economic growth. Despite the bias toward ease, however, incoming information did not lead to any policy adjustments before the next FOMC meeting. The federal funds rate and other market interest rates were basically unchanged leading up to the October FOMC meeting.

Information available at the October meeting did not lead the FOMC to change the stance of policy. Despite noticeably slower growth in industrial production and employment since midyear, pressures on productive resources remained considerable. Inflation had nonetheless slowed due to a steep drop in energy prices, marginally lower prices for other commodities, and continuing declines in import prices. Aggregate demand had continued to expand at a

moderate pace despite indications that business capital spending was less robust than in the first half of the year and evidence of persistent weakness in the housing sector.

A complicating factor in assessing the appropriate course for monetary policy was an international agreement on exchange rates. Officials from the seven major industrial economies had issued a statement on September 23 that the persistent rise of the dollar in recent months was undesirable. This statement was interpreted in some quarters as implying that U.S. monetary policy would be used to supplement exchange market intervention—which was substantial following the statement—to achieve a lower dollar. FOMC members expressed concern that an easing of monetary policy at that time would be interpreted as an attempt to force the dollar lower. The Committee agreed the Federal Reserve's policy should not be used to peg the value of the dollar because doing so could conflict with domestic policy objectives. On balance, the FOMC decided not to ease policy further immediately following the meeting.

As at the August meeting, however, the FOMC adopted a directive skewed toward possible ease. Most FOMC members believed the risks of further slowing in the economy were greater than the risks of a stronger economy; a few members expressed concern about a more serious weakening. In the majority view, the balance of risks justified a policy that gave special weight to developments that might require some further easing before the November FOMC meeting.

Soon after the October meeting, turmoil arose in financial markets. Prices of "junk bonds" deteriorated as concern grew that highly leveraged firms would fare badly if the economy entered a recession. And stock prices declined sharply on October 13. Monetary policy was eased slightly soon after the stock market break, as the federal funds rate declined to about 8¾ percent. In early November, additional ease was implemented following release of employment and other data confirming weakness in the manufacturing sector of the economy. The federal funds rate edged down to about 8½ percent. In response to the easing of policy since the October meeting and additional evidence of slower economic growth, most market interest rates, except those on low-rated corporate debt, declined appreciably before the November 14 FOMC meeting.

The mixed evidence available at that meeting led the Committee to keep monetary policy unchanged. Although the economy had continued to expand, economic conditions had softened in some regions and the manufacturing sector had weakened more generally. Staff projections suggested that economic growth was likely to slow over the next several quarters. But the near-term outlook was clouded by uncertainties related to the effects of a hurricane, an earthquake, and a major strike. Reflecting these and other uncertainties, Committee members differed somewhat in their evaluation of the risks. Some members foresaw the possibility that business activity would expand negligibly if at all in the next few quarters, while others thought that the odds were greater that the economy might grow at a rate near its potential. Views regarding the inflation outlook were similarly mixed, with some members skeptical that significant progress in reducing inflation could be made over the next few quarters but other members more optimistic in light of some evidence that inflationary momentum had been arrested. In weighing the concerns about a cumulative weakening in the economy against the desire to lower inflation, the Committee decided on a steady policy over the next few weeks. The policy directive continued to be biased toward a possible easing of policy.

Although no such action was taken before the December FOMC meeting, the conduct of open market operations immediately after that meeting led to a further one-fourth point reduc-

TABLE 1
Actual and projected economic performance

	FOMC projections for 1990[1]	1989 actual[2]
Nominal GNP	5½ to 6¾	6.4
Real GNP	1½ to 2	2.4
Consumer price index	4½ to 5	4.5
Unemployment rate (civilian)	5½ to 6	5.3

[1] Except for the unemployment rate, projections are for the percentage change from the fourth quarter of 1989 through the fourth quarter of 1990. The projection for the unemployment rate is the average level for the fourth quarter of 1990. The projections are the central tendencies of the ranges reported by the FOMC.

[2] Data for nominal and real GNP are growth rates from the fourth quarter of 1988 through the fourth quarter of 1989. Growth rates over this period excluding the effects of the drought are 5.9 percent for nominal GNP and 1.9 percent for real GNP. Comparable growth in 1988 is 8.0 percent for nominal GNP and 4.0 percent for real GNP. The unemployment rate is the average level for the fourth quarter of 1989. Data for 1989 GNP are from advance estimates by the Bureau of Economic Affairs released on January 26, 1990.

tion in the federal funds rate. The response of most short-term market interest rates was muted, however, in part because the possibility of somewhat less pressure on reserve positions had already been incorporated to some extent. The cost of funds to banks nonetheless dropped enough to precipitate a lowering of the prime lending rate by most banks soon after yearend. In contrast, most long-term market interest rates rose from early December to early January.

III. Monetary Policy for 1990: Reversing the Upward Trend in Inflation

Federal Reserve policy is focused on laying the groundwork for more definite progress in reducing inflation pressures in 1990. . . .
—Chairman Greenspan in Congressional testimony on July 20, 1989.

Economic activity and inflation

At the midyear review in July, FOMC members projected a continuation of moderate economic growth in 1990. Staff projections suggested that export growth would contribute much less to economic expansion than in recent quarters, as the persistent strength of the dollar limited foreign demand for U.S. goods. Reduced export growth would also lessen the need for U.S. firms to expand capacity, thereby contributing to more restrained business spending for plant and equipment. In contrast, residential construction activity was expected to rebound in response to lower mortgage interest rates. On balance, though, growth in sectors sensitive to interest rates and exchange rates was expected to remain subdued. The consequent slowing of growth in employment and income would keep growth of consumer spending sluggish through 1990. FOMC members concurred in the main contours of the staff outlook. Accordingly, their projections centered on GNP growth of 1½ to 2 percent for 1990, down somewhat from growth in 1989 (Table 1).

Continued moderation of economic growth was expected to reverse the upward trend in inflation. Slow growth in demand would further lessen strains on capital and labor resources. The unemployment rate, for example, was projected

TABLE 2
Ranges of growth for monetary and credit aggregates
(Percentage change, fourth quarter to fourth quarter)

	Provisional for 1990	1989 actual
M2	3 to 7	4.5
M3	3½ to 7½	3.3
Debt	6½ to 10½	8.1

by the FOMC to edge up to a range of 5½ to 6 percent by the end of 1990. Reduced pressure on resources was thought consistent with somewhat lower inflation in 1990. After containing inflation in 1989, therefore, the FOMC expected to make progress toward price stability in 1990.

Monetary policy

The FOMC at its midyear review also established provisional ranges for growth of money and credit in 1990. The Committee recognized the merits of reducing the ranges further to demonstrate its commitment to reducing inflation. Some members pointed to a potential risk that failure to reduce the ranges might be misconstrued by some as complacency about current rates of inflation. On the other hand, monetary growth could accelerate somewhat in 1990 without being inflationary, especially if necessary to counter risks of an economic downturn should such risks develop. Most members of the Committee concluded that tentatively adopting the same ranges for 1990 as for 1989 was likely to be consistent with some reduction of inflation and continued economic expansion (Table 2). The members recognized this tentative decision could be modified at the February 1990 FOMC meeting if available information warranted.

IV. Conclusion

The Federal Reserve's eclectic approach to the implementation of monetary policy worked well in 1989. By basing policy decisions on their evaluation of a wide variety of information, FOMC members were able to balance the dual risks of escalating inflation and an economic downturn. Early in the year, evidence of increased pressure on resources and worsening of wage and price inflation was instrumental in the decision to tighten policy. As monetary growth moved progressively further below target in the spring, the FOMC recognized the danger of a pronounced weakening of economic activity and employment. Monetary restraint was thus eased cautiously. During the summer and fall, incoming data suggesting a slowdown in economic growth and inflation convinced policymakers that it was safe to further ease monetary policy. And monitoring developments in domestic financial markets and foreign exchange markets enabled policymakers to assess the economic outlook more accurately throughout the year. As Chairman Greenspan said in his midyear Congressional testimony, "The complex nature of the economy and the chance of false signals demand that we cast our net broadly—gathering information on prices, real activity, financial and foreign exchange markets, and related data."

If the approach is similarly successful in 1990, the Federal Reserve stands a good chance of achieving its dual objectives of further reducing inflation while sustaining economic expansion.

Endnotes

[1] The description of FOMC deliberations in this article is taken primarily from the Record of Policy Actions of the pertinent FOMC meeting. The record of each FOMC meeting is released to the public following the subsequent meeting. In addition, the biannual reports to Congress (Board of Governors, 1989b and 1989g) and testimony by Chairman Greenspan (1989a) are also useful references for interpreting the reasons for FOMC actions.

[2] In October, Chairman Greenspan (1989b) also testified in favor of a proposal to make price stability the main objective of monetary policy. The proposal by Congressman Neal would require that "the Federal Open Market Committee of the Federal Reserve System shall adopt and pursue monetary policies...to eliminate inflation [in five years] and shall then adopt and pursue policies to maintain price stability."

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