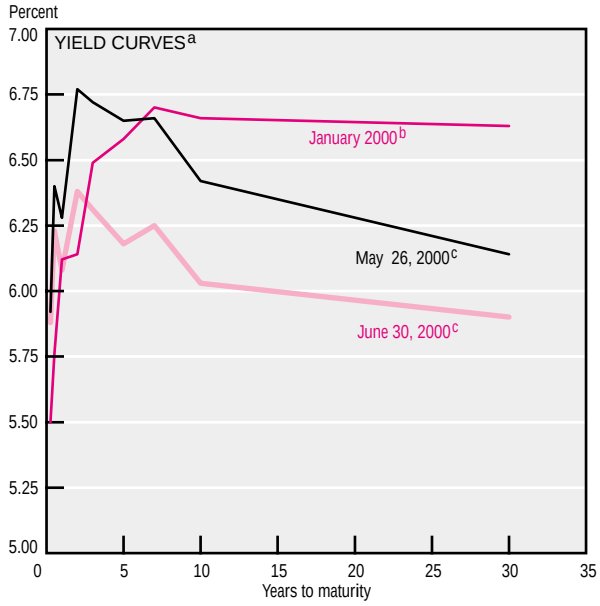
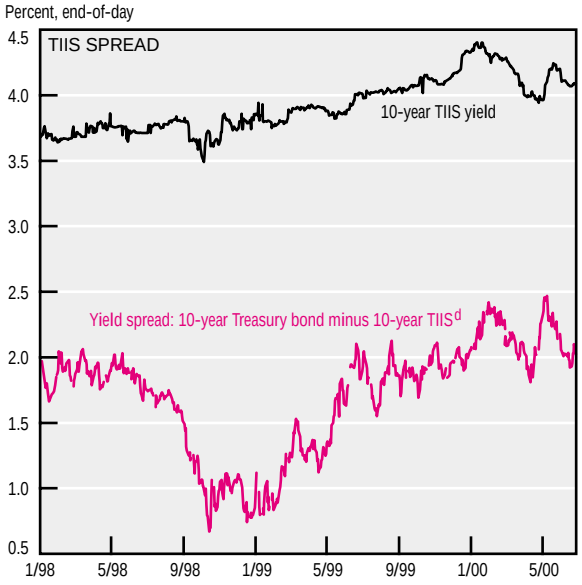
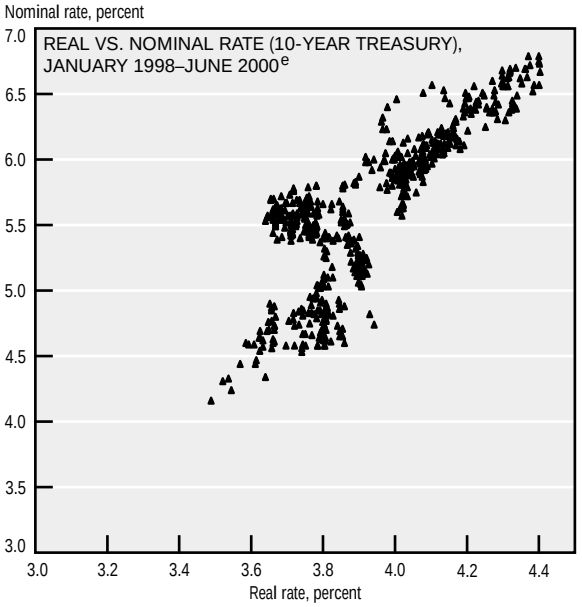
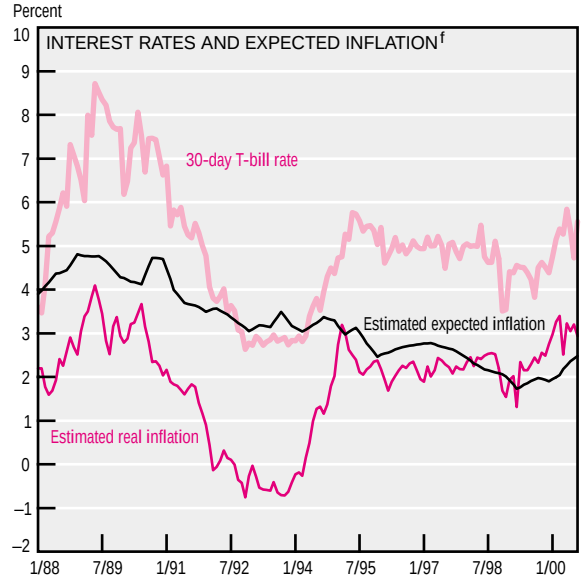
# Interest Rates




a. All yields are from constant-maturity series.
b. Monthly average.
c. Average for the week ending on this date.
d. Line breaks show dates when 10-year Treasury bonds were not traded.
e. Daily data.
f. The estimated expected inflation rate and the estimated real rate are calculated using the Pennacchi model of inflation estimation and the median forecast for the GDP implicit price deflator from the *Survey of Professional Forecasters.* Monthly data.
SOURCES: Board of Governors of the Federal Reserve System, "Selected Interest Rates," *Federal Reserve Statistical Releases,* H.15; Federal Reserve Bank of Philadelphia, *Survey of Professional Forecasters*; and Bloomberg Financial Information Services.

The yield curve has shifted downward at all maturities since last month. It retains its humped shape, with 2-year yields remaining highest. Two often-watched spreads, the 3-year, 3-month and the 10-year, 3-month, stand at 43 and 15 basis points, respectively. The supply of Treasury securities continues to be a concern, particularly at longer maturities, keeping those rates low.

Yield curves often provide a "market estimate" of expected inflation, because inflation expectations increase interest rates. Interest rates may also rise because real rates change. One may account for this by looking at the yields on Treasury inflation-indexed securities (TIIS). The spread between a nominal 10-year Treasury security and a 10-year TIIS provides an estimate of inflationary expectations (since the bonds differ in liquidity and some tax consequences, it is not an entirely pure measure). Since May this estimate has trended downward, with a small recent uptick.

Plotting nominal against real rates shows that both inflationary expectations and movements in real rates do matter: While high real rates generally mean high nominal rates, the relationship is not precise.

Another approach is to combine survey measures of expected inflation with interest rates to estimate expected inflation (and the real rate). The chart above shows one such approach, concentrating on short-term inflation expectations (over the next 30 days), which have been increasing since early 1999.