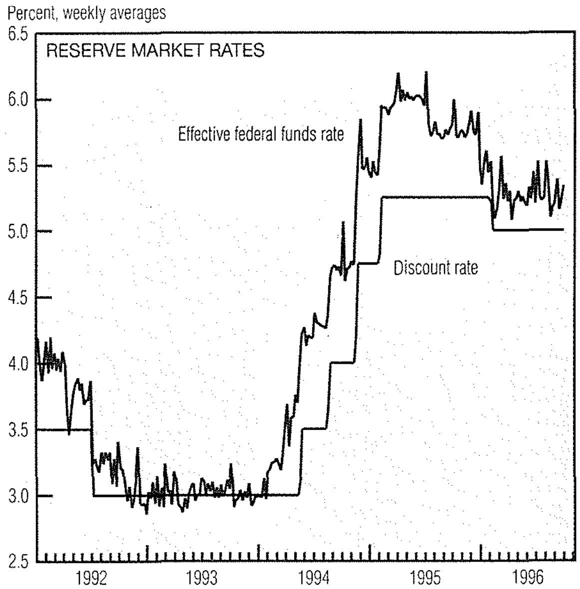
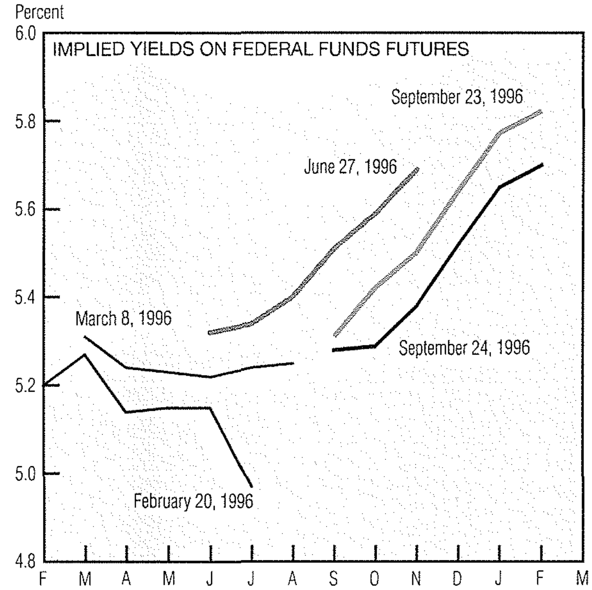
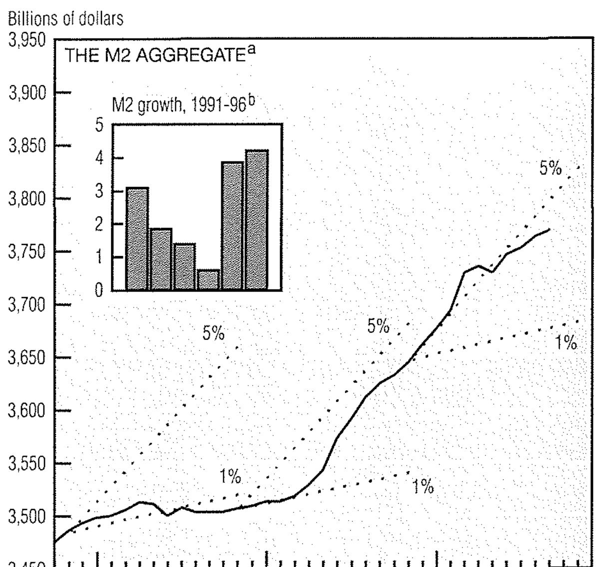
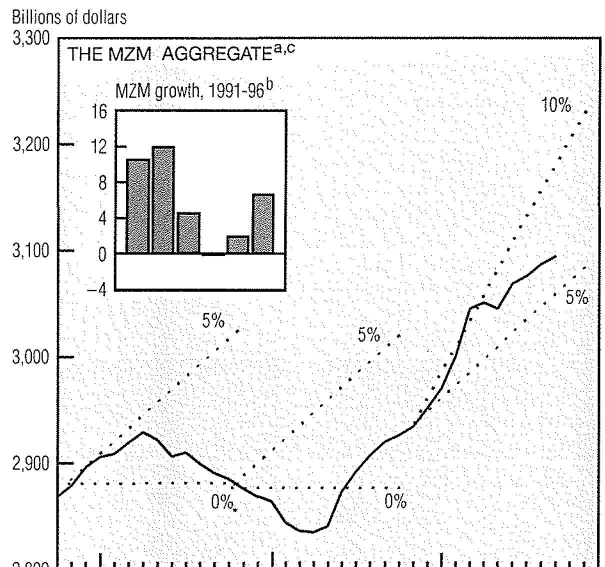
Monetary Policy









a. Last plot is estimated for September 1996.
b. Growth rates are calculated on a fourth-quarter over fourth-quarter basis. Annualized growth rate for 1996 is calculated on an estimated September over 1995:IVQ basis.
c. MZM is an alternative measure of money that includes M1 plus institutional money market mutual funds less small time deposits.
NOTE: All data are seasonally adjusted. Dotted lines represent growth ranges and are for reference only.
SOURCES: Board of Governors of the Federal Reserve System; and the Chicago Board of Trade.

The Federal Open Market Committee (FOMC) left the intended federal funds rate unchanged at its September 24 meeting. The Committee last altered the intended funds rate in February, lowering it from 5.5% to 5.25%. The federal funds rate is the interest rate that banks pay on overnight loans to one another, and it forms an anchor for other short-term rates. Banks can also obtain reserves temporarily by borrowing from the Federal Reserve System, which last lowered the rate charged on such loans—the discount rate—from 5.5% to 5.0% in February.

As the upward trajectory of implied yields on federal funds futures suggests, financial markets have been expecting the Fed to raise interest rates since June. On September 23, just prior to the FOMC meeting, the federal funds futures market seemed to expect an increase of 50 basis points in the funds rate by year's end. The shift in the implied yield curve immediately following the meeting indicates that the market revised the timing—but not the direction—of its forecast.

This year's increase in interest rates, which raised the opportunity cost of holding money, has slowed the growth of M2 and MZM. Through September, these measures of money have grown 4.2% (M2) and 6.6% (MZM) above their 1995:IVQ levels.