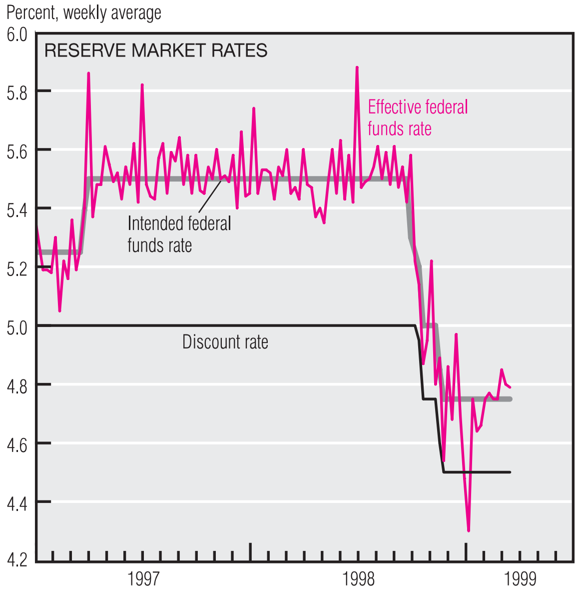
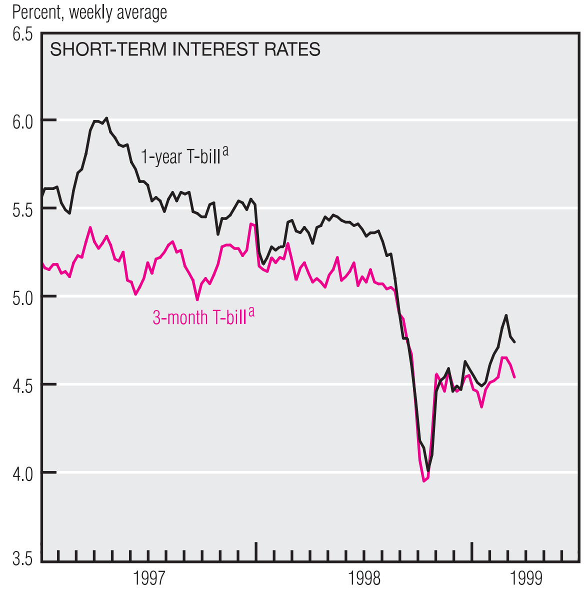
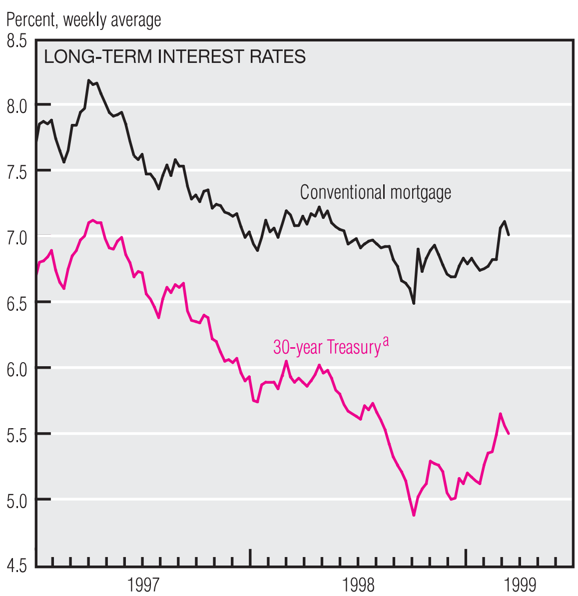
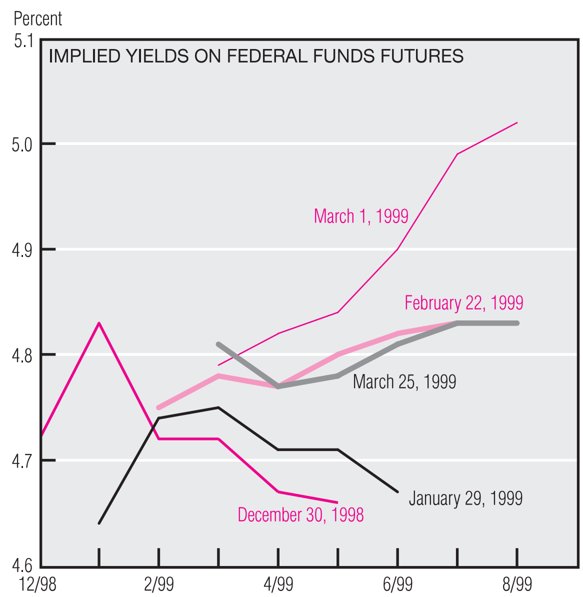
Monetary Policy









a. Constant maturity.

SOURCES: Board of Governors of the Federal Reserve System; and the Chicago Board of Trade.

After two consecutive weeks of federal funds trading, on average, at the target rate of 4.75% in late February, the rate jumped 10 basis points during the first week of March. By the week of March 19, however, the average weekly rate fell to within four basis points of the target.

A similar pattern can be seen in both long- and short-term interest rates. The weekly averages of the 3-month and 1-year T-bills, the 30-year Treasury, and conventional mortgages all peaked during the week of March 5. The 3-month rate subsided 11 basis points and the 1-year rate 15 basis points by the week of March 19. This leaves the 3-month T-bill rate very near its January 1 level, while the 1-year rate is about 15 basis points above its rate at the end of 1998. Conventional mortgage rates have risen near the level of mid-1998. This may affect the brisk pace of home sales seen in the first several months of 1999.

Implied yields on federal funds futures spiked on March 1, but have since returned to the levels of a week earlier. Why the temporary jump? One likely explanation is that it was a reaction to Chairman Greenspan's Humphrey–Hawkins testimony on February 23. His statements were widely interpreted as a harbinger of future policy tightening. He stated, for example, that "The Federal Reserve must continue to evaluate, among other issues, whether the full extent

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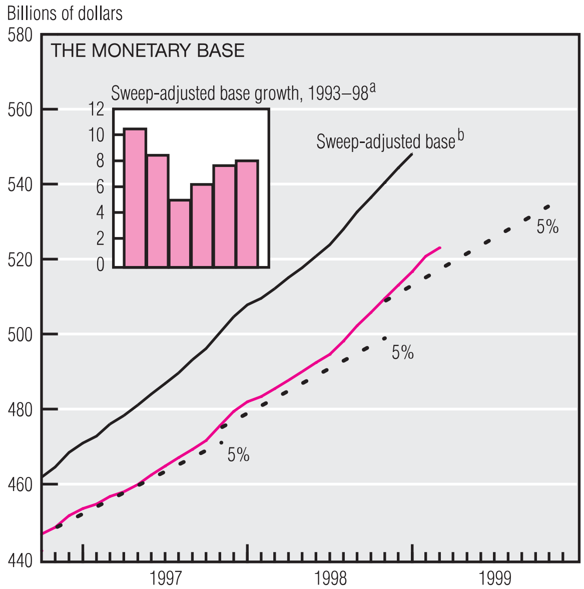
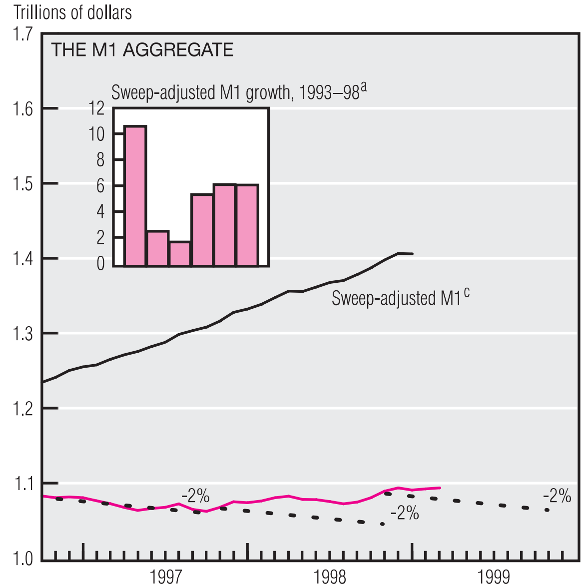
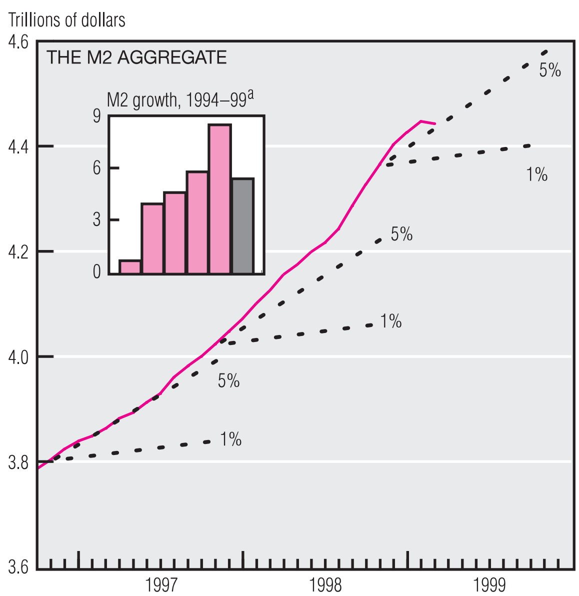
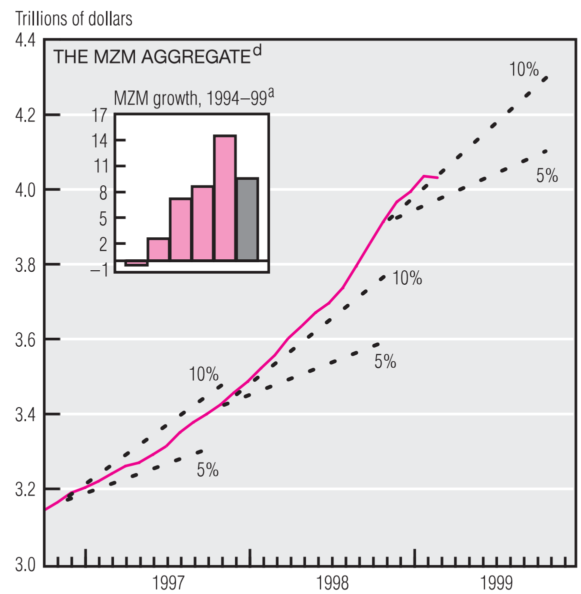
Monetary Policy (cont.)









a. Growth rates are percentage rates calculated on a fourth-quarter over fourth-quarter basis. The 1999 growth rates for MZM and M2 are calculated on an estimated March over 1998:IVQ basis.

b. The sweep-adjusted base includes an estimate of required reserves saved when balances are temporarily shifted from reservable to nonreservable accounts.

c. Sweep-adjusted M1 includes an estimate of balances temporarily shifted from M1 to non-M1 accounts.

d. MZM is an alternative measure of money that is equal to M2 plus institutional money market mutual funds less small time deposits.

NOTE: Data are seasonally adjusted. Last plots for M1, M2, and MZM are estimated for March 1999. Dotted lines for M2 are FOMC-determined provisional ranges. All other dotted lines represent growth in levels and are for reference only.

SOURCE: Board of Governors of the Federal Reserve System.

of the policy easings undertaken last fall to address the seizing-up of financial markets remains appropriate as those disturbances abate." The anticipation of rate increases that this statement may have spurred among fed funds futures traders has now largely abated, as futures yields have returned to levels only slightly above the current target for contracts as far out as August 1999.

The monetary base leveled off somewhat in March, with preliminary estimates indicating an annualized monthly change of about 5%. Growth in unadjusted M1, however, accelerated slightly in March according to preliminary estimates. Sweep-adjusted M1 remained steady in January, but the effects of the recent movement in unadjusted M1 on the sweep-adjusted aggregate are not yet known.

Two broader aggregates, M2 and MZM, both slowed their rapid pace. For the first time since 1997, M2 seems to be near its FOMC-determined provisional range, the upper limit of which is 5%. MZM growth seems to be moderating as well, though it is not reasonable to assume a change in trend based on preliminary estimates of only one month's data. On the other hand, this apparent moderation in money growth, if it continues, may ease the minds of those who anticipate imminent inflation as the by-product of the swift monetary growth of the last two years.