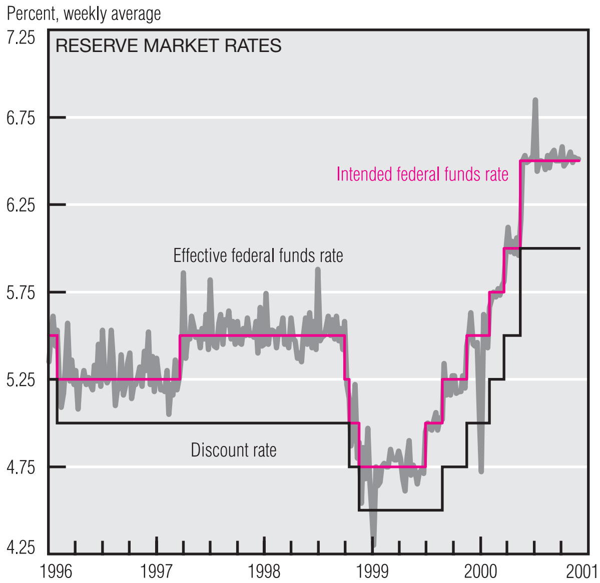
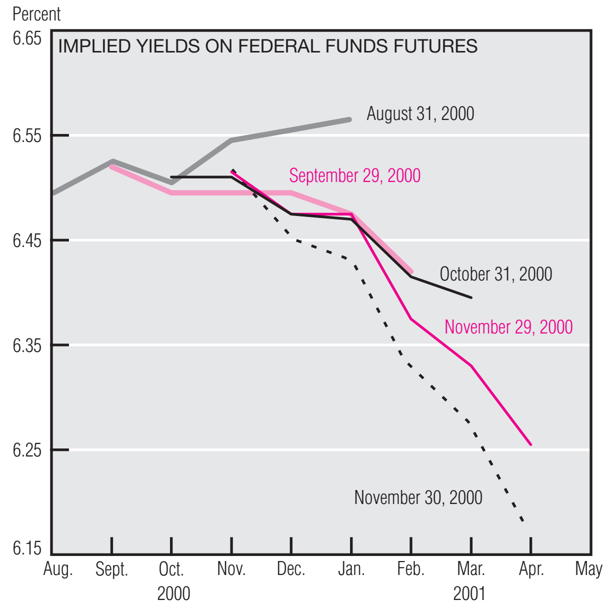
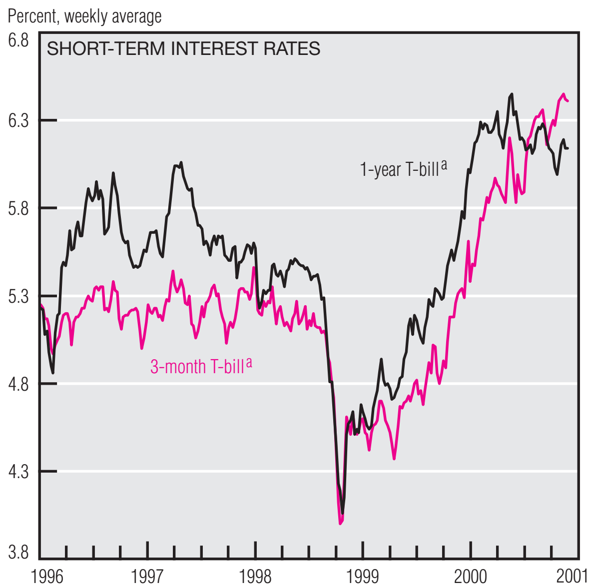
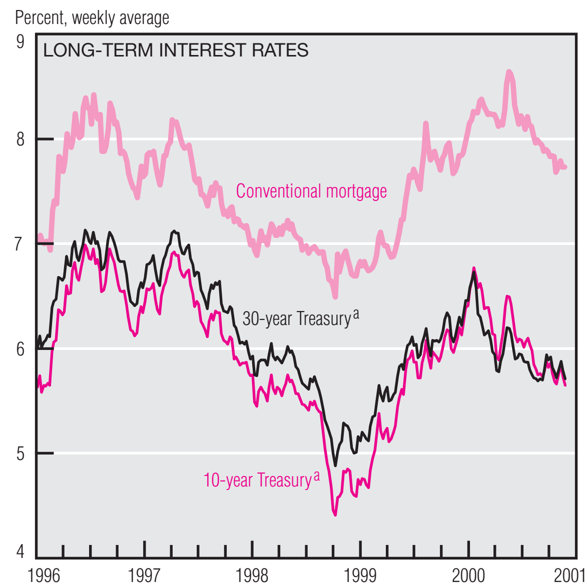
Monetary Policy









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

The Federal Open Market Committee (FOMC) left the intended federal funds rate at 6.5% on November 15, the fourth consecutive meeting that has resulted in no change. Most market participants had expected this decision; they focused instead on the portion of the press release in which the FOMC noted that despite a recent slowdown in some economic indicators, the balance of risks had not changed, that is, they were weighted toward "conditions that may generate heightened inflation pressure for the foreseeable future."

Subsequent data releases and revisions (most notably durable goods and GDP on November 28 and 29) have led participants in the federal funds futures market to increase substantially the probability they assign to future interest rate cuts. The implied yield curve for fed funds futures, often used to gauge policy's expected path, has been sloping downward for some months. The curve has steepened noticeably of late, shifting down abruptly the day after the GDP release. As of November 30, the April contract was trading 33 bp below the current intended fed funds rate.

The continued inversion of short-term interest rates corroborates that the market expects interest rates to fall in the coming months. As of November 24, the 6.36% yield on 3-month T-bills was 27 bp above the yield on 1-year T-bills. To the extent

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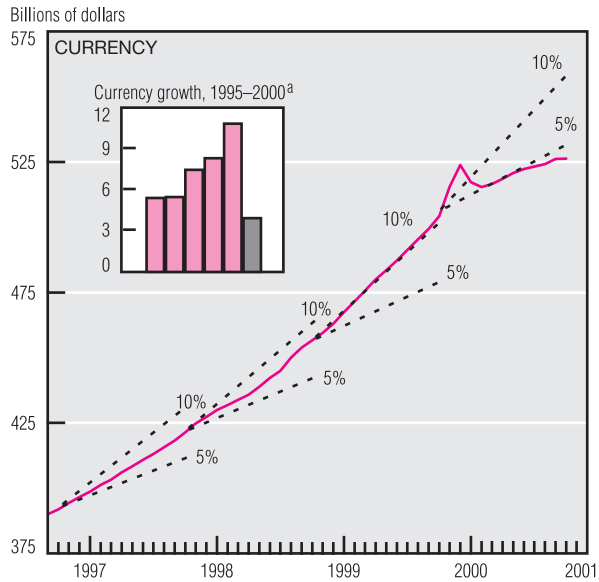
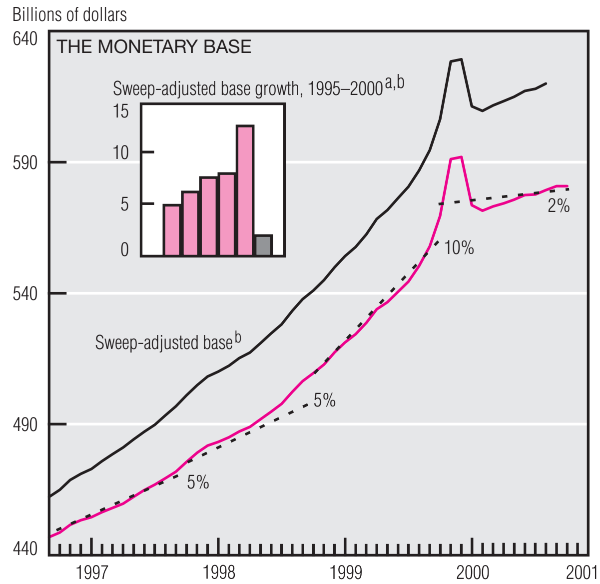
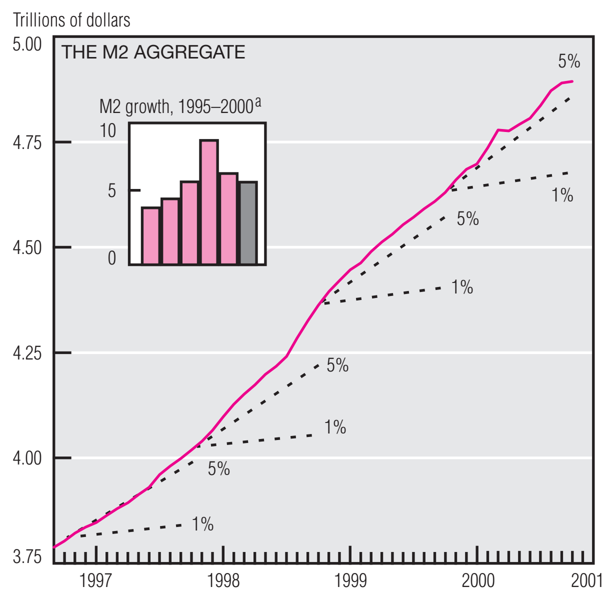
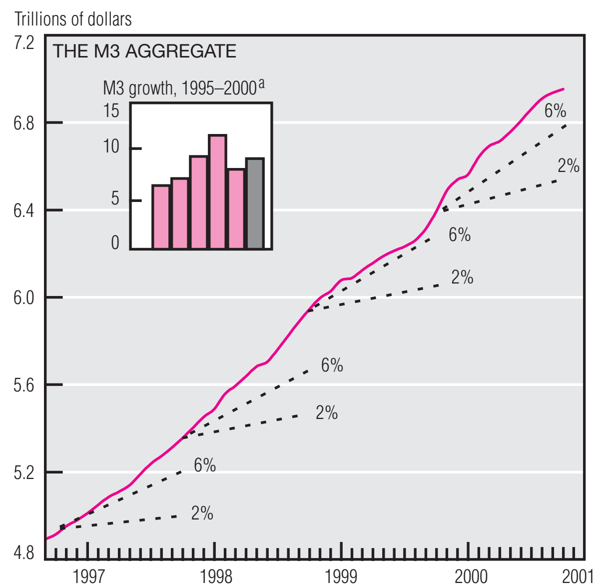
Monetary Policy (cont.)









a. Growth rates are percentage rates calculated on a fourth-quarter over fourth-quarter basis. The 2000 growth rates for M2, M3, currency, and the monetary base are calculated on an estimated November over 1999:IVQ basis. The 2000 growth rate for the sweep-adjusted base is calculated on a September over 1999:IVQ basis.

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

NOTE: Data are seasonally adjusted. Last plots for M2, M3, currency, and the monetary base are estimated for November 2000. Last plot for the sweep-adjusted base is September 2000. Dotted lines for M2 and M3 are FOMC-determined provisional ranges. All other dotted lines represent growth rates and are for reference only.

SOURCE: Board of Governors of the Federal Reserve System.

that shorter-term interest rates reflect current conditions, while longer-term interest rates mirror expected future conditions, this measure also points to an anticipated rate decline.

Long-term interest rates on the whole have dropped back from highs experienced early in the year and are currently at levels comparable to those prevailing just before the Russian default in 1998. As of November 24, the 10-year Treasury rate was 5.56% and the 30-year rate was 5.71%.

Growth in the narrow monetary aggregates was extremely rapid in 1999 in response to Y2K-related liquidity concerns. Currency and the monetary base retraced most of those gains early this year. These series have been sluggish ever since. Estimated year-to-date currency growth for November is 3.9%. Year-to-date sweep-adjusted base growth of 2.0% for September (the most recent sweeps data available) is also depressed.

M2 growth showed signs of slowing during October and November. Estimated year-to-date M2 growth for November was 5.7%, down 0.3 percentage point from one month earlier. Similarly, November M3 growth was slower than the previous month (8.7% versus. 9.1%).