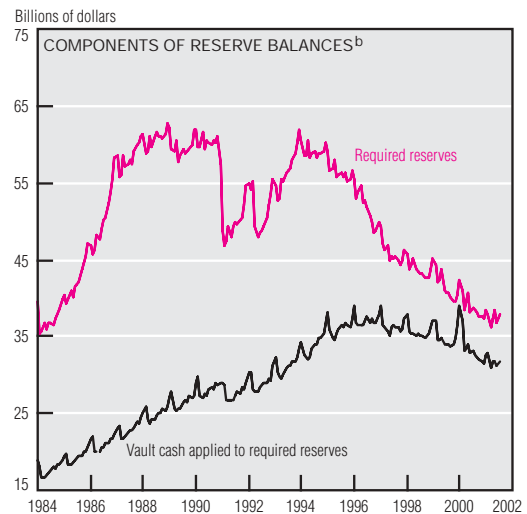
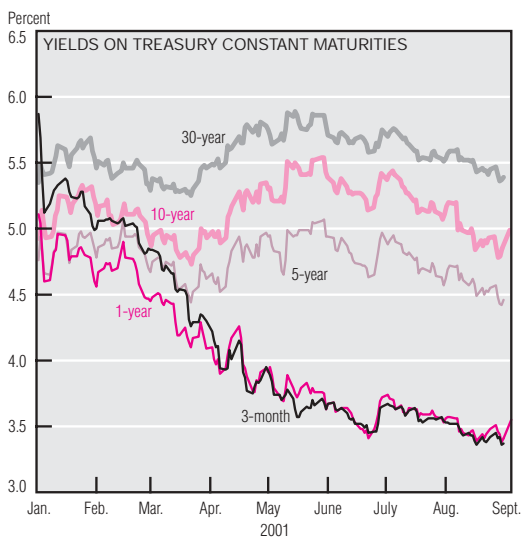
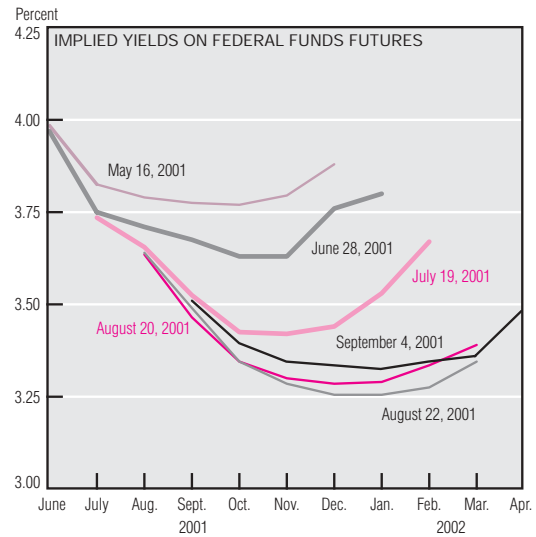
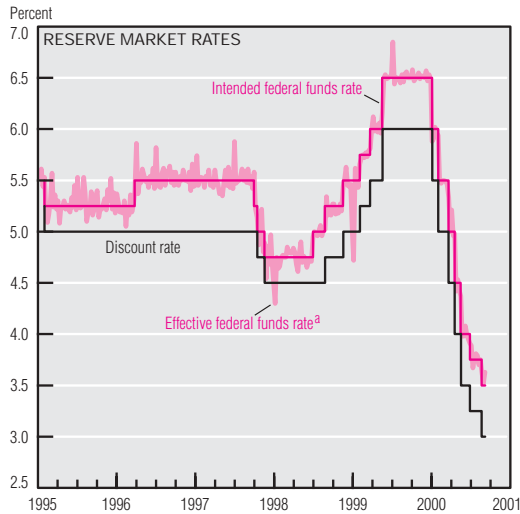


# Monetary Policy



a. Weekly average.

b. Monthly average.

SOURCES: Board of Governors of the Federal Reserve System, "Selected Interest Rates," *Federal Reserve Statistical Releases*, H.15; Chicago Board of Trade; and Bloomberg Financial Information Services.

At its August 21 meeting, the Federal Open Market Committee lowered the intended federal funds rate 25 basis points (bp) to 3½%. Its press release cited softening business profitability and capital spending as contributing to risks "weighted mainly toward conditions that may generate economic weakness in the foreseeable future." Separately, the Board of Governors approved Reserve Bank requests for a 25 bp reduction in their discount rates to 3%. The discount rate and federal funds rate have been cut a total of 300 bp each since the start of the year.

Although implied yields on federal funds futures fell slightly after the rate cut was announced, they have since rebounded. Nevertheless, market participants still attach a significant probability to a further 25 bp cut by the end of the year.

Short-term Treasury yields continue to trend downward, having fallen about 150 bp since the beginning of the year. Yields on longer-term Treasury issues have been relatively flat over this horizon. After rising from April through May, longer-term yields have since fallen between 20 bp and 40 bp.

Depository institutions are required to hold reserves based on a fraction of certain liabilities. Banks can satisfy these reserve requirements by holdings of vault cash and balances at Federal Reserve Banks. Since the mid-1990s, increased use of sweep accounts has lowered the level of required reserves. Vault cash was used to meet less than half of reserve requirements in 1990, but now accounts for more than 80%. One reason for this is the increased need to service public cash demand, particularly through ATMs.