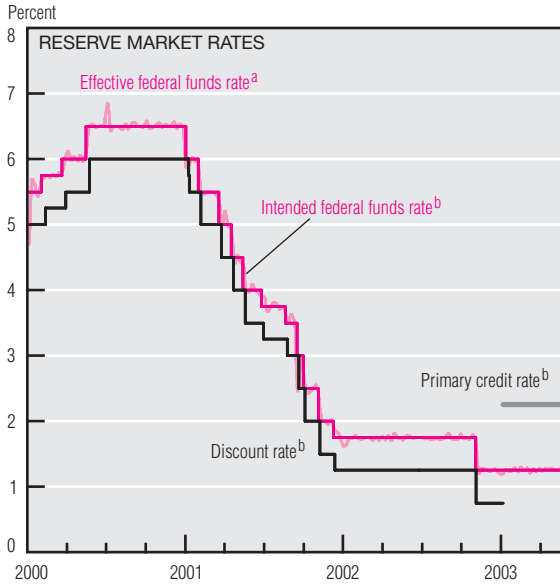


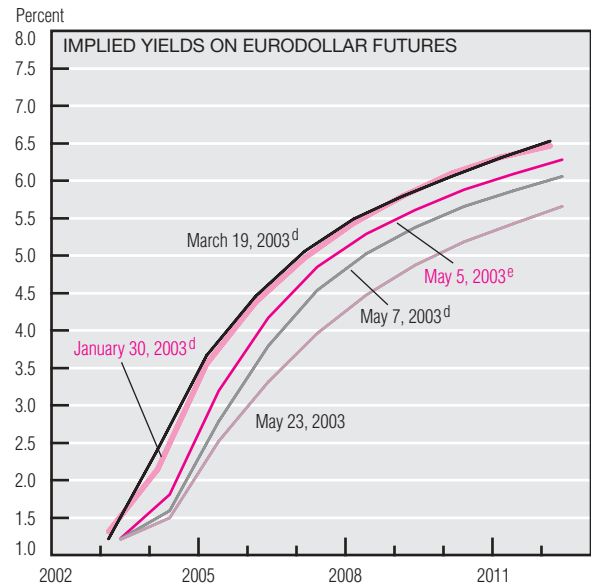
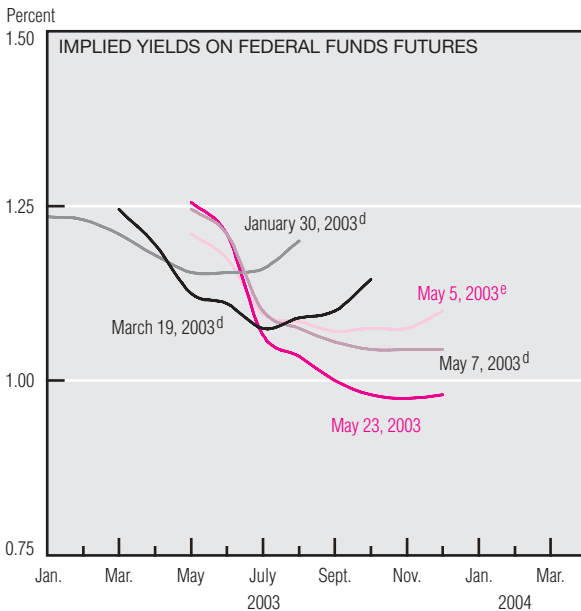
# Monetary Policy



## Balance of Risks<sup>c</sup>

### Change in federal funds target rate

Statement prior to change	-0.5	-0.25	0	0.25	0.50
Inflationary	0	0	5	3	1
Balanced	0	0	7	2	0
Weakness	6	3	3	0	0
No statement	3	0	1	0	0



- a. Weekly average of daily figures.  
 b. Daily observations.  
 c. Data taken from immediate press releases beginning in May 1999.  
 d. One day after the FOMC meeting.  
 e. One day before the FOMC meeting.  
 SOURCES: Board of Governors of the Federal Reserve System, "Selected Interest Rates," *Federal Reserve Statistical Releases*, H.15; and Bloomberg Financial Information Services.

At its May 6 meeting, the Federal Open Market Committee (FOMC) left the federal funds rate target unchanged at 1.25% and left the primary credit rate unchanged at 2.25%. Although the timing and extent of the economic recovery remain uncertain, the FOMC perceives that "over the next few quarters the upside and downside risks to the attainment of sustainable growth are roughly equal." However, their statement expressed concern over the possibility of disinflation, saying that "the probability of an unwelcome substantial fall in inflation, though minor,

exceeds that of a pickup in inflation from its already low level." For this reason, the FOMC believes that the balance of risks facing the U.S. economy is "weighted toward weakness over the foreseeable future."

One way market participants determine the direction of future policy is through the balance-of-risk statement. After a statement of either inflationary risk or balanced risk, the most common response at the next meeting has been no change. However, 75% of the time, a statement that indicates weakness has been followed by a rate cut.

Not surprisingly, the implied yield on federal funds futures moved down after the May 6 meeting. Implied yields reached a minimum of 0.975% for November 2003, suggesting that the FOMC's next move will be a cut. Eurodollar futures are another way to gauge expectations about long-term changes in the federal funds rate. As of May 2003, the eurodollar futures market suggests that the federal funds rate will start increasing significantly in another year. This, however, represents a slight decline from the market's expectations before the May meeting.