

## Meeting of the Federal Open Market Committee December 14, 2004 Presentation Materials -- Text Version

[Presentation Materials \(2.41 MB PDF\)](#)

Pages 104 to 118 of the Transcript

### Appendix 1: Materials used by Mr. Kos

#### Page 1

##### Top panel

**Title:** Current U.S. and Euro-area 3-Month Deposit Rates and Rates Implied by Traded Forward Rate Agreements

**Series:** 3-month USD Libor, USD 9-month forward rate agreement, 3-month Euro-area Libor, Euro-area 9-month forward rate agreement

**Horizon:** September 10, 2004 - December 10, 2004

**Description:** U.S. forward rate agreements and LIBOR increase slightly while Euro-area rates decline.

##### Bottom-left panel

**Title:** U.S. - German Interest Rate Differentials

**Series:** 3-month U.S. Treasury note yield less German sovereign debt yield

**Horizon:** January 2, 2004 - December 10, 2004

**Description:** 3-month U.S. - German interest rate differential widens.

##### Bottom-right panel

**Title:** U.S. - German Interest Rate Differentials

**Series:** 10-Year U.S. Treasury note yield less German sovereign debt yield

**Horizon:** January 2, 2004 - December 10, 2004

**Description:** 10-year U.S. - German interest rate differential widens.

#### Page 2

##### Top panel

**Title:** Select Foreign Currencies Against Dollar

**Series:** Foreign exchange rates against the U.S. dollar for Canadian dollar, Japanese Yen, Australian dollar, Swiss franc, British pound, and euro

**Horizon:** October 1, 2004 - December 10, 2004

**Description:** Dollar appreciates against foreign currencies.

### **Middle panel**

**Title:** IMM Commitment of Traders Report: Net Non-Commercial Currency Futures Positions Against the Dollar

**Series:** Net non-commercial currency futures positions against the U.S. dollar for the Japanese yen, euro, and British pound

**Horizon:** January 6, 2004 - December 7, 2004

**Description:** Non-commercial currency futures short the U.S. dollar.

### **Bottom panel**

**Title:** Year-to-Date Returns by Asset Class

**Series:** Year-to-date return for Treasury coupon securities, GSE debt, 30-year MBS, AA corporate, BBB corporate, high yield, S&P 500 index, and the trade-weighted U.S. dollar

**Horizon:** Through December 10, 2004

**Description:** Asset classes have positive year-to-date returns except the U.S. dollar, with a -5% year-to-date return.

Source: Lehman Brothers, Standard & Poor's and Federal Reserve Board

## **Page 3**

### **Top panel**

**Title:** Dollar-Yuan Exchange Value Implied by the NDF Market

**Series:** Dollar-yuan 1-month NDF, 6-month NDF, and 12-month NDF

**Horizon:** January 1, 2004 - December 10, 2004

**Description:** Implied dollar-Yuan exchange rate declines in the 6-month and 12-month terms.

### **Middle panel**

**Title:** Select Asian Currencies Against the Dollar

**Series:** Dollar foreign exchange rate against the South Korean won, Singapore dollar, Taiwan dollar, Indian rupee, Thai baht, and Philippine peso

**Horizon:** August 2, 2004 - December 10, 2004

**Description:** U.S. dollar depreciates against Korean won, Singapore dollar, Taiwan dollar, Indian rupee and Thai baht.

### **Bottom panel**

**Title:** FRBNY Custody Holdings

**Series:** Federal Reserve Bank of New York custody holdings of Treasury securities and Agency debt securities

**Horizon:** January 2004 - December 2004

**Description:** FRBNY custody holdings increase and agency debt securities surpass Treasuries.

## **Page 4**

### **Top panel**

**Title:** Yield Spread between 2- and 10-Year Treasury Notes

**Series:** Spread between 2- and 10-year Treasury notes

**Horizon:** January 1, 2004 - December 10, 2004

**Description:** Treasury yield curve flattens.

### **Middle panel**

**Title:** Absolute Yield Level of Non-Investment Grade Debt Indices

**Series:** EMBI+ index and high yield bond index

**Horizon:** January 1997 - December 2004

**Description:** EMBI+ and high yield bond indices decline.

Source: Merrill Lynch & JP Morgan

### **Bottom-left panel**

**Title:** MBS Spread to Treasuries

**Series:** MBS spread to Treasuries

**Horizon:** January 2000 - December 2004

**Description:** MBS spread to Treasuries narrows.

### **Bottom-right panel**

**Title:** Percent of Bank Assets Invested in MBS

**Series:** Percent of bank assets invested in MBS

**Horizon:** January 2000 - December 2004

**Description:** Percent of bank assets invested in MBS decreasing recently though still higher than historical levels.

## **Page 5**

### **Top panel**

**Title:** Annual SOMA Expansion

**Series:** Annual System Open Market Account expansion

**Horizon:** 1994 - 2004

**Description:** SOMA expansion year-to-date higher than average.

### **Middle panel**

**Title:** Currency in Circulation

**Series:** Currency in circulation

**Horizon:** December to December change, 1994 - 2004

**Description:** Currency in circulation December to December change lower than recent years.

### **Bottom panel**

**Title:** Direct Currency Shipments Abroad (Net)

**Series:** Payments less receipts for direct currency shipments abroad

**Horizon:** Annual totals for 1990 - 2004

**Description:** Direct currency shipments abroad are negative year-to-date.

## Appendix 2: Materials used by Mr. Madigan

### Material for FOMC Briefing on Monetary Policy Alternatives

Brian Madigan

December 14, 2004

Strictly Confidential (FR) Class I - FOMC

### Exhibit 1

### Market Developments and Policy Expectations

#### Top-left panel

#### Yields and Stock Prices

	Dec. 13	Net change from Nov. 9
U.S. Treasury yields*	-percent-	-basis points-
1. Two-year	2.98	17
2. Five-year	3.52	2
3. Ten-year	4.27	-9
4. Five-year TIPS	0.96	-2
5. Ten-year TIPS	1.66	-9
Equity Indexes	-level-	-percent-
6. Wilshire	11790	3.4
7. Nasdaq	2148	5.1

\* Nominal yields derived from smoothed yield curve based on off-the-run securities. TIPS yields based on smoothed yield curve. [Return to table](#)

#### Top-right panel

#### Expected Federal Funds Rates\*

A line chart displays the expected path of the federal funds rate embedded in futures quotes as of November 9 and December 13, 2004. This chart indicates that the December 13 expected path of monetary policy edged up relative to the November 9 path for the next year or so, but declined slightly in the longer-term. Current futures quotes suggest that the federal funds rate will rise to around 3½ percent by the fourth quarter of 2007.

\* Estimates from federal funds and eurodollar futures, with an allowance for term premia and other adjustments. [Return to text](#)

#### Middle panel

#### Desk Survey of Primary Dealers

- Unanimously expect 25-basis-point firming today.
- Unanimously expect retention of balanced risks and "measured pace" language.
- Apparently none expects signal of a pause today.

#### Bottom panel

## Longer-term Policy Expectations

- Two dealers expect a pause in February and seven in March.
- Futures quotes can be read as implying a pause in March and a move roughly every other meeting over the rest of year.
- Blue Chip consensus consistent with two pauses before Fall 2005.

## Exhibit 2

### Case For Firming Policy

#### Top panel

##### Arguments For Firming Policy Today

- Expansion seems well entrenched, with labor market conditions improving gradually
- Concern about a buildup of inflationary pressure
  - possible slowing of productivity growth
  - actual inflation has risen
  - short-term inflation expectations up
  - anecdotal information on price pressures
  - inflation surprises to the upside of market expectations
  - dollar depreciation
- Real federal funds rate well below most estimates of its equilibrium level

#### Middle panel

##### Short-Run Equilibrium Real Federal Funds Rate

A line chart shows the actual federal funds rate with bands of shading representing the confidence interval of model-based estimates and a dashed line charting the Greenbook forecast. The actual rate is currently a bit below the 70 percent confidence interval of the model-based estimates and noticeably below the estimate implicit in the Greenbook forecast.

#### Bottom-left panel

##### Arguments For Alternative B

Policy firming can now proceed at slower pace:

- Some output gap remains; not closing rapidly
- Significant reduction in policy accommodation already accomplished
- Unusual business caution may persist

#### Bottom-right panel

##### Arguments For Alternative C

Recent pace of tightening should be maintained:

- Substantial remaining policy accommodation
- Policy works with long lags
- Signs of pressure on inflation and inflation expectations
- Buoyant attitudes toward risk in financial markets

### Exhibit 3

**Table 1: Alternative Language for the December FOMC Announcement**

[Note: In Table 1, emphasis (*italic*) has been added to indicate red text in the original document. Strong emphasis (**bold**) indicates bold text in the original document.]

	<b>November FOMC</b>	<b>Alternative A</b>	<b>Alternative B</b>	<b>Alternative C</b>
<b>Policy Decision</b>	1. The Federal Open Market Committee decided today to raise its target for the federal funds rate by 25 basis points to 2 percent.	The Federal Open Market Committee decided today to <i>keep its target for the federal funds rate at 2 percent.</i>	The Federal Open Market Committee decided today to raise its target for the federal funds rate by 25 basis points to <i>2¼ percent. The Committee's policy actions since mid-2004 have resulted in a significant reduction in the degree of monetary policy accommodation.</i>	The Federal Open Market Committee decided today to raise its target for the federal funds rate by 25 basis points to <i>2¼ percent.</i>
<b>Rationale</b>	2. The Committee believes that, even after this action, the stance of monetary policy remains accommodative and, coupled with robust underlying growth in productivity, is providing ongoing support to economic activity.	The Committee believes that the stance of monetary policy remains <i>somewhat</i> accommodative and, coupled with robust underlying growth in productivity, is providing ongoing support to economic activity.	<i>Nonetheless, the</i> Committee believes that, even after this action, the stance of monetary policy remains <i>somewhat</i> accommodative and, coupled with robust underlying growth in productivity, is providing ongoing support to economic activity.	[Unchanged from November statement]
	3. Output appears to be growing at a moderate pace despite the rise in energy prices, and labor market conditions have improved.	Output appears to be growing at a moderate pace, <i>but</i> labor market conditions <i>have been improving only gradually, apparently evidencing continued business caution.</i>	Output appears to be growing at a moderate pace despite the <i>earlier</i> rise in energy prices, and labor market conditions <i>continue to improve gradually.</i>	Output appears to be growing at a moderate pace despite the <i>earlier</i> rise in energy prices, and labor market conditions <i>continue to improve gradually.</i>
	4. Inflation and longer-term inflation expectations remain well contained.	[Unchanged from November statement]	[Unchanged from November statement]	[Unchanged from November statement]
<b>Assessment of Risk</b>	5. The Committee perceives the upside and downside risks to the attainment of both sustainable growth and price stability for the next few quarters to be roughly	[Unchanged from November statement]	[Unchanged from November statement]	[Unchanged from November statement]

	November FOMC	Alternative A	Alternative B	Alternative C
	equal.			
	6. With underlying inflation expected to be relatively low, the Committee believes that policy accommodation can be removed at a pace that is likely to be measured. Nonetheless, the Committee will respond to changes in economic prospects as needed to fulfill its obligation to maintain price stability.	With underlying inflation expected to be relatively low, the Committee believes that policy accommodation can be removed at a pace that is likely to be measured. Nonetheless, the Committee will respond to changes in economic prospects as needed to fulfill its obligation to <i>promote price stability and sustainable growth</i> .	[Unchanged from November statement]	[Unchanged from November statement]

### Appendix 3: Materials used by Mr. Reinhart

#### Exhibit 1

##### Top panel

##### Arguments For and Against Expediting the Release of the Minutes:

###### For:

- Provide more timely and nuanced information to the public
- Convey the range of views within the Committee
- The policy statement could potentially be shortened

###### Against:

- Lead to undue market attention to the minutes
- Complicate the Committee's deliberations
- Lead to the minutes becoming more sanitized and unhelpful over time
- May be operationally difficult

##### Middle panel

##### Schedule for the Experiment with Expediting the Release of the Minutes

Week	Monday	Tuesday	Wednesday	Thursday	Friday
0		FOMC meeting			
+1				C.O.B.: First draft posted	
+2	Noon: Comments from the FOMC	C.O.B.: Second draft posted	C.O.B.: Final draft posted;		Noon: FOMC vote closes

Week	Monday	Tuesday	Wednesday	Thursday	Friday
			Voting begins		2:00 P.M.: PUBLISH <i>(hypothetically)</i>

## Bottom panel

### Changes in the Production of the Minutes

- Contracted with a private firm to produce a transcript quickly
- Distributed drafting responsibilities among more staff
- Provided more systematic feedback on comments in the final week
- Developed a procedure for secure voting
- Collaborated with staff in Public Affairs and the FRBNY to assess the likely financial market reaction to the minutes

## Exhibit 2

### Top panel

#### Lessons Learned

1. Using more resources to produce and distribute the minutes soon after the meeting is helpful.
2. Not all participants were familiar with all the rules governing the drafting of the minutes.
3. The expedited schedule poses the risks that:
  - a. Not all members will be able to vote by the deadline.
  - b. The schedule may be too tight to guarantee achieving a consensus.
4. Friday afternoon is a terrible time to release the minutes.

### Bottom panel

#### Untested Aspects

The experiment was conducted during a period in which:

1. There were no significant disagreements among members about the overall direction of policy.
2. There were no intermeeting conference calls.

The experiment stopped short of actually releasing the statement early, implying that:

3. It is unclear how much increased scrutiny more timely minutes will receive or how members will adjust their editing behavior.
4. It is unclear how the public will react to conditional statements.

## Exhibit 3

### Three Possibilities for Today's Meeting

#### 1. Vote today to expedite the release of the minutes



If so, I recommend beginning expedited release with the minutes of the February 2005 meeting and adopting a schedule of releasing the minutes of regular meeting three weeks after the day of the policy decision.

- By beginning with the February meeting, the decision would be noted in the minutes of today's meeting, which would be released after the February meeting and thus give the public advance notice of the new policy.
- Adding a few days to the schedule by releasing the minutes after three weeks would:
  - Give staff more time to draft and participants more time to comment.
  - Position the release in the middle of the week, which would be less likely to cause difficulties.

## **2. Extend the experiment**

If so, I recommend shifting to a three-week schedule because it seems more sustainable.

## **3. Stop the experiment**

If so, I recommend continuing approximately the same production and distribution schedule so that the minutes are prepared while the memory of the meeting is still fresh.

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