

## Meeting of the Federal Open Market Committee September 18, 2007 Presentation Materials -- Text Version

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

Pages 169 to 188 of the Transcript

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

Class II FOMC - Restricted FR

#### Page 1

##### Top panel

(1)

**Title:** Spread between Jumbo and Conforming Mortgage Rates Widens

**Series:** Jumbo mortgage rates and conforming mortgage rates

**Horizon:** January 1, 2007 - September 14, 2007

**Description:** Jumbo mortgage rates have been increasing quicker than conforming mortgage rates.

Source: Bloomberg

##### Middle panel

(2)

**Title:** ABCP Spreads Widen as Concerns Increase Regarding Underlying Collateral

**Series:** Unsecured and secured commercial paper discount rates

**Horizon:** January 1, 2007 - September 14, 2007

**Description:** Since early August, the spread between secured and unsecured commercial paper rates has been widening.

Source: Federal Reserve Board

##### Bottom panel

(3)

**Title:** Outstanding ABCP Declines Sharply as Average Rate Increases Significantly

**Series:** Outstanding volume of ABCP and average rate of ABCP

**Horizon:** January 1, 2007 - September 12, 2007

**Description:** While rates on ABCP rise, the outstanding ABCP volume has been declining.

Source: Federal Reserve Board

## Top panel

(4)

**Title:** Asset-Backed Commercial Paper Maturities

**Series:** Volume of ABCP maturing each day.

**Horizon:** September 12, 2007

**Description:** The volume of ABCP maturing overnight as compared to longer tenors has grown significantly since the August FOMC meeting

Source: Federal Reserve Board

## Middle panel

(5)

**Title:** While Prime Funds Decline, Treasury Only Funds Increase Significantly

**Series:** Prime Fund and Treasury Only Fund investment amounts

**Horizon:** January 1, 2007 - September 11, 2007

**Description:** While the amount of investments being made in prime fund declined, investment in Treasury Only funds increased.

Source: iMoneyNet

## Bottom panel

(6)

**Title:** Treasury Bills Yields Decline as Investor Demand for Safer Assets Increases

**Series:** One-month, Three-month, and Six-month Treasury yields

**Horizon:** January 1, 2007 - September 14, 2007

**Description:** Treasury bill yields have declined sharply since the August FOMC meeting.

Source: Bloomberg

## Page 3

## Top panel

### (7) Asset-Backed Commercial Paper by Type

As of September 14, 2007

Type of ABCP	Billions of dollars	Percent
Multi-Seller	487	52
Single-Seller	61	6
Extendible	14	1
Hybrid	71	8
Securities Arbitrage	121	13
CDO	36	4
SIV	63	7
Other	92	10

Source: Federal Reserve Board

### **Middle panel**

**(8)**

**Title:** Asset-Backed Commercial Paper by Underlying Collateral

**Series:** Volume of ABCP backed by mortgages, equipment, student loans, ABS other, auto loans, trade receivables, credit cards, auto, financial, and other collateral

**Horizon:** March 2007

**Description:** Mortgages make up a significant portion of collateral used to back ABCP.

Source: Moody's

### **Bottom panel**

**(9)**

**Title:** CLO and CDO Issuance Declines

**Series:** CLO and CDO issuance volume by month

**Horizon:** January 2006 - August 2007

**Description:** As demand for CLOs and CDOs declined due to recent credit problems, issuance of these securities has also declined.

Source: Merrill Lynch

## **Page 4**

### **Top panel**

**(10)**

**Title:** High-Yield Issuance Declines

**Series:** High-yield and investment grade issuance volume by month

**Horizon:** January 2006 - August 2007

**Description:** Issuance for high-yield securities has declined due to declining demand for these securities.

Source: Bloomberg

### **Middle panel**

**(11)**

**Title:** Repo Bid/Ask Spread: Median

**Series:** Repurchase agreement bid-ask spreads for repurchase agreements backed by high-yield corporate debt collateral, prime MBS collateral, and GSE MBS collateral for overnight, one-week, and one-month tenors.

**Horizon:** July 2, 2007 - September 14, 2007

**Description:** The most significant widening in bid-ask spreads was seen in the one-month tenor for repurchase agreements backed by prime MBS.

Source: Survey of 10 Primary Dealers

### **Bottom panel**

**(12)**

**Title:** Repo Collateral Haircuts: Median

**Series:** Repurchase agreement collateral haircuts for repurchase agreements backed by high-yield corporate debt collateral, prime MBS collateral, and GSE MBS collateral for overnight, one-week, and one-month tenors.

**Horizon:** July 2, 2007 - September 14, 2007

**Description:** The most significant increase in repurchase agreement haircuts was seen in the one-month tenor for repurchase agreements backed by high-yield corporate debt.

Source: Survey of 10 Primary Dealers

## Page 5

### Top panel

(13)

**Title:** Banks' Balance Sheet Pressures Raise U.S. Term Funding Rates

**Series:** One-month Libor rate, one-month interest rate swap rate, and one-month one-month forward policy rate expectations

**Horizon:** August 1, 2007 - September 14, 2007

**Description:** One-month Libor rate increases while expectation for the policy rate easing increases.

Source: Bloomberg

### Middle panel

(14)

**Title:** Euro Term Funding Pressures Also Evident

**Series:** One-month Euribor and one-month EONIA swap rates

**Horizon:** August 1, 2007 - September 14, 2007

**Description:** One-month Euribor rates increase while policy expectations for the Euro-area remain unchanged.

Source: Bloomberg

### Bottom panel

(15)

**Title:** Overnight and Term Primary Credit Facility Borrowing

**Series:** Level of overnight and term primary credit borrowing and the discount window rate

**Horizon:** July 2, 2007 - September 14, 2007

**Description:** After the discount rate was lowered by 50 basis points, primary credit borrowing increased slightly.

Source: FRBNY

## Page 6

### Top panel

(16) Correlation of Daily Price/Yield Changes

August 7, 2007 - September 14, 2007

Blue boxes denote correlations greater than 0.50 or less than -0.50

<i>Variables</i>	<b>2YR Yield</b>	<b>10YR Yield</b>	<b>S&amp;P</b>	<b>USD/JPY</b>	<b>Swap Spreads</b>	<b>VIX</b>	<b>CDX IG</b>
<b>2YR Yield</b>							
<b>10YR Yield</b>	0.89						
<b>S&amp;P</b>	0.73	0.74					
<b>USD/JPY</b>	0.80	0.77	0.72				
<b>Swap Spreads</b>	-0.55	-0.36	-0.56	-0.39			
<b>VIX</b>	-0.63	-0.53	-0.82	-0.66	0.58		
<b>CDX IG</b>	0.62	0.64	0.72	0.49	-0.60	-0.60	
<b>Merrill-HY</b>	-0.84	-0.78	-0.54	-0.77	0.53	0.46	-0.55

Source: Bloomberg and JP Morgan

## Middle panel (17)

**Title:** Dollar Weakens

**Series:** Yen vs. USD, Euro vs. USD

**Horizon:** January 1, 2007 - September 14, 2007

**Description:** Since mid-June, the U.S. dollar has softened against the Euro and Japanese Yen. Consistent with this, the Broad Trade-Weighted Dollar has also been declining.

Source: Bloomberg and Federal Reserve Board

## Bottom panel (18)

**Title:** Dollar Tracks Interest Rate Differentials

**Series:** Eurodollar and Euribor contract spread and Euro-USD currency pair

**Horizon:** January 1, 2007 - September 14, 2007

**Description:** The U.S. Dollar against the Euro has been tracking closely to the change in interest rate differentials between the U.S and the Euro-area.

Source: Bloomberg

## Page 7

## Top panel (19)

**Title:** Distribution of Expected Policy Target Among Primary Dealers Prior to September 18 FOMC Meeting

**Series:** Dealer expectations for policy target rate by quarter, average forecast for policy target by quarter, and market rate for policy expectation by quarter as of 9/10/2007

**Horizon:** Q3 2007 - Q4 2008

**Description:** There is less dispersion regarding where dealers expect the policy rate to be in Q4 2007. Dealers on average expect higher rates than what is currently priced into overnight index swaps.

Source: Dealer Policy Survey

### **Middle panel (20)**

**Title:** Distribution of Expected Policy Target Among Primary Dealers Prior to August 7 FOMC Meeting

**Series:** Dealer expectations for policy target rate by quarter, average forecast for policy target by quarter, and market rate for policy expectation by quarter as of 7/31/2007

**Horizon:** Q3 2007 - Q4 2008

**Description:** Compared to the September policy survey, there is more dispersion of policy rate expectation for Q4 2007. Dealers on average expect higher rates than what is currently priced into Eurodollar futures.

Source: Dealer Policy Survey

### **Bottom panel (21)**

**Title:** Probability Distribution on Eurodollar Futures Contract

**Series:** Probability distribution on Eurodollar futures contract as of 8/6/2007 and 9/14/2007

**Horizon:** August 6, 2007 - September 14, 2007

**Description:** Since the August FOMC meeting, the probability of policy rate cut has increased significantly.

Source: CME Option

## **Page 8**

### **Top panel (22)**

**Title:** Daily Excess Reserves and the Federal Funds Rate

**Series:** Daily excess excluding borrowing, Fed Funds effective rate, 9am Fed Funds rate, and average excess since January 2006

**Horizon:** July 2, 2007 - September 14, 2007

**Description:** After a large excess level on August 8<sup>th</sup>, the fed funds rate declined sharply and traded below the target rate for much of the remaining inter-meeting period.

Source: FRBNY

## **APPENDIX: Reference Exhibits**

### **Page 9**

#### **Top panel**

(23)

**Title:** Treasury Yield Curve Shift Lower and Steepens

**Series:** Constant maturity Treasury yield curve as of 6/27/2007, 8/6/2007, and 9/14/2007

**Horizon:** June 27, 2007 - September 14, 2007

**Description:** The Treasury yield curve has shifted lower and steepened since the last FOMC meetings.

Source: Bloomberg

**Middle panel**

(24)

**Title:** 10-Year Treasury Inflation Protected and Nominal Treasury Yields

**Series:** 10-Year nominal Treasury yield and 10-Year inflation protected Treasury yield

**Horizon:** January 1, 2007 - September 14, 2007

**Description:** Both nominal and inflation protected Treasury yields have declined since the last FOMC meeting.

Source: Bloomberg

**Bottom panel**

(25)

**Title:** TIPS Inflation Compensation: 5-10 Year Horizon

**Series:** 5-10 Year horizon TIPS inflation compensation

**Horizon:** June 1, 2006 - September 14, 2007

**Description:** TIPS inflation compensation over a 5-10 year horizon has increased since June.

Source: Federal Reserve Board

## Page 10

**Top panel**

(26)

**Title:** U.S. Equity Indices Partially Reverse Sharp Decline

**Series:** S&P 500 index, Nasdaq index, and Russell 2000 index

**Horizon:** January 1, 2007 - September 14, 2007

**Description:** U.S. equity indices have partially reversed the sharp decline seen in previous inter-meeting period.

Source: Bloomberg

**Middle panel**

(27)

**Title:** Implied Volatility Has Increased in Recent Weeks

**Series:** VIX index, SMOVE 1-month index, 1-month Euro-Dollar Volatility index, and 1-month Dollar-Yen volatility index

**Horizon:** January 1, 2007 - September 14, 2007

**Description:** During the inter-meeting period, implied volatility across asset classes has increased in recent weeks except for the Euro-dollar currency pair.

Source: Bloomberg

## Appendix 2: Materials used by Mr. Madigan

### Material for FOMC Briefing on September Trial-Run Projections

Brian Madigan

September 18, 2007

#### Class I FOMC - Restricted Controlled (FR)

### Page 1

#### Top panel

#### Participants' Implied Economic Projections for the second half of 2007 [1](#)

	Central Tendency	Range
Real GDP Growth (saar)	<b>1.7 to 2.3</b> (2.0 to 2.7)	<b>1.6 to 2.6</b> (1.8 to 3.0)
Unemployment Rate (% , Q4)	<b>4.7 to 4.8</b> (4.6 to 4.7)	<b>4.7 to 4.8</b> (4.5 to 4.8)
Total PCE Inflation (saar)	<b>1.7 to 2.1</b> (2.0 to 2.6)	<b>1.5 to 2.1</b> (1.9 to 3.1)
Core PCE inflation (saar)	<b>1.9 to 2.1</b> (1.9 to 2.1)	<b>1.7 to 2.3</b> (1.9 to 2.2)

<sup>1</sup> Central tendencies and ranges of projections for the second half of 2007 implied by participants' September projections for the first half of 2007 and for 2007 as a whole. (August projections for the second half of 2007 are shown in parentheses.) [Return to text](#)

#### Bottom panel

#### Participants' Full-Year Economic Projections for 2007-2010

	2007	2008	2009	2010
<b>Real GDP Growth</b>				
Central Tendency	<b>2.0 to 2.2</b>	<b>1.9 to 2.5</b>	<b>2.3 to 2.7</b>	<b>2.4 to 2.6</b>
(Central Tendency of August Projections)		(2.2 to 2.7)	(2.4 to 2.7)	
Range	<b>1.9 to 2.4</b>	<b>1.6 to 2.7</b>	<b>2 to 2.8</b>	<b>2.2 to 2.8</b>
(Range of August Projections)		(1.9 to 2.8)	(2.0 to 3.1)	
<b>Unemployment Rate</b>				
Central Tendency	<b>4.7 to 4.8</b>	<b>4.8 to 5.0</b>	<b>4.8 to 5.0</b>	<b>4.8 to 4.9</b>
(Central Tendency of August Projections)	(4.6 to 4.7)	(4.6 to 4.8)	(4.7 to 5.0)	
Range	<b>4.7 to 4.8</b>	<b>4.6 to 5.1</b>	<b>4.6 to 5.1</b>	<b>4.6 to 5.0</b>
(Range of August Projections)	(4.5 to 4.8)	(4.5 to 4.9)	(4.4 to 5.2)	
<b>Total PCE Inflation</b>				
Central Tendency	<b>2.8 to 3.0</b>	<b>1.7 to 2.0</b>	<b>1.7 to 2.0</b>	<b>1.6 to 1.9</b>
(Central Tendency of August Projections)		(1.8 to 2.1)	(1.6 to 2.0)	



	2007	2008	2009	2010
<b>Range</b>	<b>2.7 to 3.0</b>	<b>1.6 to 2.4</b>	<b>1.5 to 2.3</b>	<b>1.5 to 2.2</b>
<i>(Range of August Projections)</i>		<i>(1.7 to 2.4)</i>	<i>(1.5 to 2.2)</i>	
<b>Core PCE Inflation</b>				
<b>Central Tendency</b>	<b>1.9 to 2.0</b>	<b>1.8 to 2.0</b>	<b>1.7 to 1.9</b>	<b>1.6 to 1.9</b>
<i>(Central Tendency of August Projections)</i>		<i>(1.8 to 2.0)</i>	<i>(1.6 to 1.9)</i>	
<b>Range</b>	<b>1.8 to 2.2</b>	<b>1.7 to 2.1</b>	<b>1.5 to 2.0</b>	<b>1.5 to 2.0</b>
<i>(Range of August Projections)</i>		<i>(1.7 to 2.1)</i>	<i>(1.5 to 2.0)</i>	

Projections for real GDP growth, total PCE inflation, and core PCE inflation are Q4/Q4 percentage changes. Projections for the unemployment rate are for the average civilian unemployment rate in the fourth quarter of each year. Each respondent's projections are based on his or her assessment of an appropriate path for monetary policy. The central tendencies exclude the three highest and three lowest projections for each variable in each year.

## Appendix 3: Materials used by Mr. Madigan

**Table 1:**  
**Alternative Language for the September 2007 FOMC Announcement**

September 18, 2007

[Note: In Appendix 3, Table 1, strong emphasis (bold) has been added to indicate red text in the original document, and emphasis (italics) has been added to indicate blue text in the original document. Exception: On row 4 (Assessment of Risk), strong emphasis indicates red text in the original document, and emphasis indicates underlined red text in the original document.]

	Alternative A	Alternative B	Alternative C	Alternative D
<b>Policy Decision</b>	1. The Federal Open Market Committee decided today to <b>lower</b> its target for the federal funds rate <b>50 basis points to 4¾ percent</b> .	The Federal Open Market Committee decided today to <b>lower</b> its target for the federal funds rate <b>50 basis points to 4¾ percent</b> .	The Federal Open Market Committee decided today to <b>lower</b> its target for the federal funds rate <b>25 basis points to 5 percent</b> .	The Federal Open Market Committee decided today to keep its target for the federal funds rate at 5¼ percent.
<b>Rationale</b>	2. <i>Tighter credit conditions and the intensification of the housing correction appear likely to exert appreciable restraint on economic growth. Moreover, the potential for significant spillovers from credit market disruptions to business and household spending poses a risk to the outlook. Today's action is intended to help mitigate the adverse effects on the broader economy arising from the disruptions in financial markets and to promote moderate growth over time.</i>	Economic growth was moderate during the first half of the year, <b>but the tightening of credit conditions has the potential to intensify the housing correction and to restrain economic growth more generally. Today's action is intended to help forestall some of the adverse effects on the broader economy that might otherwise arise from the disruptions in financial markets and to promote moderate growth over time.</b>	Economic growth was moderate during the first half of the year, <b>but the tightening of credit conditions has the potential to intensify the housing correction and to restrain economic growth more generally. Today's action is intended to help forestall some of the adverse effects on the broader economy that might otherwise arise from the disruptions in financial markets and to promote moderate growth over time.</b>	Economic growth was moderate during the first half of the year. <i>Financial market conditions have deteriorated in recent weeks, leading to tighter credit and an intensification of the housing correction. These developments have the potential to restrain growth in economic activity. Nonetheless, the economy seems likely to continue to expand at a moderate pace over coming quarters, supported by solid growth outside the housing sector and a robust global economy.</i>

	Alternative A	Alternative B	Alternative C	Alternative D
	3. Readings on core inflation have improved modestly <b>this year. However, the Committee judges that some inflation risks remain, and it will continue to monitor inflation developments carefully.</b>	Readings on core inflation have improved modestly <b>this year. However, the Committee judges that some inflation risks remain, and it will continue to monitor inflation developments carefully.</b>	Readings on core inflation have improved modestly <b>this year. However, the Committee judges that some inflation risks remain, and it will continue to monitor inflation developments carefully.</b>	Readings on core inflation have improved modestly <b>this year.</b> However, a sustained moderation in inflation pressures has yet to be convincingly demonstrated. Moreover, the high level of resource utilization has the potential to sustain those pressures.
Assessment of Risk	4. <b>Even after today's action, the Committee judges that the downside risks to economic growth outweigh the upside risks to inflation.</b> Future policy adjustments will depend on the outlook for both inflation and economic growth, as implied by incoming information.	<i>Developments in financial markets since the Committee's last regular meeting have increased the uncertainty surrounding the economic outlook. The Committee will continue to assess the effects of these and other developments on economic prospects and will act as needed to foster price stability and sustainable economic growth.</i>	<b>Even after today's action, the Committee judges that the downside risks to economic growth outweigh the upside risks to inflation.</b> Future policy adjustments will depend on the outlook for both inflation and economic growth, as implied by incoming information.	<b>In the current circumstances, the Committee judges that the downside risks to economic growth are now roughly balanced by the upside risks to inflation.</b> Future policy adjustments will depend on the outlook for both inflation and economic growth, as implied by incoming information.

## Appendix 4: Materials used by Ms. Krieger

Material for **Briefing on Staff Proposals for Auction Credit Facility and Swap Arrangements**  
September 18, 2007

### Restricted Controlled (FR)

**Table 1:**  
**Basic ACF Terms and Parameters**

ACF Rate	Fixed-rate determined via centralized single-price auction; expressed to two decimal places, e.g. 5.24 percent
Term	28-day (27 or 29 days in the case of a Thursday holiday, such as Thanksgiving)
Collateral	Any collateral eligible to secure discount window loan. Reserve Banks' standard valuation and haircuts procedures apply.
Auction Cycle	Weekly auctions  Announce Friday Bid window closes Monday afternoon Bids transmitted to System auction agent Monday afternoon Winning bids determined Tuesday Auction results announced Wednesday morning Winning bidders notified by local Reserve Bank Wednesday Auction settlement on Thursday
Minimum Bid (Size)	\$50 million initially; may be reduced subsequently at discretion of Auction Agent

Maximum Number of Propositions per Depository Institution	2
Maximum Bid (Size) Aggregated Across All Propositions for an Individual Depository	20 percent of announced auction amount
Maximum ACF Available to Any Single Depository, based on Lendable Collateral Value	Bids will be constrained to ensure that total ACF credit outstanding does not exceed 80 percent of lendable collateral value
Eligible Depositories	Those eligible for primary credit--that is, those determined by the lending Reserve Bank to be in generally sound financial condition. Must have borrowing agreements and collateral in place.
Prepayment	Not permitted.
Minimum Bid Rate	"Market-based term rate"; Internally, use the Overnight Index Swap rate plus 10 basis points
Auction Amount	Announced quantity determined by Board ACF subcommittee; System Auction Agent can adjust up or down by 10 percent in light of strength of propositions.
Foreign Branches	Foreign branches bid through their local Reserve Banks, but the Auction Agent will aggregate bids of each FBO and impose the single bidder requirements on the aggregated bids of the branches of the same FBO (i.e. only two bids permitted, together and individually not larger than 20 percent of the total auction amount). The Auction Agent will disaggregate the winning bids of the FBOs proportionally to the corresponding underlying bids and local Reserve Banks will book the loans accordingly.

## Auction Credit Facility

### Weekly Workflow Timeline\* and Roles/Responsibilities

<b>Board</b>	<b>Auction Announcement</b> auction parameters and minimum bid rate (noon)			<b>Auction Results Announcement</b> (10 am)	
	<b>Announcement Date</b> (Friday)	<b>Bid Submission Date</b> (Monday)	<b>Allocation Date</b> (Tuesday)	<b>Notification Date</b> (Wednesday)	<b>Settlement Date</b> (Thursday)
<b>RB Discount Window Staff</b>	Field DI questions on bidding process, auction results, settlement dates, etc.	Prepare automated report listing pledged collateral, lendable values;  Receive and verify bids; Validate auction bid criteria met; Complete Bid Submission forms and District Bid Sheet;  Provide Bid Submission to		Contact DIs with winning bids	Post awarded funds to winning bidders; Notify Auction Agent upon completion

		Auction Agent			
<b><i>Auction Agent (NY)</i></b>		Verify receipt of bid submissions	Consolidate bid submissions; Determine auction awards and stop-out rate based on Dutch Auction principles; Communicate proposed awards to RBs for confirmation; Confirmation required ;		
			<div> <b>Dutch Auction:</b> Bids accepted in accordance with announced terms (e.g. maximum and minimum bid sizes, and adequate collateral); Acceptable bids sorted from high to low; Auction winners pay the stop-out rate. </div>		

\* Dates and times are illustrative [Return to text](#)

▲ [Return to top](#)

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