Appendix 1: Materials used by Mr. Dudley
(1) U.S. Equity Indices
August 1, 2007 – June 20, 2008

Source: Bloomberg

(2) Corporate Credit Spreads and Yields
January 1, 2007 – June 20, 2008

Source: Bloomberg

(3) Global Credit Default Swap Spreads
May 1, 2007 – June 20, 2008

Source: Bloomberg, Lehman Brothers
(4) Investment Bank Equity Prices
January 1, 2008 – June 20, 2008

Source: Bloomberg

(5) Investment Bank CDS Spreads
January 1, 2008 – June 20, 2008

Source: Markit

(6) Investment Bank Financial Leverage Ratios

Source: Bloomberg
(7) Financial Guarantor Equity Prices
January 1, 2008 – June 20, 2008

Source: Bloomberg

(8) Financial Guarantor CDS Spreads
January 1, 2008 – June 20, 2008

Source: Markit

(9) Ten- and Thirty-Year AAA–Rated Municipals*
January 1, 2007 – June 20, 2008

Source: Bloomberg

*This chart shows the ratio of municipal debt yields to Treasury yields.
(10) One-Month Libor–OIS Spreads  
August 14, 2007 – June 20, 2008

Source: Bloomberg

(11) Three-Month Libor – OIS Spreads  
August 14, 2007 – June 20, 2008

Source: Bloomberg
(12) Federal Reserve Term Auction Facility Results

Source: Federal Reserve Board

(13) Central Bank Term Funding Facilities’ Bid-to-Cover Ratios

Source: Federal Reserve Board, European Central Bank, Swiss National Bank
(14) Commodity Prices
January 1, 2008 – June 20, 2008

Source: Bloomberg

(15) Dollar Stabilizes
January 1, 2008 – June 20, 2008

Source: Bloomberg and Federal Reserve Board

(16) Correlation Between Weekly Changes in Spot WTI Crude Oil and the Trade-Weighted Dollar

**One-year rolling correlation of percentage changes in the weekly average of daily closing prices of the WTI spot crude oil price and the Federal Reserve Board’s nominal trade-weighted dollar index (vis-à-vis major currencies).

Source: Federal Reserve Board, CEIC
(17) University of Michigan Inflation Expectations
June 1, 1980 – June 20, 2008

Source: Bloomberg

(18) TIPS Implied Average Rate of Inflation: 5-10 Year Horizon
August 1, 2007 – June 20, 2008

Source: Federal Reserve Board, Barclays Capital
(19) Fed Funds Futures Curves

Source: Bloomberg

(20) Eurodollar Futures Curves

Source: Bloomberg
(21) Distribution of Expected Policy Target Rate Among Primary Dealers Prior to June 25 FOMC Meeting

Source: Dealer Policy Survey

(22) Distribution of Expected Policy Target Rate Among Primary Dealers Prior to April 29-30 FOMC Meeting

Source: Dealer Policy Survey
(23) Probabilities for Policy Rate Outcomes for June FOMC Meeting
April 1, 2008 – June 20, 2008

Source: Federal Reserve Bank of Cleveland

(24) Probabilities for Policy Rate Outcomes for August FOMC Meeting
May 9, 2008 – June 20, 2008

Source: Federal Reserve Bank of Cleveland

(25) Considerable Tightening Expected Over the Next Year
June 24–25, 2008

*BPS

*Adjusted based on forward Libor-fed funds basis swap spreads

Note: Dates represent last interest rate cut of previous cycles and assumes 4/30/08 is the last interest rate cut of the current cycle.

Source: Bloomberg
### (26) Federal Reserve Term Auction Facility Results

<table>
<thead>
<tr>
<th>Settlement</th>
<th>Term</th>
<th>Amount</th>
<th>Minimum Bid Rate</th>
<th>Stop-out Rate</th>
<th>Propositions</th>
<th>Bid/Cover</th>
<th>Bidders</th>
</tr>
</thead>
<tbody>
<tr>
<td>12/20/2007</td>
<td>28 Days</td>
<td>$20 b</td>
<td>4.17%</td>
<td>4.65%</td>
<td>$61.6 b</td>
<td>3.08</td>
<td>93</td>
</tr>
<tr>
<td>12/27/2007</td>
<td>35 Days</td>
<td>$20 b</td>
<td>4.15%</td>
<td>4.67%</td>
<td>$57.7 b</td>
<td>2.88</td>
<td>73</td>
</tr>
<tr>
<td>1/17/2008</td>
<td>28 Days</td>
<td>$30 b</td>
<td>3.88%</td>
<td>3.95%</td>
<td>$55.5 b</td>
<td>1.85</td>
<td>56</td>
</tr>
<tr>
<td>1/31/2008</td>
<td>28 Days</td>
<td>$30 b</td>
<td>3.10%</td>
<td>3.12%</td>
<td>$37.5 b</td>
<td>1.25</td>
<td>52</td>
</tr>
<tr>
<td>2/14/2008</td>
<td>28 Days</td>
<td>$30 b</td>
<td>2.86%</td>
<td>3.01%</td>
<td>$58.4 b</td>
<td>1.95</td>
<td>66</td>
</tr>
<tr>
<td>2/28/2008</td>
<td>28 Days</td>
<td>$30 b</td>
<td>2.81%</td>
<td>3.08%</td>
<td>$68.0 b</td>
<td>2.27</td>
<td>72</td>
</tr>
<tr>
<td>3/13/2008</td>
<td>28 Days</td>
<td>$50 b</td>
<td>2.39%</td>
<td>2.80%</td>
<td>$92.6 b</td>
<td>1.85</td>
<td>82</td>
</tr>
<tr>
<td>3/27/2008</td>
<td>28 Days</td>
<td>$50 b</td>
<td>2.19%</td>
<td>2.62%</td>
<td>$88.9 b</td>
<td>1.78</td>
<td>88</td>
</tr>
<tr>
<td>4/10/2008</td>
<td>28 Days</td>
<td>$50 b</td>
<td>2.11%</td>
<td>2.82%</td>
<td>$91.6 b</td>
<td>1.83</td>
<td>79</td>
</tr>
<tr>
<td>4/24/2008</td>
<td>28 Days</td>
<td>$50 b</td>
<td>2.05%</td>
<td>2.87%</td>
<td>$88.9 b</td>
<td>1.77</td>
<td>89</td>
</tr>
<tr>
<td>5/8/2008</td>
<td>28 Days</td>
<td>$75 b</td>
<td>2.00%</td>
<td>2.22%</td>
<td>$96.8 b</td>
<td>1.29</td>
<td>71</td>
</tr>
<tr>
<td>5/22/2008</td>
<td>28 Days</td>
<td>$75 b</td>
<td>1.99%</td>
<td>2.10%</td>
<td>$84.4 b</td>
<td>1.13</td>
<td>75</td>
</tr>
<tr>
<td>6/5/2008</td>
<td>28 Days</td>
<td>$75 b</td>
<td>2.00%</td>
<td>2.26%</td>
<td>$95.9 b</td>
<td>1.28</td>
<td>73</td>
</tr>
<tr>
<td>6/19/2008</td>
<td>28 Days</td>
<td>$75 b</td>
<td>2.05%</td>
<td>2.36%</td>
<td>$89.4 b</td>
<td>1.19</td>
<td>76</td>
</tr>
</tbody>
</table>

Source: Federal Reserve Board
## (27) Term Securities Lending Facility Auction Results

<table>
<thead>
<tr>
<th>Auction Settlement</th>
<th>Term</th>
<th>Collateral</th>
<th>Amount</th>
<th>Minimum Fee Rate</th>
<th>Stop-out Rate</th>
<th>Propositions</th>
<th>Bid/Cover</th>
</tr>
</thead>
<tbody>
<tr>
<td>3/28/2008</td>
<td>28 Days</td>
<td>Schedule 2</td>
<td>$75 b</td>
<td>0.25%</td>
<td>0.33%</td>
<td>$86.1 b</td>
<td>1.15</td>
</tr>
<tr>
<td>4/4/2008</td>
<td>28 Days</td>
<td>Schedule 1</td>
<td>$25 b</td>
<td>0.10%</td>
<td>0.16%</td>
<td>$46.9 b</td>
<td>1.88</td>
</tr>
<tr>
<td>4/11/2008</td>
<td>28 Days</td>
<td>Schedule 2</td>
<td>$50 b</td>
<td>0.25%</td>
<td>0.25%</td>
<td>$40.0 b</td>
<td>0.68</td>
</tr>
<tr>
<td>4/18/2008</td>
<td>28 Days</td>
<td>Schedule 1</td>
<td>$25 b</td>
<td>0.10%</td>
<td>0.10%</td>
<td>$35.1 b</td>
<td>1.40</td>
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<tr>
<td>4/25/2008</td>
<td>28 Days</td>
<td>Schedule 2</td>
<td>$75 b</td>
<td>0.25%</td>
<td>0.25%</td>
<td>$59.5 b</td>
<td>0.79</td>
</tr>
<tr>
<td>5/2/2008</td>
<td>28 Days</td>
<td>Schedule 1</td>
<td>$25 b</td>
<td>0.10%</td>
<td>0.10%</td>
<td>$24.1 b</td>
<td>0.96</td>
</tr>
<tr>
<td>5/9/2008</td>
<td>28 Days</td>
<td>Schedule 2</td>
<td>$50 b</td>
<td>0.25%</td>
<td>0.25%</td>
<td>$28.7 b</td>
<td>0.58</td>
</tr>
<tr>
<td>5/16/2008</td>
<td>28 Days</td>
<td>Schedule 1</td>
<td>$25 b</td>
<td>0.10%</td>
<td>0.10%</td>
<td>$7.2 b</td>
<td>0.29</td>
</tr>
<tr>
<td>5/23/2008</td>
<td>28 Days</td>
<td>Schedule 2</td>
<td>$75 b</td>
<td>0.25%</td>
<td>0.25%</td>
<td>$46.1 b</td>
<td>0.62</td>
</tr>
<tr>
<td>5/30/2008</td>
<td>28 Days</td>
<td>Schedule 1</td>
<td>$25 b</td>
<td>0.10%</td>
<td>0.10%</td>
<td>$16.4 b</td>
<td>0.66</td>
</tr>
<tr>
<td>6/6/2008</td>
<td>28 Days</td>
<td>Schedule 2</td>
<td>$50 b</td>
<td>0.25%</td>
<td>0.25%</td>
<td>$26.9 b</td>
<td>0.54</td>
</tr>
<tr>
<td>6/13/2008</td>
<td>28 Days</td>
<td>Schedule 1</td>
<td>$25 b</td>
<td>0.10%</td>
<td>0.10%</td>
<td>$27.2 b</td>
<td>1.09</td>
</tr>
<tr>
<td>6/20/2008</td>
<td>28 Days</td>
<td>Schedule 2</td>
<td>$75 b</td>
<td>0.25%</td>
<td>0.25%</td>
<td>$36.8 b</td>
<td>0.49</td>
</tr>
</tbody>
</table>

Source: Federal Reserve Bank of New York
(28) Spread Between Nominal and Inflation Protected Treasury Yields
January 1, 2007 – June 20, 2008

Source: Bloomberg

(29) Treasury Yield Curve

Source: Bloomberg

(30) Implied Volatility Across Markets
January 1, 2007 – June 20, 2008

Source: Bloomberg
Appendix 2: Materials used by Messrs. Sheets, Slifman, and Wascher
Material for

Staff Presentation on the Economic Outlook

June 24, 2008
### Outlook for Foreign Growth

#### Real GDP Projections*

<table>
<thead>
<tr>
<th></th>
<th>2007</th>
<th>2008</th>
<th>2009p</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Q1-Q3</td>
<td>Q4</td>
<td>Q1</td>
</tr>
<tr>
<td>1. Total Foreign</td>
<td>4.5</td>
<td>3.0</td>
<td>2.9</td>
</tr>
<tr>
<td>2. Advanced Foreign</td>
<td>2.9</td>
<td>1.4</td>
<td>1.5</td>
</tr>
<tr>
<td>3. Canada</td>
<td>3.4</td>
<td>0.8</td>
<td>-0.3</td>
</tr>
<tr>
<td>4. Japan</td>
<td>0.9</td>
<td>2.9</td>
<td>4.0</td>
</tr>
<tr>
<td>5. Euro Area</td>
<td>2.4</td>
<td>1.3</td>
<td>3.2</td>
</tr>
<tr>
<td>6. United Kingdom</td>
<td>3.0</td>
<td>2.5</td>
<td>1.6</td>
</tr>
<tr>
<td>7. Emerging Markets</td>
<td>6.7</td>
<td>5.1</td>
<td>4.8</td>
</tr>
<tr>
<td>8. Mexico</td>
<td>4.2</td>
<td>3.3</td>
<td>2.1</td>
</tr>
<tr>
<td>9. China</td>
<td>11.6</td>
<td>10.6</td>
<td>11.7</td>
</tr>
</tbody>
</table>

* Aggregates weighted by U.S. merchandise export shares.
** Year is Q4/Q4; half year is Q4/Q2; Q1-Q3 is Q3/Q4.

#### Japan

- Ratio Index, Jan. 2006 = 100
- Job openings to applicants
- Manufacturing output

#### Euro Area

- Index, 50+ = Expansion
- 12-month percent change
- Total PMI*
- Retail sales

#### Real GDP Growth*

- United States
- Advanced foreign economies
- Emerging market economies

* GDP aggregates weighted by U.S. merchandise export shares. Gray shading represents U.S. recessions. Blue shading represents the forecast period.
**Oil Market**

### West Texas Intermediate

- **Spot price**
- **Far-dated futures**
- **Jan.GB**

### OECD Private Inventories of Oil and Products*

- **Millions of barrels, n.s.a.**

### World Oil Balance

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>% change 05-08</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Consumption</strong></td>
<td>83.8</td>
<td>84.9</td>
<td>86.0</td>
<td>86.8</td>
<td>3.6</td>
</tr>
<tr>
<td>1. Advanced Economies</td>
<td>45.4</td>
<td>45.2</td>
<td>44.8</td>
<td>44.4</td>
<td>-2.2</td>
</tr>
<tr>
<td>2. United States</td>
<td>21.2</td>
<td>21.0</td>
<td>21.2</td>
<td>20.6</td>
<td>-2.8</td>
</tr>
<tr>
<td>3. Emerging Markets</td>
<td>38.4</td>
<td>39.7</td>
<td>41.1</td>
<td>42.4</td>
<td>10.4</td>
</tr>
<tr>
<td>4. China</td>
<td>6.7</td>
<td>7.2</td>
<td>7.5</td>
<td>8.0</td>
<td>19.4</td>
</tr>
<tr>
<td>5. Middle East</td>
<td>6.0</td>
<td>6.2</td>
<td>6.5</td>
<td>6.8</td>
<td>13.3</td>
</tr>
<tr>
<td><strong>Production</strong></td>
<td>84.6</td>
<td>85.4</td>
<td>85.5</td>
<td>87.0</td>
<td>2.8</td>
</tr>
<tr>
<td>7. OPEC</td>
<td>34.3</td>
<td>34.4</td>
<td>33.9</td>
<td>35.1</td>
<td>2.3</td>
</tr>
<tr>
<td>8. Non-OPEC</td>
<td>50.3</td>
<td>51.0</td>
<td>51.6</td>
<td>51.9</td>
<td>3.2</td>
</tr>
<tr>
<td><strong>Implied Stockbuild and Discrepancy</strong></td>
<td>0.8</td>
<td>0.5</td>
<td>-0.5</td>
<td>0.2</td>
<td>--</td>
</tr>
</tbody>
</table>

### World Oil Production and GDP

- **Index, 2002:Q1 = 100**

### Proved Oil Reserves

- **Including Canadian oil sands**

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* Both crude oil and petroleum products. Excludes official inventories.

** Five-year average level +/- 1 standard deviation.


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* Aggregate weighted by world oil consumption shares.

* Proved reserves/current oil production. ** Data unavailable before 1999.

Non-fuel Commodity Prices

Index, 2005:Q1 = 100

Jan. GB

Non-fuel Commodities

Inventories of Selected Commodities

Weeks of consumption*

Wheat
Corn
Zinc
Copper

* Period-end stocks/annual consumption. For grains, 2008 is USDA estimate. For metals, 2008 is stock at end of March over 2007 usage.

Prices of Selected Commodities

Dollars per bushel
Dollars per pound

Weekly
Copper
Wheat
Corn
Zinc

Correlations: Commodity Prices and the Dollar*

WTI oil price
Non-fuel commodity prices**

*60-day moving correlations of daily changes. The dollar is broad nominal index. **Commodity Research Bureau index.

Correlations: Commodity Prices and Interest Rates*

WTI oil price
Non-fuel commodity prices**

*60-day moving correlations of daily changes. Interest rate is three-month Treasury bill rate. **Commodity Research Bureau index.

Other Explanations for Recent Moves in Commodity Prices

Role of Speculators?

- Prices of commodities not traded in futures markets have also risen.
- Inventories are relatively tight.
- No evidence that positions taken by non-commercial traders predict commodity prices.
Outlook for Foreign Inflation

Outlook for Inflation

- Emerging market economies
- Advanced foreign economies

Inflation Compensation

- Euro area*
- Far-dated euro area**

Policy Interest Rates

- Bank of England
- Bank of Canada
- ECB
- April GB

Consumer Prices in Selected Emerging Markets

- Chinese headline
- Mexican headline
- Mexican core*
- Chinese core*

* Excluding food and energy prices.
U.S. External Sector

Broad Real Dollar

Index, Jan. 2006 = 100

Core Import Prices

Percent change, a.r.

U.S. Trade Outlook

<table>
<thead>
<tr>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>H1</td>
<td>H2</td>
<td>Q1³</td>
</tr>
</tbody>
</table>

Growth rates (percent, annual rate*)

1. Real exports  4.3  12.6  5.6  7.2  7.2  7.5
2. Real imports  0.5  1.4  -0.5  -6.7  1.0  2.8

Contribution to U.S. real GDP growth (percentage points, annual rate*)

3. Real net exports  0.4  1.2  0.8  2.1  0.7  0.5

Memo:

4. Current account balance (percent of GDP)  -5.7  -4.9  -5.0  -5.1  -5.4  -4.6
5. Non-oil trade balance (percent of GDP)  -3.1  -2.3  -1.8  -1.7  -1.3  -0.8

* Year is Q4/Q4; half years are Q2/Q4 or Q4/Q2.
Recent Indicators

**Consumer Sentiment Index**

**Business Sentiment**

**Change in Private Payroll Employment**

**Real Goods PCE, Excluding Motor Vehicles**

**Business Spending Indicators**

(Percent change from previous month; monthly rate)

<table>
<thead>
<tr>
<th>2008</th>
<th></th>
<th>April</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shipment*</td>
<td>-1.3</td>
<td>0.2</td>
</tr>
<tr>
<td>Order*</td>
<td>-0.9</td>
<td>-1.0</td>
</tr>
<tr>
<td>Nonresidential</td>
<td>1.1</td>
<td>1.2</td>
</tr>
</tbody>
</table>

*Nondefense capital goods, excluding aircraft.

* Index means are normalized.

* Range of industry forecasts.
Key Background Factors and Medium-Term Outlook

Factors Affecting GDP Forecast

- Revised up the forecast for Q1 and Q2 in light of the incoming information.
- Tempered our judgmental adjustments; but we still anticipate recession-like and financial turmoil effects to show through to spending for the next few quarters.
- Residential investment still a drag on economic growth well into next year.
- Ratio of household net worth to income remains on a downward trajectory.
- Higher oil prices
- Tighter monetary policy
- Faster potential GDP growth

Oil Price

Federal Funds Rate

Real GDP Forecast

(Percent change; annual rate)

<table>
<thead>
<tr>
<th></th>
<th>Current</th>
<th>April GB</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008:Q1</td>
<td>1.1</td>
<td>0.4</td>
</tr>
<tr>
<td>2008:Q2</td>
<td>1.7</td>
<td>-1.4</td>
</tr>
<tr>
<td>2008:H2</td>
<td>0.7</td>
<td>0.9</td>
</tr>
<tr>
<td>2009</td>
<td>2.4</td>
<td>2.8</td>
</tr>
</tbody>
</table>

GDP Gap

Note: Percent difference between actual and potential. A negative number indicates that the economy is operating below potential.

Note: West Texas Intermediate spot price.

Note: Half year figure is Q4/Q2; annual figure is Q4/Q4.
Housing

Vacancy Rate: Single-family Homes

Quarterly

Percent


* Vacant units for sale relative to all units (vacant plus occupied).

House Prices

Quarterly

Percent change, annual rate


Source: OFHEO purchase-only index.

Perception of Falling House Prices

Percent of homowners reporting decline in their house price

Percent of respondents

Past 12 months

Next 12 months

June

2004 2005 2006 2007 2008

Source: Homebuying attitudes: Reuters/Michigan Survey microdata files; overvaluation: staff estimate from model of price-rent ratio.

Sales of Single-family Homes

Millions

Existing homes

New homes


Single-family Housing Starts

Millions of units, annual rate


2.0

1.6

1.2

0.8

0.4

0.4

0.8

1.2

1.6

2.0
Factors Affecting PCE Forecast

- Tax rebates push up the third quarter and create a pothole in the fourth quarter
- Higher oil prices sap household purchasing power
- Hit to household wealth from falling home prices
- Restraining effects of financial turmoil and pessimistic consumer sentiment.

Factors Affecting E&S Forecast

- High-tech investment
  - Cautious comments from computer manufacturers.
  - Slowing outlays by telecom service providers
- Other investment
  - Accelerator effects
  - Tight lending standards
  - Gloomy business sentiment

Factors Affecting NRS Forecast

- Drilling and mining
  - Bottlenecks: shortages of skilled labor and supplies
  - Rig count up
  - Escalating energy prices
- Buildings
  - Vacancy rates moving up
  - Sales and prices of existing properties sagging
  - Financing conditions tight

Real PCE

E&S Spending Excluding Transportation

Nonresidential Structures
Aggregate Supply and the Labor Market

Staff Assumptions
(Percent change)

<table>
<thead>
<tr>
<th></th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Potential output</td>
<td>2.5</td>
<td>2.5</td>
<td>2.5</td>
</tr>
<tr>
<td>2. (April GB)</td>
<td>(2.4)</td>
<td>(2.3)</td>
<td>(2.2)</td>
</tr>
<tr>
<td>3. Structural productivity</td>
<td>2.1</td>
<td>2.0</td>
<td>2.0</td>
</tr>
<tr>
<td>4. (April GB)</td>
<td>(2.1)</td>
<td>(1.9)</td>
<td>(1.8)</td>
</tr>
<tr>
<td>5. Trend hours</td>
<td>1.0</td>
<td>0.9</td>
<td>0.9</td>
</tr>
<tr>
<td>6. (April GB)</td>
<td>(0.9)</td>
<td>(0.8)</td>
<td>(0.8)</td>
</tr>
<tr>
<td>7. Technical factors</td>
<td>-0.5</td>
<td>-0.4</td>
<td>-0.4</td>
</tr>
</tbody>
</table>

Labor Productivity: Nonfarm Business Sector
Four-quarter percent change

Kalman Filter Estimates
Apr. GB 2.1
Jun. GB 2.3

Labor Force Participation Rate
Percent
66.4
66.3
66.2
66.1
66.0
65.9
65.8
65.7

Note: Adjusted for changes in population controls.

Payroll Employment

Average monthly change
Thousands

Unemployment Rate

Apr. 5.0
May 5.5
Jun. 5.3

Percent
7
6
5
4
3
Exhibit 11

Inflation

Recent Price Data
(Percent change)

<table>
<thead>
<tr>
<th></th>
<th>2008 Q1º</th>
<th>2008 Q2º</th>
<th>Aprilº</th>
<th>Mayº</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Total PCE</td>
<td>3.6</td>
<td>4.1</td>
<td>0.2</td>
<td>0.5</td>
</tr>
<tr>
<td>2. (April GB)</td>
<td>(3.5)</td>
<td>(4.3)</td>
<td>(0.3)</td>
<td>(0.6)</td>
</tr>
<tr>
<td>3. Core PCE</td>
<td>2.2</td>
<td>2.0</td>
<td>0.1</td>
<td>0.2</td>
</tr>
<tr>
<td>4. (April GB)</td>
<td>(2.1)</td>
<td>(2.3)</td>
<td>(0.2)</td>
<td>(0.2)</td>
</tr>
</tbody>
</table>

Note: Quarterly figures are at annual rates.

Total and Core PCE Prices
12-month percent change

Spot and Futures Prices for Food Commodities

Index, 1987Q4 = 100, ratio scale

PCE Energy Prices
Four-quarter percent change

PCE Food Prices
Four-quarter percent change

Gasoline and Natural Gas Prices
$/Million BTUs, ratio scale
$/Gallon, ratio scale

Retail Gasoline (right scale)
Natural Gas spot (left scale)

Jun. 23

Apr. GB
Livestock
Crops
**Indicators of Input Costs**

**Intermediate Materials Prices**
- Diffusion index
- 12-month percent change
- Core PPI (right axis)
- ISM prices paid* (left axis)

* Three-month moving average; manufacturing firms.

**Core Nonfuel Import Prices**
- Four-quarter percent change
- Apr. GB

**Transportation Costs**
- 12-month percent change
- Rail transport
- Trucking

Note: Producer price indexes.

**Direct Effects of Commodity and Import Prices on Core Inflation**
- Percentage points
- Imports and other commodities
- Energy

**Labor Compensation**
- Percent change from year earlier
- NFB compensation per hour
- Employment cost index
- Average hourly earnings

**Unit Labor Costs**
- Percent change, Q4/Q4
- Actual
- Trend

2006 | 4.2 | 2.9
2007 | 1.4 | 2.3
2008* | 2.3 | 2.1
2009* | 2.0 | 2.1

* Nonfarm business sector.
Inflation Projection

Short-Run Inflation Expectations

Long-Run Inflation Expectations

PCE Price Projections

Alternative Simulation

- Long-run inflation expectations move up ¾ percentage point relative to baseline.
- Monetary policy responds according to the estimated Taylor rule.

Unemployment Rate

Core PCE Prices

Federal Funds Rate

Note: Annual figures are Q4/Q4 percent changes.
Appendix 3: Materials used by Mr. Madigan
Class I FOMC – Restricted Controlled (FR)

Material for Briefing on
FOMC Participants’ Economic Projections

Brian Madigan
June 24, 2008
### Table 1: Economic Projections of Federal Reserve Governors and Reserve Bank Presidents

<table>
<thead>
<tr>
<th></th>
<th>2008:H1</th>
<th>2008:H2</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Central Tendencies</strong> (percent, annual rate)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Real GDP Growth</td>
<td>1.2 to 1.4</td>
<td>0.6 to 2.1</td>
</tr>
<tr>
<td>April projections</td>
<td>-0.4 to 0.5</td>
<td>1.0 to 1.9</td>
</tr>
<tr>
<td>PCE Inflation</td>
<td>3.7 to 4.0</td>
<td>3.6 to 4.6</td>
</tr>
<tr>
<td>April projections</td>
<td>3.5 to 4.0</td>
<td>2.5 to 3.1</td>
</tr>
<tr>
<td>Core PCE Inflation</td>
<td>2.1 to 2.2</td>
<td>2.3 to 2.5</td>
</tr>
<tr>
<td>April projections</td>
<td>2.2 to 2.4</td>
<td>2.2 to 2.4</td>
</tr>
</tbody>
</table>

| **Ranges** (percent, annual rate) |               |               |
| Real GDP Growth                 | 1.0 to 1.5    | 0.4 to 2.2    |
| April projections               | -0.5 to 0.6   | 0.4 to 2.9    |
| PCE Inflation                   | 3.6 to 4.6    | 3.2 to 4.8    |
| April projections               | 3.0 to 4.4    | 2.3 to 3.6    |
| Core PCE Inflation              | 2.0 to 2.4    | 2.0 to 2.6    |
| April projections               | 2.0 to 2.5    | 1.7 to 2.7    |

**Memo: Greenbook** (percent, annual rate)

<p>| Real GDP Growth             | 1.4         | 0.7        |
| April Greenbook             | -0.5        | 0.9        |
| PCE Inflation               | 3.8         | 4.5        |
| April Greenbook             | 3.9         | 2.7        |
| Core PCE Inflation          | 2.1         | 2.5        |
| April Greenbook             | 2.2         | 2.4        |</p>
<table>
<thead>
<tr>
<th>Central Tendencies</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(percent)</td>
<td>(percent)</td>
<td>(percent)</td>
</tr>
<tr>
<td>Real GDP Growth</td>
<td>1.0 to 1.6</td>
<td>2.0 to 2.8</td>
<td>2.5 to 3.0</td>
</tr>
<tr>
<td>April projections</td>
<td>0.3 to 1.2</td>
<td>2.0 to 2.8</td>
<td>2.6 to 3.1</td>
</tr>
<tr>
<td>Unemployment Rate</td>
<td>5.5 to 5.7</td>
<td>5.3 to 5.8</td>
<td>5.0 to 5.6</td>
</tr>
<tr>
<td>April projections</td>
<td>5.5 to 5.7</td>
<td>5.2 to 5.7</td>
<td>4.9 to 5.5</td>
</tr>
<tr>
<td>PCE Inflation</td>
<td>3.8 to 4.2</td>
<td>2.0 to 2.3</td>
<td>1.8 to 2.0</td>
</tr>
<tr>
<td>April projections</td>
<td>3.1 to 3.4</td>
<td>1.9 to 2.3</td>
<td>1.8 to 2.0</td>
</tr>
<tr>
<td>Core PCE Inflation</td>
<td>2.2 to 2.4</td>
<td>2.0 to 2.2</td>
<td>1.8 to 2.0</td>
</tr>
<tr>
<td>April projections</td>
<td>2.2 to 2.4</td>
<td>1.9 to 2.1</td>
<td>1.7 to 1.9</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Ranges</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
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</thead>
<tbody>
<tr>
<td>(percent)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Real GDP Growth</td>
<td>0.9 to 1.8</td>
<td>1.9 to 3.0</td>
<td>2.0 to 3.5</td>
</tr>
<tr>
<td>April projections</td>
<td>0.0 to 1.5</td>
<td>1.8 to 3.0</td>
<td>2.0 to 3.4</td>
</tr>
<tr>
<td>Unemployment Rate</td>
<td>5.5 to 5.8</td>
<td>5.2 to 6.1</td>
<td>5.0 to 5.8</td>
</tr>
<tr>
<td>April projections</td>
<td>5.3 to 6.0</td>
<td>5.2 to 6.3</td>
<td>4.8 to 5.9</td>
</tr>
<tr>
<td>PCE Inflation</td>
<td>3.4 to 4.6</td>
<td>1.7 to 3.0</td>
<td>1.6 to 2.1</td>
</tr>
<tr>
<td>April projections</td>
<td>2.8 to 3.8</td>
<td>1.7 to 3.0</td>
<td>1.5 to 2.0</td>
</tr>
<tr>
<td>Core PCE Inflation</td>
<td>2.0 to 2.5</td>
<td>1.8 to 2.3</td>
<td>1.5 to 2.0</td>
</tr>
<tr>
<td>April projections</td>
<td>1.9 to 2.5</td>
<td>1.7 to 2.2</td>
<td>1.3 to 2.0</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Memo: Greenbook</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>(percent)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Real GDP Growth</td>
<td>1.0</td>
<td>2.4</td>
<td>3.1</td>
</tr>
<tr>
<td>April Greenbook</td>
<td>0.2</td>
<td>2.8</td>
<td>3.1</td>
</tr>
<tr>
<td>Unemployment Rate</td>
<td>5.6</td>
<td>5.6</td>
<td>5.4</td>
</tr>
<tr>
<td>April Greenbook</td>
<td>5.7</td>
<td>5.5</td>
<td>5.2</td>
</tr>
<tr>
<td>PCE Inflation</td>
<td>4.2</td>
<td>2.1</td>
<td>1.9</td>
</tr>
<tr>
<td>April Greenbook</td>
<td>3.3</td>
<td>1.8</td>
<td>1.8</td>
</tr>
<tr>
<td>Core PCE Inflation</td>
<td>2.3</td>
<td>2.2</td>
<td>2.0</td>
</tr>
<tr>
<td>April Greenbook</td>
<td>2.3</td>
<td>2.0</td>
<td>1.8</td>
</tr>
</tbody>
</table>
Exhibit 3
Risks and Uncertainty in Economic Projections

Risk Weighting around Outlook for Real GDP Growth

- Weighted to Downside
- Broadly Balanced
- Weighted to Upside

Number of participants

January
April
June

Degree of Uncertainty about Outlook for Real GDP Growth

- Lower
- Historically Normal
- Higher

Number of participants

January
April
June

Risk Weighting around Outlook for Total PCE Inflation

- Weighted to Downside
- Broadly Balanced
- Weighted to Upside

Number of participants

January
April
June

Degree of Uncertainty about Outlook for Total PCE Inflation

- Lower
- Historically Normal
- Higher

Number of participants

January
April
June
### Exhibit 4

**Consideration of Long-Term Projections**

**Issue**

- Current three-year horizon for projections does not always reveal your views of:
  - Steady-state characteristics of economy
    - Sustainable rate of unemployment
    - Sustainable rate of output growth
  - Rate of inflation consistent with dual mandate

**Alternative approaches**

1. Extend entire set of projections for four variables and forecast narratives out to five years.
   - Advantage: full, coherent presentation
   - Disadvantage: burden on participants

2. Maintain three-year projection horizon for four variables but add fifth-year projections for output growth, unemployment, and total inflation
   - Advantage: less burden on participants
   - Disadvantage: less complete explanation of transition to steady state

3. Maintain three-year projection horizon for four variables but add estimates of long-run averages of output growth, unemployment, and total inflation five to ten years ahead
   - Advantage: no need for participants to project fourth and fifth years for four variables
   - Disadvantages:
     - Less complete explanation of transition to steady state
     - Need to forecast long-run demographic and productivity trends
Appendix 4: Materials used by Mr. Madigan
Class I FOMC – Restricted Controlled (FR)

Material for
FOMC Briefing on Monetary Policy Alternatives

Brian Madigan
June 24-25, 2008
<table>
<thead>
<tr>
<th>Policy Decision</th>
<th>April FOMC</th>
<th>Alternative A</th>
<th>Alternative B</th>
<th>Alternative C</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Policy Decision</td>
<td>The Federal Open Market Committee decided today to lower its target for the federal funds rate 25 basis points to 1-3/4 percent.</td>
<td>The Federal Open Market Committee decided today to lower its target for the federal funds rate 25 basis points to 1-3/4 percent.</td>
<td>The Federal Open Market Committee decided today to keep its target for the federal funds rate at 2 percent.</td>
<td>The Federal Open Market Committee decided today to raise its target for the federal funds rate 25 basis points to 2-1/4 percent.</td>
</tr>
</tbody>
</table>

**Rationale**

2. Recent information indicates that economic activity remains weak. Household and business spending has been subdued and labor markets have softened further. Financial markets remain under considerable stress, and tight credit conditions and the deepening housing contraction are likely to weigh on economic growth over the next few quarters.

3. Although readings on core inflation have improved somewhat, energy and other commodity prices have increased, and some indicators of inflation expectations have risen in recent months. The Committee expects inflation to moderate in coming quarters, reflecting a projected leveling-out of energy and other commodity prices and an easing of pressures on resource utilization. Still, uncertainty about the inflation outlook remains high. It will be necessary to continue to monitor inflation developments carefully.

4. The substantial easing of monetary policy to date, combined with ongoing measures to foster market liquidity, should help to promote moderate growth over time and to mitigate risks to economic activity. The Committee will continue to monitor economic and financial developments and will act as needed to promote sustainable economic growth and price stability.

**Assessment of Risk**

Although energy prices have increased further and some indicators of inflation expectations have risen in recent months, core inflation has been stable of late. The Committee expects inflation to moderate later this year and next year, reflecting a projected leveling-out of energy prices and an easing of pressures on resource utilization. Still, uncertainty about the inflation outlook remains high. It will be necessary to continue to monitor inflation developments carefully.

3. The substantial easing of monetary policy to date, combined with ongoing measures to foster market liquidity, should help to promote moderate growth over time and to mitigate risks to economic activity. The Committee will continue to monitor economic and financial developments and will act as needed to promote sustainable economic growth and price stability.

4. The substantial easing of monetary policy to date, combined with ongoing measures to foster market liquidity, should help to promote moderate growth over time and to mitigate risks to economic activity. The Committee will continue to monitor economic and financial developments and will act as needed to promote sustainable economic growth and price stability.

**Bluebook version, slightly revised**

Overall inflation has been elevated, energy prices have continued to increase, and some indicators of inflation expectations have risen further. The Committee expects inflation to moderate later this year and next year, partly reflecting today’s policy action. Still, uncertainty about the inflation outlook remains high. It will be necessary to continue to monitor inflation developments carefully.

Future policy adjustments will depend on the evolution of the outlook for both inflation and economic growth, as implied by incoming information on the economy and financial conditions.
Exhibit 2

Optimal Policy Under Alternative Inflation Goals

1½ Percent Inflation Goal

Federal funds rate

- Current Bluebook
- April Bluebook

Civilian unemployment rate

Core PCE inflation

Four-quarter average

2 Percent Inflation Goal
Exhibit 3
Equilibrium Real Federal Funds Rate

Short-Run Estimates with Confidence Intervals

The actual real funds rate based on lagged core inflation
red Range of model-based estimates
blue 70 Percent confidence interval
light blue 90 Percent confidence interval
dashed Greenbook-consistent measure

Short-Run and Medium-Run Measures

<table>
<thead>
<tr>
<th>Current Estimate</th>
<th>Previous Bluebook</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Short-Run Measures</strong></td>
<td></td>
</tr>
<tr>
<td>1. Single-equation model</td>
<td>2.2</td>
</tr>
<tr>
<td>2. Small structural model</td>
<td>-0.6</td>
</tr>
<tr>
<td>3. Large model (FRB/US)</td>
<td>0.4</td>
</tr>
<tr>
<td>Confidence intervals for three model-based estimates</td>
<td></td>
</tr>
<tr>
<td>4a. 70 percent confidence interval</td>
<td>-1.2 - 2.6</td>
</tr>
<tr>
<td>4b. 90 percent confidence interval</td>
<td>-2.2 - 3.8</td>
</tr>
<tr>
<td>5. Greenbook-consistent measure</td>
<td>-0.1</td>
</tr>
<tr>
<td><strong>Medium-Run Measures</strong></td>
<td></td>
</tr>
<tr>
<td>6. Single-equation model</td>
<td>2.2</td>
</tr>
<tr>
<td>7. Small structural model</td>
<td>1.8</td>
</tr>
<tr>
<td>Confidence intervals for two model-based estimates</td>
<td></td>
</tr>
<tr>
<td>8a. 70 percent confidence interval</td>
<td>1.1 - 2.9</td>
</tr>
<tr>
<td>8b. 90 percent confidence interval</td>
<td>0.5 - 3.7</td>
</tr>
<tr>
<td>9. TIPS-based factor model</td>
<td>2.0</td>
</tr>
<tr>
<td><strong>Measures of Actual Real Federal Funds Rate</strong></td>
<td></td>
</tr>
<tr>
<td>10. Based on lagged core inflation</td>
<td>-0.2</td>
</tr>
<tr>
<td>11. Based on lagged headline inflation</td>
<td>-1.3</td>
</tr>
<tr>
<td>12. Based on Greenbook projection of headline inflation</td>
<td>-1.3</td>
</tr>
<tr>
<td>* This measure was not reported in the April Bluebook.</td>
<td></td>
</tr>
</tbody>
</table>

Note: Appendix A provides background information regarding the construction of these measures and confidence intervals.
Appendix 5: Materials used by Messrs. Angulo, Alvarez, and Parkinson
Class I FOMC – Restricted Controlled (FR)

Material for
Supervisory Report Concerning Investment Banks and Related Policy Issues

June 25, 2008
Primary Dealer Monitoring Update

June 25, 2008
Presentation Overview

- Objectives and Approach
- Current Focus at Four Investment Banks
  - Capital
  - Liquidity
- PDCF (and TSLF) Usage
- Near-Term Issues
Objectives

- Tied closely to Primary Dealer Credit Facility (PDCF) and FRA 13(3) authority

- Build the capability to exercise informed judgment about the capital and liquidity positions of the primary dealers given their access to the PDCF

- Minimize the risk that the availability of financing under the PDCF undermines the incentives for primary dealers to manage capital and liquidity more conservatively
Approach

- Focus is on the firms that own primary dealers not affiliated with financial holding companies -- primarily the four largest investment banks.
  - Limited on-site presence + off-site staff
  - Direct contact with management
  - Information sharing and communication with SEC
  - ...but we are not engaged in traditional bank supervision
  - Current focus at the four investment banks is on capital and liquidity
    - Capital – increasing (but not sole) focus on risk-based capital (RBC)
    - Liquidity – iterative approach
Leverage Trend as Reported by the Firms

Gross Leverage

Goldman Sachs
Morgan Stanley
Merrill Lynch
Lehman Brothers
Capital – Current View

Tier 1 Capital Ratios: 4 Largest Securities Firms

Comparison of FRBNY Adjusted Leverage Ratios*

* Note: For May this ratio would be 12.5% with June capital raise included

* Note: FRBNY Leverage Ratio = Tangible Equity / Total Assets less Secured Financing Assets and Intangible Assets
Recent Trend in Parent Company Liquidity Pools

Goldman Liquidity Pool Trend ($ in billions)

Morgan Liquidity Pool Trend ($ in billions)

Merrill Liquidity Pool Trend ($ in billions)

Lehman Liquidity Pool Trend ($ in billions)
Liquidity Stress Approach

- Iterate with the 4 firms
- Current scenario:
  - Severe stress but short of full Bear Stearns scenario
  - 30 day liquidity horizon
  - NO access to the PDCF
- Compare and converge assumptions
- Construct cash flow analysis
- Relate cash needs under stress to available liquidity (liquidity pool + additional funding sources)

<table>
<thead>
<tr>
<th>As of dates: 5/22/08 - 6/10/08</th>
<th>Severity Assumption</th>
</tr>
</thead>
<tbody>
<tr>
<td>UNSECURED FUNDING - Percent not rolling</td>
<td></td>
</tr>
<tr>
<td>Total Unsecured Funding</td>
<td>100%</td>
</tr>
<tr>
<td>SECURED FUNDING - Percent not rolling</td>
<td></td>
</tr>
<tr>
<td>Fixed Income Finance</td>
<td></td>
</tr>
<tr>
<td>OMO Eligible</td>
<td>0%</td>
</tr>
<tr>
<td>Liquid</td>
<td>20%</td>
</tr>
<tr>
<td>Less Liquid</td>
<td>50%</td>
</tr>
<tr>
<td>Illiquid</td>
<td>100%</td>
</tr>
<tr>
<td>Equity Finance</td>
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<tr>
<td>Liquid</td>
<td>20%</td>
</tr>
<tr>
<td>Less Liquid</td>
<td>50%</td>
</tr>
<tr>
<td>ON-BORADING AND OTHER COMMITMENTS</td>
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</tr>
<tr>
<td>Off-Balance Sheet Assets On-Boarded</td>
<td>Institution Specific</td>
</tr>
<tr>
<td>Loan Commitments/Other Contractual Uses</td>
<td>Institution Specific</td>
</tr>
<tr>
<td>Other Liabilities/Commitments</td>
<td>Institution Specific</td>
</tr>
<tr>
<td>OPERATING CASH FLOWS</td>
<td></td>
</tr>
<tr>
<td>Prime Brokerage, Withdrawal of Free Credits</td>
<td>50%</td>
</tr>
<tr>
<td>Customer Shorts with Liquidity Risk</td>
<td>11%</td>
</tr>
<tr>
<td>Release of Lockup Cash Flows</td>
<td>90% - 100%</td>
</tr>
<tr>
<td>Collateral and Margin Calls: Payments / Receipts</td>
<td>100% / 90%</td>
</tr>
<tr>
<td>Derivatives / Margin Mismatches: Payments / Receipts</td>
<td>100% / 90%</td>
</tr>
<tr>
<td>ADDITIONAL FUNDING</td>
<td></td>
</tr>
<tr>
<td>Affiliated Banks / Unaffiliated Bank Lines / Other</td>
<td>Institution Specific</td>
</tr>
</tbody>
</table>
PDCF Usage

- Bear Stearns has been by far the largest and most regular borrower
- Until very recently, there were 3 other “chronic” users
  - Cantor Fitzgerald
  - Countrywide Securities
  - Barclays Capital
TSLF Usage – Schedule 1

Dealer Evolution of Top 5* Schedule 1 Awards:
Total Amounts Outstanding

*Based on total Schedule 1 TSLF awards
**Excludes top 5

$ Billions

TSLF Usage – Schedule 2

Dealer Evolution of Top 5* Schedule 2 Awards:
Total Amounts Outstanding

*Based on total Schedule 2 TSLF awards; Citigroup and Goldman are tied for fifth
**Excludes top 5
Near-Term Issues

- For how much longer should our monitoring program continue with its current focus in its current form?

- How do we limit the reputational risk to the Federal Reserve that increases with the length of our on-site presence at the investment banks?

- If our monitoring program needs to evolve, in which areas should we alter the depth and/or breadth of our activities?
<table>
<thead>
<tr>
<th>Dealer</th>
<th>Total Assets¹ (in billions of dollars)</th>
<th>Regulators</th>
<th>Legal Entity (4)</th>
<th>Consolidated (5)</th>
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</thead>
<tbody>
<tr>
<td>1. Goldman Sachs</td>
<td>705</td>
<td>1,189</td>
<td>117</td>
<td>SEC CSE/SEC</td>
</tr>
<tr>
<td>2. Deutsche Bank Securities</td>
<td>574</td>
<td>3,642</td>
<td>366</td>
<td>SEC FHC/FRS</td>
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<tr>
<td>3. Morgan Stanley</td>
<td>568</td>
<td>1,091</td>
<td>129</td>
<td>SEC CSE/SEC</td>
</tr>
<tr>
<td>4. Lehman Brothers</td>
<td>488</td>
<td>786</td>
<td>147</td>
<td>SEC CSE/SEC</td>
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<tr>
<td>5. UBS Securities</td>
<td>458</td>
<td>2,244</td>
<td>159</td>
<td>SEC FHC/FRS</td>
</tr>
<tr>
<td>7. Citigroup Global Markets</td>
<td>354</td>
<td>2,200</td>
<td>154</td>
<td>SEC FHC/FRS</td>
</tr>
<tr>
<td>8. Credit Suisse Securities</td>
<td>336</td>
<td>1,215</td>
<td>170</td>
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<tr>
<td>9. JP Morgan Securities</td>
<td>280</td>
<td>1,643</td>
<td>90</td>
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<tr>
<td>10. Banc of America Securities</td>
<td>272</td>
<td>1,737</td>
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<td>11. BNP Paribas Securities</td>
<td>245</td>
<td>2,496</td>
<td>102</td>
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<td>12. Merrill Lynch Govt Securities</td>
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<td>1,042</td>
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<td>14. Bear Stearns</td>
<td>131</td>
<td>399</td>
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</tr>
<tr>
<td>15. HSBC Securities USA</td>
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<td>2,354³</td>
<td>34</td>
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<tr>
<td>16. Dresdner Kleinwort</td>
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<td>1,780</td>
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<tr>
<td>Wasserstein Securities</td>
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<tr>
<td>17. Cantor Fitzgerald</td>
<td>31</td>
<td>29³</td>
<td>NA</td>
<td>SEC None</td>
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<tr>
<td>18. Daiwa Securities America</td>
<td>29</td>
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<td>SEC Japan FSA</td>
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<tr>
<td>19. Countrywide Securities</td>
<td>24</td>
<td>199</td>
<td>12</td>
<td>SEC THC/OTS</td>
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<td>20. Mizuho Securities USA</td>
<td>23</td>
<td>1,374³</td>
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<td>SEC FHC/FRS</td>
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</table>

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¹ As of Q1 2008, except where noted.
² Average for May 27 through June 6. In some cases includes collateral financed by affiliates of the primary dealer.
³ Q4 2007.
Liquidity Facilities and the Prudential Supervision of
Investment Banks and Other Primary Dealers
Key Issues for Discussion

Liquidity Facilities

1. When and under what circumstances should we decide to extend, modify, or eliminate our current credit facilities for primary dealers (PDCF and TSLF)? Should the timing and circumstances differ for the two facilities?

2. If we decide to eliminate one or both credit facilities, how should that be done? How much notice should be provided? Should the terms of credit extension be gradually tightened prior to closing the facility, or should the facility be closed in one step? When notice is given, should we give assurances that the closing of the facilities will be delayed if conditions in financial markets warrant?

3. Should we seek legislation that would permit us to provide some type of liquidity backstop to primary dealers in the longer term? Under what conditions should a primary dealer be permitted to draw on such a backstop? What is the rationale for any such backstop?

Prudential Supervision

1. How do we limit the moral hazard risk that our current credit facilities undermine the incentives for primary dealers and the holding companies that own them to manage liquidity and capital to appropriately conservative levels?
   a. On what principles should supervisory expectations for investment banks’ capital, liquidity, and risk management be based? Should these expectations be codified in a formal document? How?
   b. To what liquidity standard should the SEC-regulated investment banks be held? Is it appropriate to expect the firms to maintain liquidity sufficient to withstand a Bear Stearns-type scenario? Should bank-affiliated primary dealers (and their parent companies) be held to the same liquidity standard as investment banks?  
   c. Should investment banks be held to the same capital standards as bank holding companies? What about the leverage ratio?

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1 For purposes of this discussion an investment bank is a primary dealer whose consolidated supervisor is the SEC. Of the twenty primary dealers, four (including Bear Stearns) are subsidiaries of investment bank holding companies subject to consolidated supervision by the SEC, thirteen are subsidiaries of Financial Holding Companies (FHCs), one (Countrywide) is a subsidiary of a thrift holding company, and one (Cantor Fitzgerald) is not subject to consolidated supervision.

2 Under the SEC’s program for consolidated supervision, investment banks are required to maintain liquidity pools at the parent company sufficient to meet expected cash outflows in specified stress scenarios. Those scenarios include the loss of access to unsecured funding for an entire year.
2. In the longer term, can we rely on an MOU with the SEC to provide the prudential supervision that is necessary to limit moral hazard? Or is legislation needed to enhance the effectiveness of prudential supervision of primary dealers? Is there a need for legislation only if we provide primary dealers with an ongoing liquidity backstop or is legislation needed even if their access is only in unusual and exigent circumstances?

3. If legislation is needed, what type of legislation? Legislation requiring consolidated supervision of investment banks? By whom? Should the securities laws be amended to provide the SEC with explicit authority to conduct consolidated supervision of investment banks? Should all primary dealers and their affiliates be regulated as FHCs? Are changes to the functional regulation provisions of Gramm-Leach-Bliley needed to make effective consolidated supervision of primary dealers that are part of FHCs?

4. If we provide primary dealers with an ongoing liquidity backstop, do we need to alter the criteria for becoming a primary dealer (which have worked well to define appropriate counterparties for desk transactions) to require a primary dealer and its consolidated organization to be subject to effective prudential supervision?