NEWS RELEASE

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St. Louis Fed's *Review:* The New Risk Management; Recent Developments in Wholesale Payments Systems; Using Federal Funds Futures Rates to Predict Federal Reserve Actions

ST. LOUIS — The latest edition of ***Review***, the Federal Reserve Bank of St. Louis' bimonthly journal of economic and business issues, features the following articles:

• **"The New Risk Management: The Good, the Bad, and The Ugly."** The financial practice of hedging has come under fire recently due to some widely publicized losses at firms such as Barings, Daiwa Bank and Sumitomo. Financial economists Philip H. Dybvig of the John M. Olin School of Business at Washington University and William J. Marshall of NISA Investment Advisors lay out the policy choices facing firms when they use this tool of risk management. They conclude that firms need to have clearer reasons for hedging, a better understanding of the different financial instruments available to them, and more effective systems to monitor their traders and account for the profits and losses from hedging.

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• **"Recent Developments in Wholesale Payments Systems."** In recent years, central banks have sought to increase the safety and reliability of their wholesale payments and settlement systems. Economist William R. Emmons describes the two approaches that have been pursued. One has been to strengthen net settlement, which accumulates a record of financial obligations among participants over a pre-specified period of time, at the end of which the net amount of funds, securities or other financial obligations owed by each participant is transferred. The other is the addition of new or improved gross settlement systems, which involve real-time payment.

• **"Using Federal Funds Futures Rates to Predict Federal Reserve Actions."** Market watchers believe that the Federal Reserve's adjustments to its target for the federal funds rate have significant implications for other short-term interest rates. As a result, they expend considerable resources to forecast the timing and magnitude of the Fed's next move. But, as economists John C. Robertson and Daniel L. Thornton explain, analysts cannot identify Fed policy from the behavior of the federal funds futures rate without making additional — and arbitrary — assumptions. Robertson and Thornton investigated the predictive accuracy of the federal funds futures rate using a particular identifying rule for the period of October 1988 through August 1997. They found that this rule correctly predicts a target change only about one-third of the time.

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