Prefatory Note

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[1] In some cases, original copies needed to be photocopied before being scanned into electronic format. All scanned images were deskewed (to remove the effects of printer- and scanner-introduced tilting) and lightly cleaned (to remove dark spots caused by staple holes, hole punches, and other blemishes caused after initial printing).

[2] A two-step process was used. An advanced optical character recognition computer program (OCR) first created electronic text from the document image. Where the OCR results were inconclusive, staff checked and corrected the text as necessary. Please note that the numbers and text in charts and tables were not reliably recognized by the OCR process and were not checked or corrected by staff.

Content last modified 5/26/2009.

Strictly Confidential (F.R.) **December 4, 2003**
Class II – FOMC

MONETARY POLICY ALTERNATIVES

Recent Developments

(1) The FOMC's decision at its October meeting to leave the target federal funds rate unchanged had been widely anticipated in markets.[1] However, the Committee's retention of both an unchanged risk assessment and its indication that policy could remain accommodative for a considerable period, which were apparently seen as less certain outcomes, sparked a short-lived rally in Treasury markets. Over the balance of the intermeeting period, Treasury coupon rates rose on stronger-than-expected economic releases, but those increases were partly offset by the market response to several statements by policymakers reiterating that policy could remain accommodative (chart 1). On net, most Treasury coupon rates were up 10 to 25 basis points.[2] Yields on Treasury indexed notes increased about in line with those on comparable nominal issues, leaving inflation compensation about unchanged following its appreciable rise in earlier months.

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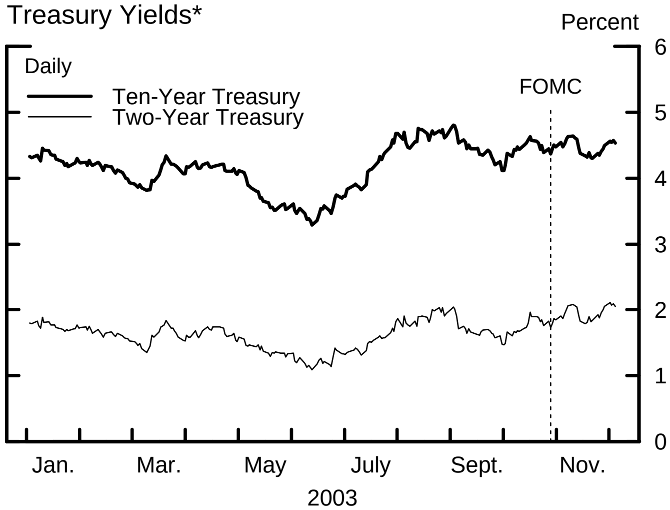
[1] Federal funds traded over the intermeeting period at an average rate very close to 1 percent. The Desk purchased $1.3 billion of Treasury bills from foreign official institutions and $5.4 billion of Treasury coupon securities in the market. The outstanding amount of long-term RPs increased $1 billion, to a level of $21 billion.

[2] The May 2013 Treasury note continued to experience an elevated level of fails to deliver for much of the period. In its mid-quarter refunding announcement, the Treasury noted the fails problem but stated its belief in "market participants' ability to resolve this matter," which investors read as all but ruling out a reopening of this note. In the past few days, fails in this security have dropped sharply, as foreign central banks reportedly became more willing to lend their holdings of the security in the RP market. Although this note continues to command a premium in cash and repo markets, very recently it has traded at a slightly positive interest rate for overnight repurchase agreements for the first time in months.

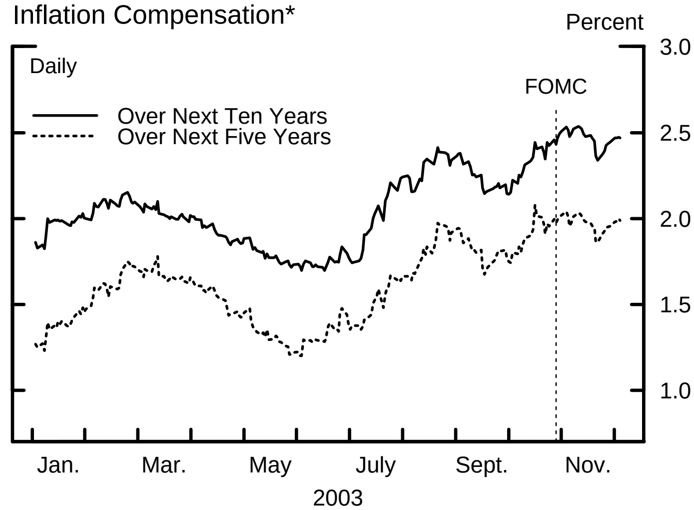
Chart 1
Interest Rate Developments

Treasury Yields*



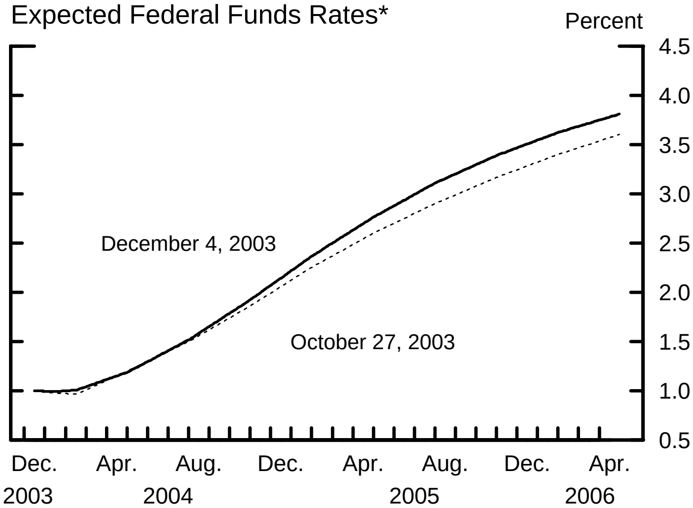
*Par yields from an estimated off-the-run Treasury yield curve.

Inflation Compensation*



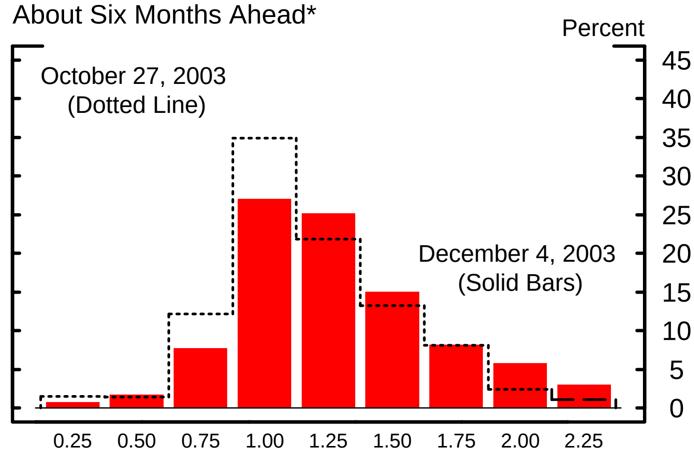
*Based on a comparison of an estimated TIIS yield curve to an estimated nominal off-the-run Treasury yield curve.

Expected Federal Funds Rates*



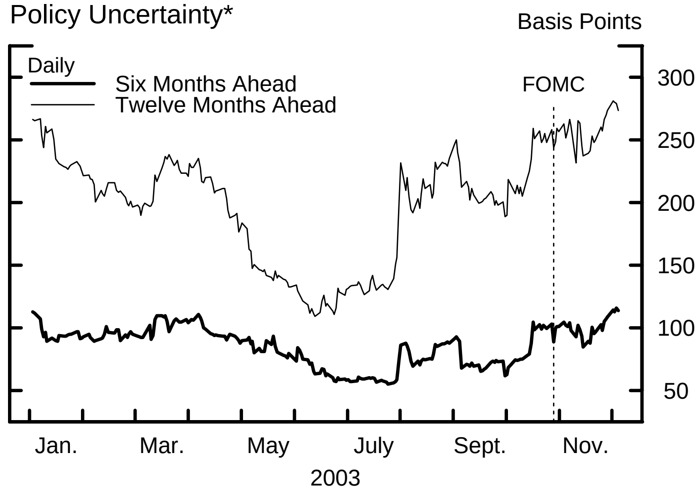
*Estimates from federal funds and eurodollar futures, with an allowance for term premia and other adjustments.

Implied Distribution of the Federal Funds Rate About Six Months Ahead*



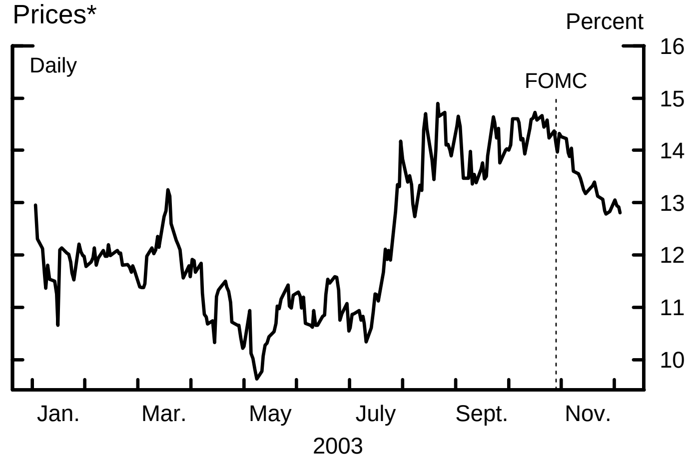
*Based on the distribution of the three-month eurodollar rate five months ahead (adjusted for a risk premium), as implied by options on eurodollar futures contracts.

Policy Uncertainty*



*Width of a 90 percent confidence interval computed from the term structures for the expected federal funds rate and implied volatility.

Implied Volatility of Long-Term Treasury Bond Prices*



*Derived from options on futures contracts.

Note: Vertical lines indicate October 28, 2003. Last daily observations are for December 4, 2003 .

(2) The expected path of the federal funds rate remained essentially flat through the first quarter of 2004, likely held down by policymakers' statements, but steepened somewhat beyond that point on the gathering evidence of a more vigorous economic expansion. Judging from interest rate options data, investors' sense of uncertainty about the future course of policy rose over the period, especially at longer horizons. A recent Desk survey of primary dealers indicated that none anticipates a change in policy at this meeting and only a few foresee any changes in the balance-of-risks assessment. However, about two-thirds of the dealers said that they expect the reference to a "considerable period" will be removed or modified. Reportedly, many believe the considerable period phrase will be replaced with language that provides the Committee with greater flexibility in adjusting policy going forward.

(3) The better economic news promoted a narrowing of risk spreads, particularly for lower-tier instruments (chart 2).[3] Market participants appeared unconcerned about risk and liquidity over year-end, with spreads on money-market instruments spanning the turn evidencing little of the usual end-of-year rise. (See box entitled "(Lack of) Year-End Pressures.") Equity markets advanced noticeably over the intermeeting period, with some indexes touching new highs for the year and implied volatility remaining very low. The Wilshire 5000 rose about 4 percent and indexes of stock prices for smaller and for high-tech firms recorded larger gains.

(4) The dollar dropped about 1¼ percent on net over the intermeeting period against an index of major trading partners' currencies (chart 3). During the

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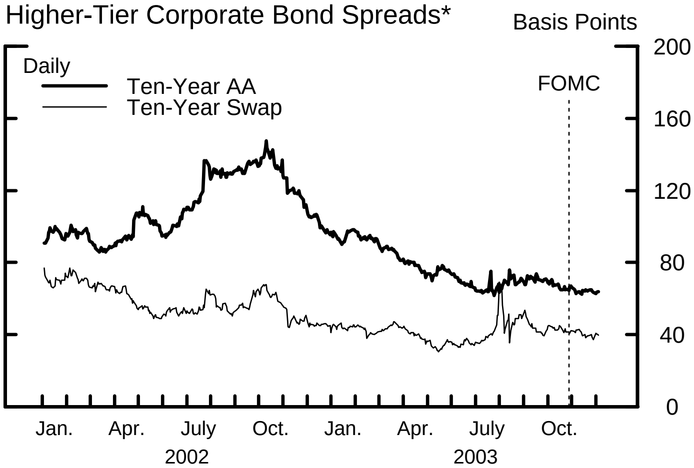
[3] The narrowing of spreads over Treasuries included those on Federal Home Loan Bank consolidated obligations even though Standard & Poor's placed three more FHLBs under negative credit watch for their counterparty risk ratings. Meanwhile, Freddie Mac announced a $5 billion upward revision to earnings for the 2000 to 2002 period but stated that quarterly and full-year results for 2003 would not be available until the middle of next year. Nonetheless, its stock moved up on the day of the restatement, apparently as a result of the resolution of uncertainty.

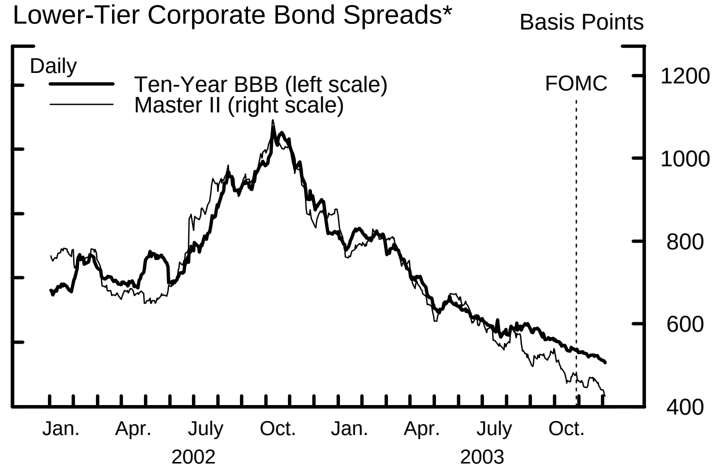
Chart 2
Financial Market Indicators

Higher-Tier Corporate Bond Spreads*



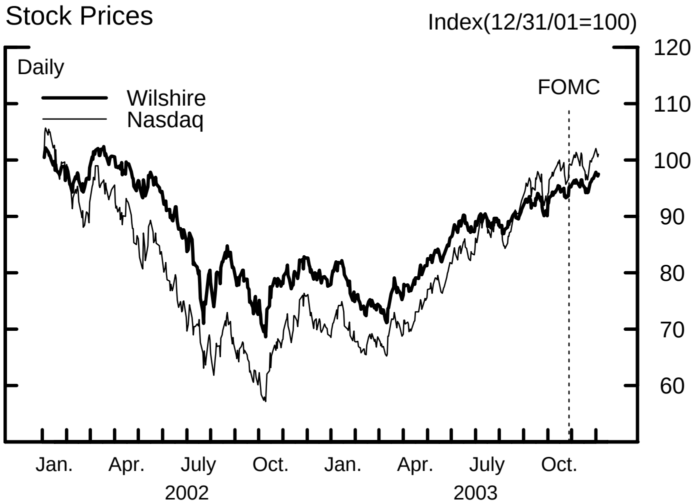
*AA spread measured relative to an estimated off-the-run Treasury yield curve. Swap spread measured relative to the on-the-run Treasury security.

Lower-Tier Corporate Bond Spreads*

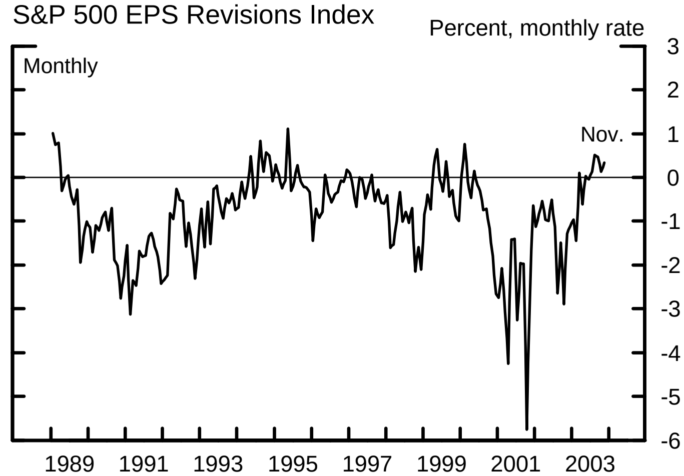


*Measured relative to an estimated off-the-run Treasury yield curve.

Stock Prices

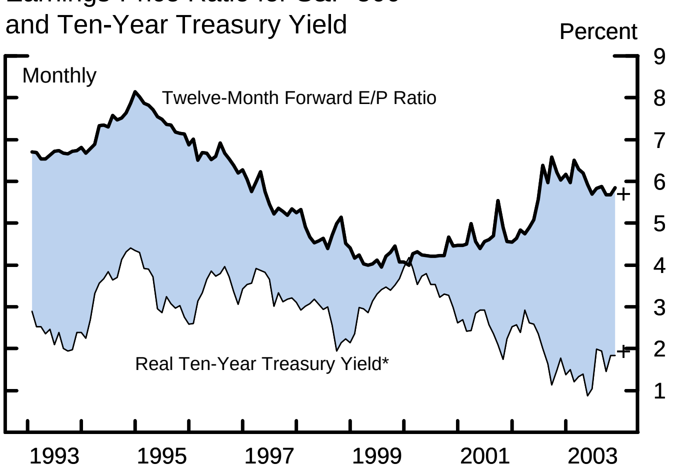


S&P 500 EPS Revisions Index



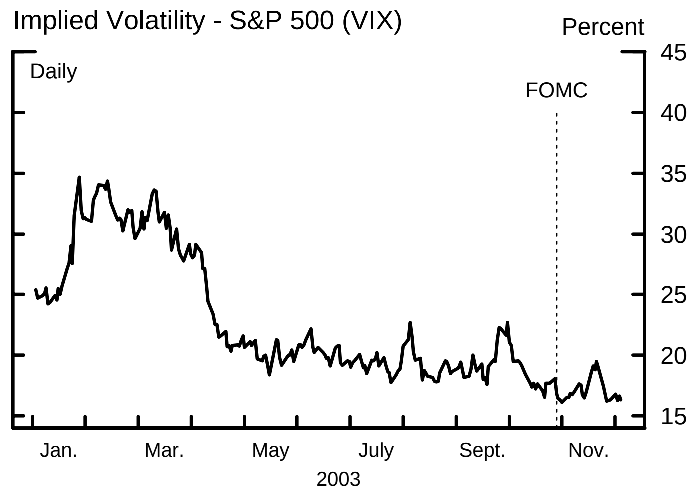
Note. Index is a weighted average of the percent change in the consensus forecasts of current-year and following-year EPS.

Earnings-Price Ratio for S&P 500 and Ten-Year Treasury Yield



*End-of-month ten-year Treasury yield minus Philadelphia Fed ten-year expected inflation.
+ Denotes latest daily observation, December 4, 2003 .

Implied Volatility - S&P 500 (VIX)

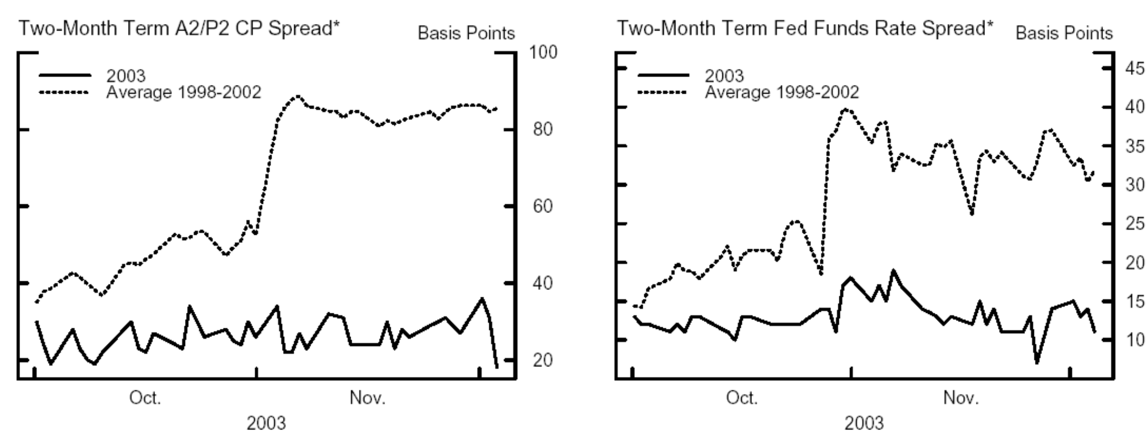


Note: Vertical lines indicate October 28, 2003. Last daily observations are for December 4, 2003 .

(Lack of) Year-end Pressures

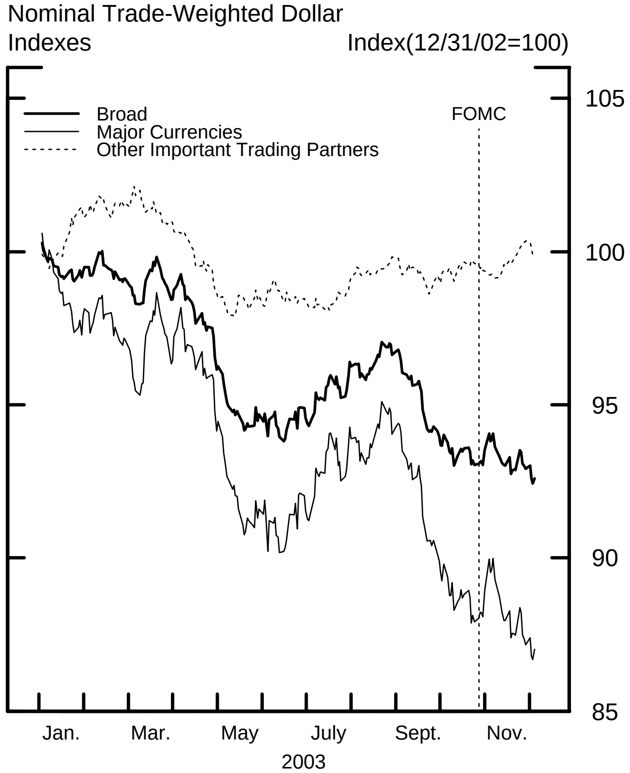
To date in 2003, year-end pressures in money markets have been negligible. In the commercial paper market, the spread of yields on two-month A2/P2 paper over those on comparable-maturity Treasury RPs was largely unchanged as the maturity of that paper crossed year-end, a considerable departure from typical behavior in recent years (left-hand panel of chart below). Similarly, term federal funds spreads point to muted year-end pressures in the interbank market (right-hand panel). Rates on federal funds futures contracts suggest that the expected deviation of the effective federal funds rate from its target on December 31 is within historical norms.

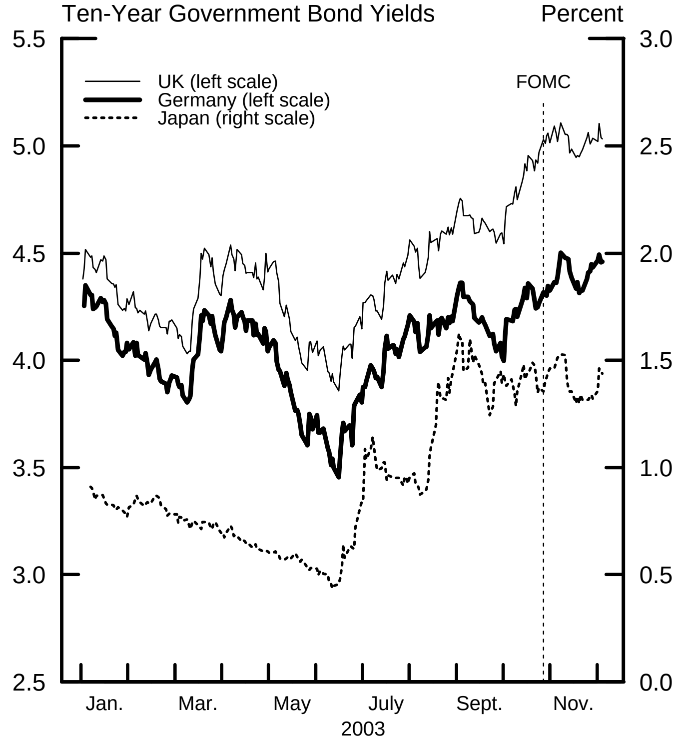
A number of factors may be contributing to the lack of year-end pressures in these markets. The recent absence of major adverse credit events in the commercial paper market, the generally improving credit climate, and the continued contraction in paper outstanding have reportedly attenuated perceptions of rollover risk. Further declines in the volatility of the federal funds rate this year to a very low level may have helped convince market participants that conditions in the federal funds market will remain tame around year-end.

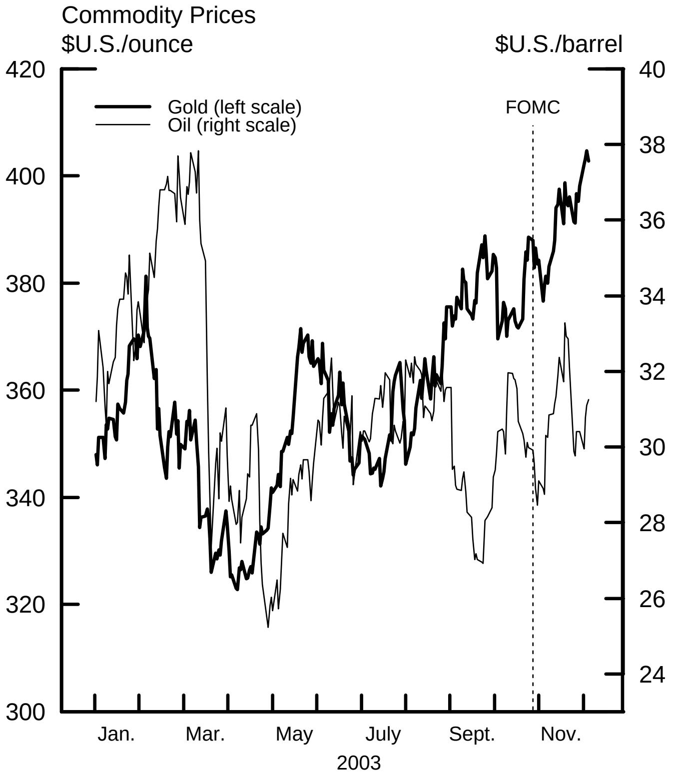


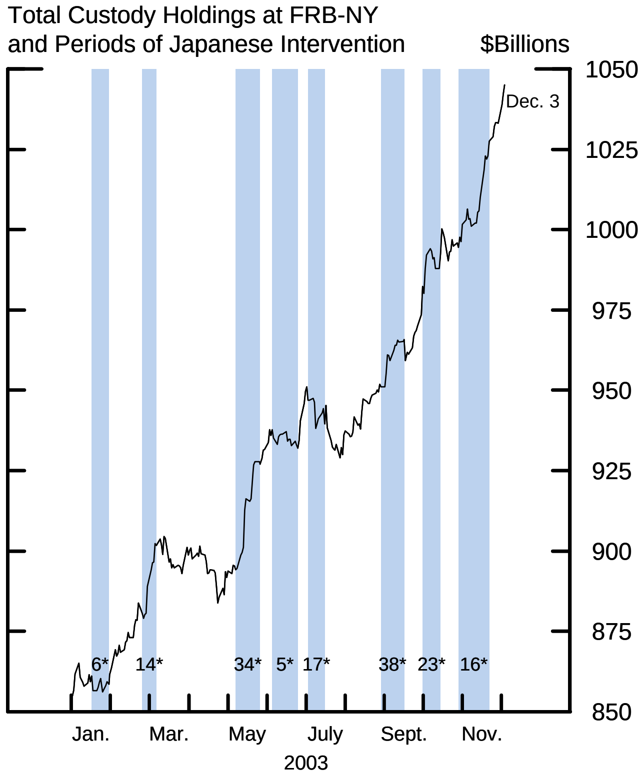
*Spread relative to two-month term RP rate.

Chart 3
International Financial Indicators
(Daily Data)









*Total purchases of U.S. dollars in billions per episode of intervention by Japanese monetary authorities. Cumulative total purchases in 2003: $152.9 billion.

Note: Last daily observations are for December 4, 2003, except as noted.

first two weeks of the period, the dollar was boosted by better-than-expected U.S. economic data. After early November, however, the release of capital flow data suggesting that private investors' willingness to finance the U.S. current account deficit may be diminishing, concerns about escalating trade frictions, developments in Iraq, and terrorist attacks all weighed on the dollar. Indications that economic activity in Europe is firming helped push the dollar to a new low against the euro and to a loss of more than 2½ percent over the period. The dollar also weakened somewhat against the pound but rose slightly versus the Canadian dollar. Stock markets in Europe and Canada continued to rally, with prices rising 4 to 7 percent. The dollar was about unchanged on balance against the yen as Japanese authorities made large intervention purchases of dollars.[4] With concerns resurfacing about the sustainability of the Japanese recovery, stock prices in Japan fell back early in the period, but they later recovered somewhat in part on news that the government is taking forceful action to resolve a failing regional bank. Sovereign bond yields in most major foreign countries rose by modest amounts over the intermeeting period. Central banks in the United Kingdom and Australia tightened policy rates, pointing in both cases to the possibility of increasing inflationary pressures owing to the greater economic strength at home and abroad.

(5) The dollar edged up against an index of currencies of our other important trading partners. The dollar rose more noticeably against the Mexican peso and the Brazilian *real*, as recent economic performance in those countries has been soft. Nevertheless, financial markets continued to register support for Brazil's reform program; its EMBI+ spread narrowed further during the intermeeting period to less

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[4]

. The Desk did not intervene during the period for the accounts of the System or the Treasury.

than 5 percentage points, the lowest level in more than five years. Emerging market economies in Asia continued to benefit from the global high-tech revival and a bounceback from earlier effects of the SARS epidemic. In most of these countries, stock prices recorded modest gains. In Korea, the won dropped about ¾ percent, apparently reflecting concerns about the strength of domestic demand, worries about rising financial strains, and reactions to reports that the Bank of Korea was conducting intervention sales of won.

(6) Business borrowing has remained subdued in recent months, while household debt growth appears to have slowed from its earlier rapid pace. So far in the fourth quarter, debt growth of nonfinancial businesses seems to have about matched the 3 percent rate seen in the third quarter. Although gross bond issuance has remained brisk, the proceeds reportedly have been earmarked mostly to retire maturing bonds and to pay down short-term debt, which continued to run off in October and November. Spurred by rising stock prices, gross equity issuance has picked up, with the proceeds also directed, in part, to reducing existing debt. Available data suggest that household debt growth has slowed in recent months from the double-digit expansion over the first three quarters of the year. A drop in refinancing activity from the record high levels of the summer has acted to hold down home mortgage growth, and a scaling back of auto incentive programs probably has weighed on consumer credit. With state and local debt growth also moderating some, and federal debt continuing to advance at about its third quarter pace, expansion of total domestic nonfinancial sector debt is expected to slow a percentage point to a 7 percent rate in the fourth quarter.

(7) The falloff in mortgage refinancing from its peak this summer also has contributed to a contraction of M2 in each of the past three months. Robust inflows into stock mutual funds suggest that the declines in M2 may also reflect shifts of

household portfolio preferences toward equities.[5] In contrast, a rebound in currency growth from the surprisingly weak pace of late summer has provided a little support to M2 growth. The outflows from M2 accounts were accompanied by two months of contraction in bank credit, although bank credit growth rebounded in November. Appendix B analyzes growth of money and the debt of domestic nonfinancial sectors during 2003.

[5] Allegations of criminal activities and other improprieties at some mutual funds appear to have had little effect as yet on overall flows into this sector. Some of the funds cited by prosecutors experienced substantial outflows, but those flows apparently were largely directed elsewhere within the industry. Confidential reports from a fund complex that has experienced substantial redemptions indicate that no difficulties have been encountered in meeting them.

Policy Alternatives

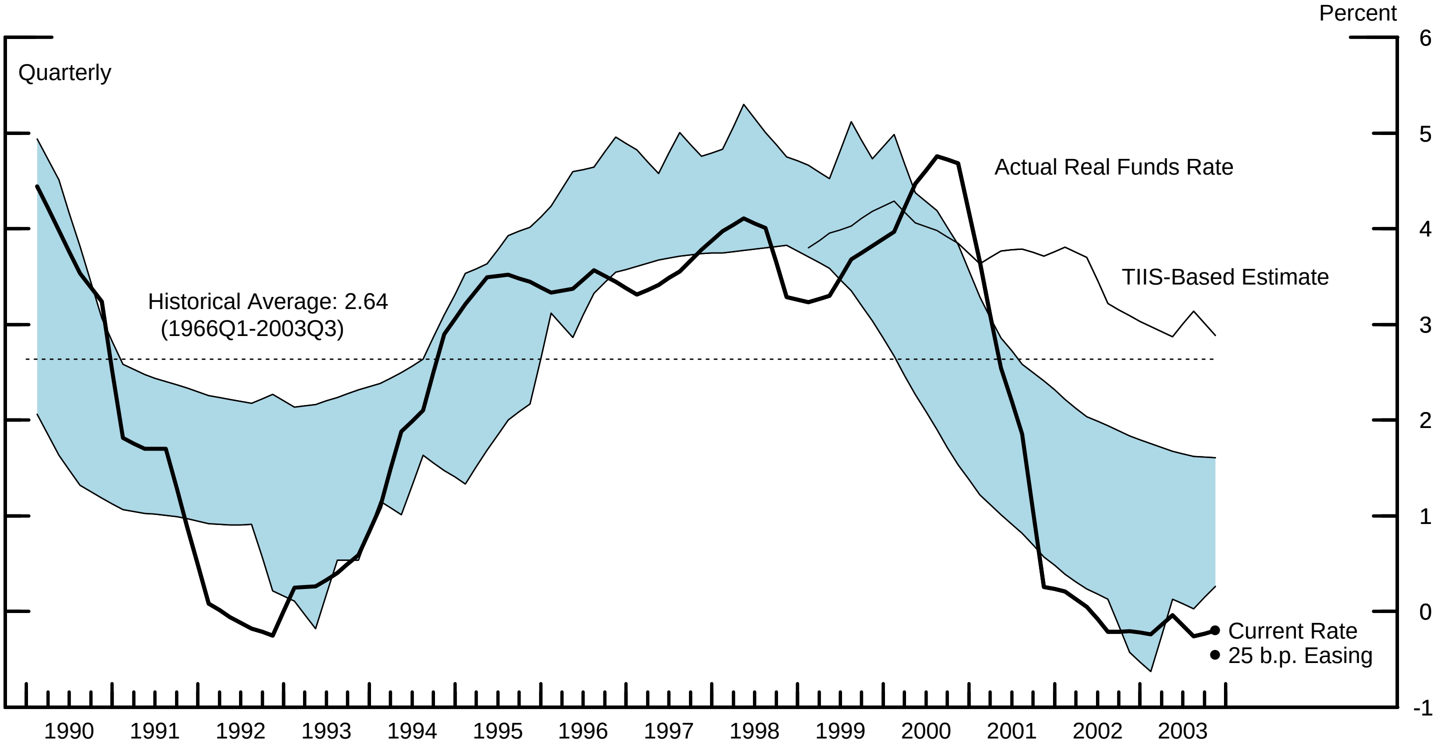
(8) Stronger-than-expected incoming data have led the staff to mark up its projection for the level of spending in the current quarter and over the forecast horizon. The staff forecast now assumes that policy tightening will begin in the first quarter of 2005–a half-year earlier than in the October Greenbook–and will push the funds rate up to 2 percent by the end of that year–50 basis points higher than in the last round. Longer-term corporate yields are projected to edge lower next year as market expectations for policy converge toward the shallower trajectory assumed by the staff and as the improvement in the economic outlook further narrows risk spreads. Over the forecast interval, equity prices are assumed to rise enough from their current levels to yield risk-adjusted returns in line with those on fixed-income instruments, while the dollar is assumed to move gradually lower in 2004 at the same rate as in the last Greenbook. Given these accommodative financial conditions, output is projected to expand about 5¼ percent in 2004. A shift toward fiscal restraint in 2005, combined with the assumed monetary policy tightening, contributes to a moderation of the advance in GDP to about 3¾ percent in that year. Despite the upward revisions to projected output, the output gap over the forecast interval is only a touch narrower than in the last round, as the staff has also marked up the paths for structural productivity and potential output. With actual growth exceeding that of potential next year, the civilian unemployment rate is projected to fall substantially by the end of 2004 before leveling out at about its estimated natural rate in the second half of 2005. Lingering resource slack is seen as putting slight further downward pressure on core PCE inflation, bringing it to a pace just above 1 percent in 2004 and 2005.

(9) If the Committee finds reasonably likely and acceptable the staff forecast that output growth will run above that of potential for the next several quarters while

core PCE inflation stabilizes near 1 percent, it might choose an **unchanged target for the federal funds rate** at this meeting. The Committee might see the recent strength in overall spending and the apparent waning of business caution evidenced by the upturn in hiring and pickup in investment as signs that a more robust expansion is now under way and that the threat of a significant decline in inflation has receded. Even if the Committee is somewhat concerned that growth could still falter, it might see that risk as being balanced by the possibility that the expansion could outpace expectations, particularly in view of recent data. And, alternatively, even if the Committee believes that the next policy move will probably be toward tightening in view of recent strong growth and the relatively low real federal funds rate (chart 4), it might also believe that the tightening process need not begin any time soon in light of the current low level of inflation and substantial degree of resource slack.

(10) If, however, the Committee is especially concerned that economic growth may not remain rapid enough to return output to its potential reasonably promptly and that resource slack may contribute to a significant further decline in inflation, then it might choose to **cut the target for the federal funds rate by 25 basis points** at this meeting. Though most incoming data of late have pointed to a strengthening in economic activity, the Committee might see this surge in demand as likely to be only temporary, perhaps along the lines of the "weaker household spending" simulation in the Greenbook. Evidence that might be taken as supporting this view could include the apparent substantial deceleration in personal consumption expenditures in the current quarter, the contraction in the broad monetary aggregates and bank credit, continued tepid growth in business debt, and a moderation in household borrowing. In such circumstances, a quarter-point easing at this meeting might be seen as desirable to foster a continuation of brisk growth in output and an acceptably rapid closing of the output gap. Furthermore, members may regard the

Chart 4
Actual Real Federal Funds Rate and Range of Estimated Equilibrium Real Rates



Note: The shaded range represents the maximum and the minimum values each quarter of four estimates of the equilibrium real federal funds rate based on a statistical filter and the FRB/US model. Real federal funds rates employ a four-quarter moving average of core PCE inflation as a proxy for inflation expectations, with the staff projection used for 2003Q4.

Equilibrium Real Funds Rate Estimates (Percent)

	2002	2003H1	2003Q3	2003Q4
Statistical Filter				
- Two-sided:				
Based on historical data and the staff forecast	0.2	0.4	0.5	0.5
October Bluebook	*0.2*	*0.2*	*0.4*	*0.4*
- One-sided:				
Based on historical data*	0.5	-0.2	0.0	0.3
October Bluebook	*0.5*	*-0.3*	*-0.1*	*0.1*
FRB/US Model				
- Two-sided:				
Based on historical data and the staff forecast	2.0	1.7	1.6	1.6
October Bluebook	*2.2*	*1.8*	*1.7*	*1.7*
- One-sided:				
Based on historical data**	1.2	0.2	0.3	0.4
October Bluebook	*1.3*	*0.2*	*0.3*	*0.4*
Treasury Inflation-Indexed Securities	3.5	2.9	3.1	2.9
October Bluebook	*3.5*	*2.9*	*3.1*	*3.1*

* Also employs the staff projection for the current and next quarters.

** Also employs the staff projection for the current quarter.

prevailing rate of inflation as near the bottom of a range that they view as desirable over the longer run and may wish to implement a policy stance that reduces downside risks to growth while increasing the scope for inflation to move up somewhat over time.

Policy Announcement, Directive, and Assessment of Risks.

(11) If the Committee chooses to maintain its current policy stance, it may want to adopt language in the **rationale paragraph** of its announcement generally similar to that in the statement following the October meeting (see appendix A), with appropriate revisions to reflect recent economic data. The rationale paragraph could again begin by noting that the accommodative stance of policy and vigorous growth in productivity are providing ongoing support to economic activity. In view of the robust performance of the economy in the third quarter and the tenor of the available indicators for the current quarter, the Committee might now wish to state that "output is expanding briskly" rather than "spending is firming." Consistent with the labor market report for October and weekly data on unemployment claims, the Committee may now want to characterize labor market conditions as "improving modestly," rather than as "stabilizing," particularly if, as the staff expects, employment registers a further gain in November. (The employment report for that month will be released on December 5, the day after this Bluebook is finalized.) The inflation sentence could again note that price increases remain muted, and it could also indicate that inflation is expected to remain low. If the Committee instead elects to ease policy, the rationale paragraph would presumably need to be augmented to note the Committee's desire to help ensure that the economic expansion remains on track and to guard against a significant further decline in inflation.

(12) In the **balance of risks paragraph**, there would appear to be two plausible settings for the assessment of the risks to the outlook for economic growth

and two for the risks to the attainment of price stability over the next few quarters. Risks to growth might now be seen as balanced or weighted to the upside, and risks to inflation might now be viewed as weighted to the downside or balanced. Table 1 displays several possibilities for the overall assessment of risks given alternative characterizations of the individual risks.

Table 1: Alternative Assessments of Balance of Risks

		Risks to Inflation	
		Unwelcome Fall	**Balanced**
Risks to sustain-able economic growth	**Balanced**	Low inflation predominant concern	Balanced
	Weighted to the Upside	Low inflation predominant concern -or- Balanced	Balanced -or- Unsustainably rapid growth predominant concern

(13) In characterizing the **risks to the outlook for sustainable economic growth**, the Committee may view economic growth as likely to moderate from its third-quarter pace but also likely to remain strong enough to return output to a level close to potential over the next few quarters. This outlook might argue for retention of an assessment that "*the upside and downside risks to the attainment of sustainable growth for the next few quarters are roughly equal.*" Such a judgment would be consistent with an interpretation of the term "sustainable economic growth" that allows for above-trend expansion for a time as long as growth appears on track to return to around that of potential once resource slack has been eliminated. Under this interpretation, the Committee might see the risk that economic growth could falter next year as roughly

balanced by the risk that economic growth could be quite robust and push the level of output appreciably above potential. If the Committee instead interprets sustainable economic growth as simply denoting the growth rate of the economy's potential to produce, then, in view of recent economic data and the low real federal funds rate, it might be appropriate to indicate that *"the risks to growth are tilted to the upside"*–unless the Committee still remains to be convinced that spending growth will stay rapid enough to support an acceptably robust expansion.

(14) In characterizing the **risks to the outlook for inflation**, even if the Committee finds the staff forecast of brisk growth in output and employment plausible, it might again conclude that *". . . the probability, though minor, of an unwelcome fall in inflation exceeds that of a rise in inflation from its already low level."* Such an assessment would be supported by the expected persistence of an output gap for several more quarters, a development that presumably would be accompanied by at least some downward pressure on inflation, as in the staff forecast. Also, the Committee might be quite uncertain about the range of possible macroeconomic outcomes and attach significant probability to those in which economic slack fails to diminish appreciably next year, perhaps because of continued rapid growth of productivity that fails to engender corresponding growth in aggregate demand and generates downward pressures on prices as a result. In contrast, the Committee may see the odds of such outcomes for resource utilization as increasingly remote given the strength of spending and output in recent months and tentative signs of improvement in the labor market. Moreover, the Committee might regard the recent depreciation of the dollar and run-up in market-based measures of inflation compensation since the summer as raising the odds somewhat that inflation pressures could emerge. In these circumstances, the Committee might now see the *risks to the inflation outlook as balanced.*

An intermediate position may be to modify the existing sentence to indicate that the risks to inflation are still tilted, but less so than in recent months.

(15) With some combinations of assessments of growth and inflation risks, the appropriate choice of the **overall risk assessment** seems obvious, but, with others, it is less so. The choice of the overall risk assessment is discussed in the next three paragraphs.

(16) As shown in *upper left cell* of Table 1, if the Committee remains especially concerned about the possibility of an unwelcome disinflation and still views the risks to sustainable growth as balanced, then its overall risk assessment would again presumably point to undesirably low inflation as its predominant concern. As noted in the *upper right cell*, if the Committee views the risks to its outlooks for both inflation and growth as balanced, it likely would also adopt a balanced overall assessment.

(17) As indicated in the *bottom left cell*, two possibilities for the overall risk assessment seem most plausible for the case in which the Committee sees inflation risks weighted toward an unwelcome decline and risks to sustainable economic growth weighted to the upside. If the Committee believes the costs of an unwelcome decline in inflation would be large relative to those of unsustainably rapid growth, it might cite undesirably low inflation as its predominant concern. This combination would be particularly appropriate if the Committee interprets "sustainable economic growth" simply as the growth of potential but does not believe that above-trend expansion over the next several quarters threatens to push the level of output beyond potential and thus spur inflation. Alternatively, the Committee might perceive the overall risks to its dual objectives as roughly balanced if the risk of an unwelcome fall in inflation–albeit still present–was less of a concern than at recent meetings, while unsustainably rapid growth posed a risk of pushing output above potential. Although concluding that unsustainably rapid growth is the predominant concern is a logical

possibility in this cell, it seems unlikely that the Committee would make such a sharp shift to the overall assessment even while maintaining that the risks to inflation were still tilted to the downside.

(18) As shown in the *bottom right cell*, the Committee would seem to face two choices for its overall risk assessment in the event that it judges that inflation risks are balanced and that risks to sustainable growth are weighted to the upside. If sustainable growth is interpreted to mean expansion at the same rate as potential output and the Committee believes that the level of output is unlikely to rise above potential, then it might view overall risks as balanced. However, if the Committee sees some risk that above-trend expansion of economic activity could push the level of output above potential before very long, it might choose to report that unsustainably rapid growth is its predominant concern.

(19) The final issue relating to the policy announcement is whether to retain, modify, or delete the sentence *"In these circumstances, the Committee believes that policy accommodation can be maintained for a considerable period."* This sentence has been the focus of much discussion in markets in recent weeks, and its treatment in the Committee's statement will influence investors' assessments of the near-term policy outlook. In particular, investors are likely to respond sharply to any change in the sentence that suggests tightening is becoming imminent. The Committee might choose to leave the sentence unchanged if it believes that economic growth will most likely moderate considerably from the surge in the third quarter and that an appreciable output gap and attendant risks of an unwelcome decline in inflation from its current low level remain the dominant considerations, implying that the need to firm policy is still well in the future. Even if the Committee sees increasing odds that it will need to begin tightening policy before too long and that it will thus soon want to modify or drop the sentence, it might prefer to defer such changes at this meeting pending further

evidence on whether an acceptably vigorous economic recovery is likely to be sustained. Moreover, the Committee might find it desirable to make any changes to that sentence in tandem with other adjustments in the statement that might be implemented following the review of communications policy in January.

(20) The Committee might see a modification or elimination of the considerable period sentence as warranted by any of several considerations. It might simply feel that the need for policy precommitment has diminished and that it is now appropriate to loosen a potential constraint on policy. Or, more specifically, it might anticipate that tighter policy could be needed relatively soon and judge that dropping or altering the sentence would be advisable in advance of any tightening move. Or it might feel that such a change would be especially congruent with a move to upside risks on growth or to balanced risks on inflation. One approach to modifying the sentence slightly at this time, with the intention of dropping it eventually, would be to declare that the Federal Reserve "*. . . can be patient in adjusting the stance of monetary policy."* Another would be to say that policy accommodation can be maintained *". . . for a while."* Still another would be to make continued accommodation contingent on developments affecting the economic outlook or inflation prospects. The Committee could accompany such changes by noting that the real federal funds rate is below its long-run equilibrium level. Market participants would likely read any such modification as the first step in an exit strategy from the Committee's current highly accommodative policy stance, and interest rates could back up as investors brought forward somewhat the anticipated onset of policy tightening, but the increases might be contained by an implication that tightening is probably still some time off and, when it did occur, need not be aggressive.

(21) Should the Committee wish to follow the same procedure as at the last three meetings, it could vote on the directive and on language providing guidance to

the drafters of the announcement regarding the risk assessment. Draft language with a range of options is provided below.

1) Directive Wording

The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. To further its long-run objectives, the Committee in the immediate future seeks conditions in reserve markets consistent with maintaining/INCREASING/REDUCING the federal funds rate at/TO an average of around ___ ~~1~~ percent.

(2) Risk Assessment

Against the background of its long-run goals of price stability and sustainable economic growth and of the information currently available, the Committee believes the risks to its outlook for sustainable economic growth over the next several quarters [ARE WEIGHTED TOWARD THE DOWNSIDE] [are balanced] [ARE WEIGHTED TOWARD THE UPSIDE]; the risks to its outlook for inflation over the next several quarters [are weighted toward the downside] [ARE BALANCED] [ARE WEIGHTED TOWARD THE UPSIDE]; and, taken together, the balance of risks to its objectives [are weighted toward the downside] [ARE BALANCED] [ARE WEIGHTED TOWARD THE UPSIDE] in the foreseeable future.

Market Reaction

(22) Market participants expect no change in the stance of monetary policy at this meeting, and most do not foresee an alteration in the three-sentence assessment of risks. As noted above, the market's reaction to the announcement of such a policy choice would be shaped to an important extent by the Committee's decision regarding

the "considerable period" sentence. Judging from recent surveys, better-than-expected economic news has led a majority of market participants to put significant odds on a modification of this sentence. Consequently, a statement encompassing no change in policy, no change in the Committee's overall risk assessment or its components, and no change in the considerable-period sentence could well prompt some drop in yields. Market participants' fixation on the last sentence of the announcement suggests that, if it were kept unchanged, shorter-term yields might not move much even if the Committee shifted its assessment of inflation risks to balance, or if it noted risks of unsustainably rapid growth but continued to indicate that undesirably low inflation remained its predominant concern. By contrast, interest rates could rise, perhaps substantially, in response to any statement that completely eliminated the considerable period sentence, and such increases would probably be amplified by any accompanying change in the individual or overall balance of risk assessments that pointed to lessened concerns about disinflationary pressures or increased concerns about excessively rapid economic growth. As noted above, the market reaction probably would be muted by a statement that modified the considerable period language but retained the sense that tightening was not imminent and implied that, when it did occur, might well be implemented relatively gradually.

(23) A decision to ease policy at this meeting would surprise investors, and other short-term interest rates would follow the federal funds rate lower. The consequences for longer-maturity yields would depend in part on the market's reading of the risk assessment and the considerable period sentence. If the balance of risks and the considerable period sentence were left unchanged from those in the October announcement, it seems likely that intermediate- and longer-term yields would fall as market participants came to see the Federal Reserve as intent on keeping short-term rates even lower for some time to counter a significant risk that the economic

expansion could falter next year. Alternatively, longer-term yields could rise if the announcement led investors to believe that the Federal Reserve wanted to see a higher long-run level of inflation or was at least willing to tolerate some risk of more inflation to foster a brisker return of output to its potential.

Monetary and Credit Aggregates

(24) The staff anticipates that M2 will expand a little in December and accelerate somewhat further over coming months. Refinancing effects should exert less drag, and faster growth of nominal income will provide a lift to money growth. Still, the velocity of M2 is expected to increase modestly as investors continue to favor capital market instruments at the expense of M2 assets. On balance, M2 is projected to expand at a 5½ percent annual rate from November through June.

(25) Growth of total domestic nonfinancial sector debt is projected to moderate next year but to a pace that still exceeds that of nominal income. Much of the deceleration in total debt reflects a slowing in the expansion of mortgage credit, as mortgage rates are expected to remain close to current levels throughout next year. Borrowing by state and local governments is also expected to slow some, largely reflecting a decline in the pace of advance refundings. Federal debt growth is projected to pick up a bit next year but then to drop back substantially in 2005 following an anticipated turn toward fiscal restraint. Borrowing in the business sector is expected to strengthen over the forecast horizon, buoyed by an increase in capital outlays and inventories and a corresponding increase in the business financing gap.

Alternative Growth Rates for M2

		Ease 25 bp	No Change	Greenbook Forecast*
Monthly Growth Rates				
	Nov-03	-4.3	-4.3	-4.3
	Dec-03	2.2	2.0	2.0
	Jan-04	5.1	4.5	4.5
	Feb-04	9.8	9.0	9.0
	Mar-04	5.7	5.0	5.0
	Apr-04	6.6	6.0	6.0
	May-04	6.4	6.0	6.0
	Jun-04	6.4	6.0	6.0
Quarterly Growth Rates				
	2003 Q3	9.1	9.1	9.1
	2003 Q4	-2.7	-2.7	-2.7
	2004 Q1	4.5	4.0	4.0
	2004 Q2	6.7	6.1	6.1
Annual Growth Rates				
	2002	6.8	6.8	6.8
	2003	5.4	5.4	5.4
	2004	5.8	5.4	5.4
Growth From	To			
2002 Q4	Nov-03	5.2	5.2	5.2
2003 Q2	Nov-03	2.8	2.8	2.8
Nov-03	Mar-04	5.8	5.2	5.2
Nov-03	Jun-04	6.1	5.6	5.6

* This forecast is consistent with nominal GDP and interest rates in the Greenbook forecast.

Appendix A: The October FOMC Announcement

Paragraph	Text
1. Policy decision	The Federal Open Market Committee decided today to keep its target for the federal funds rate at 1 percent.
2. Rationale	The Committee continues to believe that an accommodative stance of monetary policy, coupled with robust underlying growth in productivity, is providing important ongoing support to economic activity. The evidence accumulated over the intermeeting period confirms that spending is firming, and the labor market appears to be stabilizing. Business pricing power and increases in core consumer prices remain muted.
3. Assessment of risks	The Committee perceives that the upside and downside risks to the attainment of sustainable growth for the next few quarters are roughly equal. In contrast, the probability, though minor, of an unwelcome fall in inflation exceeds that of a rise in inflation from its already low level. The Committee judges that, on balance, the risk of inflation becoming undesirably low remains the predominant concern for the foreseeable future. In these circumstances, the Committee believes that policy accommodation can be maintained for a considerable period.
4. Vote	Voting for the FOMC monetary policy action were: Alan Greenspan, Chairman; Ben S. Bernanke; Susan S. Bies; J. Alfred Broaddus, Jr.; Roger W. Ferguson, Jr.; Edward M. Gramlich; Jack Guynn; Donald L. Kohn; Michael H. Moskow; Mark W. Olson; Robert T. Parry; and Jamie B. Stewart, Jr.

Appendix B: Review of Debt and Money Growth in 2003

Rapid expansion in household and federal debt pushed the growth of total debt of domestic nonfinancial sectors higher in 2003 despite continued sluggish business borrowing. The pattern of nonfederal borrowing within the year was shaped importantly by the path of longer-term interest rates, which fell over the first half, but then jumped considerably in early summer in response to evolving views of the economic outlook and changing policy expectations.

Over the year, the level of business debt rose modestly, as low investment spending was largely financed internally. As long-term rates fell through mid-year and credit spreads–especially for riskier borrowers–narrowed, there was considerable substitution toward bond financing and away from shorter-term debt. Household mortgage borrowing continued at a torrid pace for the year as a whole, although it moderated in the fourth quarter. Mortgage rates followed Treasury rates lower in the spring, and both new mortgage originations and mortgage refinancings surged. Some of the refinancing activity may have depressed consumer credit growth as households extracted equity from their homes. Nevertheless, consumer debt posted a moderate rise, buoyed by heavy spending on durables, especially autos. A substantial widening of the federal deficit, reflecting tax cuts and increased federal spending, forced the Treasury to increase its borrowing significantly.

Despite a pickup in nominal GDP growth, the expansion of M2 for 2003 as a whole was somewhat below the pace of last year. Deposits associated with the refinancing of mortgages underlying mortgage-backed securities surged in the summer, reflecting record refinancing activity, but subsequently ran off as refinancing slowed. In addition, the improved economic outlook and sustained rally in equity markets may have encouraged households to limit their accumulation of the safe and liquid assets in M2.

Domestic Nonfinancial Sector Debt

Aggregate debt of domestic nonfinancial sectors grew 8½ percent in 2003, significantly faster than nominal income and well above last year's pace. Nonfederal debt expanded about 8 percent, a percentage point faster than in 2002. Business borrowing, though not robust, was stronger than it had been last year. Household debt increased 11¼ percent, a bit more than in 2002. State and local government debt rose 8½ percent this year, down somewhat from the rapid pace in 2002, while larger deficits caused federal debt growth to pick up to 11 percent.

Overall demand for business credit was weak and its composition was tilted toward long-term securities. Higher profits in concert with subdued investment spending restrained the growth of business credit, and the decline in long-term interest rates in the first half of the year made bonds an attractive source of funding for nonfinancial firms. Moreover, corporate risk spreads–especially on speculative-grade issues–narrowed significantly, reflecting the increasing strength of the economic recovery and an apparent rise in investors' appetite for risk, perhaps owing as well to the waning influence of recent accounting and governance scandals. As a result of lower interest rates and narrowed spreads, corporate bond issuance was robust, particularly over the first half of the year, and a good deal of the proceeds was used to pay down short-term debt, including C&I loans and commercial paper. The contraction in business loans was concentrated at the largest commercial banks as demand from larger corporate customers was further restrained by a dearth of merger and acquisition activity; business lending at small banks, by contrast, grew moderately over the year. Firms that issued commercial paper found a very receptive market because of the relative scarcity of commercial paper outstanding and lower perceived risk resulting from the restructuring of corporate balance sheets.

Despite persistently high vacancy rates and falling rents, the growth of commercial mortgages was strong for most of the year. Because delinquencies remained low and property values continued to rise, credit ratings for borrowers were well maintained. Anecdotal reports suggest that many firms that own real estate tapped this market, issuing relatively cheap, collateralized debt in lieu of other, more costly debt. The issuance of commercial mortgage-backed securities remained correspondingly brisk throughout the year.

The strong growth in household debt reflected both robust home buying and substantial consumer spending. Record-low mortgage rates in the first half of the year gave rise to exceptionally high levels of household mortgage originations for both new purchases and refinancing activity. Many households used cash-out refinancings to fund consumer spending or to pay down other debt. Nevertheless, consumer credit grew at a moderate rate over the year, supported by spending on durable goods, especially autos. Consumer credit may have been boosted especially by attractive terms on car loans from automakers' captive finance companies.

Even with the rapid growth in debt, most measures of the financial condition of households did not deteriorate over the past year. With the effects of lower interest rates offsetting those of higher debts, household debt-service and financial obligation ratios were little changed, although household filings for bankruptcy were about 7 percent above the level posted in 2002. The climb in equity prices over the year, coupled with a continued rise in house prices, noticeably boosted household assets relative to disposable income. On net, gains in assets outstripped the increase in household debt, and the ratio of household net worth to disposable income rose.

The rally in equity markets was associated with a reallocation of household portfolios out of bond funds—especially government bond funds—and into equity funds. Later in the year, allegations of wrongdoing spurred some investors to withdraw their money from certain mutual fund companies, but evidently not from the industry as a whole. Anecdotal reports suggest that such outflows did not cause a significant cash squeeze for the funds experiencing withdrawals.

Gross issuance of debt by state and local governments was robust as municipalities borrowed for short-term cash needs and for capital expenditures in the face of tax shortfalls. Because of widespread financial distress, several states, most notably California, were downgraded. Municipal borrowing was strongest earlier in the year, as governments took advantage of low longer-term rates to fund capital expenditures and to advance refund existing higher-cost debt. Later, as interest rates backed up and the pool of debt eligible for advance refunding dwindled, the rate of growth of municipal debt slowed.

Large tax cuts and increased spending caused the Treasury to ramp up federal borrowing in 2003. As had been the case in 2002, the Treasury was forced temporarily to resort to accounting devices when the statutory debt ceiling became a constraint in the spring. However, Congress then raised the ceiling from $6.4 trillion to $7.4 trillion and there was essentially no disruption to debt markets. Given the rapid pace of federal borrowing, the current debt ceiling will likely bind again some time in the spring of 2004.

With large deficits expected to last for the foreseeable future, the Treasury altered its regular auction cycle to accommodate a greater need for borrowing. The Treasury re-introduced the three-year note in its May refunding auctions to ease its reliance on the two-year note. In addition, the Treasury increased the frequency of five-year note auctions, making them monthly, and added a reopening of the ten-year note in the month following each new quarterly offering. As a result of these changes, the average maturity of outstanding Treasury debt, which had reached its lowest level in decades, began to rise in the latter half of the year.

Depository Credit

Depository credit grew 6-1/4 percent in 2003, quite a bit slower than the overall expansion in domestic nonfinancial debt. Growth in depository credit importantly reflected mortgage lending and the acquisition of mortgage-backed securities at both banks and thrifts. Consumer lending was also substantial, reflecting robust spending on durable goods. In stark contrast, business loans ran off, as large banks shed far more C&I loans than small banks added.[6] Although banks' standards and terms on such loans were tightened somewhat further in the first half of the year before flattening out, the decline in business loans appears

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[6] In January, the Financial Accounting Standards Board issued Interpretation 46 ("Consolidation of Variable Interest Entities") which required the consolidation of some variable interest entities onto the balance sheets of banks. Although implementation initially was mandated for the first reporting period starting after June 15, it subsequently was pushed back to the end of the year. Some institutions nevertheless did consolidate assets in July, and the reported figures for depository credit growth have been adjusted to remove the effects of those consolidations.

to have reflected primarily a drop in demand. The high reported levels of bank capital and bank profits throughout 2003–as well as banks' apparent willingness to lend to other borrowers–support this view.

Monetary Aggregates

The velocity of M2 declined in the first two quarters of 2003, in part reflecting the lagged effect of policy easings over the past couple of years. Nevertheless, the contraction in money in the fourth quarter pulled growth for the year down to 5½ percent, a bit lower than the expansion in nominal income. Much of the robust growth in the aggregate around mid-year was in liquid deposits and likely owed to the wave of mortgage refinancings, which boosted M2 as the proceeds were temporarily placed in non-interest-bearing accounts pending disbursement to the holders of mortgage-backed securities. As mortgage rates retraced their decline, however, and the wave of refinancing slowed, this special factor unwound. In addition, the sustained rally in equity markets may have caused a substitution away from money, an interpretation consistent with the rapid inflows into equity mutual funds. In the event, M2 contracted for several months in the fall. Within M2, the low yields on money market mutual funds caused a reallocation away from such funds and toward liquid deposits.

Chart B-1
Debt and Money Growth

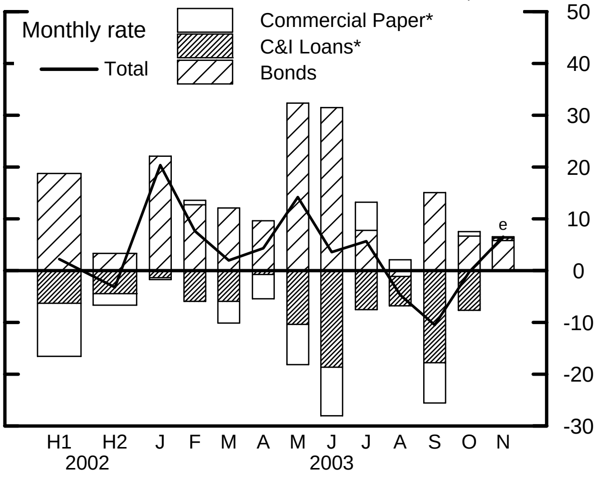
Growth of Nonfinancial Debt

Annualized growth rate

		Total	Nonfederal
2002	H1	6.8	6.5
	H2	7.2	7.3
2003	Q1	6.1	7.0
	Q2	12.1	9.6
	Q3	7.9	7.8
	Q4e	6.9	6.7

e Estimated.

Changes in Selected Components of Nonfinancial Business Debt



* Seasonally adjusted. e Estimated.
Note. C&I loans are adjusted for the estimated effects of FIN 46.

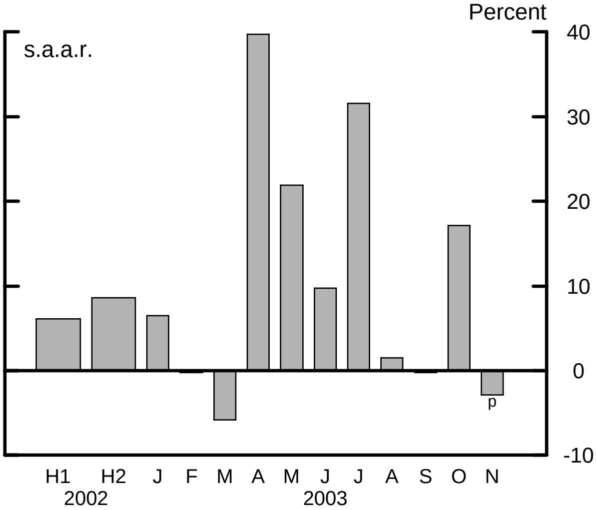
Growth of Household Debt

Annualized growth rate

		Consumer Credit	Home Mortgage
2002	H1	5.8	10.8
	H2	2.6	13.3
2003	Q1	4.9	11.8
	Q2	4.6	14.3
	Q3	6.8	13.4
	Q4e	5.3	11.2

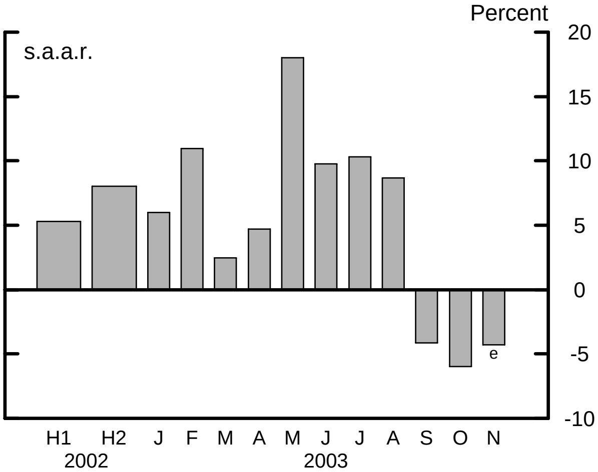
e Estimated.

Growth of Federal Debt



Note. Treasury debt held by the public at month-end.
p Preliminary.

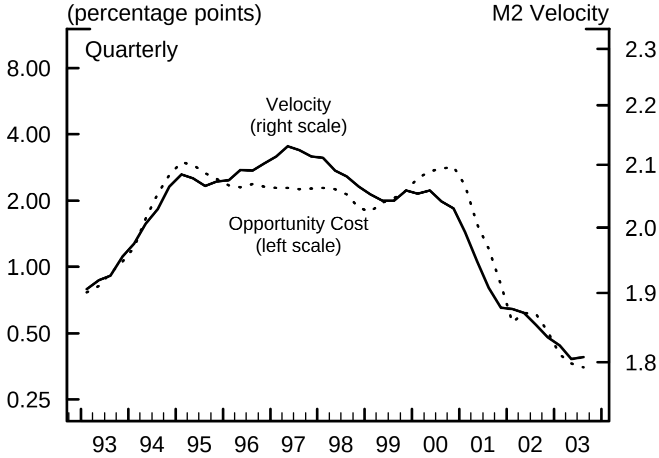
Growth of M2



e Estimated.

Opportunity Cost*

(percentage points)



*Two-quarter moving average.

SELECTED INTEREST RATES
(percent)

	Short-term						Long-term									
	Federal funds	Treasury bills secondary market			CDs secondary market	Comm. paper	Off-the-run Treasury yields				Indexed yields		Moody's Baa	Municipal Bond Buyer	Conventional home mortgages primary market	
		4-week	3-month	6-month	3-month	1-month	2-year	5-year	10-year	30-year	5-year	10-year			Fixed-rate	ARM
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
02 -- High	1.92	1.82	1.88	2.16	1.98	1.81	3.75	4.99	5.73	6.04	3.33	3.56	8.23	5.67	7.18	5.26
-- Low	1.15	1.07	1.16	1.23	1.31	1.26	1.59	2.72	3.94	4.85	1.54	2.19	7.30	5.02	5.93	4.01
03 -- High	1.45	1.26	1.22	1.28	1.32	1.28	2.11	3.60	4.80	5.61	1.84	2.48	7.48	5.50	6.44	4.06
-- Low	0.86	0.79	0.81	0.82	0.93	0.91	1.09	2.06	3.29	4.37	0.77	1.56	6.01	4.78	5.21	3.45
Monthly																
Dec 02	1.24	1.20	1.21	1.27	1.34	1.31	1.84	3.09	4.31	5.12	1.90	2.46	7.45	5.20	6.05	4.12
Jan 03	1.24	1.17	1.19	1.22	1.29	1.25	1.76	3.07	4.30	5.14	1.68	2.32	7.35	5.19	5.92	3.99
Feb 03	1.26	1.20	1.19	1.20	1.27	1.24	1.64	2.92	4.14	5.01	1.28	2.03	7.06	5.15	5.84	3.86
Mar 03	1.25	1.18	1.15	1.16	1.23	1.21	1.59	2.81	4.04	4.98	1.13	1.99	6.95	5.12	5.75	3.76
Apr 03	1.26	1.16	1.15	1.17	1.24	1.22	1.65	2.94	4.16	5.07	1.39	2.21	6.85	5.17	5.81	3.80
May 03	1.26	1.08	1.09	1.10	1.22	1.21	1.41	2.53	3.74	4.70	1.19	1.94	6.38	4.92	5.48	3.66
Jun 03	1.22	0.98	0.94	0.94	1.04	1.06	1.23	2.27	3.51	4.56	0.95	1.75	6.19	4.87	5.23	3.52
Jul 03	1.01	0.89	0.92	0.97	1.05	1.01	1.50	2.84	4.14	5.06	1.33	2.12	6.62	5.14	5.63	3.57
Aug 03	1.03	0.95	0.97	1.05	1.08	1.03	1.89	3.36	4.64	5.46	1.53	2.32	7.01	5.43	6.26	3.79
Sep 03	1.01	0.91	0.96	1.03	1.08	1.02	1.70	3.16	4.45	5.30	1.34	2.19	6.79	5.30	6.15	3.86
Oct 03	1.01	0.91	0.94	1.02	1.10	1.02	1.75	3.17	4.45	5.30	1.24	2.07	6.73	5.27	5.95	3.74
Nov 03	1.00	0.94	0.95	1.04	1.11	1.02	1.92	3.27	4.45	5.27	1.29	1.97	6.66	5.15	5.93	3.75
Weekly																
Oct 3 03	1.06	0.86	0.95	1.01	1.10	1.01	1.54	2.92	4.21	5.11	1.13	2.02	6.60	5.20	5.77	3.72
Oct 10 03	0.99	0.87	0.92	1.00	1.10	1.02	1.66	3.11	4.42	5.30	1.27	2.14	6.76	5.34	5.95	3.69
Oct 17 03	1.03	0.90	0.93	1.02	1.11	1.01	1.85	3.29	4.58	5.42	1.30	2.17	6.85	5.34	6.05	3.79
Oct 24 03	1.00	0.91	0.95	1.03	1.11	1.02	1.84	3.24	4.48	5.32	1.26	2.06	6.73	5.25	6.05	3.76
Oct 31 03	1.01	0.97	0.96	1.04	1.10	1.03	1.82	3.20	4.45	5.29	1.20	1.96	6.69	5.24	5.94	3.74
Nov 7 03	1.00	0.96	0.96	1.05	1.11	1.02	1.96	3.36	4.56	5.35	1.35	2.02	6.75	5.23	5.98	3.73
Nov 14 03	0.99	0.92	0.95	1.05	1.12	1.03	1.97	3.33	4.52	5.31	1.32	1.99	6.71	5.17	6.03	3.76
Nov 21 03	0.99	0.94	0.95	1.03	1.11	1.02	1.83	3.14	4.33	5.18	1.21	1.89	6.57	5.09	5.83	3.72
Nov 28 03	1.00	0.96	0.95	1.04	1.11	1.02	1.95	3.25	4.41	5.24	1.30	1.97	6.61	5.09	5.89	3.77
Dec 5 03	--	0.96	0.94	1.05	1.11	1.01	2.08	3.42	4.56	5.32	1.43	2.07	--	--	6.02	3.77
Daily																
Nov 18 03	0.98	0.95	0.96	1.04	1.11	1.02	1.81	3.11	4.32	5.16	1.15	1.83	6.55	--	--	--
Nov 19 03	0.98	0.94	0.95	1.03	1.11	1.02	1.90	3.20	4.38	5.23	1.24	1.91	6.61	--	--	--
Nov 20 03	1.00	0.93	0.95	1.01	1.11	1.02	1.82	3.12	4.32	5.18	1.25	1.93	6.56	--	--	--
Nov 21 03	0.98	0.93	0.94	1.02	1.11	1.03	1.83	3.13	4.31	5.17	1.26	1.95	6.54	--	--	--
Nov 24 03	0.98	0.94	0.96	1.04	1.11	1.00	1.92	3.22	4.38	5.22	1.29	1.99	6.61	--	--	--
Nov 25 03	1.02	0.97	0.95	1.03	1.11	1.01	1.87	3.18	4.35	5.19	1.24	1.93	6.57	--	--	--
Nov 26 03	1.01	0.97	0.94	1.04	1.10	1.04	1.95	3.26	4.41	5.23	1.30	1.96	6.60	--	--	--
Nov 27 03	1.01	--	--	--	--	--	--	--	--	--	1.30	1.96	--	--	--	--
Nov 28 03	1.01	0.96	0.93	1.04	1.11	1.02	2.06	3.36	4.50	5.30	1.39	2.03	6.67	--	--	--
Dec 1 03	1.03	0.96	0.95	1.06	1.11	1.02	2.11	3.44	4.57	5.33	1.45	2.07	6.70	--	--	--
Dec 2 03	0.97	0.96	0.94	1.04	1.11	1.00	2.07	3.41	4.55	5.31	1.42	2.06	6.68	--	--	--
Dec 3 03	0.98	0.96	0.94	1.04	1.11	1.01	2.09	3.44	4.57	5.34	1.43	2.08	6.70	--	--	--
Dec 4 03	--	0.94	0.93	1.04	1.11	--	2.05	3.40	4.54	5.32	1.40	2.05	--	--	--	--

NOTE: Weekly data for columns 1 through 13 are week-ending averages. Columns 2 through 4 are on a coupon equivalent basis. Data in column 6 are interpolated from data on certain commercial paper trades settled by the Depository Trust Company. Column 14 is the Bond Buyer revenue index, which is a 1-day quote for Thursday. Column 15 is the average contract rate on new commitments for fixed-rate mortgages (FRMs) with 80 percent loan-to-value ratios at major institutional lenders. Column 16 is the average initial contract rate on new commitments for 1-year, adjustable-rate mortgages (ARMs) at major institutional lenders offering both FRMs and ARMs with the same number of discount points.

MFMA

Money Aggregates

Seasonally adjusted

Period	M1	M2	nontransactions components: In M2	nontransactions components: In M3 only	M3
	1	2	3	4	5
Annual growth rates(%):					
Annually (Q4 to Q4)					
2000	-1.7	6.1	8.5	17.3	9.2
2001	6.8	10.2	11.2	18.5	12.7
2002	3.2	6.8	7.7	5.6	6.4
Quarterly(average)					
2002-Q4	4.9	7.0	7.6	9.5	7.8
2003-Q1	7.5	6.4	6.1	3.9	5.6
Q2	9.1	8.5	8.3	1.9	6.4
Q3	9.0	9.1	9.2	14.2*	10.7*
Monthly					
2002-Nov.	-0.4	8.4	10.8	38.1	17.7
Dec.	8.2	3.2	1.9	17.9	7.9
2003-Jan.	2.4	6.0	6.9	-12.6	0.0
Feb.	20.4	11.0	8.5	-2.8	6.6
Mar.	3.2	2.5	2.3	6.4	3.7
Apr.	0.2	4.7	5.9	-2.1	2.6
May	20.3	18.0	17.4	2.4	13.1
June	13.5	9.8	8.8	8.7	9.4
July	5.6	10.3	11.6	36.3*	18.4*
Aug.	7.4	8.7	9.0	-3.5	4.8
Sep.	2.1	-4.1	-5.8	5.7	-1.0
Oct.	-1.0	-6.0	-7.3	-12.8	-8.1
Nov. e	-4.0	-4.3	-4.3	-6.4	-4.9
Levels ($billions):					
Monthly					
2003-June	1271.9	6047.5	4775.6	2732.7	8780.2
July	1277.8	6099.5	4821.7	2815.4†	8915.0†
Aug.	1285.7	6143.6	4857.9	2807.2†	8950.8†
Sep.	1288.0	6122.4	4834.3	2820.6†	8943.0†
Oct.	1286.9	6091.9	4804.9	2790.5†	8882.3†
Weekly					
2003-Oct. 6	1289.9	6103.2	4813.4	2798.5†	8901.7†
13	1273.5	6101.5	4827.9	2788.3†	8889.8†
20	1283.9	6092.9	4809.0	2786.2†	8879.1†
27	1289.8	6079.4	4789.6	2789.4†	8868.8†
Nov. 3	1305.1	6074.5	4769.3	2790.2†	8864.6†
10	1286.2	6083.5	4797.2	2772.4†	8855.8†
17p	1281.1	6085.5	4804.4	2773.5†	8859.1†
24p	1280.7	6057.8	4777.1	2782.2†	8840.1†

p preliminary
e estimated
* FIN 46-adjusted growth rates for non-M2 M3 and M3 in 2003-Q3 are 6.9 and 8.4 percent, respectively. FIN 46-adjusted growth rates for non-M2 M3 and M3 in July 2003 are 14.4 and 11.6 percent, respectively. FIN 46 has had no material impact on M2 as yet.
† As of July 7, includes $50 billion due to FIN 46 effects.

Strictly Confidential
Class II FOMC

Changes in System Holdings of Securities [1]
(Millions of dollars, not seasonally adjusted)

December 4, 2003

	Treasury Bills			Treasury Coupons						Federal Agency	Net change total outright holdings [4]	Net RPs [5]		
	Net Purchases [2]	Redemptions (-)	Net Change	Net Purchases [3] < 1	Net Purchases [3] 1-5	Net Purchases [3] 5-10	Net Purchases [3] Over 10	Redemptions (-)	Net Change	Redemptions (-)		Short-Term [6]	Long-Term [7]	Net Change
2000	8,676	24,522	-15,846	8,809	14,482	5,871	5,833	3,779	31,215	51	15,318	-2,163	7,133	4,970
2001	15,503	10,095	5,408	15,663	22,814	6,003	8,531	16,802	36,208	120	41,496	3,492	636	4,128
2002	21,421	---	21,421	12,720	12,748	5,074	2,280	---	32,822	---	54,242	-5,366	517	-4,850
2002 QIII	6,117	---	6,117	2,835	3,676	1,318	143	---	7,972	---	14,089	-3,067	-5,225	-8,291
QIV	250	---	250	---	339	314	---	---	653	---	903	4,892	-304	4,588
2003 QI	6,024	---	6,024	1,796	2,837	1,291	50	---	5,974	---	11,998	1,957	3,770	5,727
QII	6,259	---	6,259	2,209	1,790	234	---	---	4,232	---	10,491	-2,578	1,056	-1,522
QIII	2,568	---	2,568	---	---	1,232	150	---	1,382	---	3,950	1,712	-554	1,158
2003 Apr	3,543	---	3,543	1,422	733	---	---	---	2,155	---	5,699	-265	816	551
May	1,684	---	1,684	786	1,057	234	---	---	2,077	---	3,761	-515	346	-170
Jun	1,032	---	1,032	---	---	---	---	---	---	---	1,032	-3,302	1,354	-1,948
Jul	808	---	808	---	---	---	---	---	---	---	808	2,486	-1,548	938
Aug	981	---	981	---	---	---	---	---	---	---	981	3,195	-935	2,259
Sep	780	---	780	---	---	1,232	150	---	1,382	---	2,162	-1,562	1,817	256
Oct	880	---	880	---	1,447	280	---	---	1,728	---	2,608	-73	-527	-600
Nov	925	---	925	2,561	1,503	787	---	---	4,851	---	5,775	-382	894	512
2003 Sep 10	235	---	235	---	---	1,232	150	---	1,382	---	1,617	-9,930	-1,000	-10,930
Sep 17	347	---	347	---	---	---	---	---	---	---	347	5,972	-2,000	3,972
Sep 24	47	---	47	---	---	---	---	---	---	---	47	-4,707	-1,000	-5,707
Oct 1	187	---	187	---	---	---	---	---	---	---	187	8,983	---	8,983
Oct 8	71	---	71	---	---	---	---	---	---	---	71	-8,795	-2,000	-10,795
Oct 15	207	---	207	---	---	---	---	---	---	---	207	6,370	1,000	7,370
Oct 22	252	---	252	---	---	---	---	---	---	---	252	-5,360	4,000	-1,360
Oct 29	178	---	178	---	1,447	280	---	---	1,728	---	1,905	2,958	---	2,958
Nov 5	192	---	192	---	---	---	---	---	---	---	192	-3,785	-1,000	-4,785
Nov 12	293	---	293	1,100	---	---	---	---	1,100	---	1,393	1,798	-3,000	-1,202
Nov 19	166	---	166	1,461	786	---	---	---	2,247	---	2,412	1,220	714	1,935
Nov 26	295	---	295	---	717	787	---	---	1,504	---	1,799	-823	5,143	4,320
Dec 3	132	---	132	---	237	283	20	---	540	---	672	3,702	-857	2,845
2003 Dec 4	---	---	---	---	---	---	---	---	---	---	---	870	---	870
Intermeeting Period														
Oct 28-Dec 4	1,254	---	1,254	2,561	1,740	1,070	20	---	5,391	---	6,645	-4,360	1,000	-3,360
Memo: LEVEL (bil. $)														
Dec 4			243.4	114.3	179.1	51.3	77.2		421.9	0.0	665.2	-15.4	21.0	5.6

1. Change from end-of-period to end-of-period. Excludes changes in compensation for the effects of inflation on the principal of inflation-indexed securities.
2. Outright purchases less outright sales (in market and with foreign accounts).
3. Outright purchases less outright sales (in market and with foreign accounts). Includes short-term notes acquired in exchange for maturing bills. Excludes maturity shifts and rollovers of maturing issues, except the rollover of inflation compensation.
4. Includes redemptions (-) of Treasury and agency securities.
5. RPs outstanding less reverse RPs.
6. Original maturity of 13 days or less.
7. Original maturity of 14 to 90 days.

MRA:HAW