Appendix 1: Materials used by Messrs. Wilcox, Elmendorf, and Reinhart

RESTRICTED CONTROLLED (FR) CLASS I (FOMC)

Material for Board Staff Presentation on:

Considerations Pertaining to the Establishment of a Specific, Numerical, Price-Related Objective for Monetary Policy

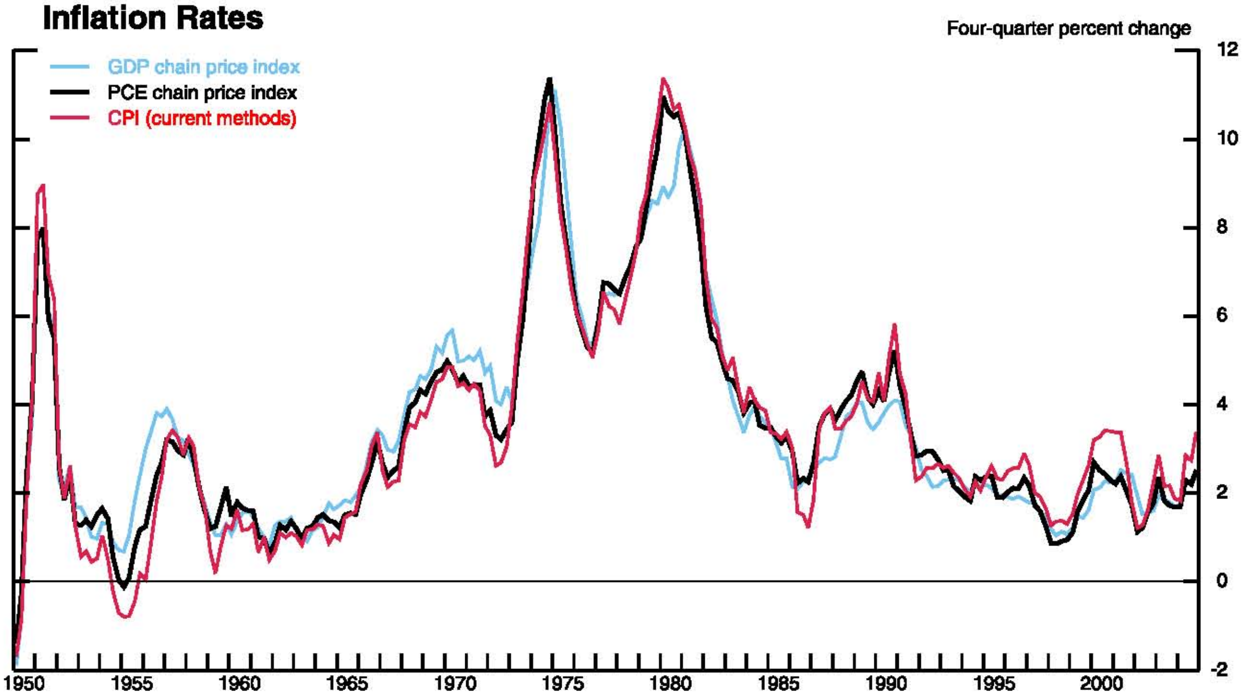
Divisions of Research & Statistics and Monetary Affairs

February 1, 2005

Exhibit 1 2-1-05

A Specific, Numerical, Price-Related Objective for Monetary Policy?

Inflation Rates



Key characteristics of a specific, numerical, price-related objective:

- Numerical rather than qualitative;
- Stated in terms of a particular published index; and
- Either inflation control or price-level control.

A premise of the paper:

- A price objective should be chosen to minimize the costs of deviations from price stability.
- The premise suggests that the objective should be defined with respect to the price index most closely related to such costs.

Exhibit 2 2-1-05

Potential Benefits and Costs of Adopting a Specific Price-Related Objective

Potential Benefits:

- Could help preserve the present commitment to price stability.
- Could better anchor long-run inflation expectations and thereby reduce the volatility of both inflation and real activity.
- Could improve public understanding of monetary policy.
- Could help focus policy debates within the FOMC.

Potential Costs:

- Could mislead the public into believing that emphasis had shifted toward the price objective.
- Could cause the FOMC inadvertently to place more emphasis on the price objective.
- Could diminish the FOMC's credibility when inflation differed from the stated objective.
- Could constrain future actions of the FOMC in an unhelpful manner.

Empirical Evidence:

- Little to no evidence regarding the likely influence on FOMC decision-making or the quality of communications with the public.
- Some hints from foreign experience that specific price objectives have helped anchor long-term inflation expectations.
- Disputed evidence that the reduced volatility of inflation and real output owes to improved conduct of U.S. monetary policy.
- Simulation-based evidence that better-anchored inflation expectations would reduce the volatility of inflation and real output.

Exhibit 3 2-1-05

Operational Issues Related to Specifying a Numerical Price-Related Objective

A checklist for policymakers:

- Which price index?
- The inflation rate or the price level?
- What average rate?
- Point objective or range?

For index, we favor consumer prices on the grounds of:

- Familiarity.
- Quality of measurement.
- Empirical result that inflation rates move together in the long run.

If an inflation objective, at what rate?

- Measurement bias: Nearly 1 percentage point for CPI; about ½ percentage point for PCE prices.
- Rationales for aiming for zero true inflation: Traditional costs of inflation.
- Rationales for aiming for positive true inflation: Downward nominal wage rigidity; zero lower bound on nominal interest rates.

Effect of zero lower bound under an updated Taylor rule:

	Target PCE inflation rate (measured rate, with bias-adjusted rate in parentheses)		
	½ (0)	1 ½ (1)	2 ½ (2)
Fraction of time with funds rate at zero	.16	.10	.06
Standard deviation of output gap*	2.53	2.31	2.21
Standard deviation of unemployment rate*	1.40	1.27	1.22

**measured in percentage points*

Exhibit 4 2-1-05

Accuracy in Achieving an Inflation Objective

Imperfect controllability:

- Inflation is volatile, and monetary policy influences it only indirectly and with a lag.
- The FOMC could not hit a point objective precisely or guarantee a narrow range.

Percent of time that PCE inflation averaged over four quarters could be held within ± 1 percentage point of desired rate:

	Total	Core
Volatility of economic shocks matters:		
1. Drawn from 1968 to 2004 experience	59	64
2. Drawn from 1984 to 2004 experience	68	73
Expectations formation matters:		
3. VAR-based expectations with imperfect credibility	68	73
4. VAR-based expectations with perfect credibility	80	89

Summary:

- The FOMC could likely keep four-quarter total PCE inflation within a ± 1-percentage-point band about ⅔ to ¾ of the time.

Exhibit 5 2-1-05

Governance Issues Related to the Specification of Price Stabilty

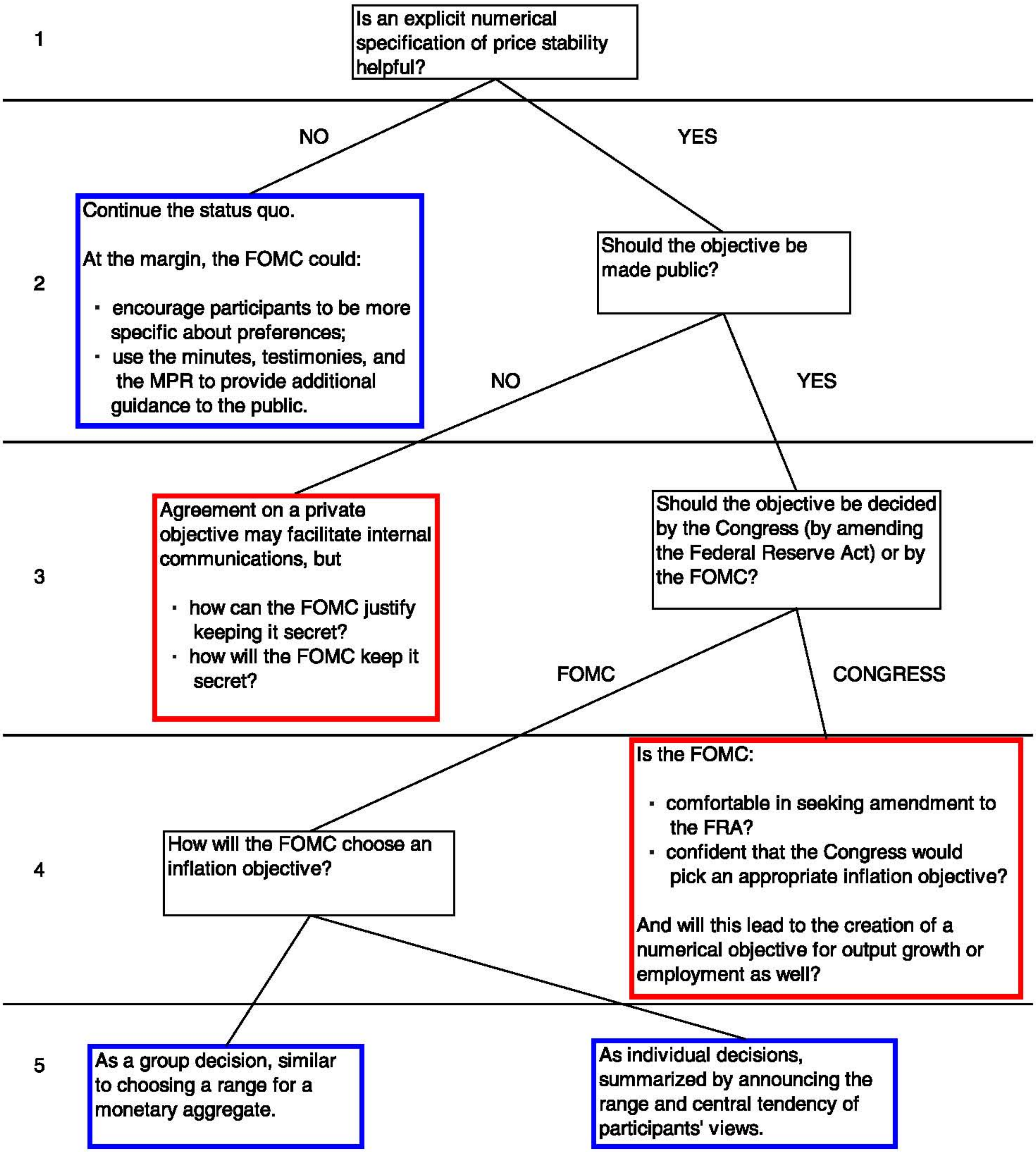


Exhibit 6 2-1-05

Key Questions for Today's Discussion

How do you define price stability?

- Is it known by inference about behavior of by a numerical specification?
- If the latter,
    - What price index do you prefer?
    - Should the objective be stated in terms of a path for the price level or as the rate of inflation?
    - What are the desired point estimates or ranges for the inflation objective?

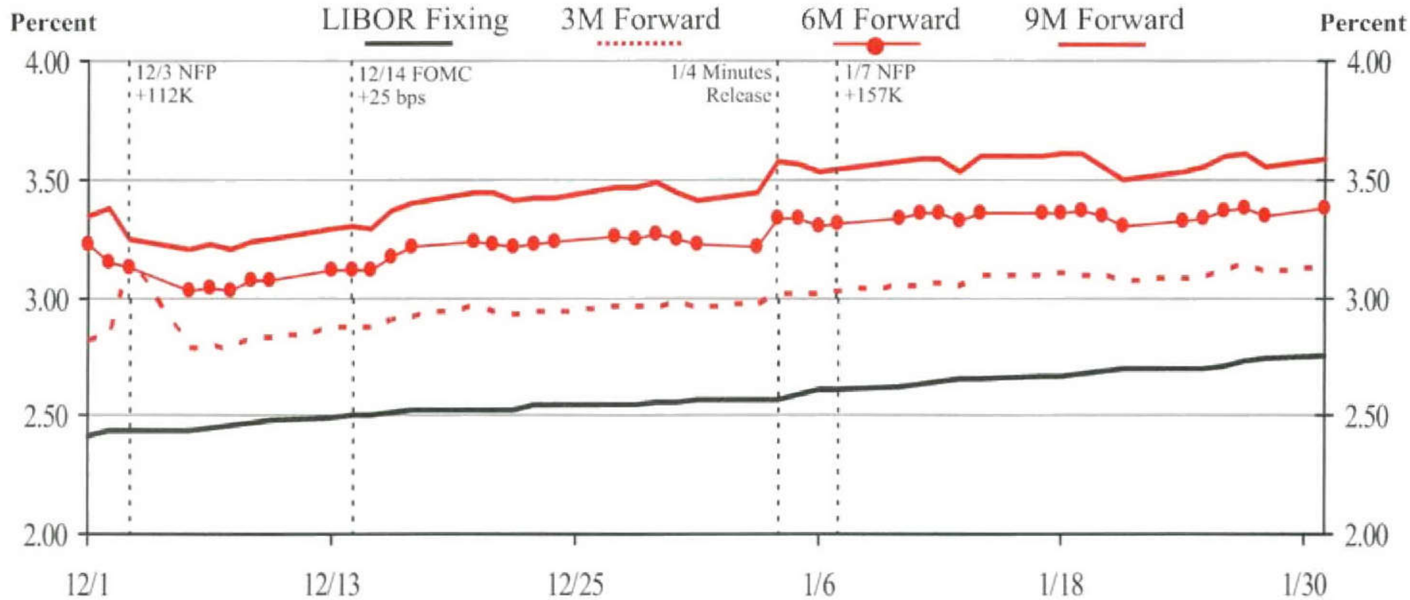
What role should the price objective play in the Committee's policy process?

- Alternative I: Maintain the status quo
    - Perhaps provide more information to the public over time as to your attitudes toward prevailing and prospective inflation
- Alternative II: Vote formally on a numerical inflation goal
- Alternative III: Survey participants as to the appropriate inflation objective

Appendix 2: Materials used by Mr. Kos

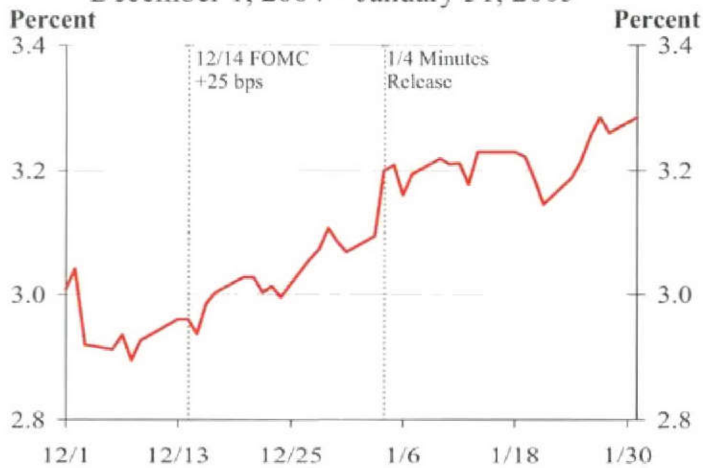
Current U.S. 3-Month Deposit Rates and Rates Implied by Traded Forward Rate Agreements

December 1, 2004 – January 31, 2005



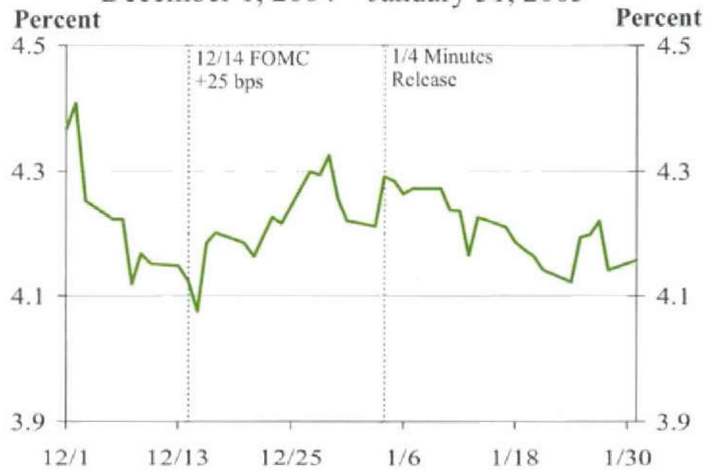
2-Year Treasury Yield

December 1, 2004 – January 31, 2005



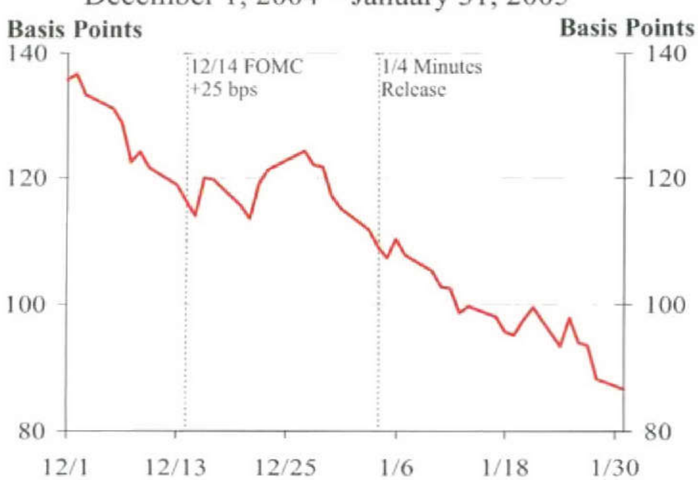
10-Year Treasury Yield

December 1, 2004 – January 31, 2005



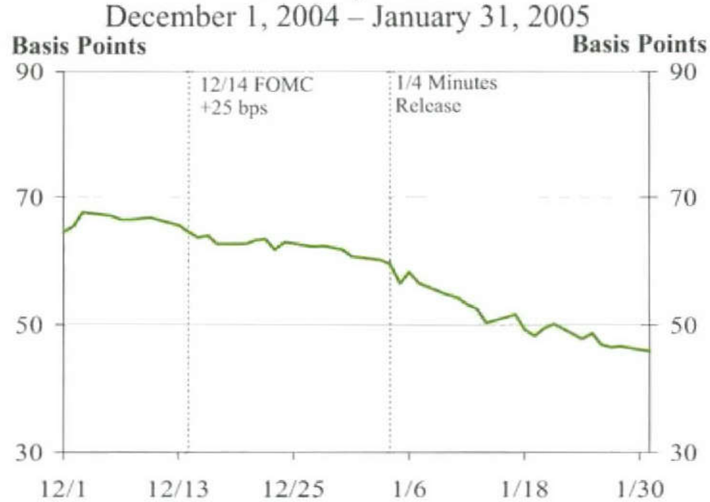
Yield Spread Between 2-and 10-Year Treasury Notes

December 1, 2004 – January 31, 2005

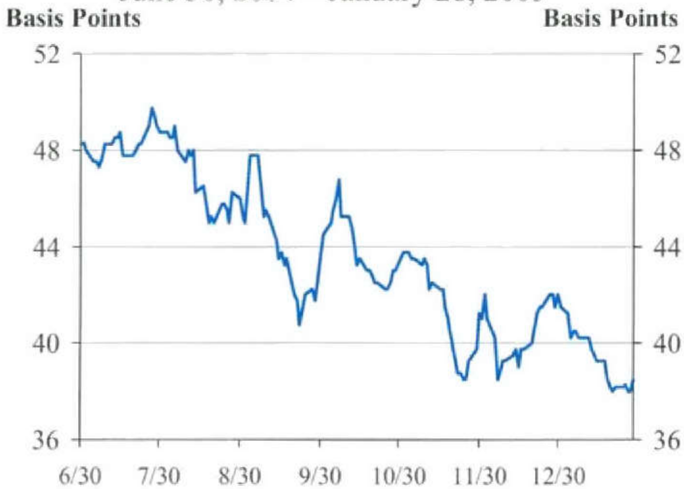


Yield Spread Between 10- and 30-Year Treasury Notes

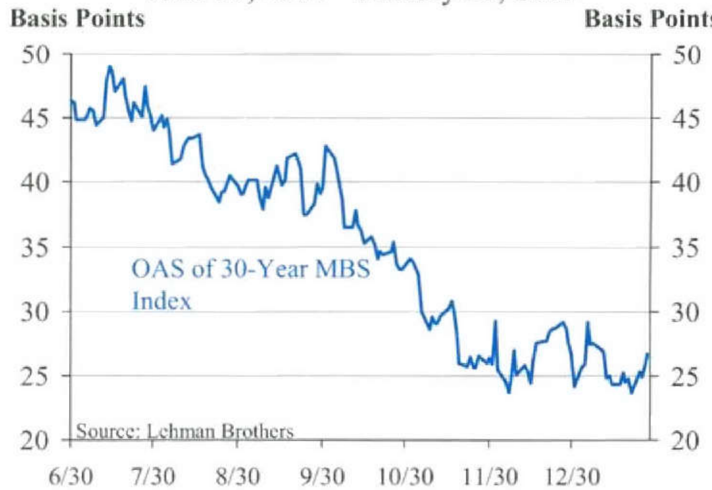
December 1, 2004 – January 31, 2005



10-Year Swap Spread
June 30, 2004 – January 28, 2005



MBS Spreads
June 30, 2004 – January 28, 2005



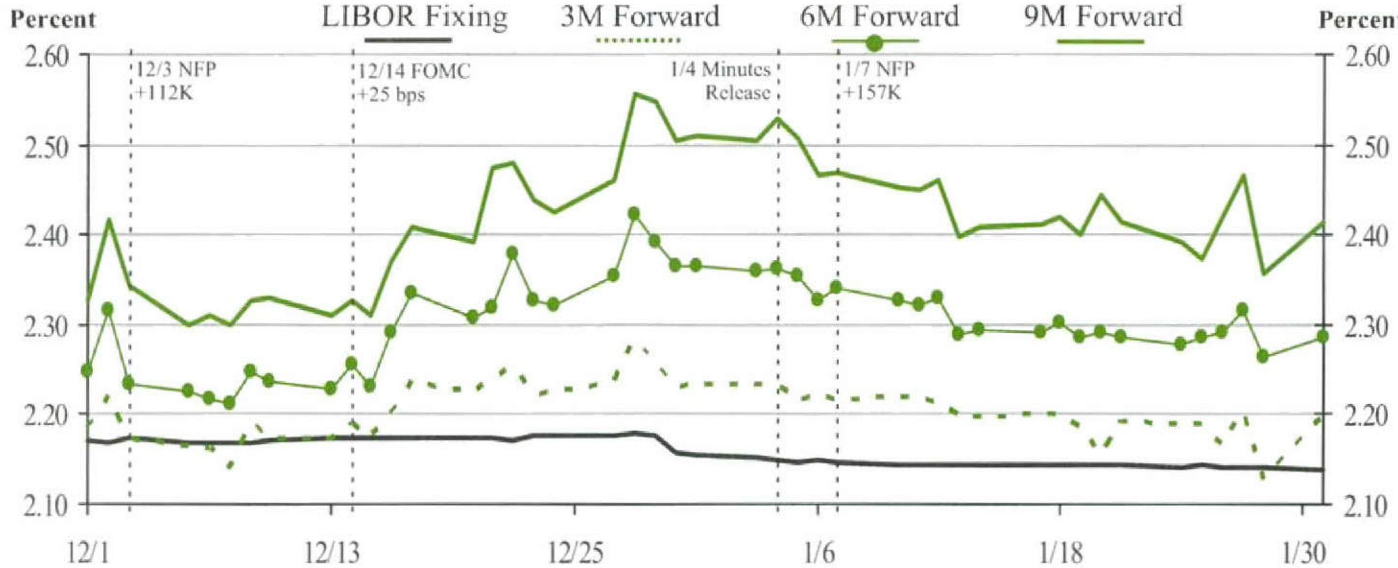
Investment Grade Corporate Debt Spreads
June 30, 2004 – January 28, 2005

High Yield and EMBI+ Spreads
June 30, 2004 – January 28, 2005

Implied Swaption Volatility
May 3, 1999 – January 28, 2005

Euro-Area 3-Month Deposit Rates and Rates Implied by Traded Forward Rate Agreements

December 1, 2004 – January 31, 2005

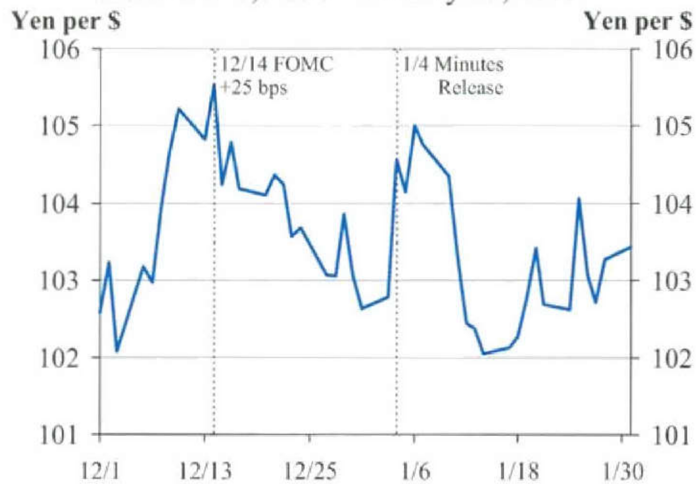


Euro-Dollar Currency Pair

December 1, 2004 – January 31, 2005

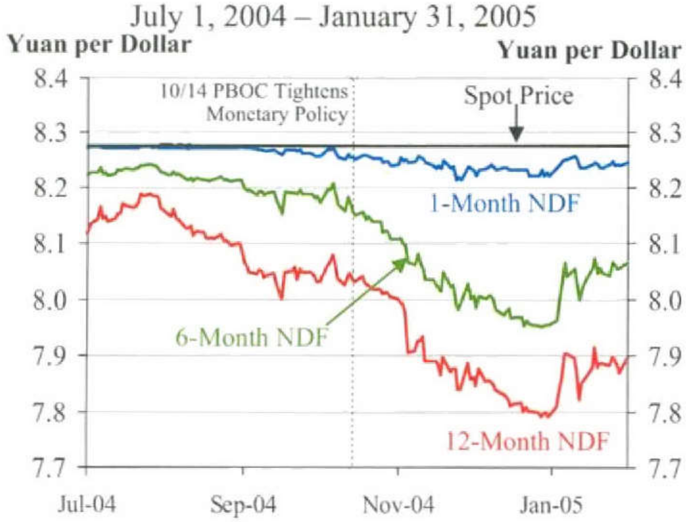
Dollar-Yen Currency Pair

December 1, 2004 – January 31, 2005



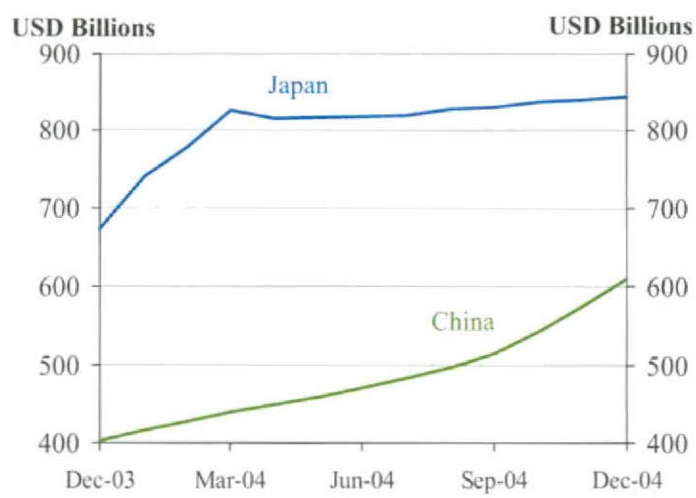
Dollar-Yuan Exchange Value Implied by the NDF Market

July 1, 2004 – January 31, 2005

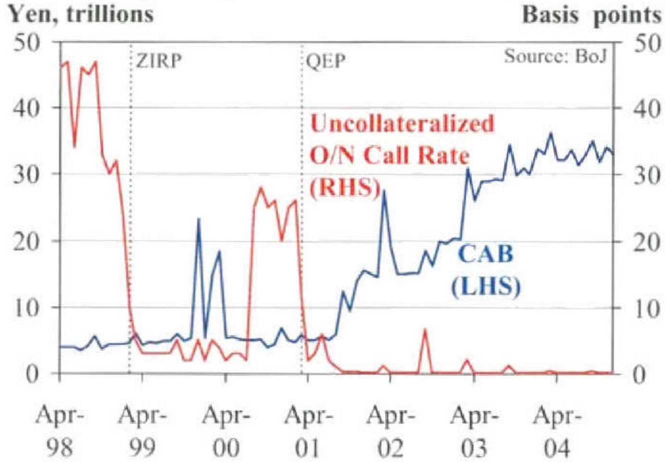


Foreign Exchange Reserves of China & Japan

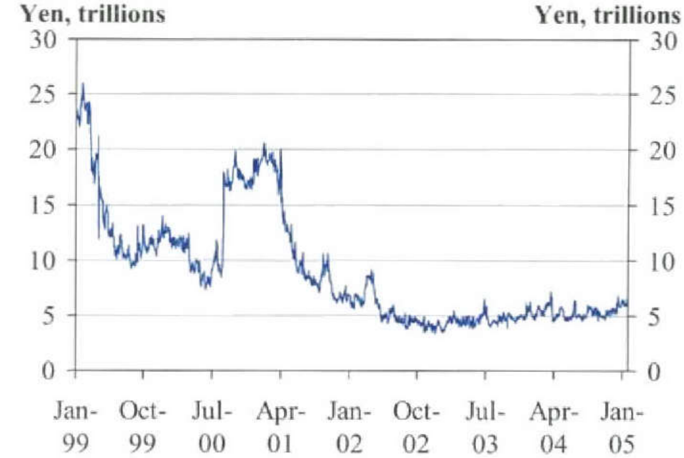
December 31, 2003 – December 31, 2004



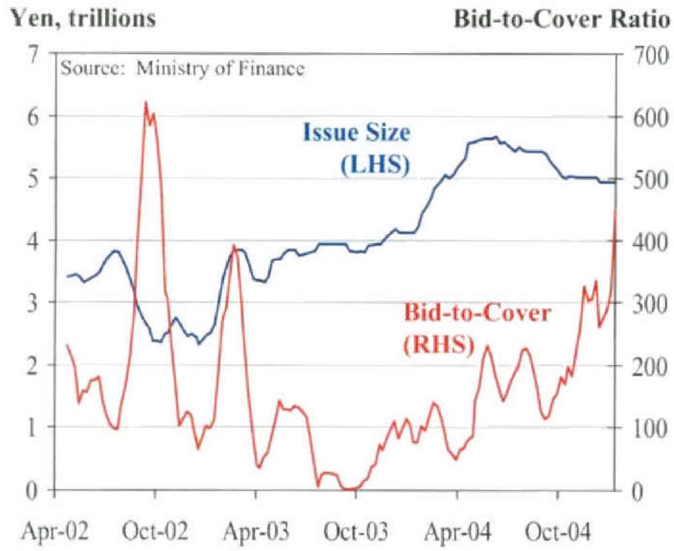
Current Account Balances (CAB) at the Bank of Japan and the Overnight Call Rate
April 30, 1998 – December 31, 2004



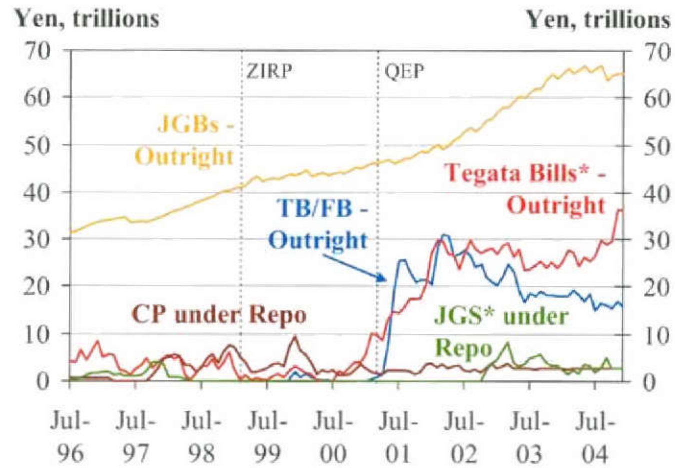
Japanese Call Market Uncollateralized Amount Outstanding
January 4, 1999 – January 28, 2005



1-month Rolling Average of the 3-month Bill Auction History
April 30, 2002 – January 19, 2005

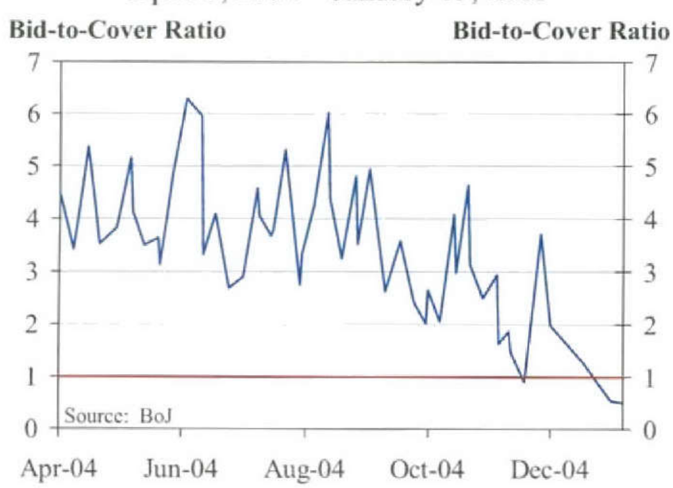


BoJ Securities Holdings
July 31, 1996 – December 31, 2004

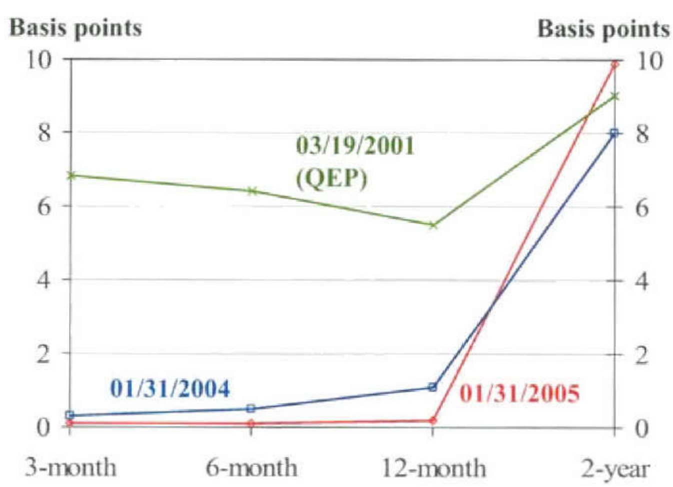


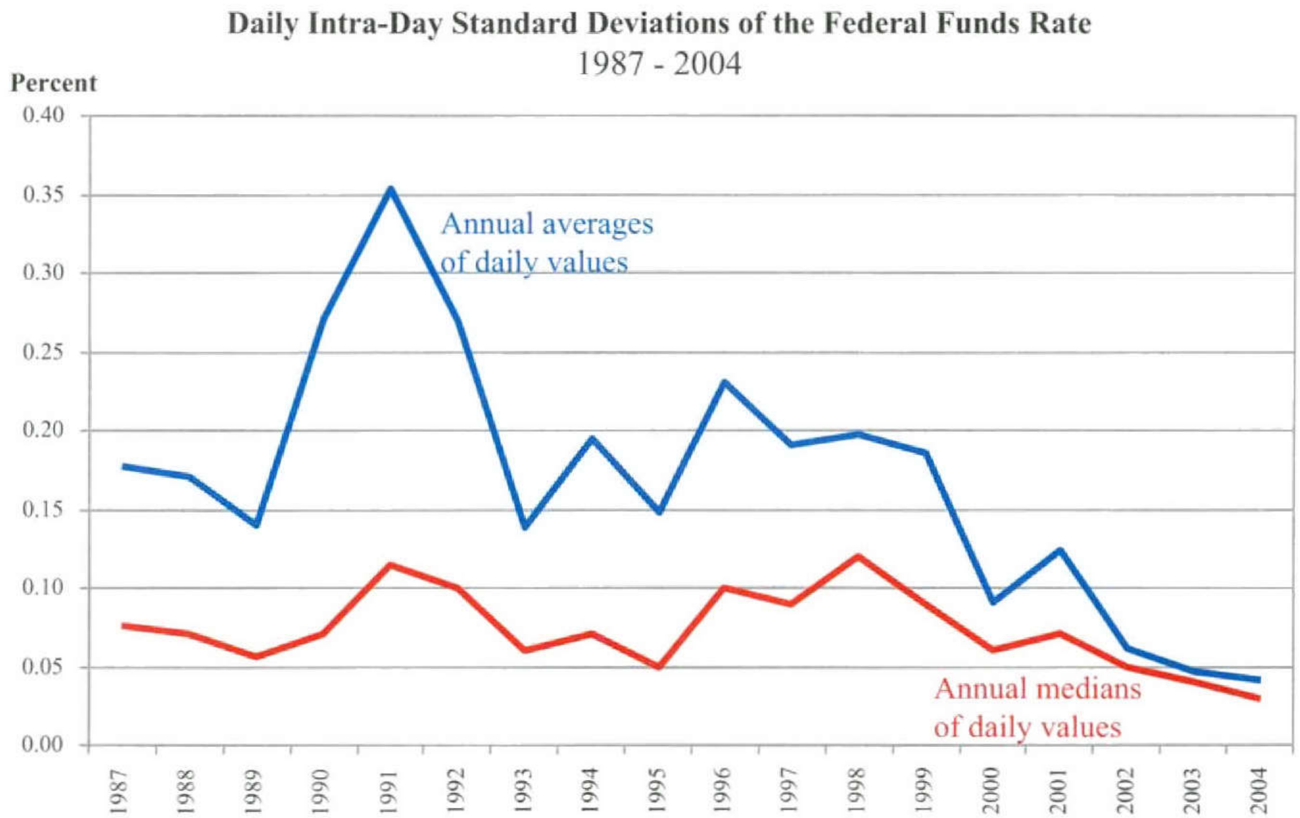
* Source: BoJ
* Tegata Bills from financial institutions incl. bills utilizing corp debt obligations
* Japanese Government Securities (JGS): amount outstanding of JGBs, TBs, and FBs purchased from financial institutions

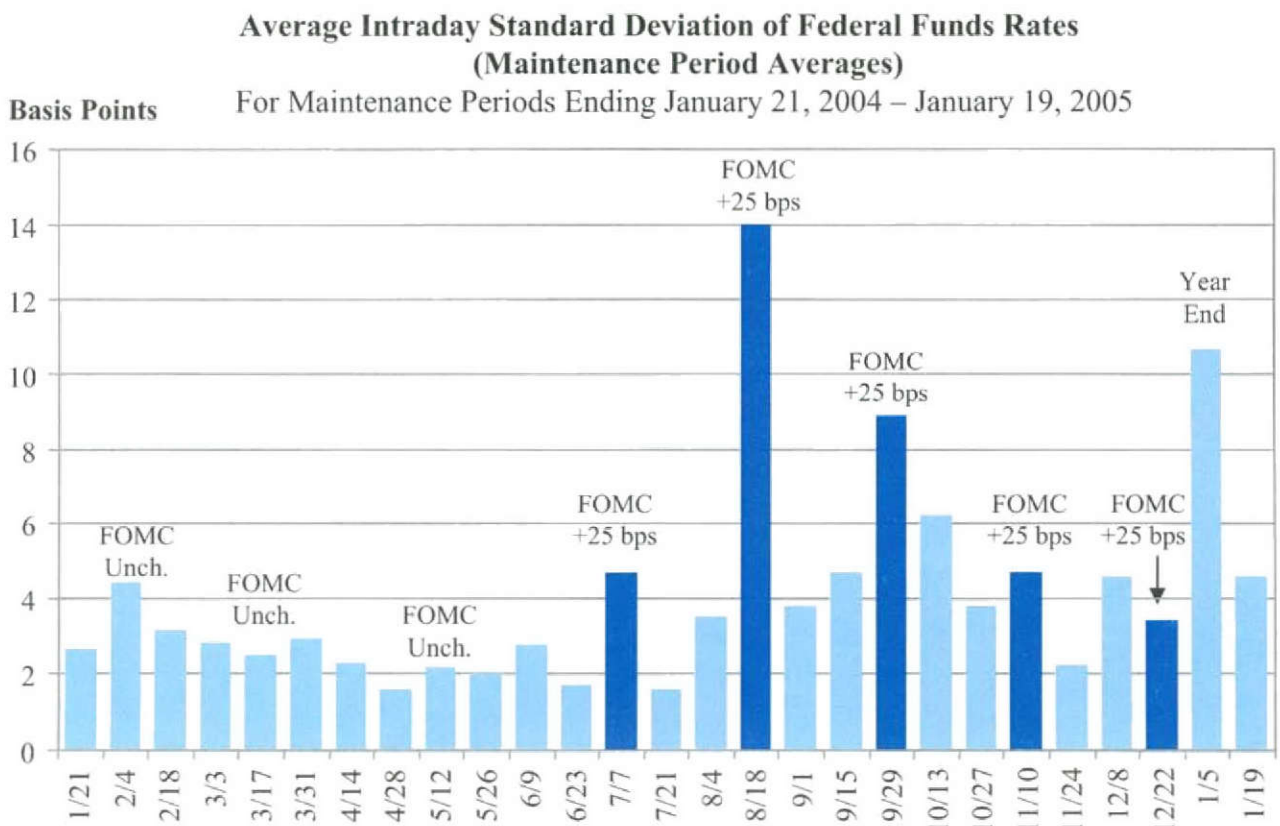
Bid-to-Cover on BoJ Outright Purchases of FB/TBs
April 8, 2004 – January 13, 2005



Changes in the Japanese Government Bill Curve Since the Start of Quantitative Easing




Daily Intra-Day Standard Deviations of the Federal Funds Rate
1987 - 2004
Percent
0.40
0.35
0.30
0.25
0.20
0.15
0.10
0.05
0.00
Annual averages of daily values
Annual medians of daily values
1987
1988
1989
1990
1991
1992
1993
1994
1995
1996
1997
1998
1999
2000
2001
2002
2003
2004


Average Intraday Standard Deviation of Federal Funds Rates
(Maintenance Period Averages)
For Maintenance Periods Ending January 21, 2004 – January 19, 2005
Basis Points
16
14
12
10
8
6
4
2
0
FOMC Unch.
FOMC Unch.
FOMC Unch.
FOMC +25 bps
FOMC +25 bps
FOMC +25 bps
FOMC +25 bps
FOMC +25 bps
Year End
1/21
2/4
2/18
3/3
3/17
3/31
4/14
4/28
5/12
5/26
6/9
6/23
7/7
7/21
8/4
8/18
9/1
9/15
9/29
10/13
10/27
11/10
11/24
12/8
12/22
1/5
1/19

Appendix 3: Materials used by Messrs. Slifman and Struckmeyer, and Ms. Johnson

STRICTLY CONFIDENTIAL (FR) CLASS I-FOMC*

Material for

Staff Presentation on the Economic Outlook

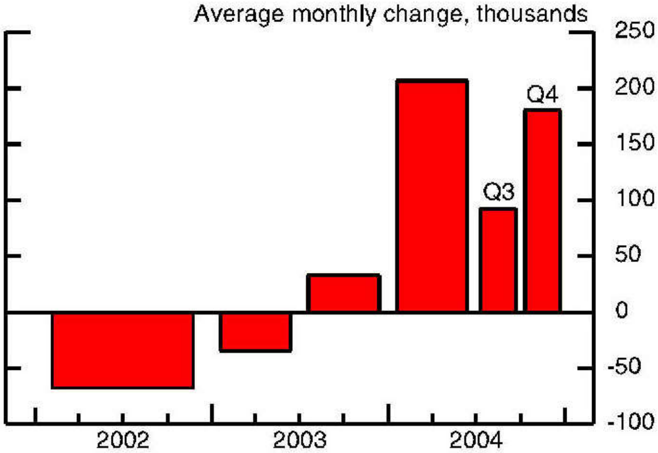
February 2, 2005

*Downgraded to Class II upon release of the February 2005 Monetary Policy Report.

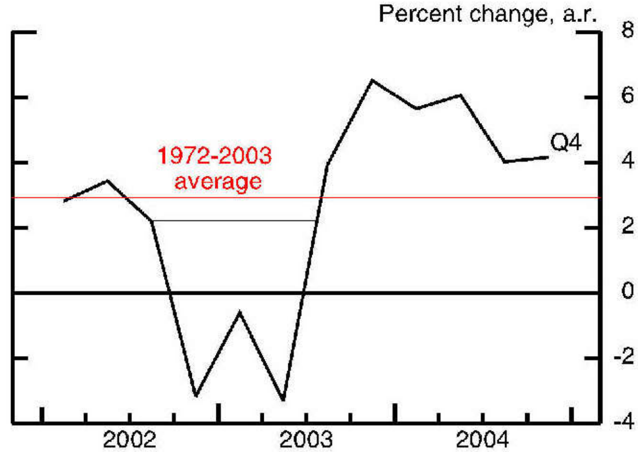
Chart 1

Recent Indicators

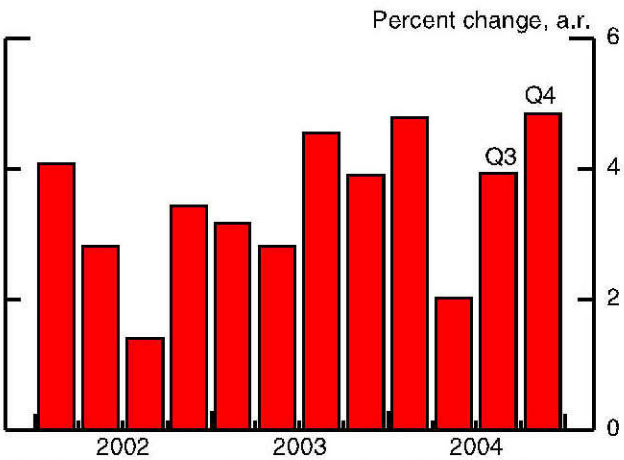
Private Payroll Employment



Manufacturing Industrial Production

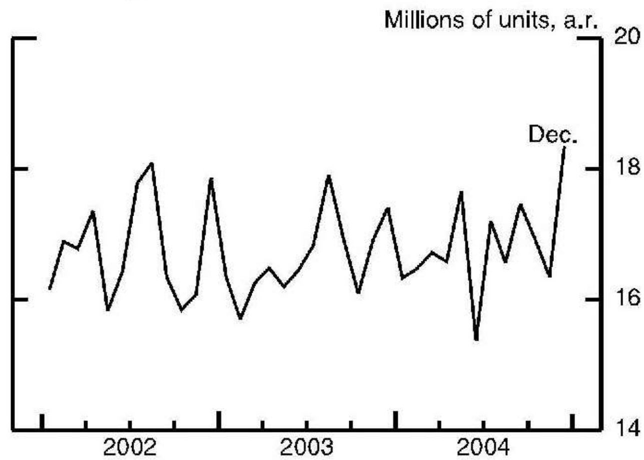


Real PCE exc. Motor Vehicles*

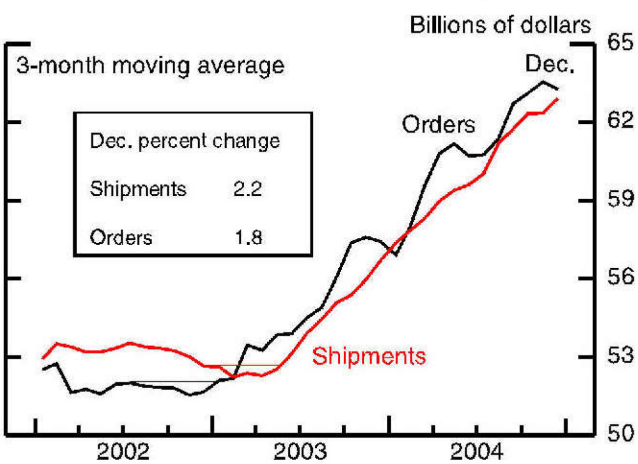


*In this and subsequent charts, NIPA series in 2004:Q4 are from the January Greenbook.

Sales of Light Vehicles



Orders and Shipments of Nondefense Capital Goods*



*Excluding aircraft.

Real GDP

Percent change, a.r.

	2004:Q4	
	Jan. GB	BEA
1. Real GDP	3.5	3.1
Contributions (percentage points)		
2. Final sales	2.7	2.7
3. Inventories	.8	.4

Chart 2

Overview

Key Background Factors

- **Monetary policy:** We assume a continuing withdrawal of monetary accommodation over the next two years. The federal funds rate reaches 3 percent in the fourth quarter of this year and 3-½ percent in the latter part of 2006 – a path quite similar to that implied by futures quotes.
- **Fiscal policy:** FI is expected to be neutral in 2005 and provide only a small positive impetus to GDP growth in 2006.
- **Oil prices:** We continue to be guided in our forecast by futures markets, which expect prices to drift down over the next two years.
- **Dollar:** The foreign exchange value of the dollar is expected to drift down.
- **Stock market:** Prices are assumed to rise 6-½ per cent per year, which would roughly maintain risk-adjusted parity with the yield on long-term bonds.
- **House prices:** The rate of increase is expected to slow from last year's torrid pace.

Real Gross Domestic Product

Percent change, Q4/Q4

	2004	2005	2006
1. GDP	3.8	3.9	3.6
Contribution from:		*Percentage points*	
2. Private consumption and fixed investment	4.1	3.4	3.5
3. Imports	-1.4	-.8	-1.2
4. Exports	.5	.9	.7
5. Government	.2	.6	.5
6. Inventory investment	.4	-.2	.1

Chart 3

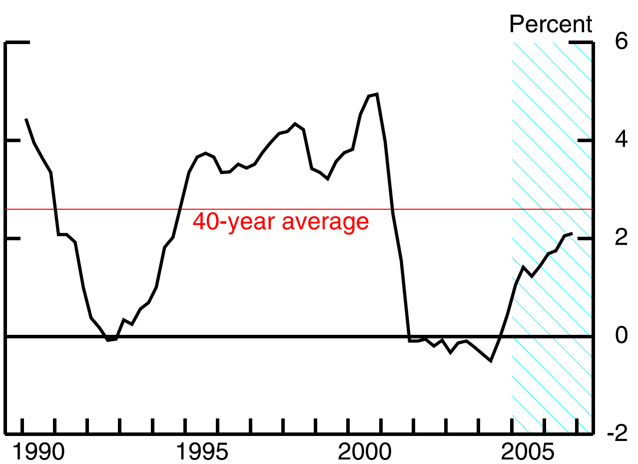
What Keeps Growth Above Potential Through 2006?

- **Monetary policy:** The real fed funds rate is projected to still be below its long-run average over the projection period and on the stimulative side of the short-run measures of r-star shown in the Bluebook.

- **Other financial market conditions:**
  - Nominal long-term rates are projected to be little changed, despite the assumed rise in short-term rates.
  - Corporate balance sheets are quite strong: Cash is abundant and interest expenses relative to cash flow are at low levels.
  - Defaults, delinquencies and risk spreads are quite low.
  - Banks continue to ease lending standards.

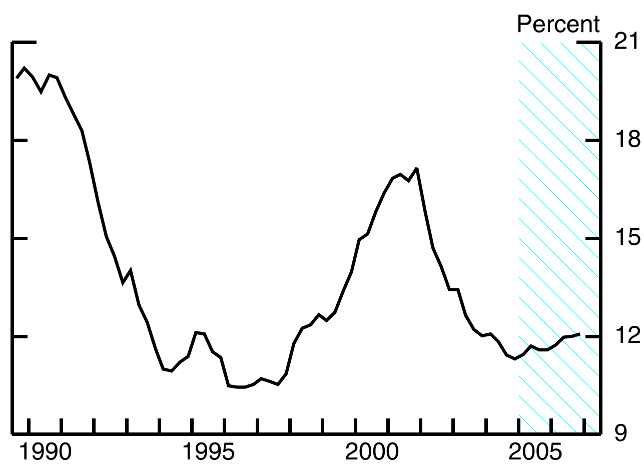
- **Oil prices**: Higher oil prices reduced GDP growth ¾ percentage point in 2004. The negative effects wane to -¼ percentage point in 2005 as oil prices begin to recede; the projected decline in prices boosts GDP growth slightly in 2006.

Real Federal Funds Rate*



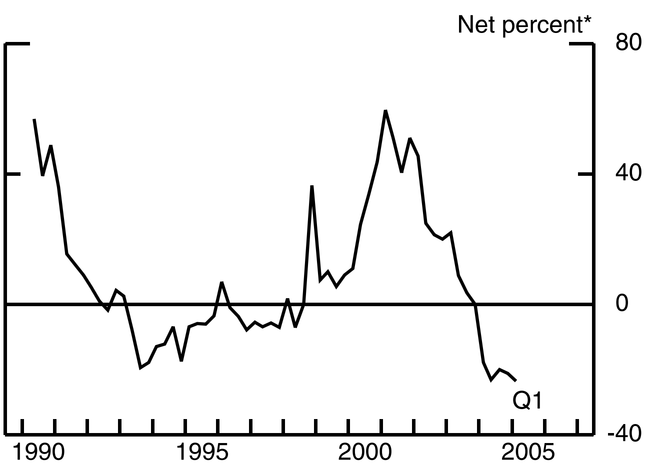
*Nominal federal funds rate less the percent change in the core PCE price index over the previous four quarters.

Interest Expense to Cash Flow



Source: Flow of Funds.

Bank Lending Standards for C&I Loans



*Percentage of banks reporting tighter standards less percentage of banks reporting easier standards. Source: Sr. Loan Officer Survey.

Crude Oil Prices - WTI

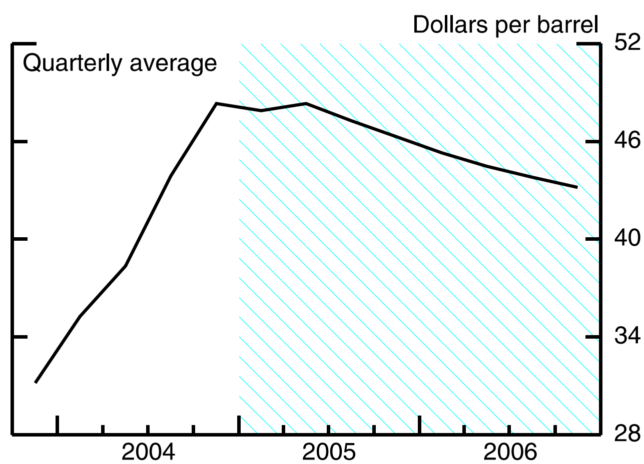
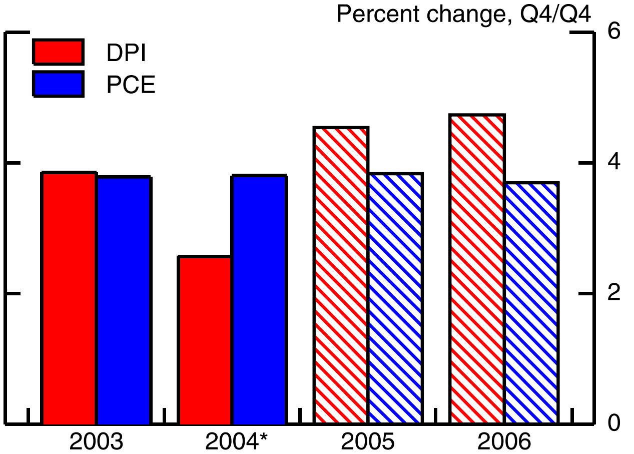


Chart 4

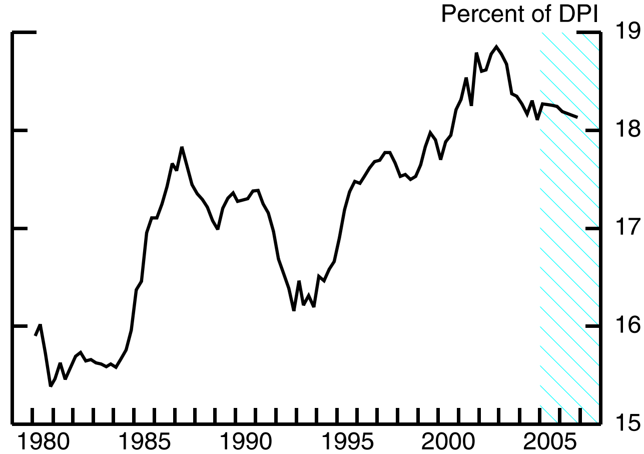
Household Sector

Real PCE and DPI

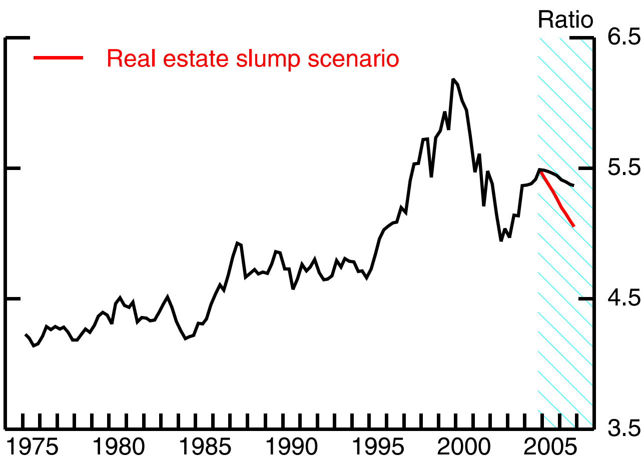


*Excluding Microsoft dividend in 2004:Q4.

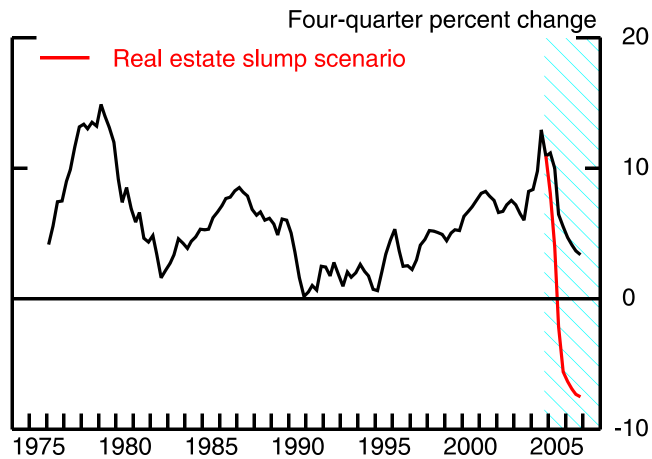
Financial Obligations Ratio



Household Net Worth to DPI

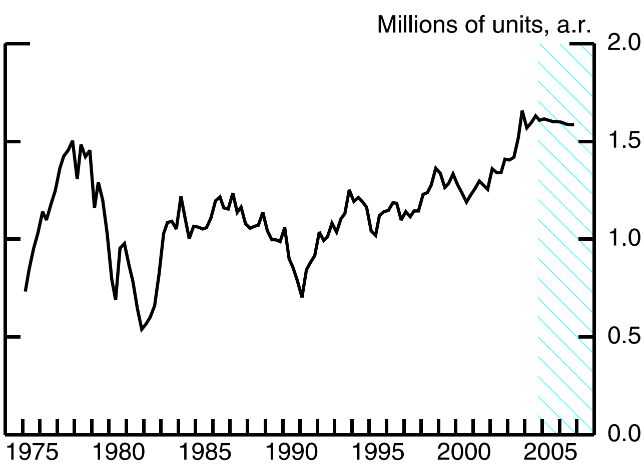


House Prices*

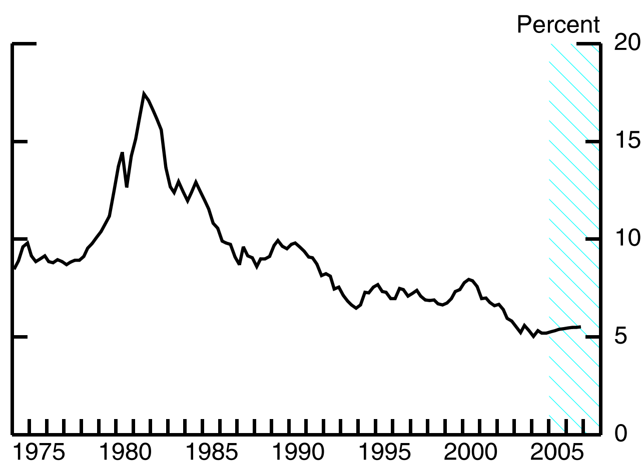


*OFHEO Repeat Sales Price Index.

Single-family Housing Starts



Weighted Average Mortgage Rate*

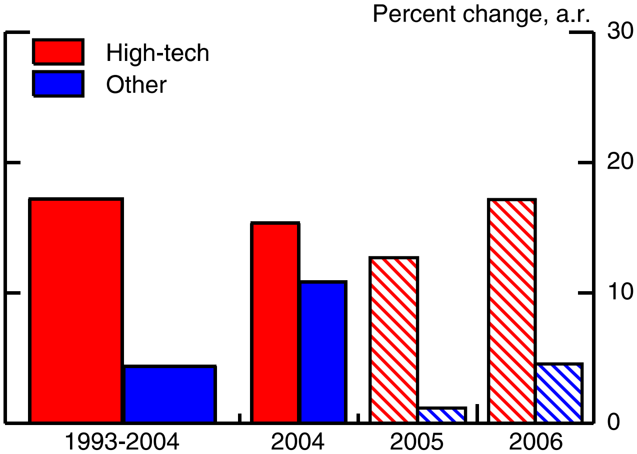


*Weighted average of 30-year fixed-rate mortgage and 1-year adjustable-rate mortgage.

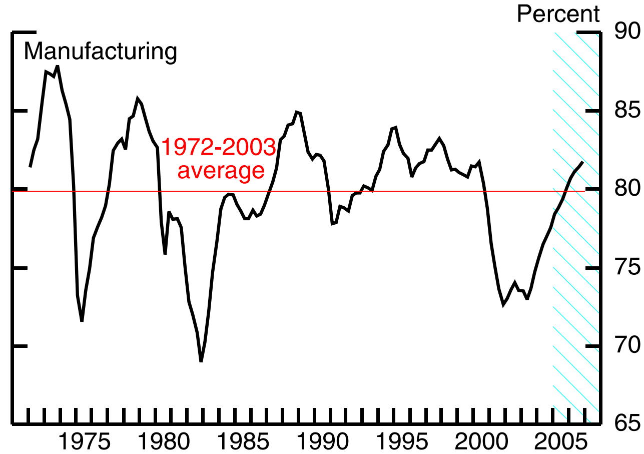
Chart 5

Business Sector

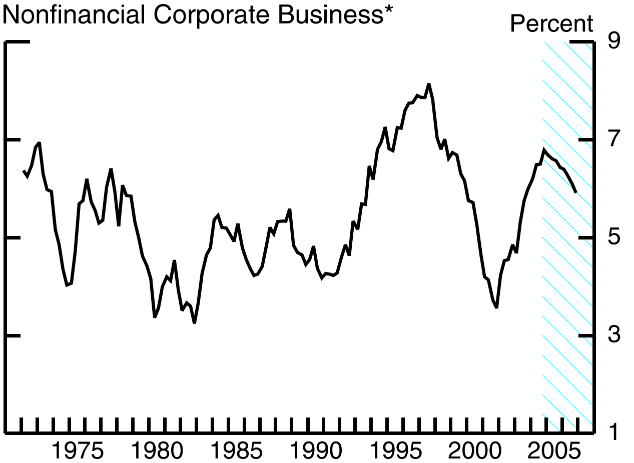
Equipment and Software exc. Transportation



Capacity Utilization Rate



Rate of Return on Capital for Nonfinancial Corporate Business*



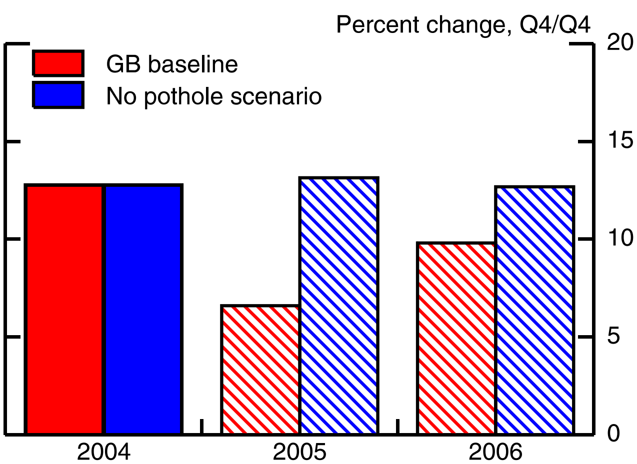
*Nonfinancial corporate profits with IVA and CADJ plus interest, divided by nonfinancial stock of fixed assets.

Reserve Bank Queries on Capital Spending Plans (Percent)

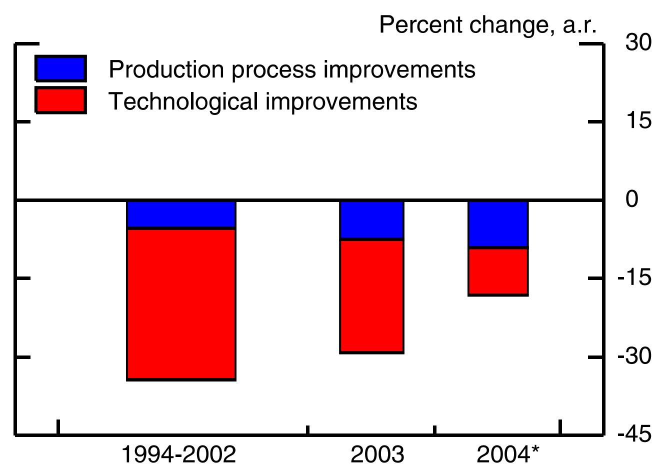
	Jan 2004	Jan 2005
Plan to increase spending over next 6 to 12 months	51.7	47.3
*Reasons cited for increase:**		
Expected sales growth	53.6	47.7
Replace IT equip.	41.1	39.9
Replace other equip.	42.3	41.5

*Percent of respondents planning to increase spending.

Equipment and Software



Price Index for Desktop Computers

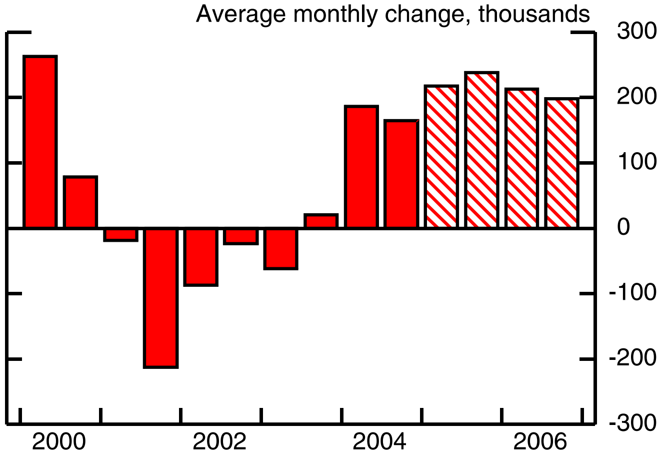


Source: Staff estimates.
*First three quarters (latest data available).

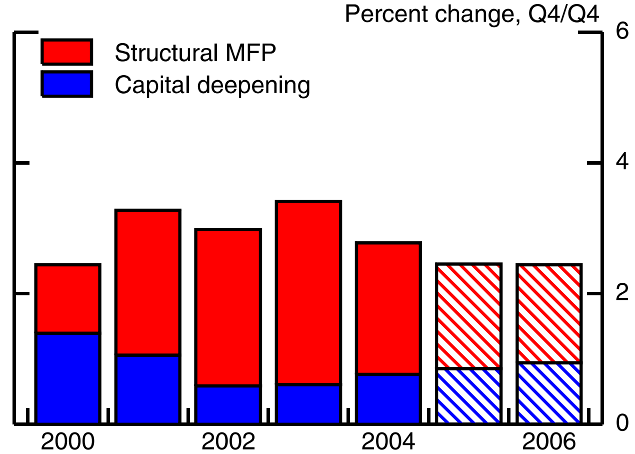
Chart 6

Labor Markets

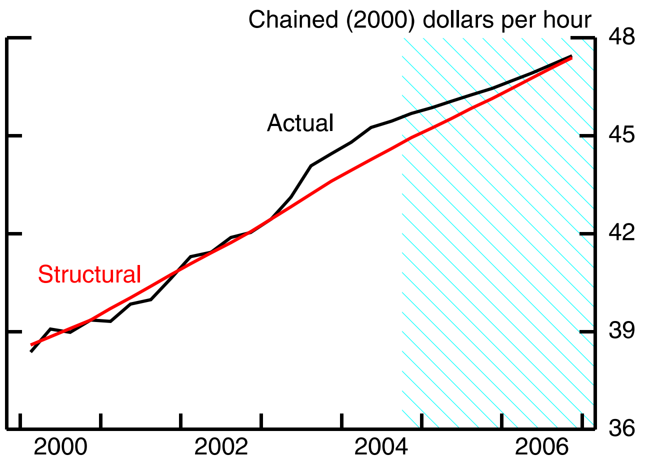
Nonfarm Payroll Employment



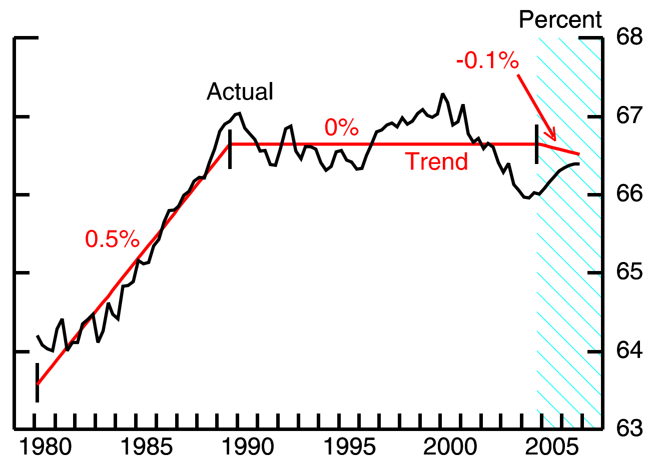
Structural Labor Productivity



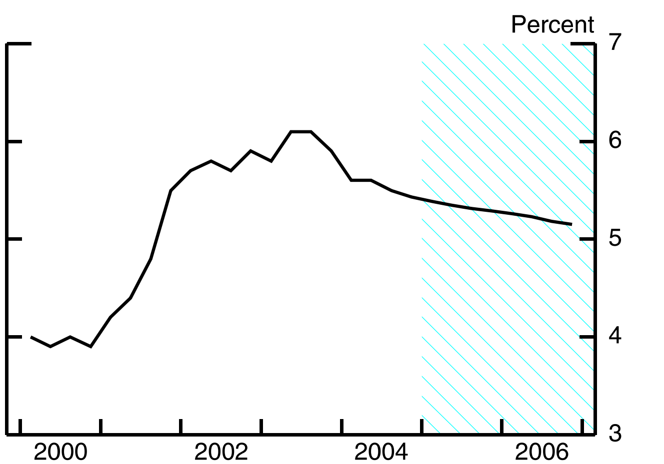
Labor Productivity



Labor Force Participation Rate



Unemployment Rate



Employment-Population Ratio

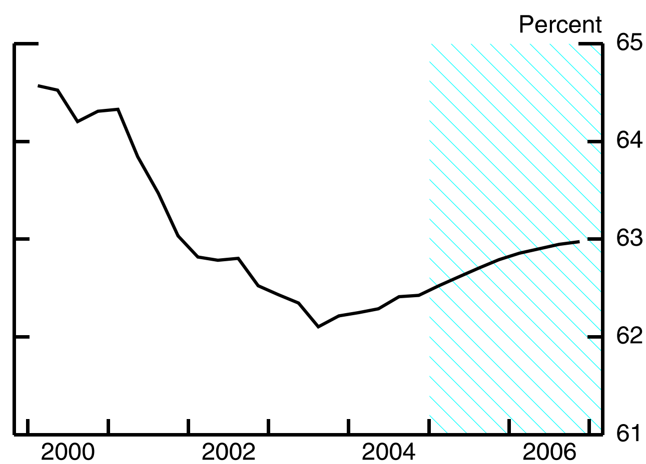
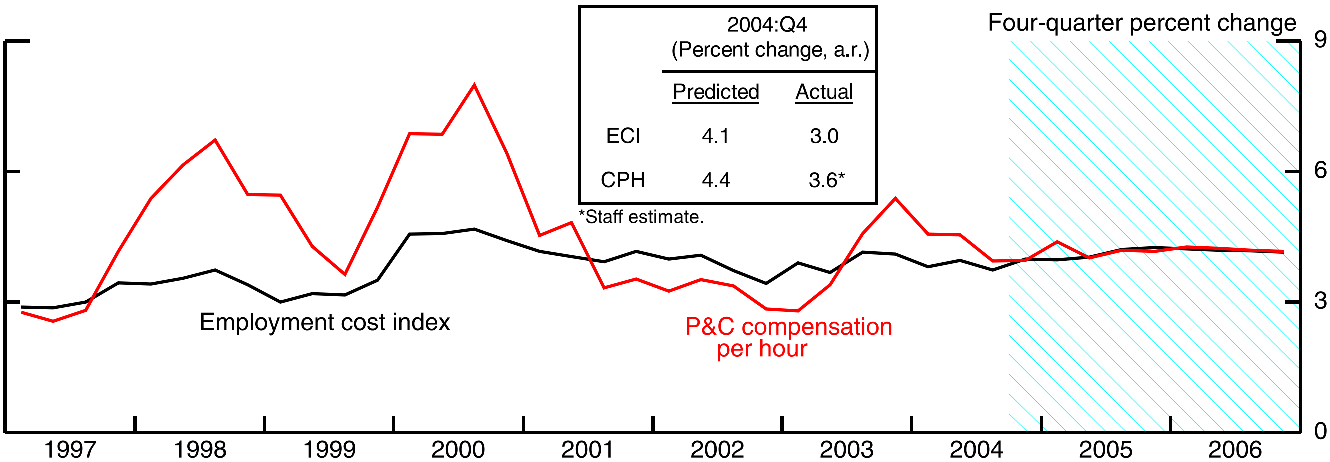


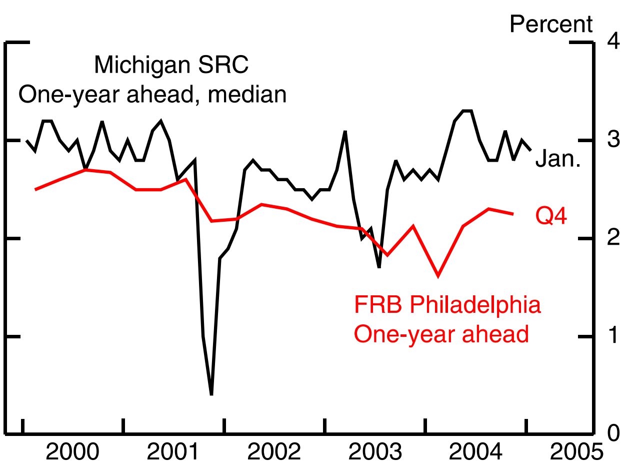
Chart 7

Compensation

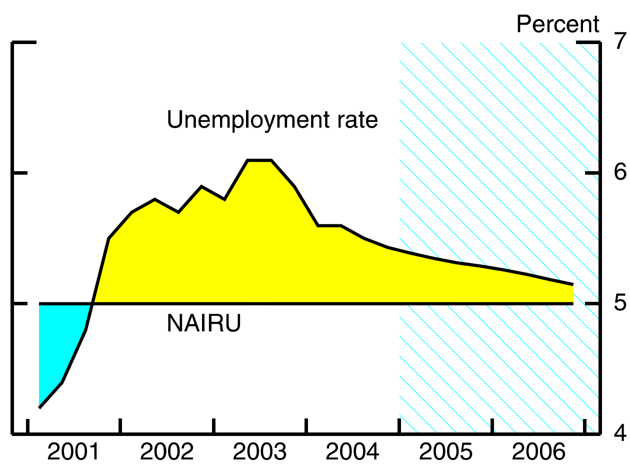
Hourly Labor Compensation



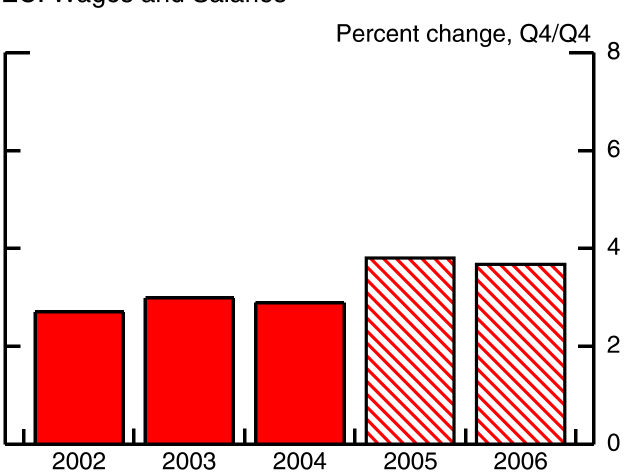
Inflation Expectations



Unemployment Gap



ECI Wages and Salaries



ECI Benefits

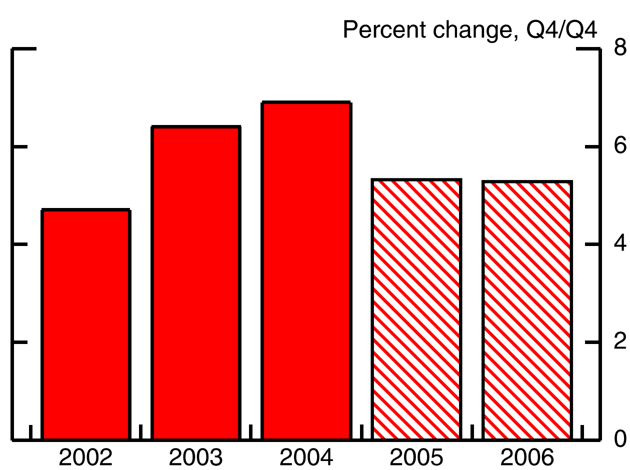
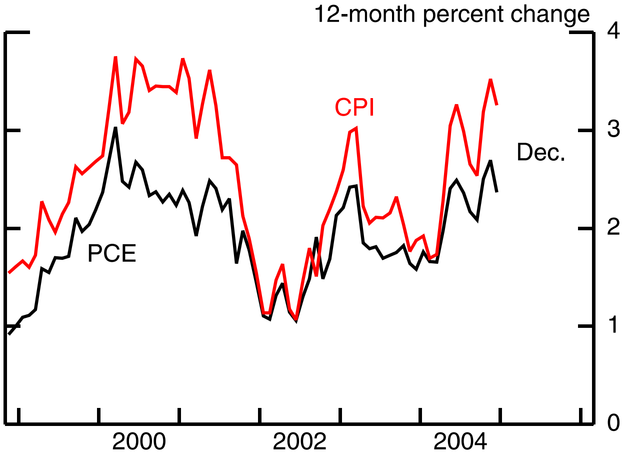


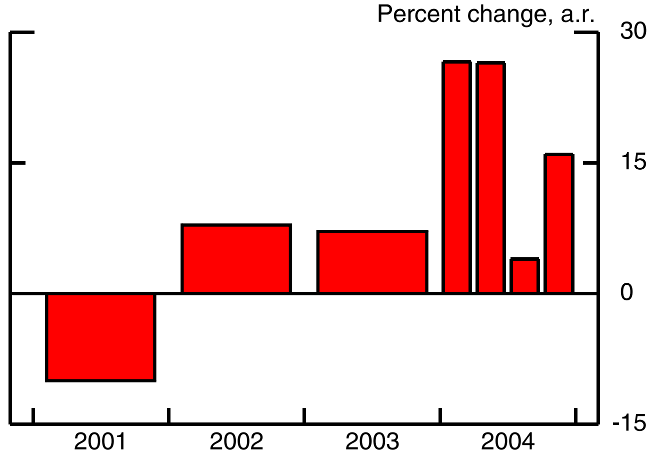
Chart 8

Recent Price Developments

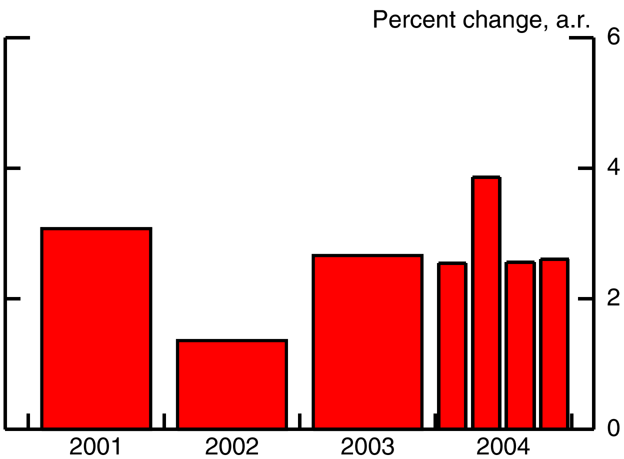
Consumer Prices



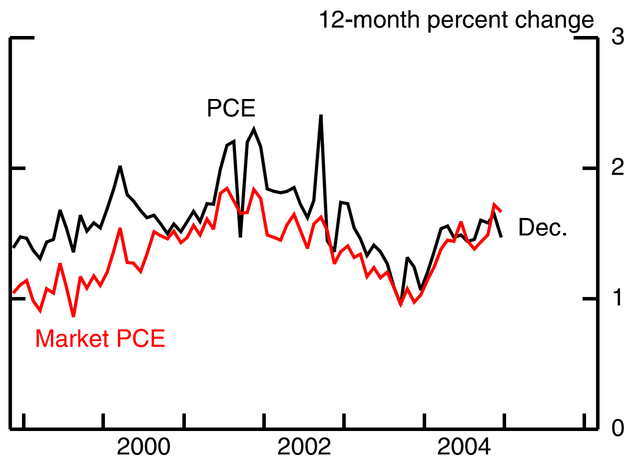
PCE Energy Prices



PCE Food Prices



Core PCE Prices



Core PCE Components

12-month percent change

	2002	2003	2004
Core PCE	1.7	1.1	1.5
Market based	1.4	1.0	1.7
Goods	-1.6	-2.3	0.0
Services	3.0	2.9	2.6
Nonmarket based	3.6	1.3	0.5

PPI-Intermediate Materials less Food and Energy

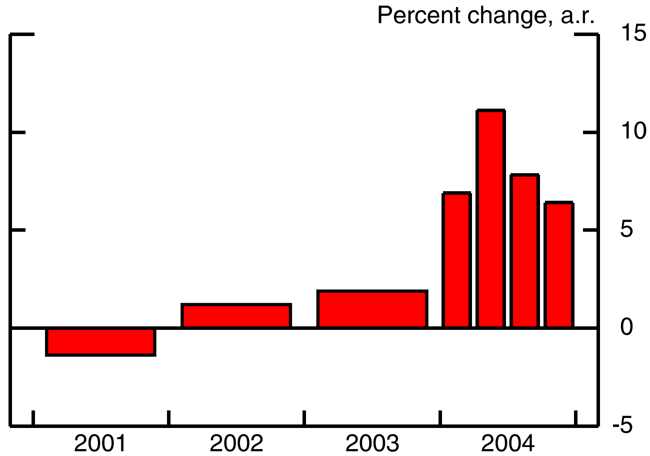
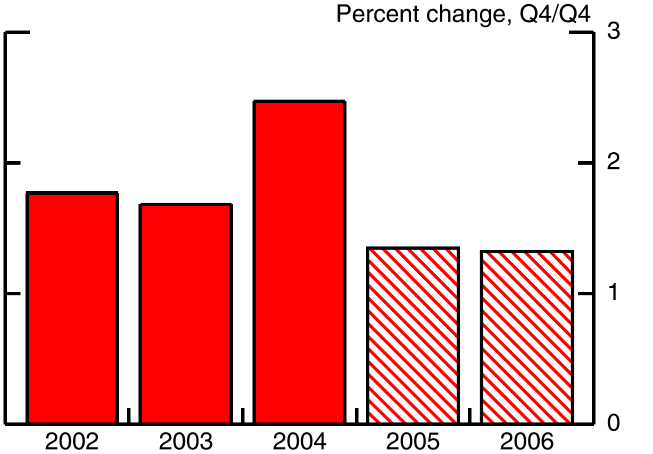


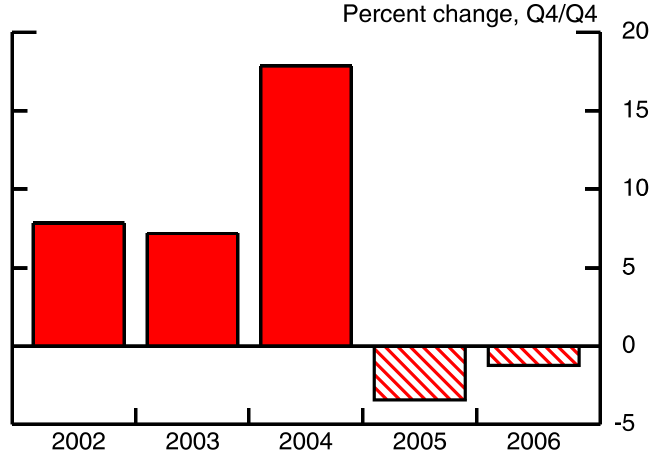
Chart 9

Inflation Outlook

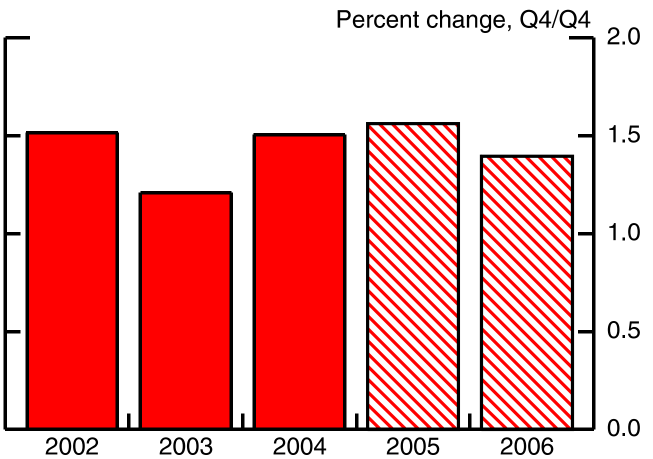
PCE Prices



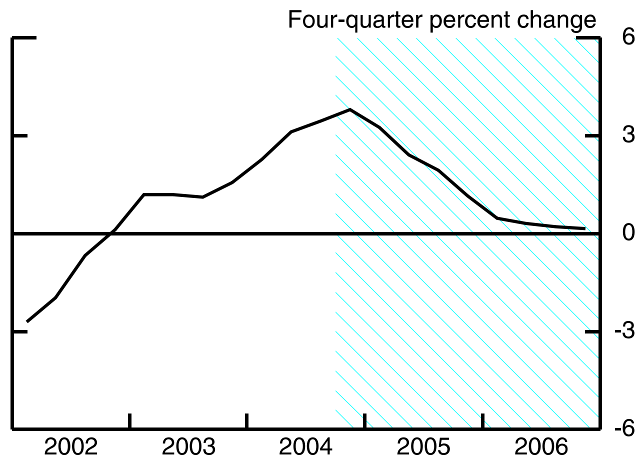
PCE Energy Prices



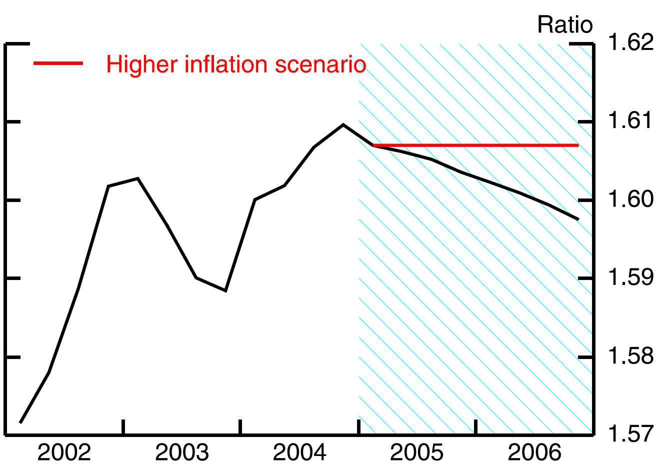
Core PCE Prices



Core Non-fuel Import Prices



Price Markup over Trend Unit Labor Costs



Alternative Projections of Core PCE Prices

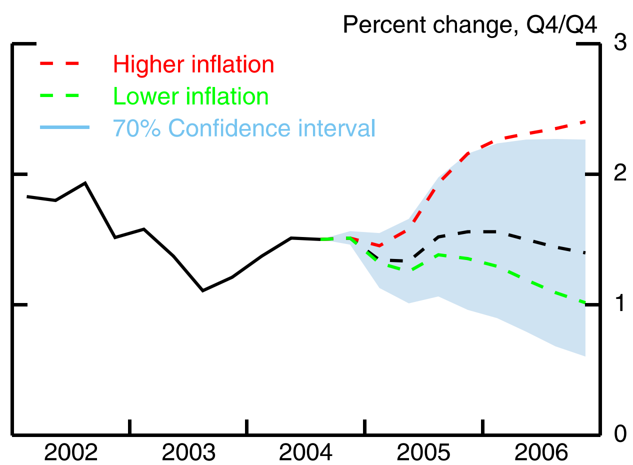
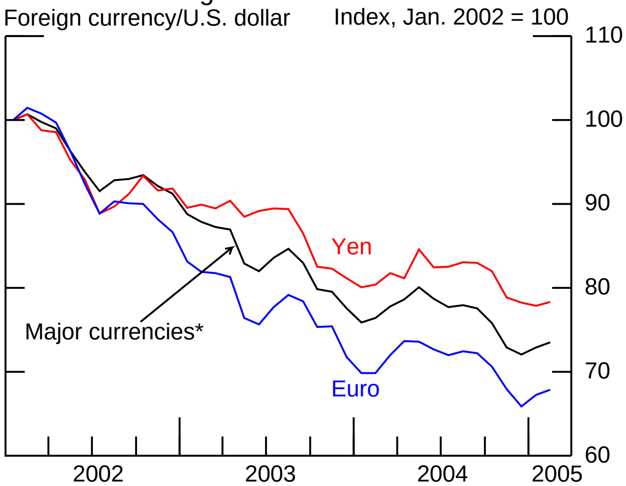


Chart 10

Financial Developments

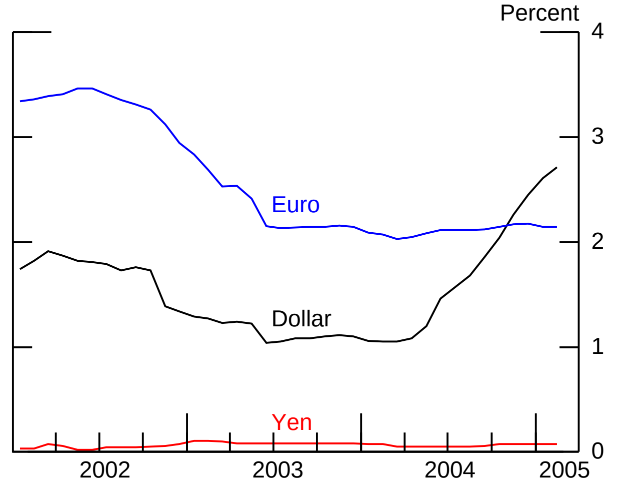
(Monthly data)

Nominal Exchange Rates

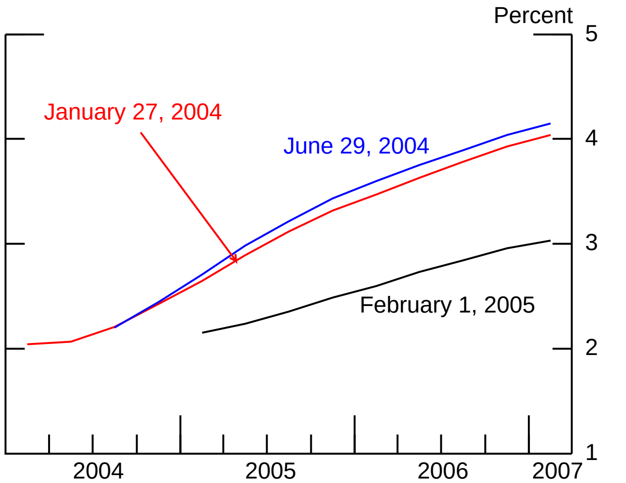


*Trade-weighted average against major currencies.

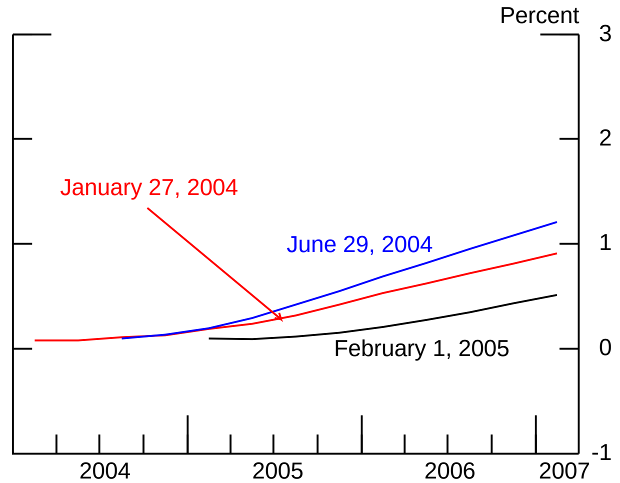
Three-Month Interest Rates



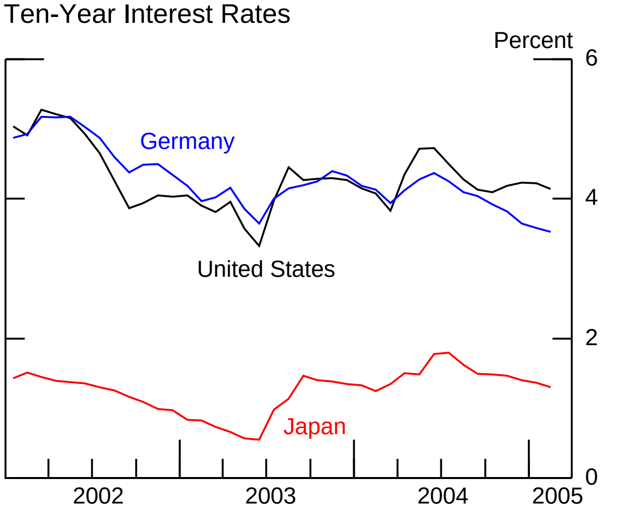
Term Structure of Three-Month Euro Futures



Term Structure of Three-Month Yen Futures



Ten-Year Interest Rates



Broad Stock Price Indexes

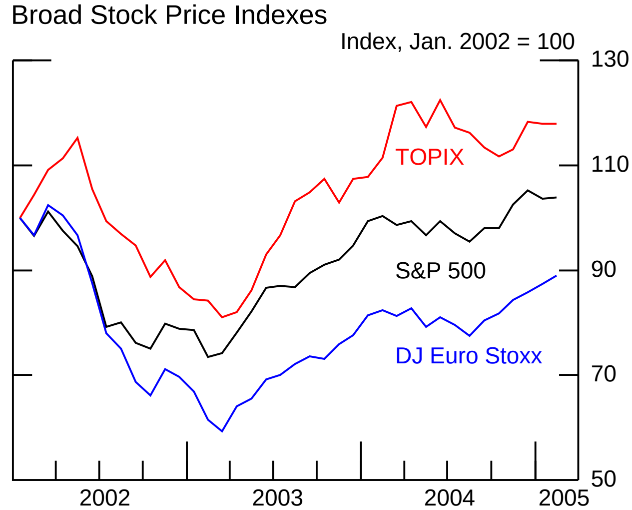


Chart 11

Foreign Outlook

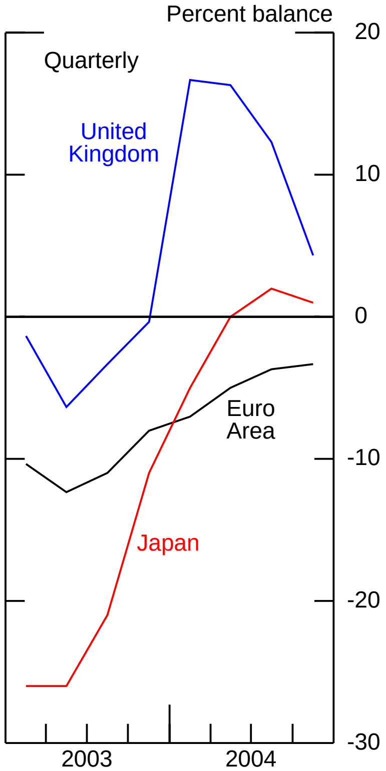
Foreign Real GDP*

Percent change, a.r.**

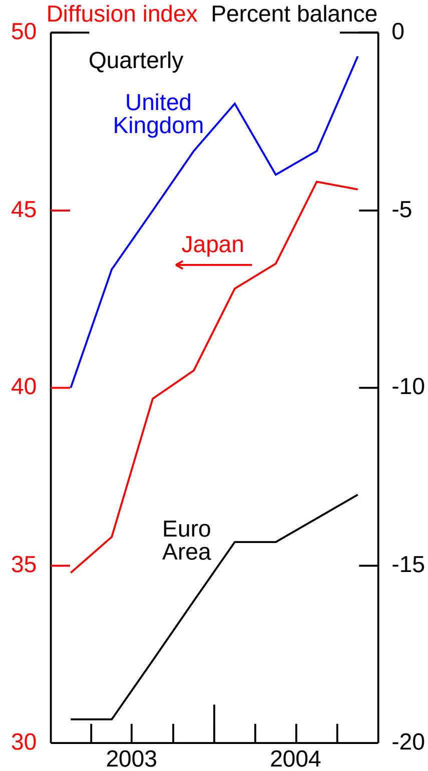
	2004 Q3	2004 Q4	2005 Q1	2005 Q2	2005 H2	2006
1. Total Foreign	**2.6**	**3.1**	**3.0**	**3.3**	**3.4**	**3.3**
2. Industrial Countries *of which:*	**1.9**	**2.0**	**2.1**	**2.4**	**2.5**	**2.4**
3. Japan	0.2	1.0	1.2	1.4	1.6	1.8
4. Euro Area	1.1	1.4	1.4	1.5	1.6	1.6
5. United Kingdom	1.8	3.0	2.1	2.6	2.6	2.2
6. Canada	3.2	2.2	2.6	2.9	3.2	3.0
7. Emerging Economies *of which:*	**3.8**	**4.8**	**4.4**	**4.6**	**4.6**	**4.5**
8. China	10.1	11.2	7.1	7.1	7.1	7.5
9. Emerging Asia exc. China	3.2	3.9	4.2	4.6	4.4	4.2
10. Mexico	2.6	4.0	4.0	4.1	4.2	4.3
11. South America	4.1	3.8	3.8	3.8	3.7	3.6

* Aggregates weighted by shares of U.S. exports.
** Year is Q4/Q4; half year is Q4/Q2; quarters are percent change from previous quarter.

Business Confidence



Consumer Confidence



Exports

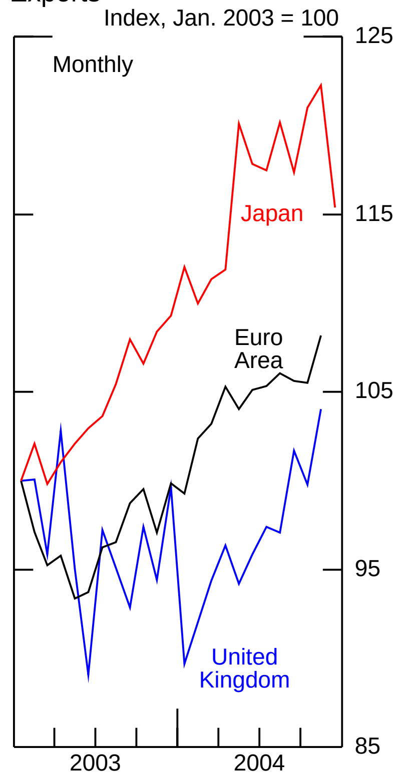
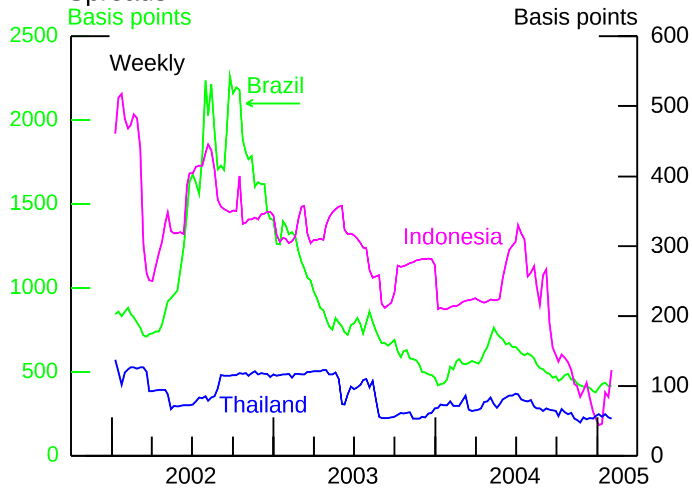


Chart 12

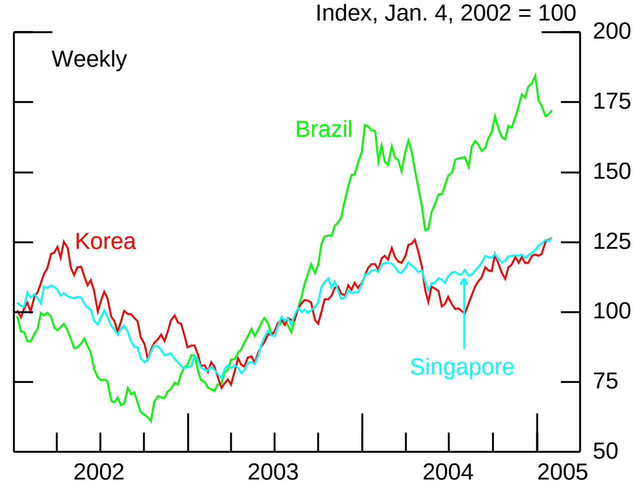
Emerging Market Economies

Spreads*

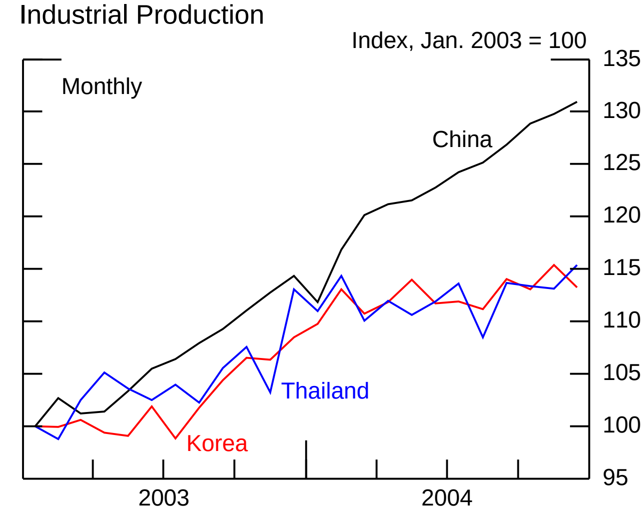


* The series shown are the EMBI+ Brazil sub-index, the EMBI Global Thailand sub-index, and the Indonesian Yankee Bond Spread.

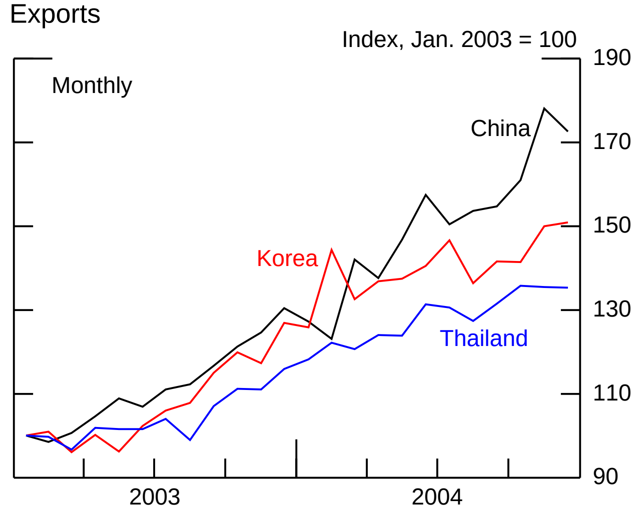
Stock Price Indexes



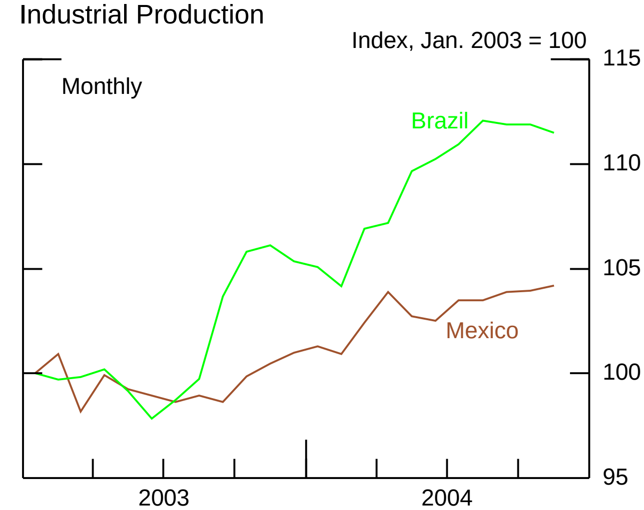
Industrial Production



Exports



Industrial Production



Exports

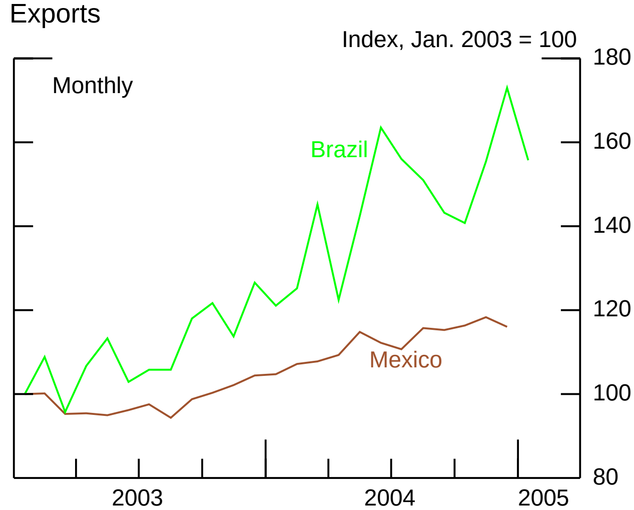


Chart 13

Trade Developments

Trade in Goods and Services

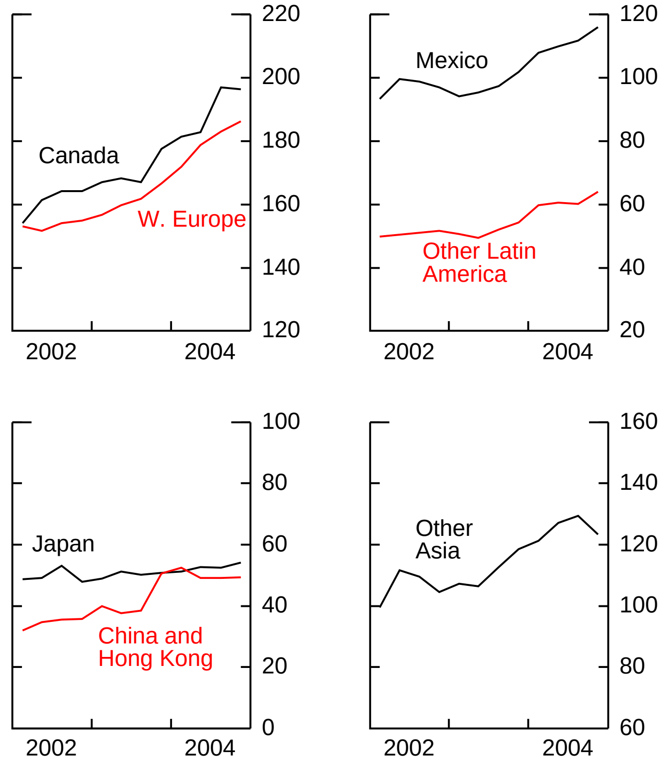
Billions of dollars, a.r.

	Q3	O-N**	Change
1. Balance	-621	-698	-77
Imports:			
2. G & S	1780	1858	78
3. Cons. Gds.	365	386	21
4. Machinery	180	182	2
5. Ind. Sup.*	241	244	3
6. Oil	180	220	40
7. Other	814	826	12
Exports:			
8. G & S	1158	1160	2
9. Machinery	169	165	-4
10. Ind. Sup.	190	195	5
11. Other	799	800	1

* Excludes oil.
** Average of October and November data.

Goods Exports By Region

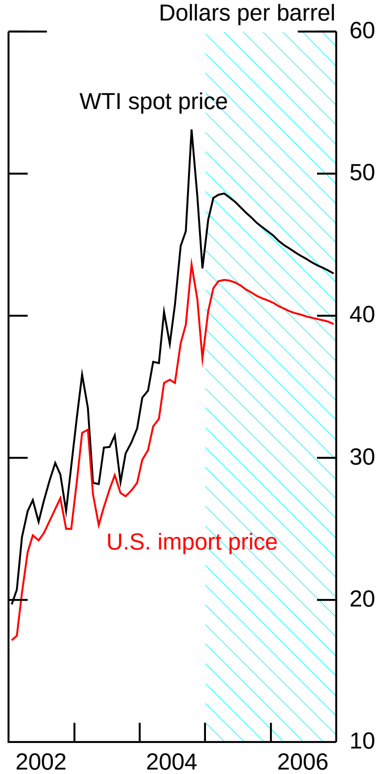
Billions of dollars, s.a.a.r.



Trade Prices

Oil Prices

Dollars per barrel



Core Import Prices

Percent change, a.r.

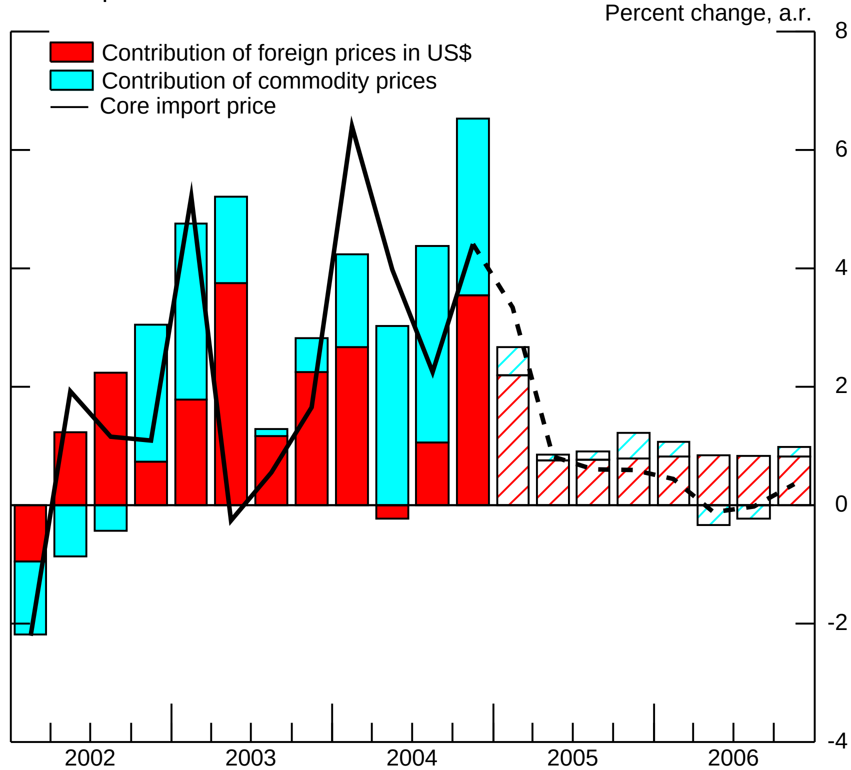


Chart 14

External Sector

Real Export Growth

Percent, Q4/Q4

	2003	2004	2005	2006
1. Goods and services	**6.1**	**4.9**	**8.7**	**7.2**
Percentage point contribution:				
2. Services	1.2	1.4	2.0	1.8
3. Goods	4.9	3.5	6.6	5.4
of which				
4. Core*	3.0	3.5	5.1	3.9

*Excludes computers and semiconductors.

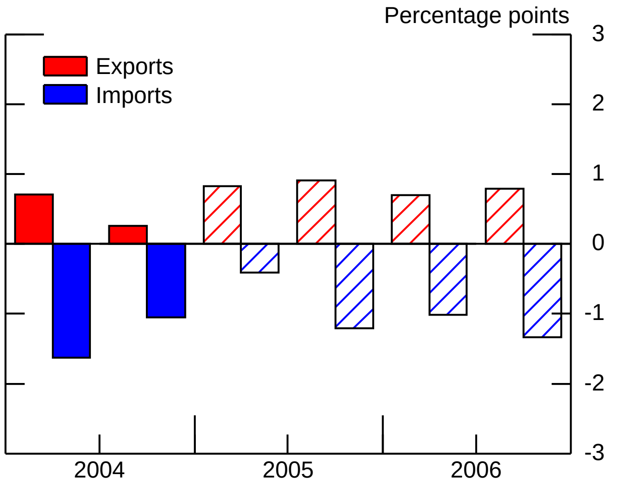
Real Import Growth

Percent, Q4/Q4

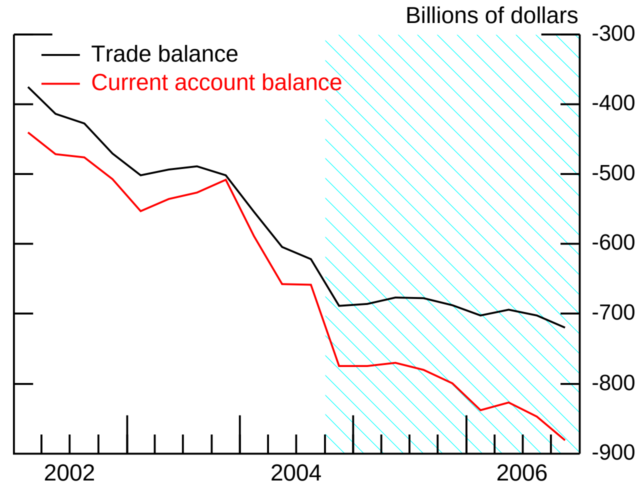
	2003	2004	2005	2006
1. Goods and services	**4.9**	**9.3**	**5.2**	**7.6**
Percentage point contribution:				
2. Services	0.6	0.3	0.6	0.7
3. Goods	4.2	9.0	4.6	6.9
of which				
4. Core*	3.3	6.7	4.5	5.6

*Excludes computers, semiconductors, and oil.

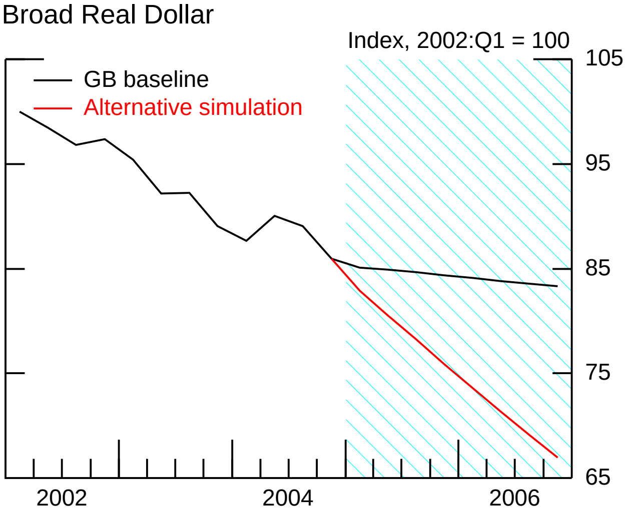
Contributions to U.S. GDP Growth



External Balances



Broad Real Dollar



Simulation Results

Billions of dollars

	2004Q4	2006Q4	Change
Trade balance			
baseline	-689	-720	-31
weaker dollar	-689	-689	0
Current account balance			
baseline	-774	-881	-107
weaker dollar	-774	-863	-89

Chart 15

ECONOMIC PROJECTIONS FOR 2005

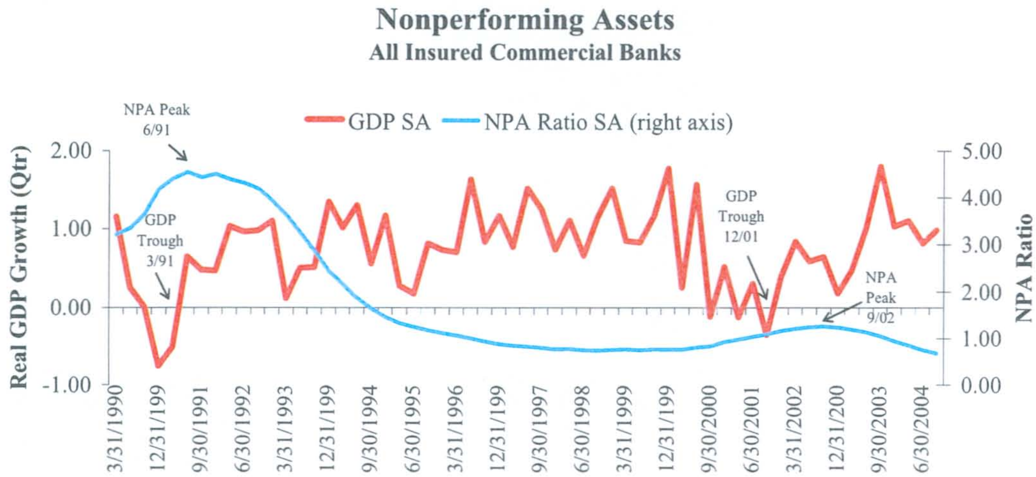
	FOMC Range	FOMC Central Tendency	Staff
	-------------Percentage change, Q4 to Q4------------		
Nominal GDP	5 to 6	5½ to 5¾	5.4
July 2004	(4¾ to 6½)	(5¼ to 6)	(5.0)
Real GDP	3½ to 4	3¾ to 4	3.9
July 2004	(3½ to 4)	(3½ to 4)	(3.6)
Core PCE Prices	1½ to 2	1½ to 1¾	1.6
July 2004	(1½ to 2½)	(1½ to 2)	(1.6)
	--------------Average level, Q4, percent---------------		
Unemployment rate	5 to 5½	5¼	5.3
July 2004	(5 to 5½)	(5 to 5¼)	(5.3)

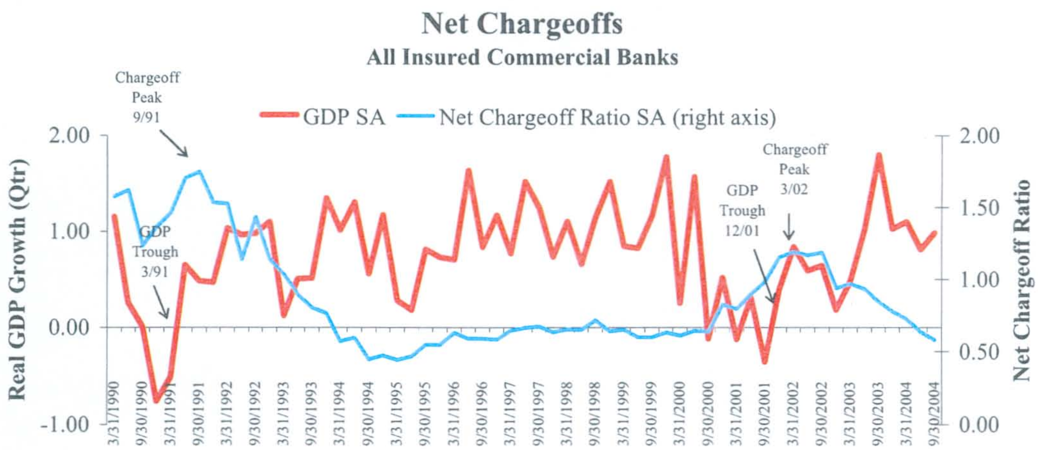
Central tendencies calculated by dropping high and low three from ranges.

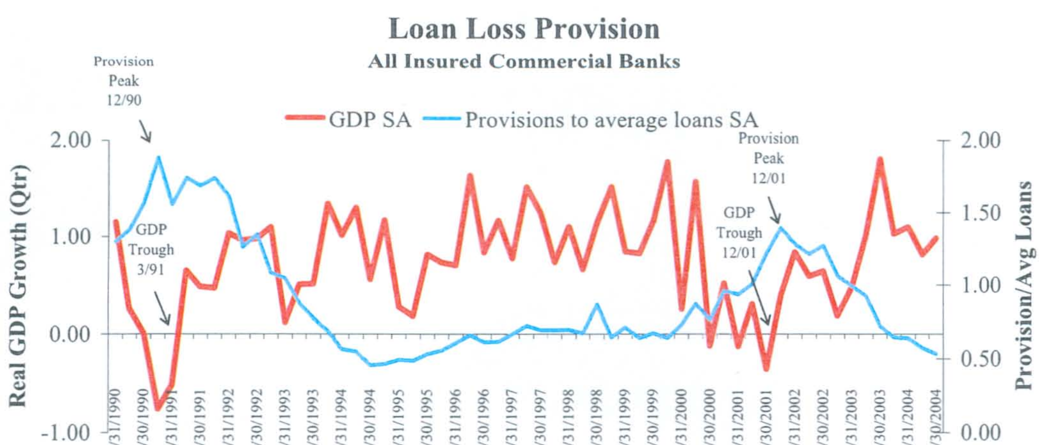
ECONOMIC PROJECTIONS FOR 2006

	FOMC Range	FOMC Central Tendency	Staff
	-------------Percentage change, Q4 to Q4------------		
Nominal GDP	5 to 5¾	5 to 5½	5.3
Real GDP	3¼ to 3¾	3½	3.6
Core PCE Prices	1½ to 2	1½ to 1¾	1.4
	--------------Average level, Q4, percent---------------		
Unemployment rate	5 to 5¼	5 to 5¼	5.1

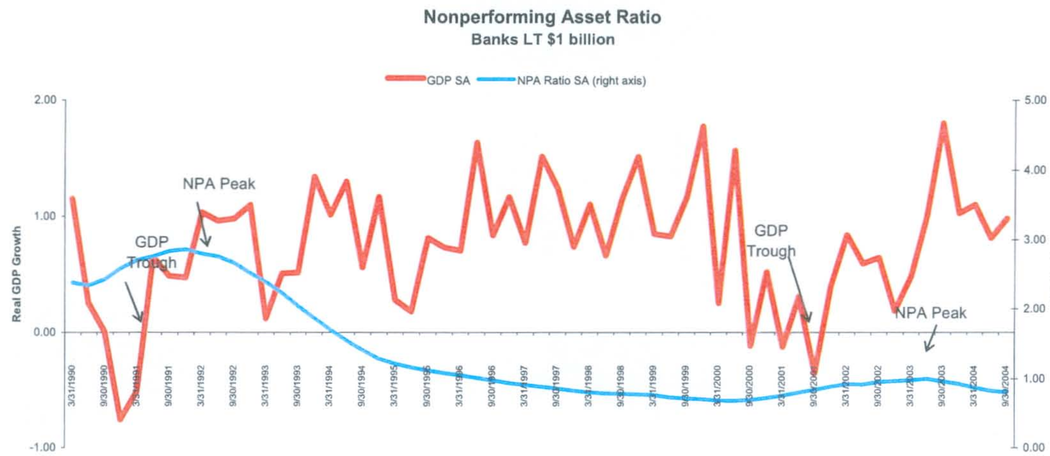
Appendix 4: Materials used by Mr. Olson

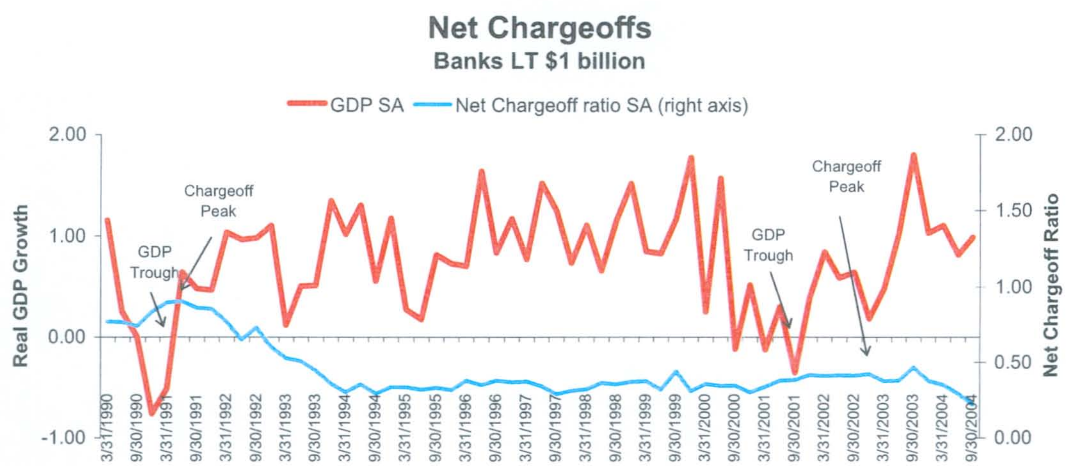


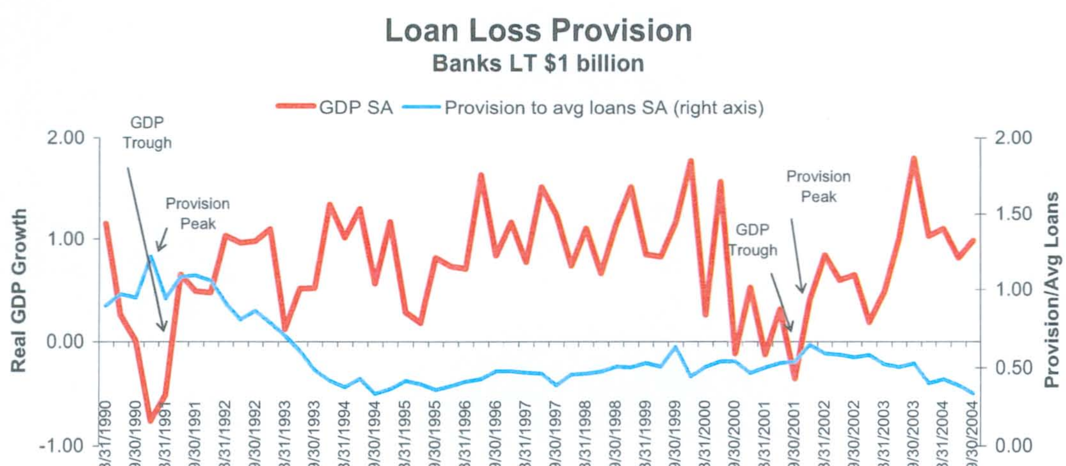




Sources: Call Report/BS&R, BEA 1/31/2005


Nonperforming Asset Ratio
Banks LT $1 billion
GDP SA
NPA Ratio SA (right axis)
NPA Peak
GDP Trough
GDP Trough
NPA Peak
Real GDP Growth
NPA Ratio


Net Chargeoffs
Banks LT $1 billion
GDP SA
Net Chargeoff ratio SA (right axis)
Chargeoff Peak
GDP Trough
GDP Trough
Chargeoff Peak
Real GDP Growth
Net Chargeoff Ratio


Loan Loss Provision
Banks LT $1 billion
GDP SA
Provision to avg loans SA (right axis)
GDP Trough
Provision Peak
GDP Trough
Provision Peak
Real GDP Growth
Provision/Avg Loans

Seasonal Factors (Out of 100 percent)									
All Insured Commercial Banks					Banks LT $1 billion				
	1Q	2Q	3Q	4Q		1Q	2Q	3Q	4Q
NPA Ratio	101.3	100.2	100.6	97.9	NPA Ratio	101.7	99.9	100.5	97.8
Net Charge-off Ratio	90.2	96.6	96.3	116.7	Net Charge-off Ratio	76.0	92.4	91.7	139.7
Prov to Avg Loans	91.9	94.6	98.9	114.3	Prov to Avg Loans	85.3	92.5	97.7	124.4
Other Key Statistics									
	Total	Mean	S.D.			Total	Mean	S.D.	
NPA Ratio	105.94	1.80	1.32		NPA Ratio	80.55	1.37	0.74	
Net Charge-off Ratio	51.75	0.88	0.35		Net Charge-off Ratio	26.54	0.45	0.18	
Prov to Avg Loans	54.21	0.92	0.38		Prov to Avg Loans	34.19	0.58	0.22	

Appendix 5: Materials used by Mr. Reinhart

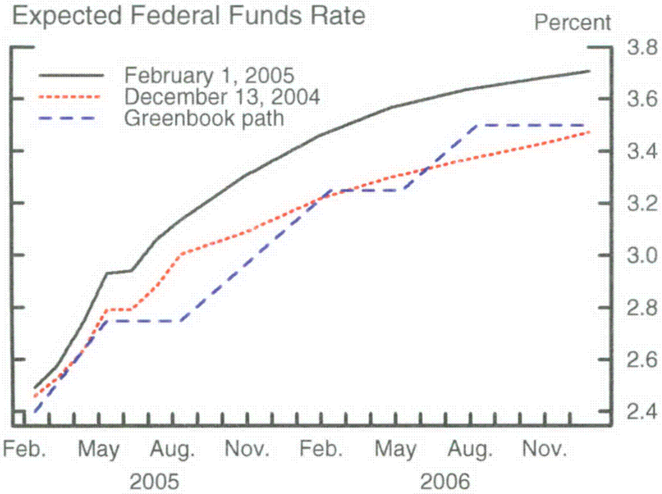
Restricted Controlled (FR) Class I (FOMC)

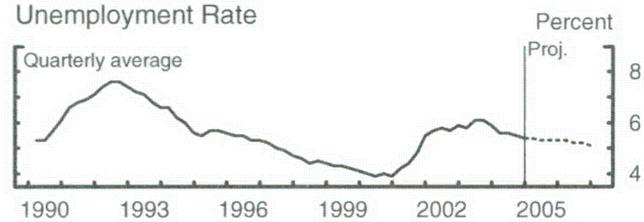
Material for

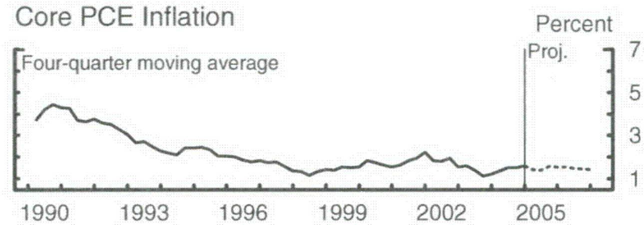
FOMC Briefing on Monetary Policy Alternatives

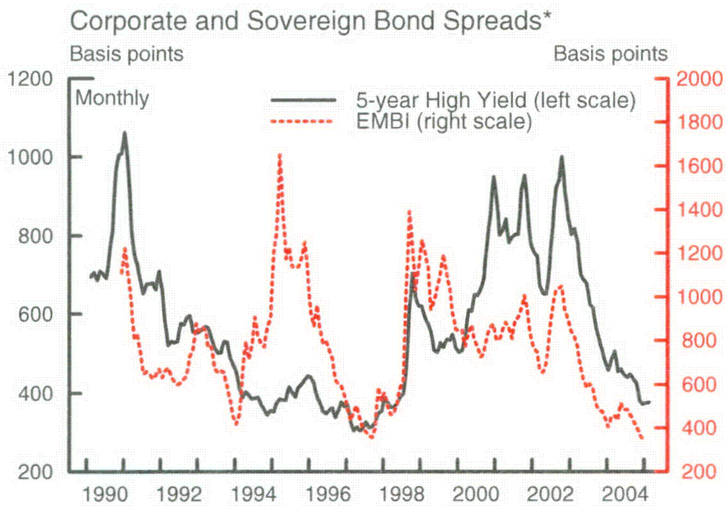
Vincent R. Reinhart
February 2, 2005

Exhibit 1
The Case for Tightening 25 Basis Points





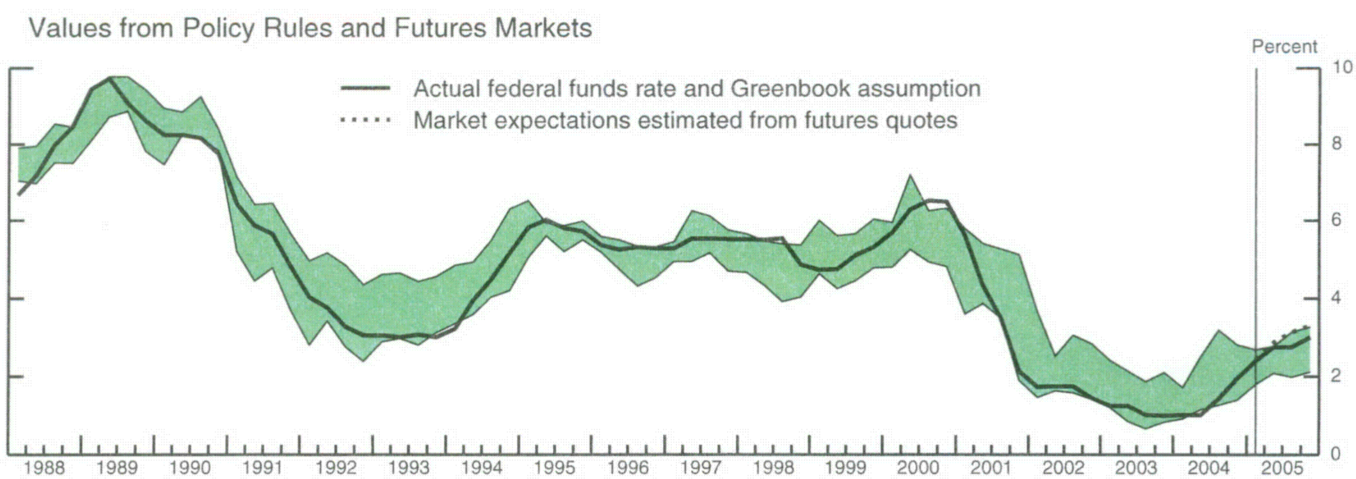




*Spreads over yields on comparable maturity Treasuries.

Asset Prices and Monetary Policy

- Asset price misalignments are hard to identify with confidence.
- Appropriate monetary policy is not clear.
- Other instruments may be better suited to dealing with such problems.



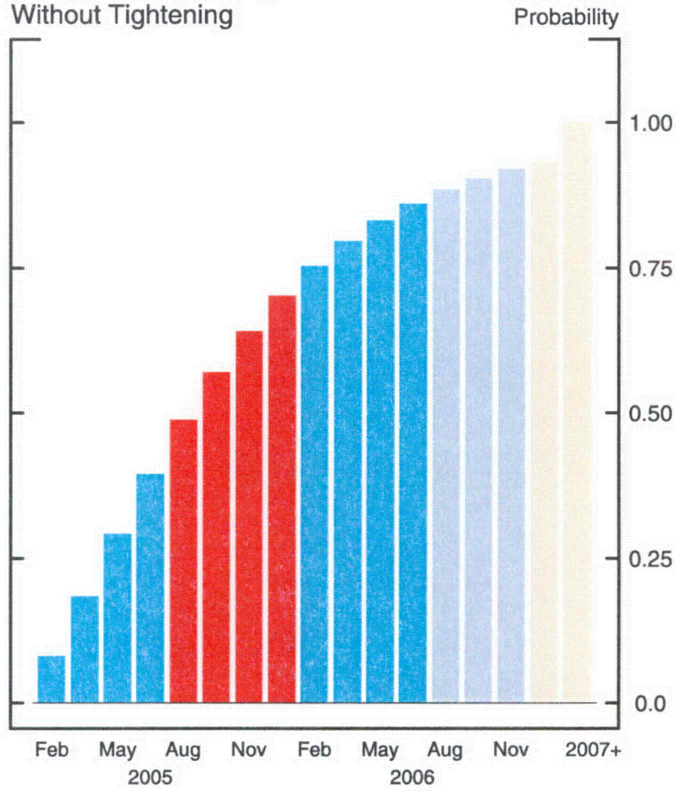
An explanatory note is provided in Chart 9 of the Bluebook.

Exhibit 2
When Will You Stop Tightening?

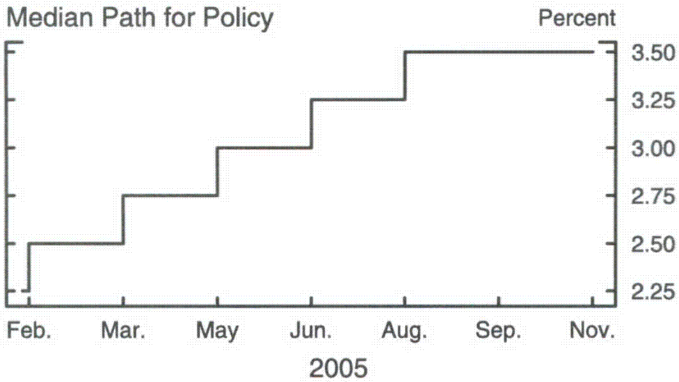
Market Participants Assume:

- Policy will be tightened 25 bps at every meeting.
- Until this tightening cycle ends.
- They are uncertain as to when tightening will end.

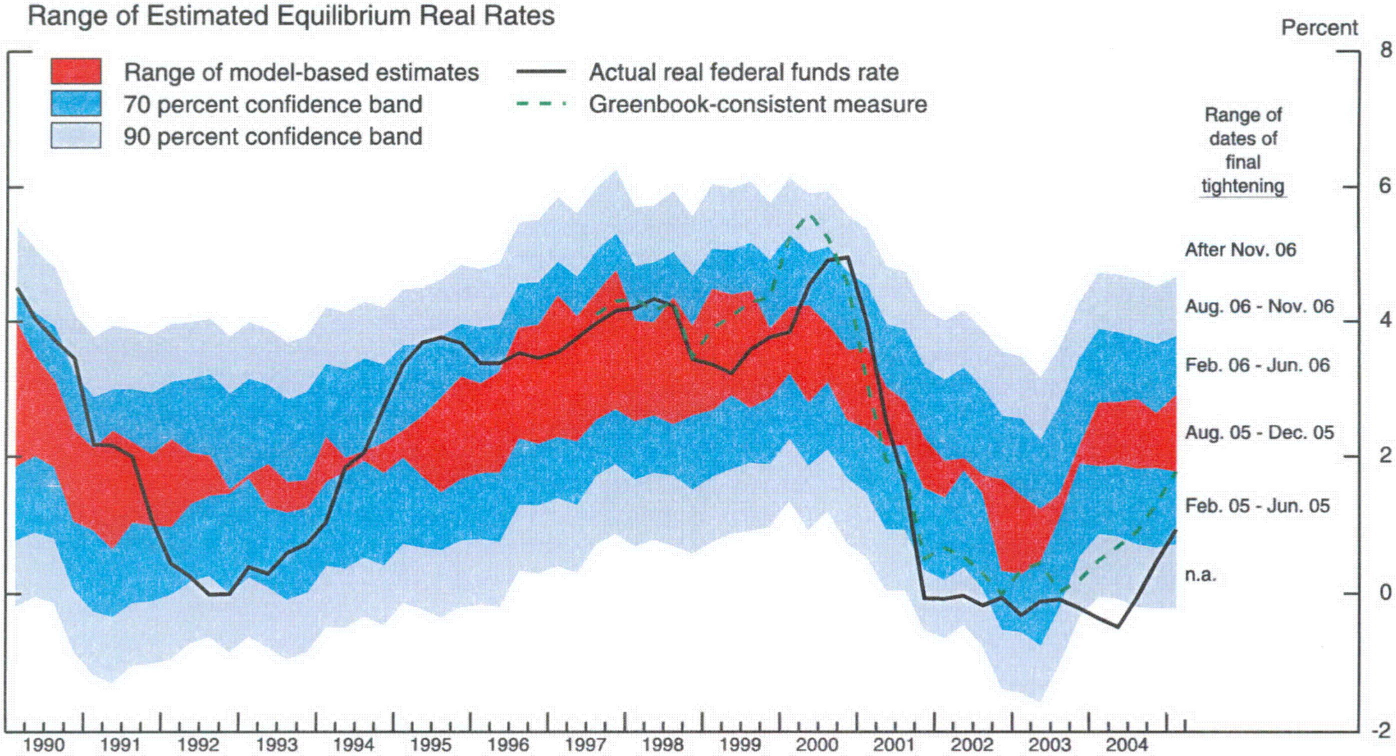
Cumulative Probability of First FOMC Meeting Without Tightening



Median Path for Policy



Range of Estimated Equilibrium Real Rates



An explanatory note is provided in Chart 8 of the Bluebook.

Exhibit 3

Assessing the Risk Assessment

From the FOMC Statement released December 14th

The Committee perceives the upside and downside risks to the attainment of both sustainable growth and price stability for the next few quarters to be roughly equal. With underlying inflation expected to be relatively low, the Committee believes that policy accommodation can be removed at a pace that is likely to be measured. Nonetheless, the Committee will respond to changes in economic prospects as needed to fulfill its obligation to maintain price stability.

Three alternatives

1. Get out of the business of hinting—either obliquely or directly—about future actions by dropping the entire paragraph.

2. Revive the first sentence assessing risks by basing it on the assumption of an unchanged stance of policy for the next few quarters and couching it in terms of probabilities, not risks.

3. Rely on the gradual evolution of the latter part of the paragraph to convey a sense of the future path of interest rates.

Table 1: Alternative Language for the January FOMC Announcement

	December FOMC	Alternative A	Alternative B	Alternative C
Policy Decision	1. The Federal Open Market Committee decided today to raise its target for the federal funds rate by 25 basis points to 2¼ percent.	The Federal Open Market Committee decided today to keep its target for the federal funds rate at 2¼ percent. The Committee's policy actions since mid-2004 have materially reduced the degree of monetary policy accommodation.	The Federal Open Market Committee decided today to raise its target for the federal funds rate by 25 basis points to 2½ percent.	The Federal Open Market Committee decided today to raise its target for the federal funds rate by 50 basis points to 2¾ percent.
Rationale	2. The Committee believes that, even after this action, the stance of monetary policy remains accommodative and, coupled with robust underlying growth in productivity, is providing ongoing support to economic activity.	The Committee believes that the stance of monetary policy remains somewhat accommodative and, coupled with robust underlying growth in productivity, is providing ongoing support to economic activity.	[Unchanged from December statement]	The Committee believes that the stance of monetary policy remains accommodative and, coupled with ~~robust~~ the underlying growth in productivity, is providing ongoing support to economic activity.
	3. Output appears to be growing at a moderate pace despite the earlier rise in energy prices, and labor market conditions continue to improve gradually. 4. Inflation and longer-term inflation expectations remain well contained.	Output appears to be growing at a moderate pace despite the ~~earlier~~ rise in energy prices, and labor market conditions seem to be improving gradually. [Unchanged from December statement]	Output appears to be growing at a moderate pace despite the ~~earlier~~ rise in energy prices, and labor market conditions continue to improve gradually. [Unchanged from December statement]	Output appears to be growing at a moderate pace despite the ~~earlier~~ rise in energy prices, and labor market conditions continue to improve ~~gradually~~. Inflation and ~~longer-term~~ inflation expectations remain well contained, but rising business costs have the potential to put upward pressure on prices.
Assessment of Risk	5. The Committee perceives the upside and downside risks to the attainment of both sustainable growth and price stability for the next few quarters to be roughly equal.	[Unchanged from December statement]	[Unchanged from December statement]	[Unchanged from December statement]
	6. With underlying inflation expected to be relatively low, the Committee believes that policy accommodation can be removed at a pace that is likely to be measured. Nonetheless, the Committee will respond to changes in economic prospects as needed to fulfill its obligation to maintain price stability.	With underlying inflation expected to be relatively low, the Committee believes that policy accommodation can be removed at a pace that is likely to be measured. Nonetheless, the Committee will respond to changes in economic prospects as needed to fulfill its obligation to promote price stability and sustainable growth.	[Unchanged from December statement]	[None]