

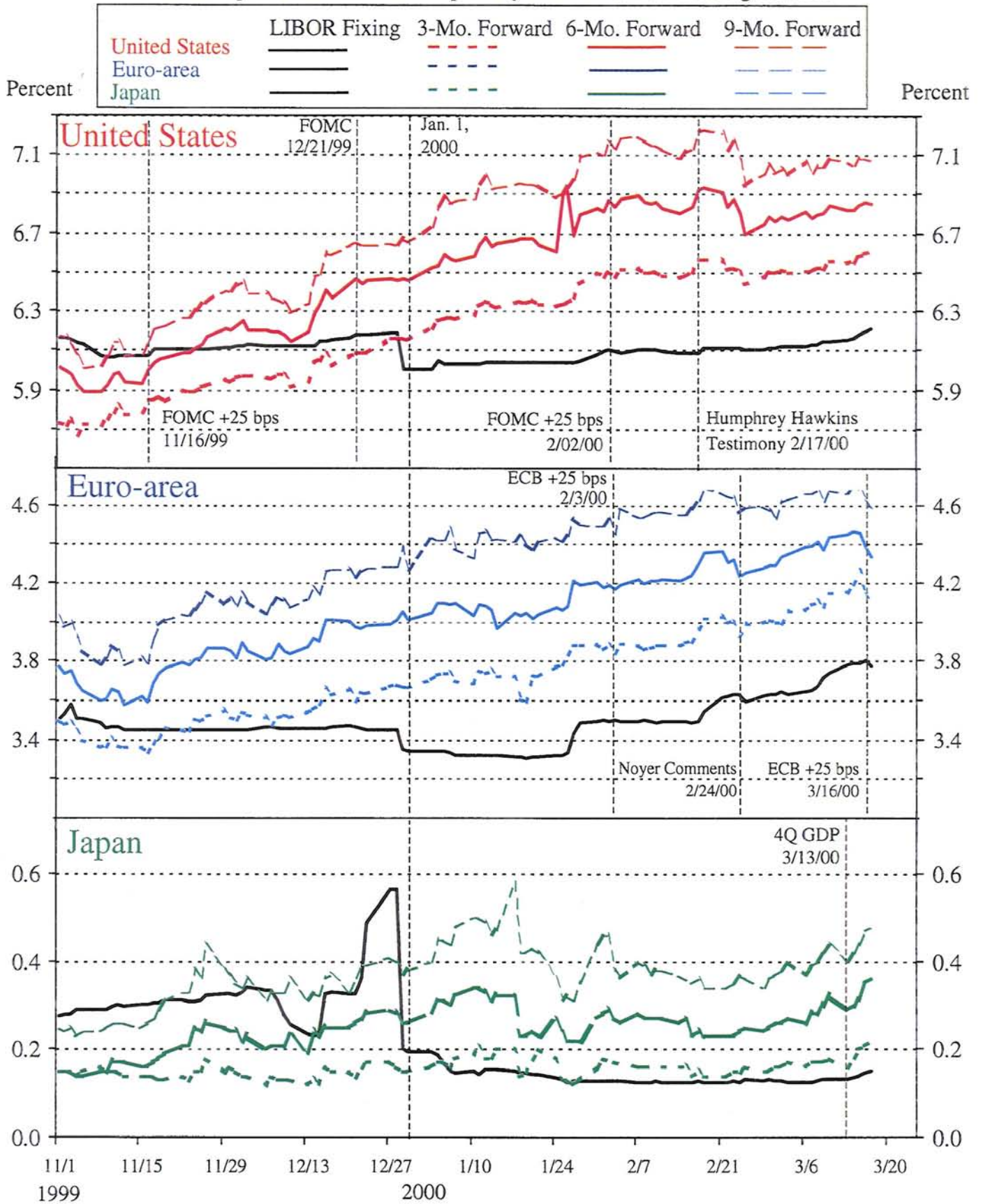
APPENDIX

Material distributed by Mr. Fisher.

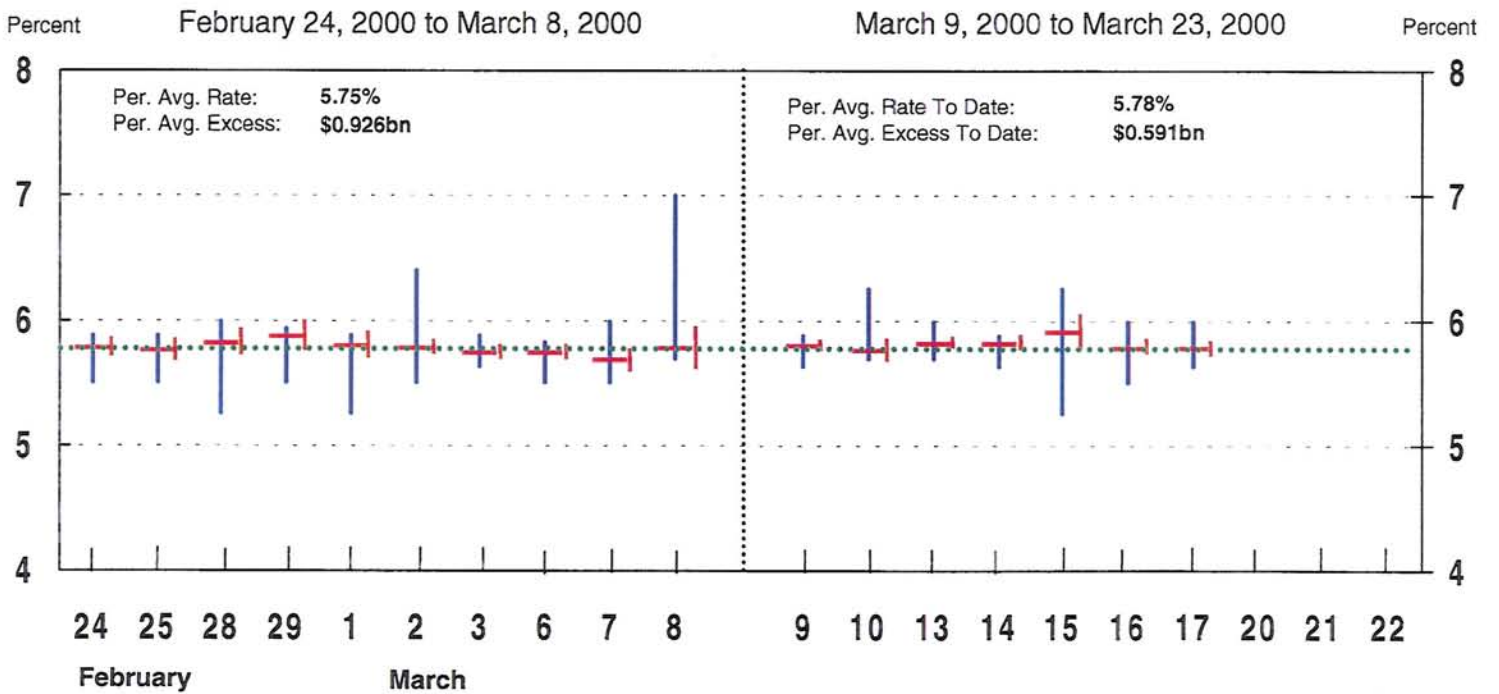
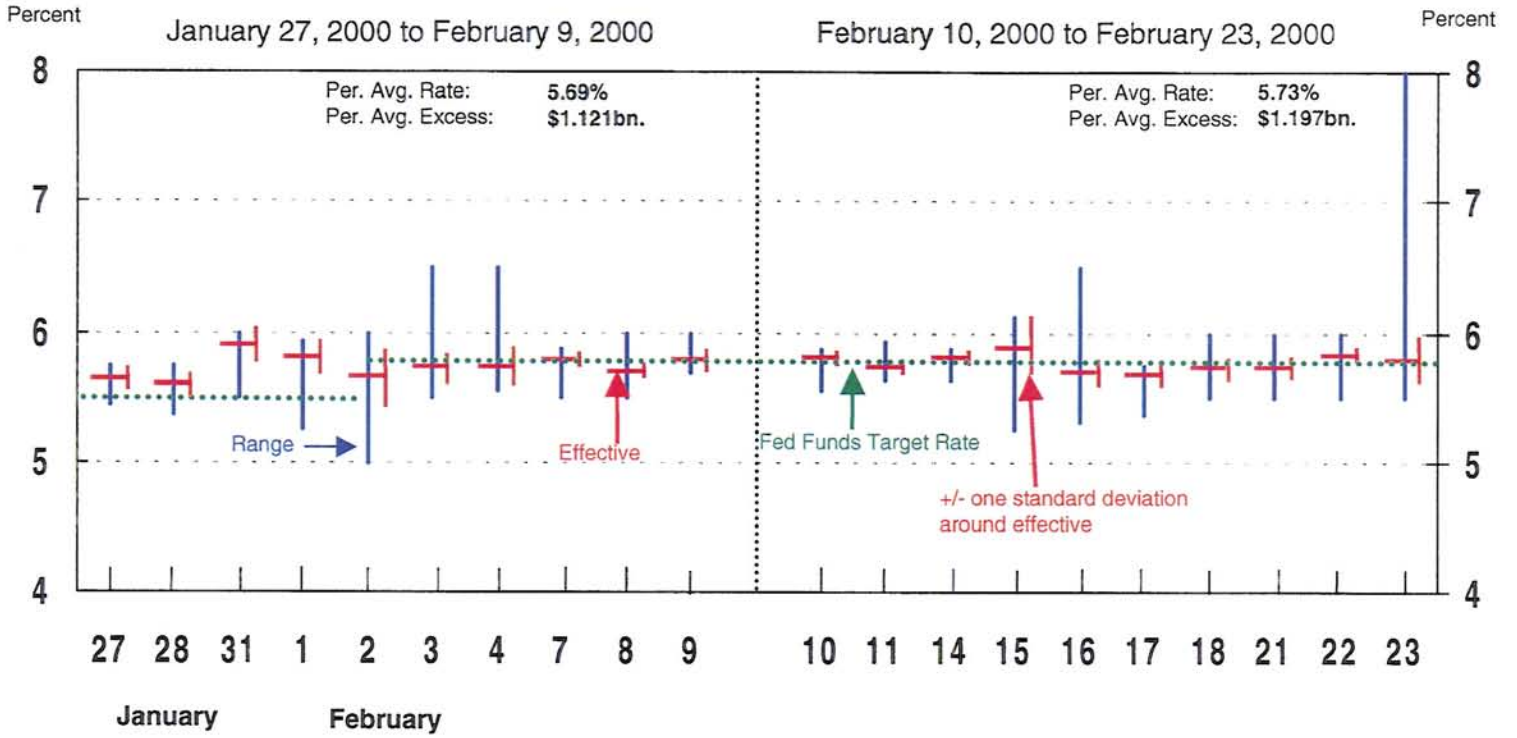
3-Month Deposit Rates

November 1, 1999 - March 17, 2000

Current Deposit Rate and Rates Implied by Traded Forward Rate Agreements



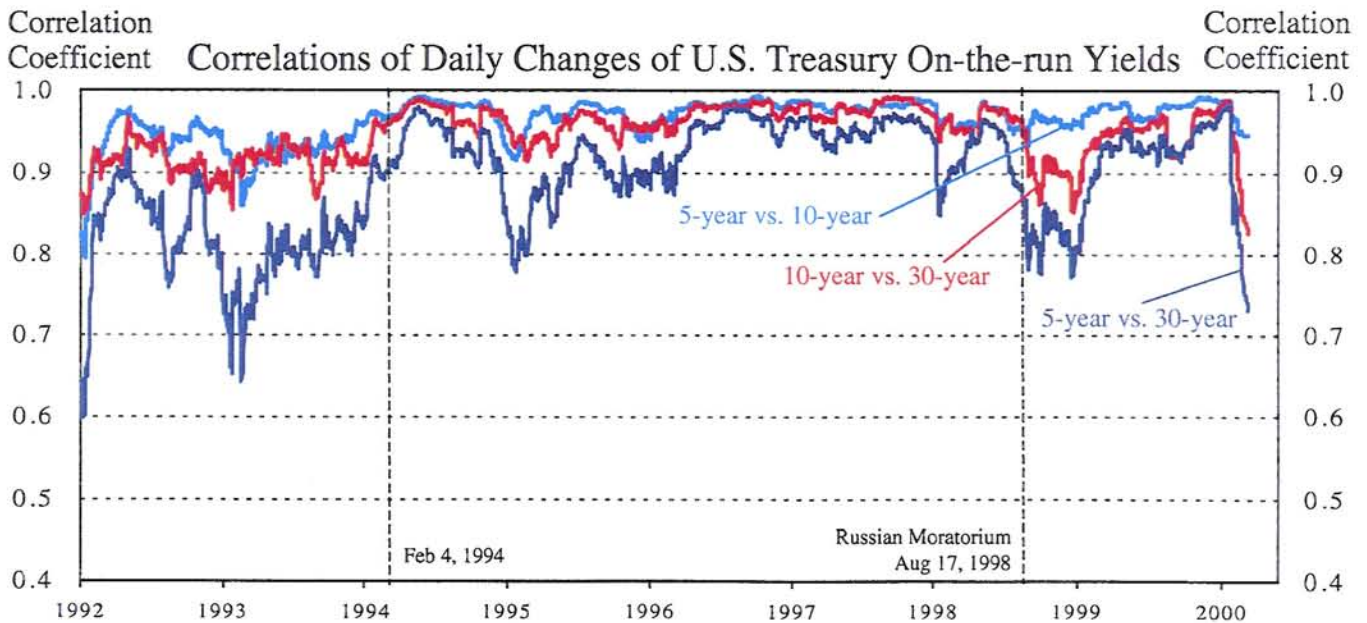
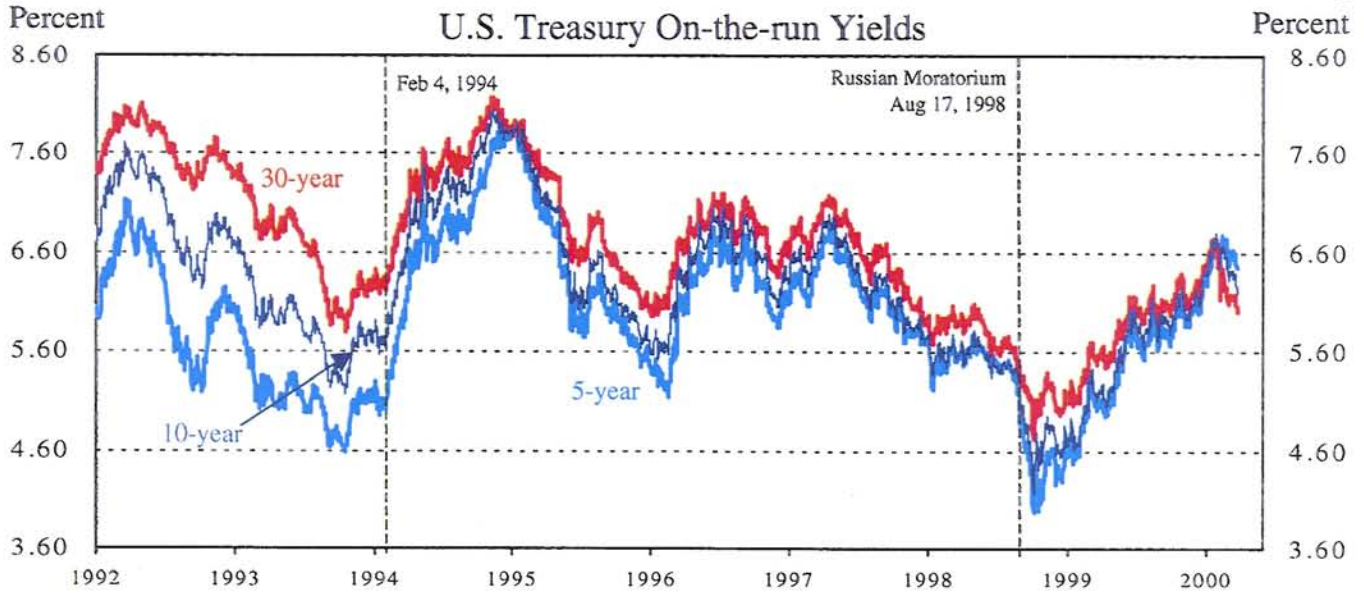
DAILY FEDERAL FUNDS TRADING RANGE, EFFECTIVE RATE & +/- ONE STANDARD DEVIATION



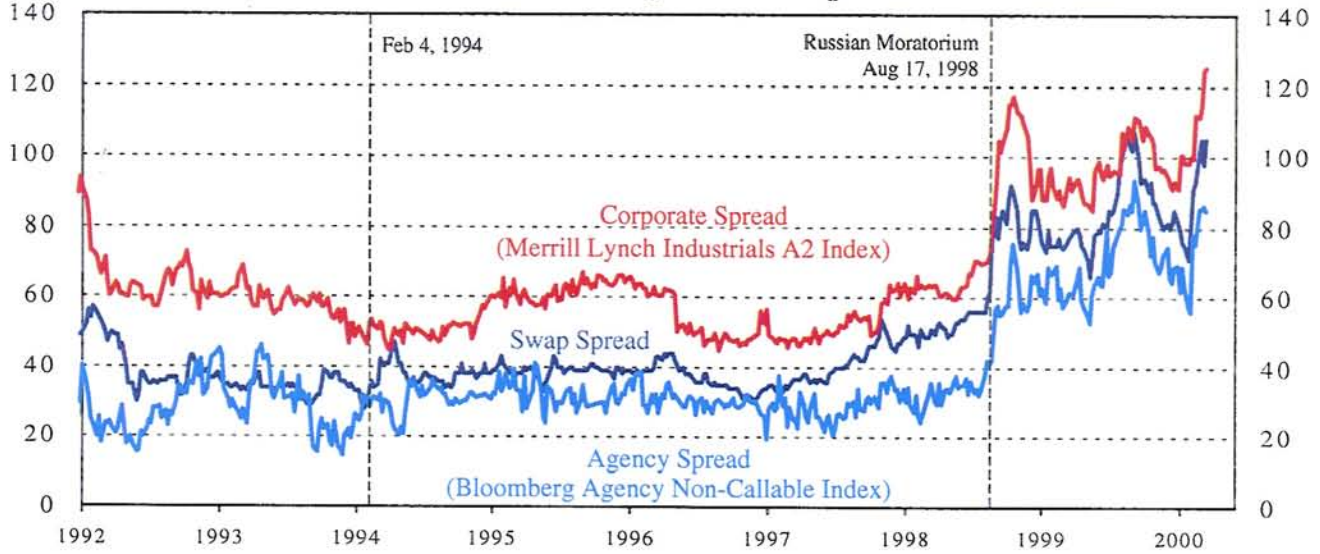
CHANGED MARKET CONDITIONS

Conditions in fixed-income markets have changed significantly in recent months.

- Coincident with the inversion of the long-end of the yield curve, the daily volatility of the 30-year bond has risen above the volatility of both the 5-year and the 10-year notes.
- 10-year credit spreads to Treasuries have widened back to their 1998 highs.
- 10-year spread relationships among private credits have become much less stable.
- Bid-ask spreads on Treasury securities have widened.
- The scarcity value of Treasury securities can be seen in lower overnight repo rates.



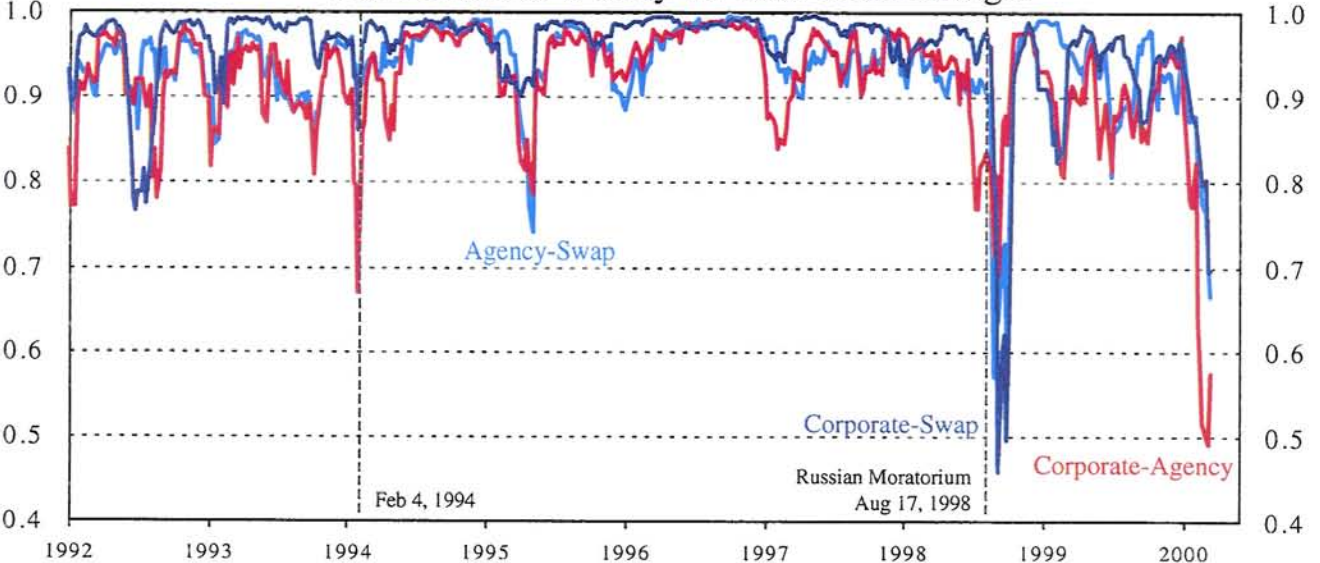
Basis Points Domestic Fixed Income Weekly 10-Year Spreads To Treasuries Basis Points



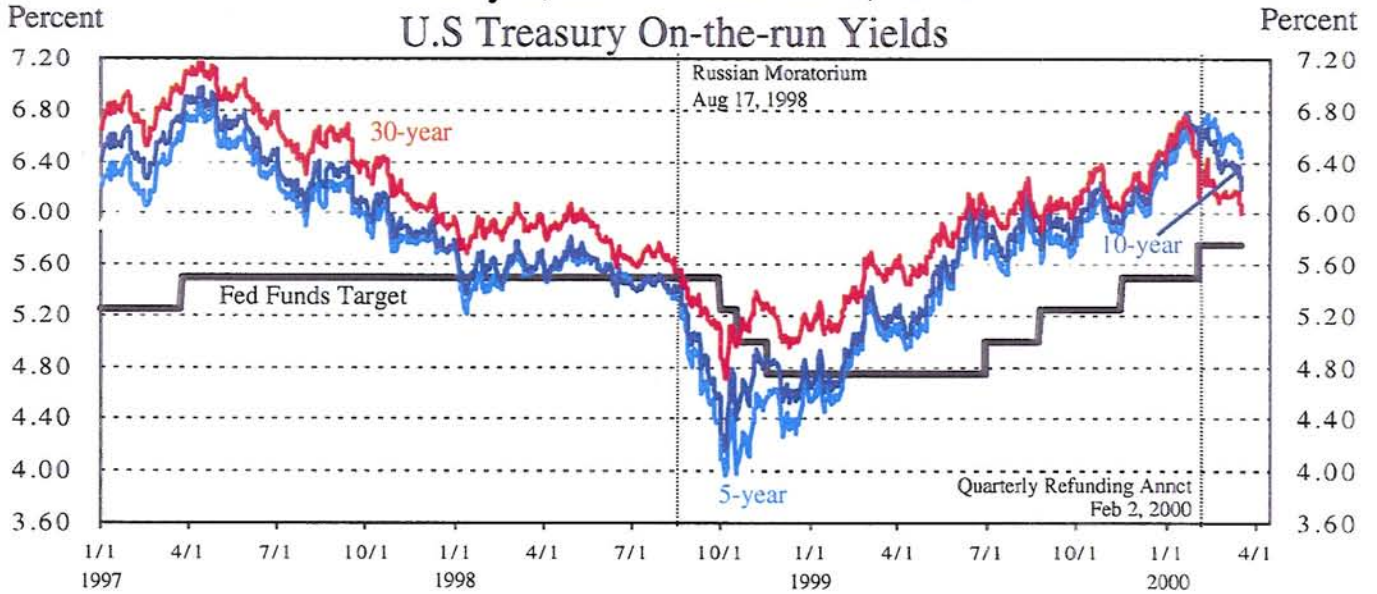
Correlation Coefficient Correlations of Weekly 10-Year Yield Changes Correlation Coefficient



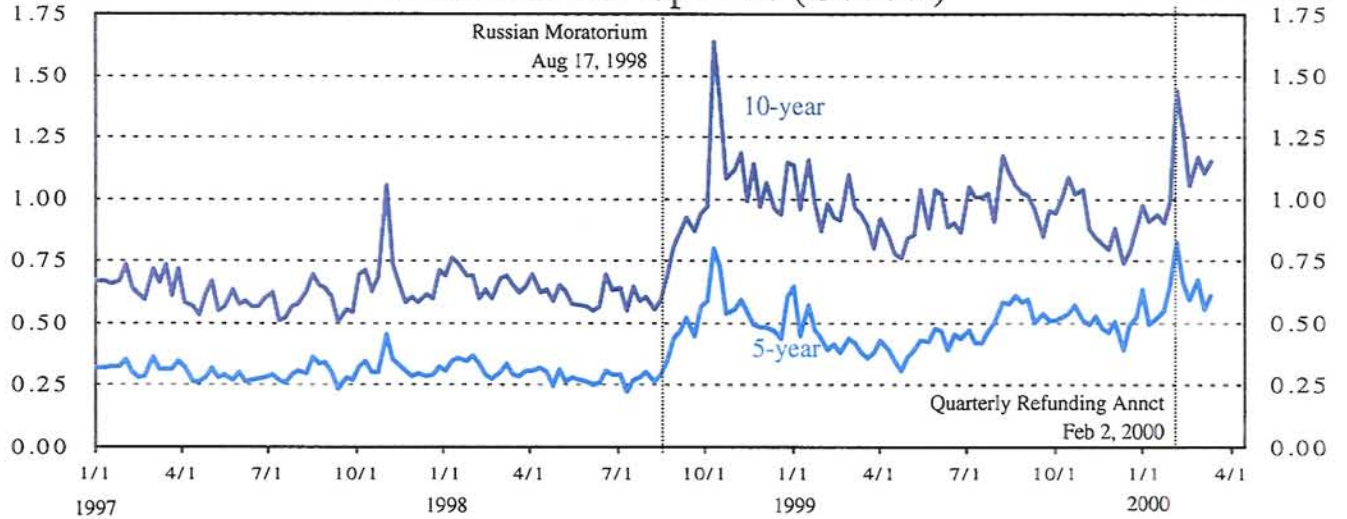
Correlation Coefficient Correlations of Weekly 10-Year Yield Changes Correlation Coefficient



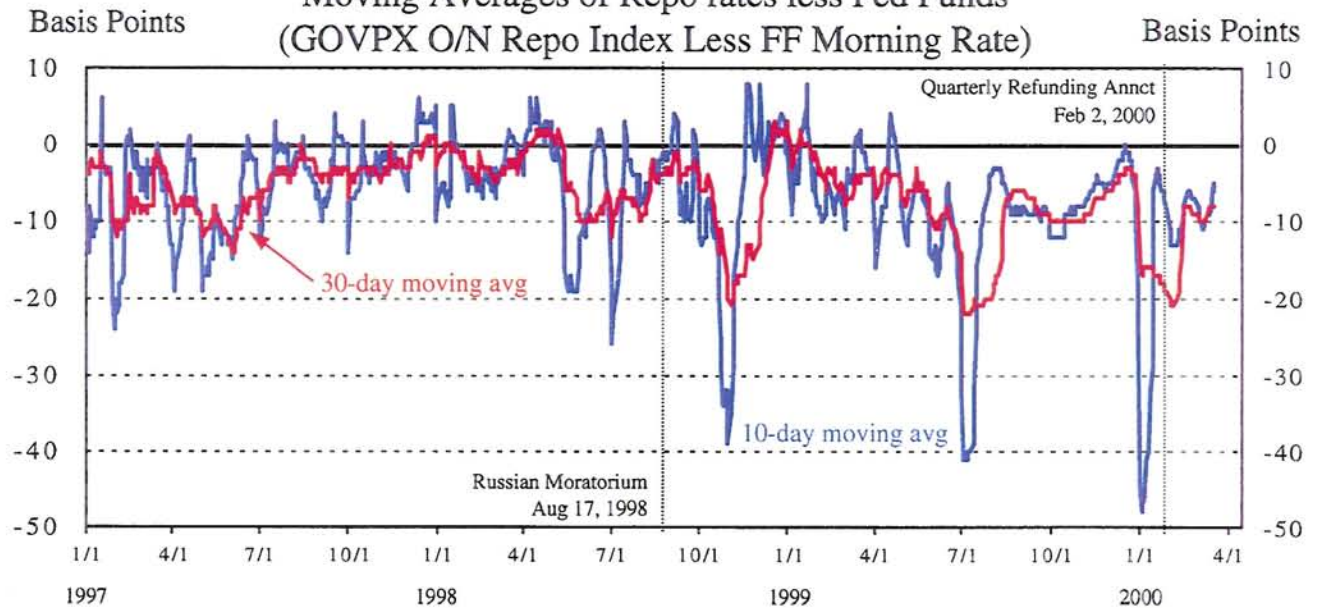
January 1, 1997 to March 16, 2000 U.S. Treasury On-the-run Yields



Mean Bid-Ask Spreads (GovPX)



Moving Averages of Repo rates less Fed Funds (GOVPX O/N Repo Index Less FF Morning Rate)



**SYSTEM OPERATIONS NEED TO CHANGE
WITH THE CHANGED ENVIRONMENT**

In order to serve the System's portfolio objectives and to avoid exacerbating the supply-demand imbalance for Treasury securities, it is my recommendation that we should:

- **Begin now to moderate our reliance on net additions to holdings of Treasury securities as the sole means of accommodating the upward trend in the asset side of the System's balance sheet; and**
- **Evaluate all plausible asset classes and operating techniques that could be appropriate for SOMA as alternatives to Treasury securities.**

Until the Committee can thoroughly consider alternative asset allocations for SOMA, my recommendation is that we should:

- **Rely on long-term temporary operations to meet the growth in underlying reserve needs that cannot comfortably be met by further outright purchases of Treasury securities; and**
- **Distribute our demand for collateral as broadly as possible so as to minimize our impact on spread relationships.**

SPECIFIC PLANS

Bill holdings:

- Set a target for SOMA of no more than 35 percent and a firm ceiling of no more than 40 percent of any one issue of bills, and manage SOMA auction participation accordingly.
- Plan no outright bill purchases;

However, after April tax season we can evaluate the likely size of future bill issues and consider targeted outright purchases of issues where SOMA holdings are well below 35 percent of expected bill sizes.

Coupon holdings:

- Continue to rollover existing holdings at auction and monitor the impact of the Treasury's buybacks and changes in note and bond issue sizes on SOMA percentage holdings of individual coupon issues.
- "Try and see" if we can meet a portion of underlying reserve needs through outright purchases of up to \$20 billion over rest of this year, spread evenly across the coupon curve.

Temporary operations:

- Meet the balance of underlying reserve needs with a rolling book of term repos, accepting Treasury, straight agency debt and mortgage-backed securities as collateral and pricing them separately—as we have since last October.

QUESTIONS FOR FOMC MEMBERS

1. Do Committee members have suggestions of assets to be included in our study of alternatives for SOMA?

Are there particular issues or concerns that members think the study should address?

2. Are Committee members comfortable with my suggested approach of aiming to hold no more than 35 percent and setting a firm ceiling of 40 percent for any single issue of Treasury bills?
3. What are Committee members' views of the desirability of further coupon purchases this year?

Are members comfortable with my suggested "try and see" approach? Would members prefer that the Desk aim to purchase more or less than \$20 billion?

FOMC VOTES REQUESTED

1. To extend temporarily the suspension of paragraphs 3 through 6 of the Guidelines for the Conduct of System Operations in Federal Agency Issues and, thus, to continue the temporary Guidelines, as adopted at the August 24, 1999 meeting, until the Committee's first meeting in 2001.
2. To retain paragraph 1.c. as a permanent amendment of the Authorization for Domestic Open Market Operations, to permit the use of reverse repurchase agreements.