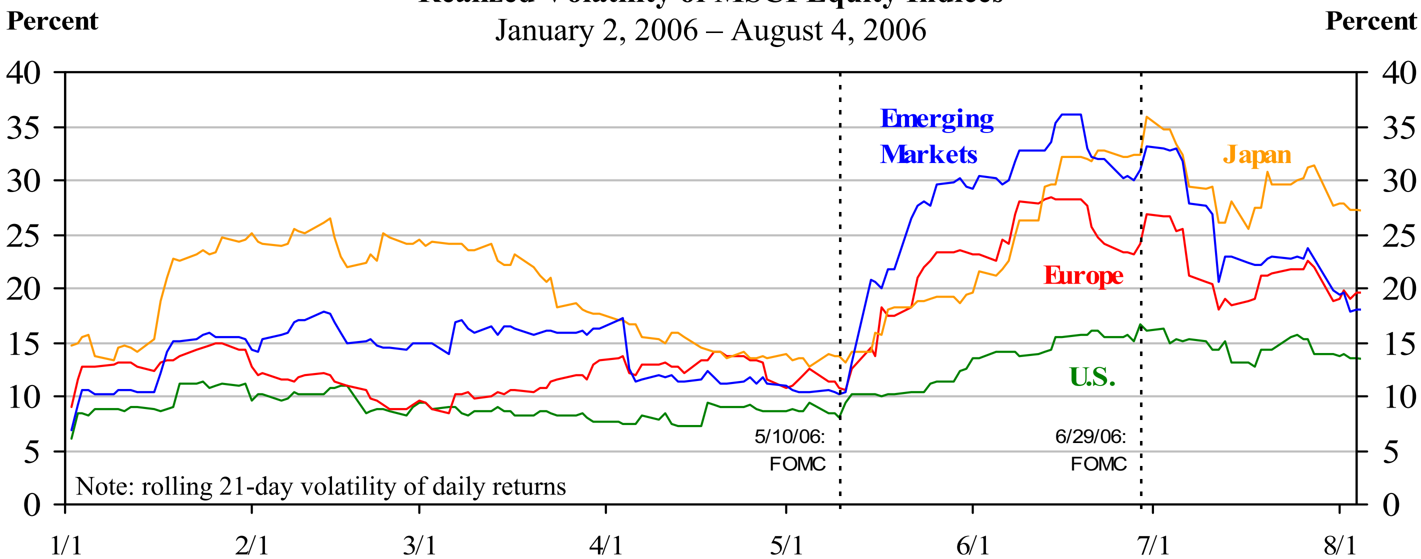
## Appendix 1: Materials used by Mr. Kos

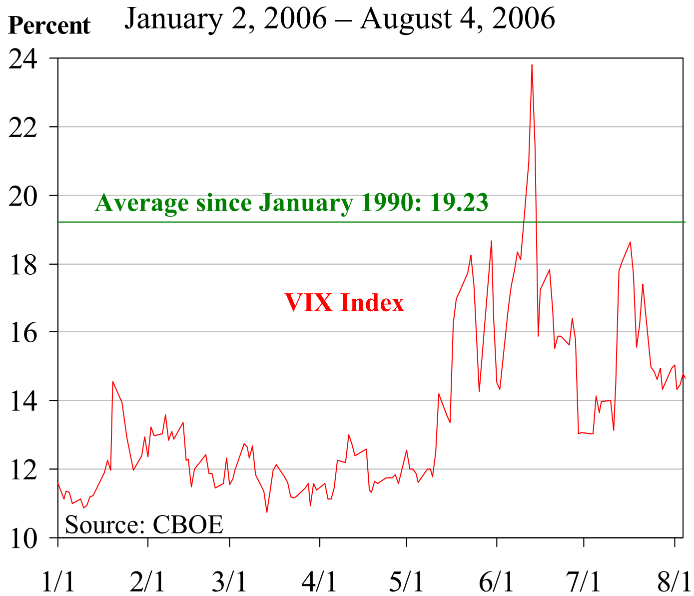
**Realized Volatility of MSCI Equity Indices**

January 2, 2006 – August 4, 2006



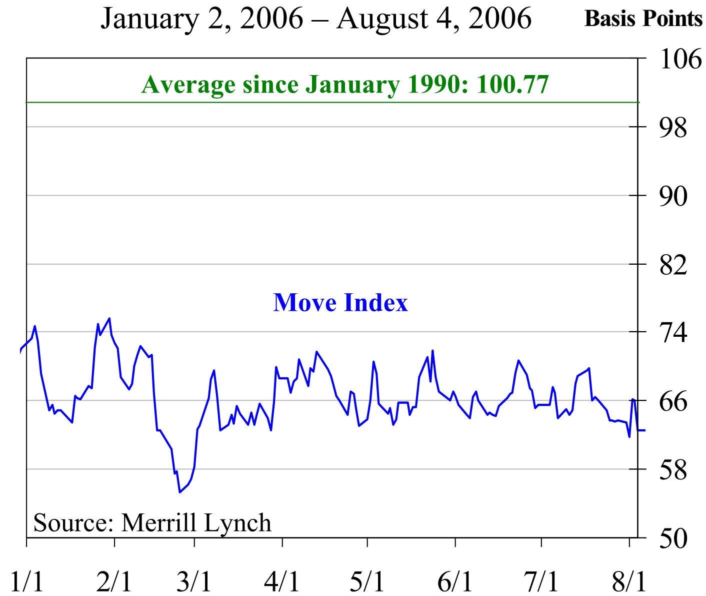

**Implied Volatility on the S&P 100**

January 2, 2006 – August 4, 2006



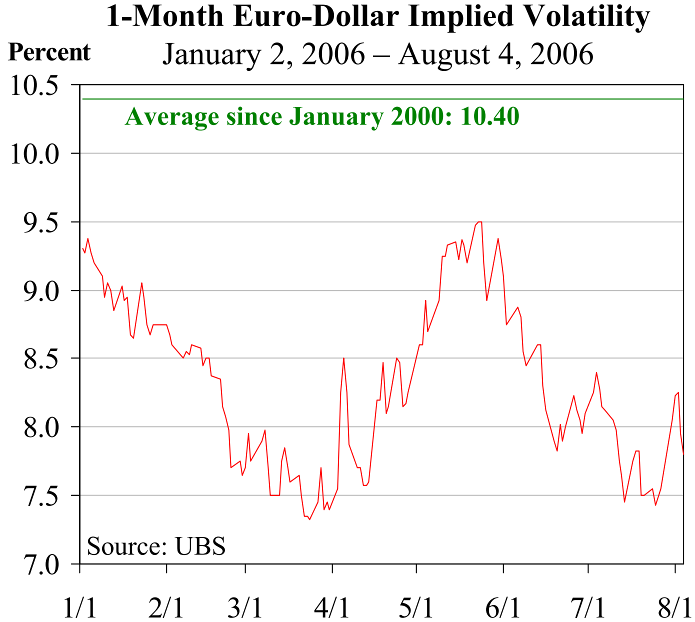

**Treasury Yield Implied Volatility**

January 2, 2006 – August 4, 2006



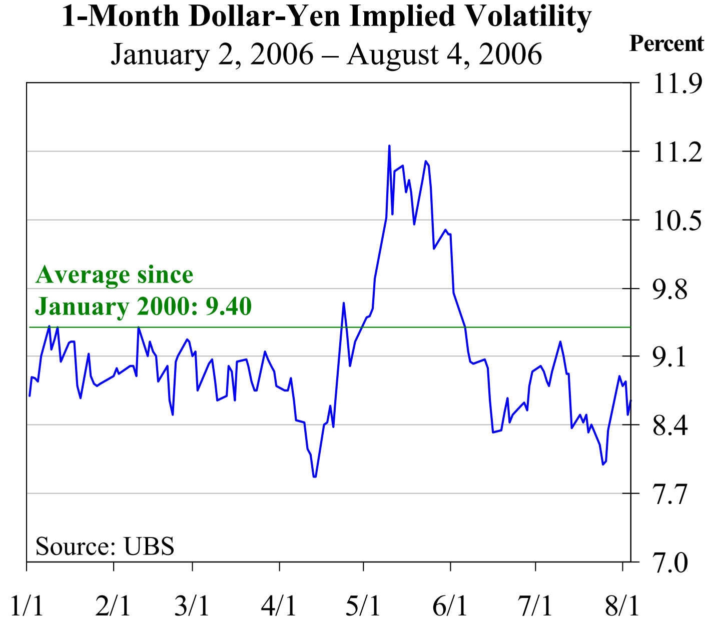

**1-Month Euro-Dollar Implied Volatility**

January 2, 2006 – August 4, 2006




**1-Month Dollar-Yen Implied Volatility**

January 2, 2006 – August 4, 2006

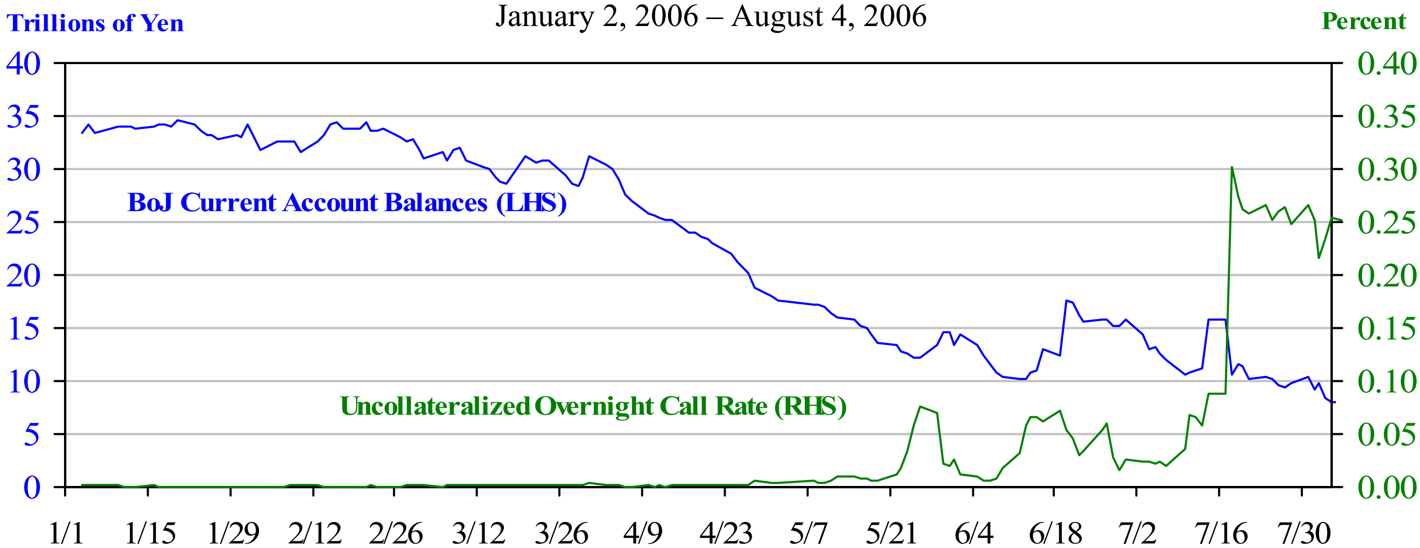


**Changes in Select Central Bank Policy Rates**
Activity Since January 2, 2006

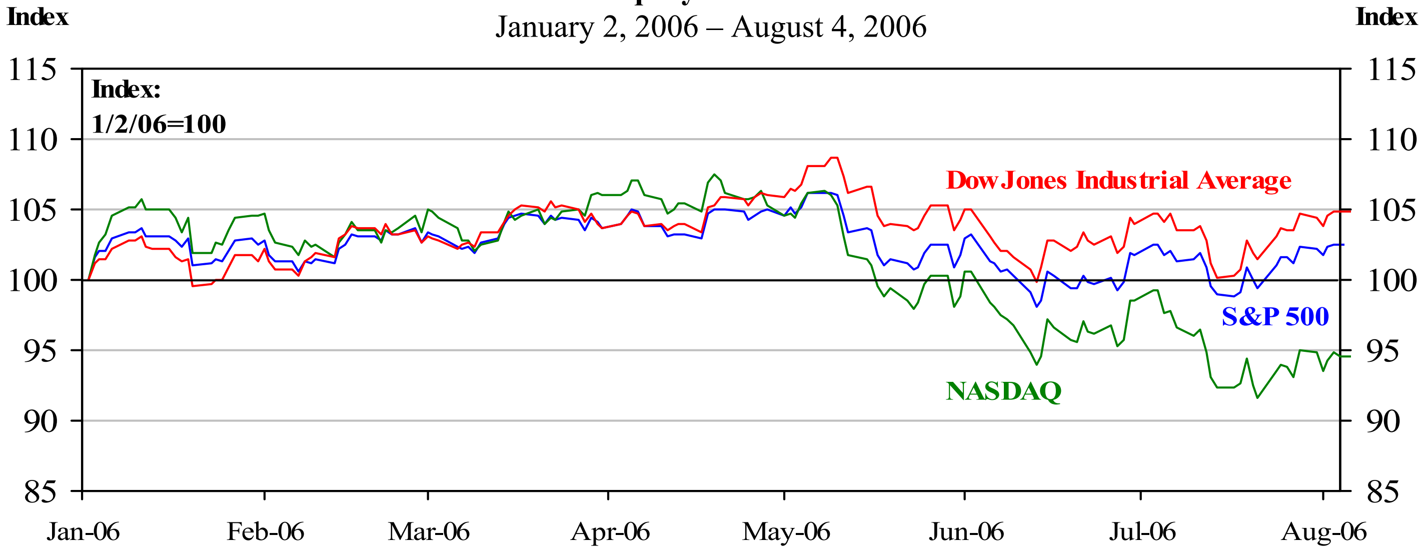
| Region | Country | Official Interest Rate | Current Rate | ▲ in Bps since 1/2/06 | Last Change |
|---|---|---|---|---|---|
| **The Americas** | | | | | |
| | United States | Federal funds rate | 5.25 | 100 | Jun-29 |
| | Canada | Overnight funding rate | 4.25 | 100 | May-24 |
| | Brazil | SELIC overnight rate | 14.75 | (325) | Jul-19 |
| | Mexico | Repo rate | 7.00 | (125) | Apr-21 |
| | Chile | Discount rate | 5.25 | 75 | Jul-14 |
| **Europe/Africa** | | | | | |
| | Euro area | Refi rate | 3.00 | 75 | Aug-03 |
| | United Kingdom | Repo rate | 4.75 | 25 | Aug-03 |
| | Sweden | Repo rate | 2.25 | 75 | Jun-20 |
| | Norway | Deposit rate | 2.75 | 50 | May-31 |
| | Czech Republic | 2-week repo rate | 2.25 | 25 | Jul-27 |
| | Hungary | 2-week deposit rate | 6.75 | 75 | Jul-24 |
| | Slovak Republic | 2-week repo rate | 4.50 | 150 | Jul-25 |
| | South Africa | Repo rate | 8.00 | 100 | Aug-03 |
| | Switzerland | 3-month Swiss Libor | 1.50 | 50 | Jun-15 |
| | Turkey | Overnight borrowing rate | 17.50 | 400 | Jul-20 |
| **Asia/Pacific** | | | | | |
| | Australia | Cash rate | 6.00 | 50 | Aug-02 |
| | Japan | Overnight call rate | 0.25 | 25 | Jul-14 |
| | Korea | Overnight call rate | 4.25 | 50 | Jun-08 |
| | India | Reverse repo rate | 6.00 | 75 | Jul-25 |
| | Thailand | 14-day repo rate | 5.00 | 100 | Jun-07 |
| | Taiwan | Official discount rate | 2.50 | 25 | Jun-29 |

*Source: JP Morgan*

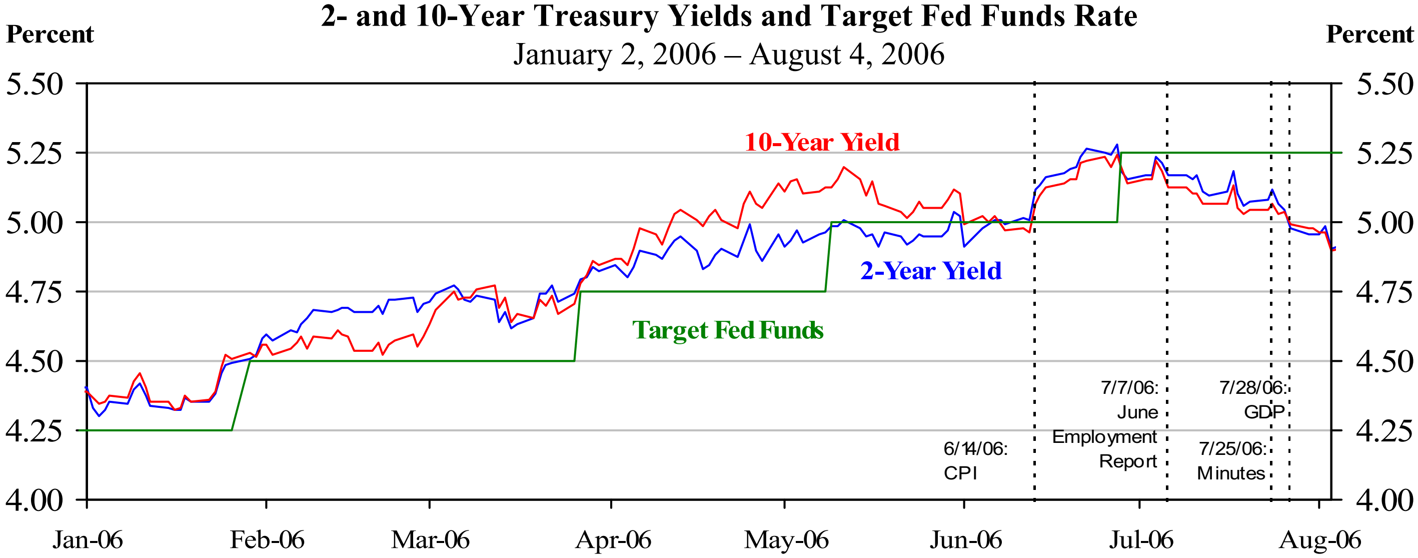
**Bank of Japan Current Account Balances and Overnight Call Rate**
January 2, 2006 – August 4, 2006



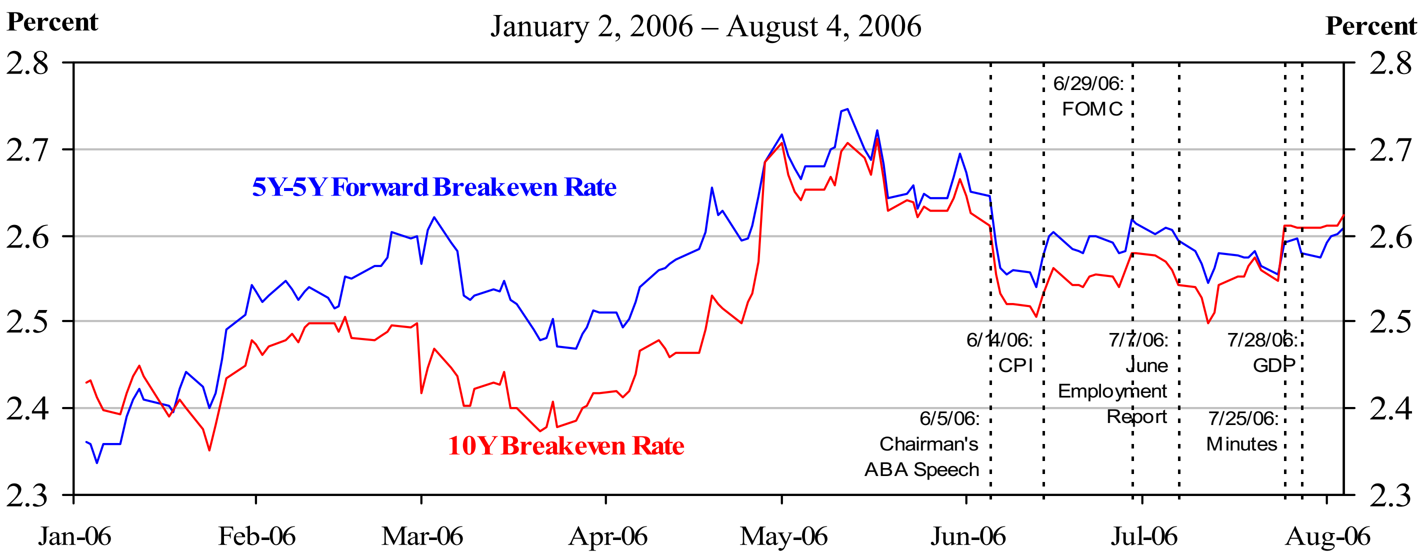
**U.S. Equity Performance**
January 2, 2006 – August 4, 2006




**2- and 10-Year Treasury Yields and Target Fed Funds Rate**
January 2, 2006 – August 4, 2006

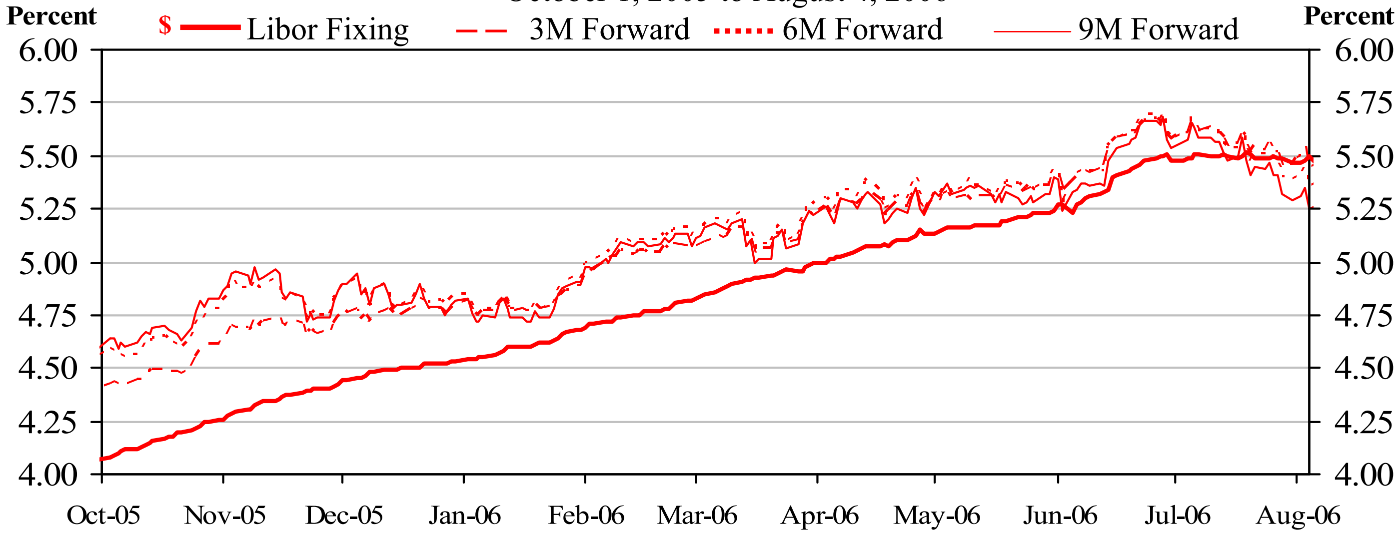



**U.S. Breakeven Inflation Rates**
January 2, 2006 – August 4, 2006

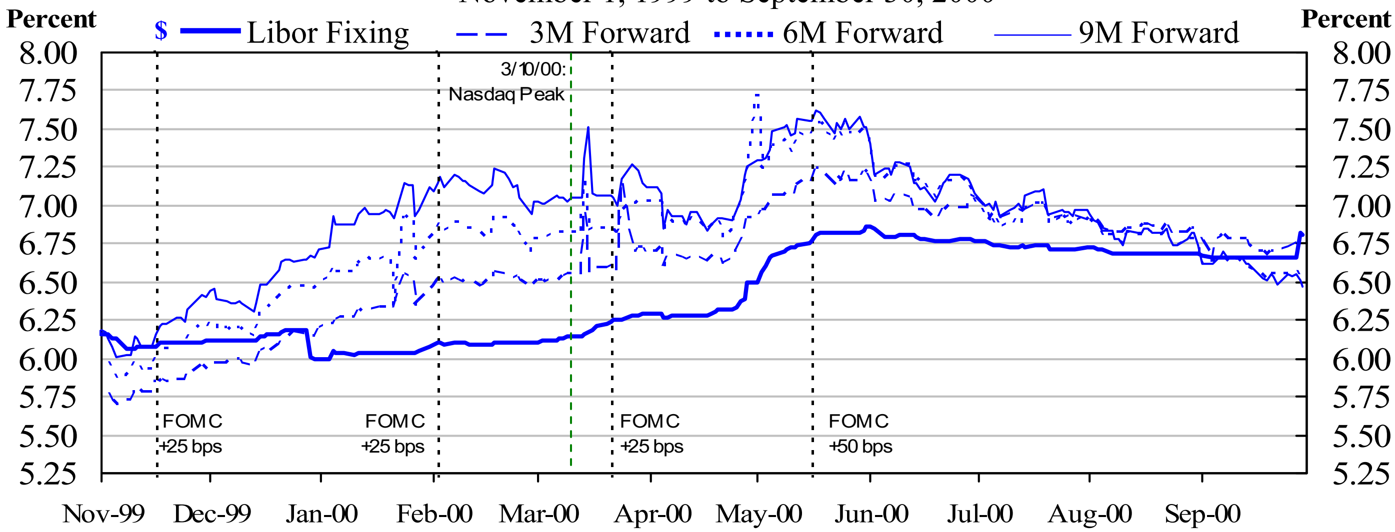


## Current U.S. 3-Month Deposit Rates and Rates Implied by Traded Forward Rate Agreements

October 1, 2005 to August 4, 2006



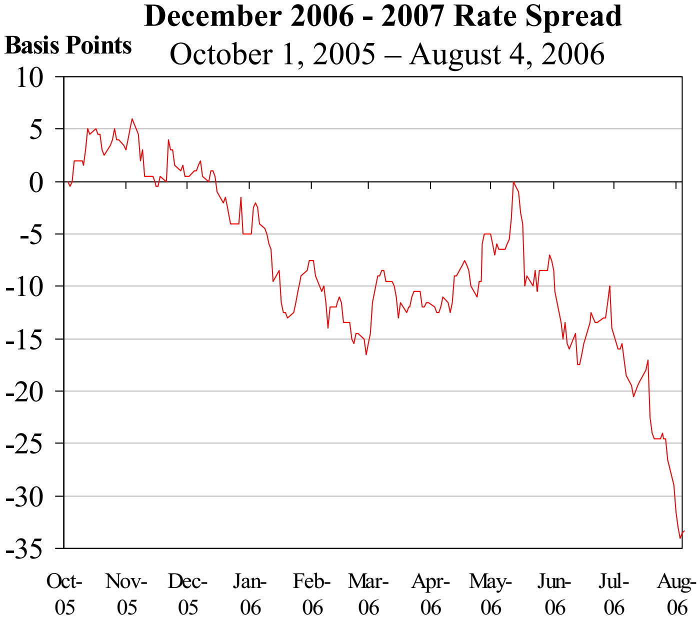

November 1, 1999 to September 30, 2000




## 3-Month Eurodollar Futures Contracts

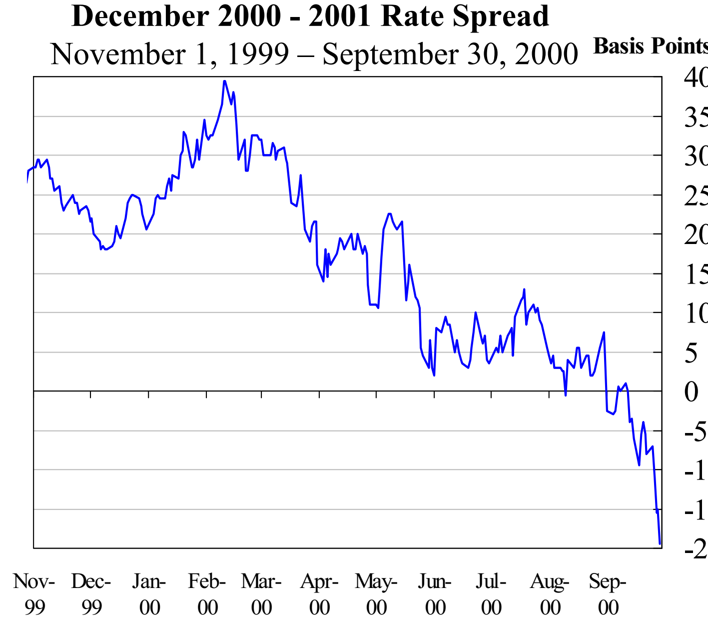
### December 2006 - 2007 Rate Spread

October 1, 2005 – August 4, 2006




### December 2000 - 2001 Rate Spread

November 1, 1999 – September 30, 2000



## Appendix 2: Materials used by Mr. Madigan

**Class I FOMC – Restricted Controlled FR**

*Material for*

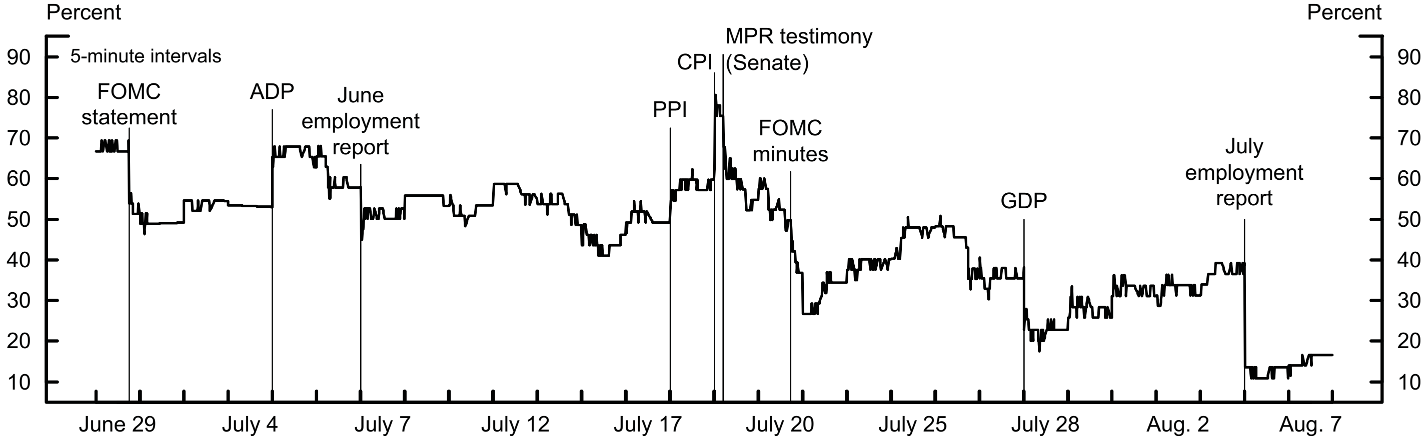
# FOMC Briefing on Monetary Policy Alternatives

**Brian Madigan**

**August 8, 2006**

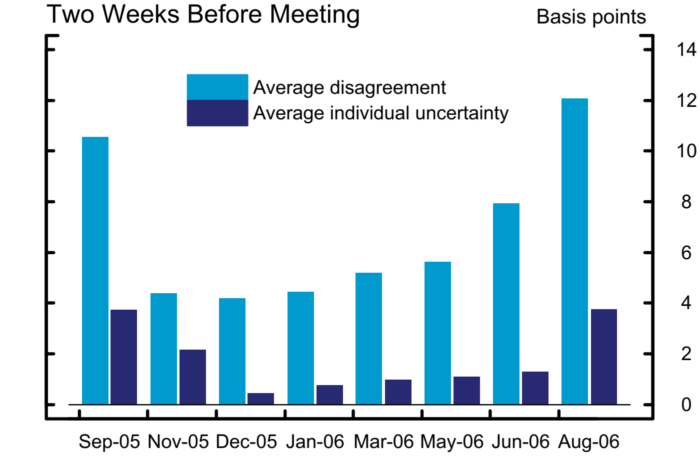
## Exhibit 1 of 4
## Monetary Policy Expectations

Probability of a 25 b.p. Firming at August FOMC Meeting*




*Estimated from federal funds futures, with an allowance for term premia.

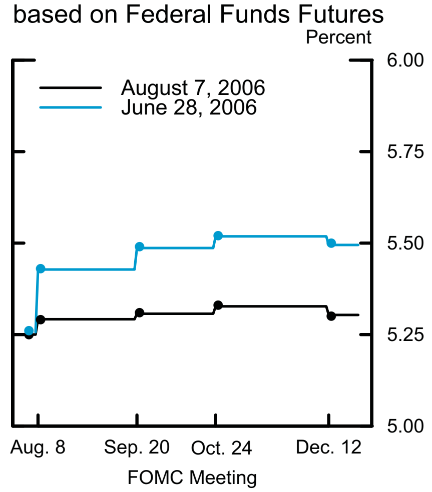
Dealer Survey: Average Disagreement and Uncertainty Regarding Policy Choice Two Weeks Before Meeting



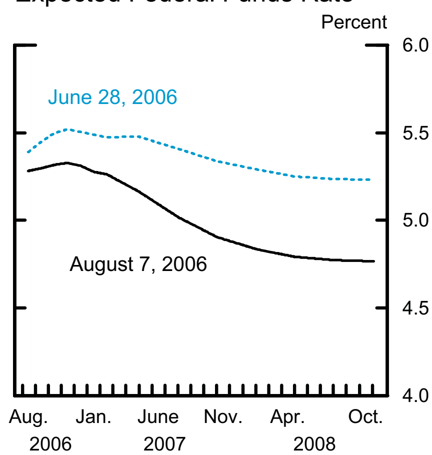

Dealer Survey:
Expectations regarding August Statement

- Express more conviction regarding moderation of growth
- Acknowledge elevated inflation ratings
- Express concern about inflation risks
- Indicate data dependence

Expected Federal Funds Rates based on Federal Funds Futures

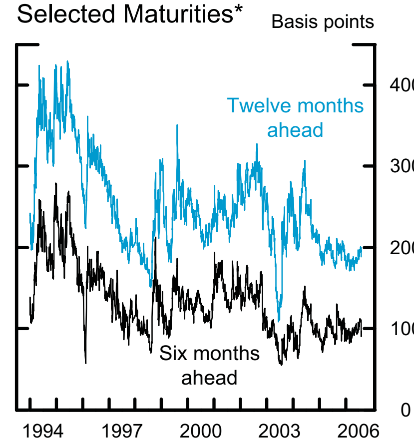



Expected Federal Funds Rate




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

Eurodollar Implied Volatility at Selected Maturities*




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

## Exhibit 2 of 4
## Leaving the Funds Rate Unchanged at this Meeting

### Case For Alternative B
(0 b.p., Upside Inflation Risks)

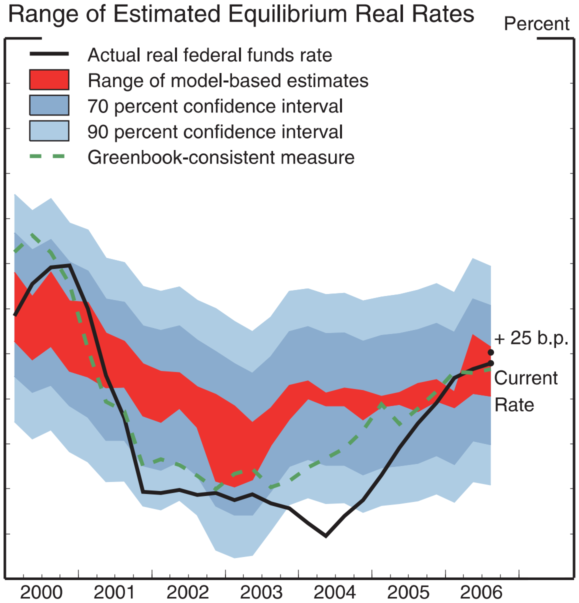
- Staff forecasts growth slightly below potential and gradually declining inflation with unchanged funds rate
- Real rates in range of estimated equilibrium values
- Consistent with some policy rules
- But significant inflation risks remain

### Staff Forecast

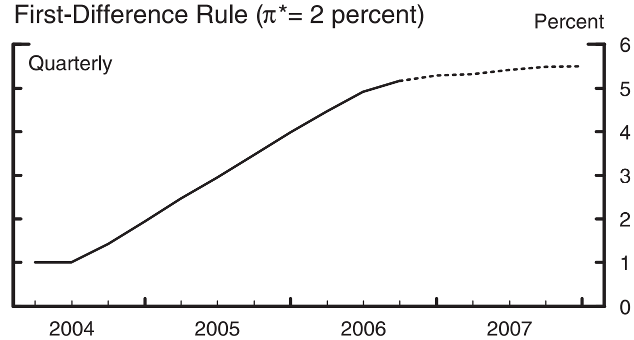
| | 2006 Q1 | 2006 Q2 | 2006 H2 | 2007 |
|---|---|---|---|---|
| Real GDP growth | 5.6 | 3.0 | 2.1 | 2.3 |
| Unemployment rate* | 4.7 | 4.7 | 4.8 | 5.2 |
| Core PCE inflation | 2.1 | 2.9 | 2.5 | 2.3 |

*Average level for last quarter of indicated period.

### Range of Estimated Equilibrium Real Rates




### First-Difference Rule (π*= 2 percent)



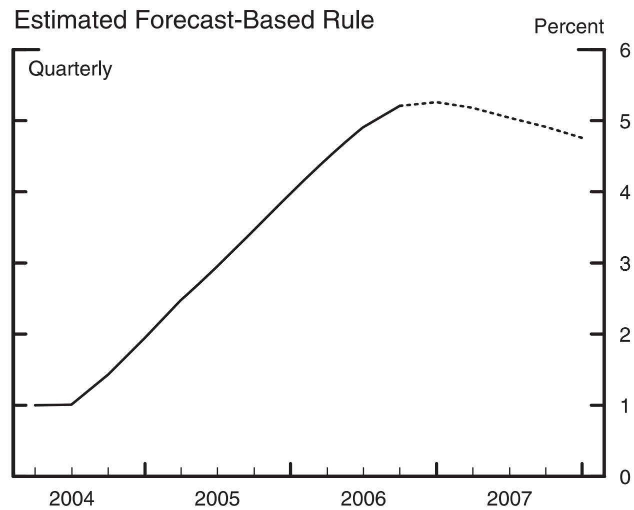

### Upside Inflation Risks

- High levels of resource utilization
- Elevated energy and commodity prices
- Potential for further increases

### Case for Alternative A
(0 b.p., No Policy Tilt)

- Emerging downside risks
  - output and employment have decelerated
  - housing may be slowing more than expected
- Consistent with staff outlook
  - optimal control simulation (π*= 2 percent)
  - estimated forecast-based policy rule

### Estimated Forecast-Based Rule



Class I FOMC - Restricted Controlled FR

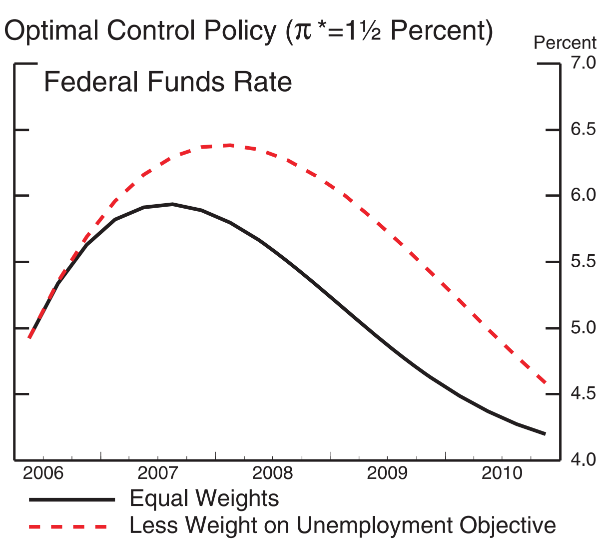
**Exhibit 3 of 4**
**Raising the Federal Funds Rate 25 b.p. at this Meeting**

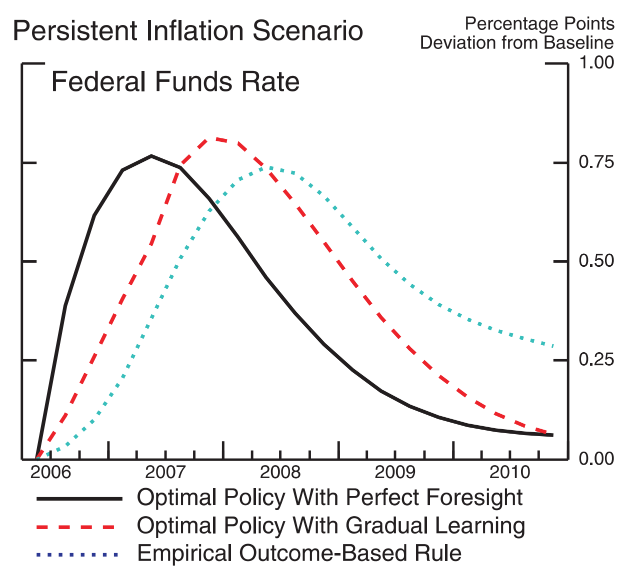
## Case For Alternative C
(+25 b.p., No Policy Tilt)

- Another firming may be seen as necessary to balance the risks
- Costs of a further increase in inflation may be high
- Signal anti-inflationary resolve

## Case For Alternative D
(+25 b.p., Upside Inflation Risks)

- Find staff forecast likely but prefer steeper downward trend to inflation
- Expect stronger aggregate demand than in Greenbook
- See greater inflation pressures than in Greenbook
  - or substantial inflation risks at a funds rate of 5-1/4 percent



# Exhibit 4 of 4

**Table 1: Alternative Language for the August FOMC Announcement**

| | Alternative A | Alternative B | Alternative C | Alternative D |
|---|---|---|---|---|
| **Policy Decision** | 1. The Federal Open Market Committee decided today to keep its target for the federal funds rate at 5¼ percent. | The Federal Open Market Committee decided today to keep its target for the federal funds rate at 5¼ percent. | The Federal Open Market Committee decided today to raise its target for the federal funds rate by 25 basis points to 5½ percent. | The Federal Open Market Committee decided today to raise its target for the federal funds rate by 25 basis points to 5½ percent. |
| **Rationale** | 2. Economic growth has moderated from its quite strong pace earlier this year, partly reflecting a gradual cooling of the housing market and the lagged effects of increases in interest rates and energy prices. | [Same as A] | [Same as A] | [Same as A] |
| | 3. Readings on core inflation have been elevated in recent months, owing in part to pass-through of increased energy and other commodity prices. However, inflation pressures seem likely to moderate over time, reflecting the cumulative effects of monetary policy actions and other factors restraining aggregate demand, ongoing productivity gains, and contained inflation expectations. | Readings on core inflation have been elevated in recent months, owing in part to the pass-through of increased energy and other commodity prices. However, inflation pressures seem likely to moderate over time, reflecting contained inflation expectations and the cumulative effects of monetary policy actions and other factors restraining aggregate demand. | Readings on core inflation have been elevated in recent months, and the high levels of resource utilization and of the prices of energy and other commodities have the potential to sustain inflation pressures. However, inflation pressures seem likely to moderate over time, reflecting contained inflation expectations and the cumulative effects of monetary policy actions and other factors restraining aggregate demand. | Readings on core inflation have been elevated in recent months. The moderation in the growth of aggregate demand and anchored inflation expectations should help to contain inflation in coming quarters. However, the high levels of resource utilization and of the prices of energy and other commodities have the potential to sustain inflation pressures. |
| **Assessment of Risk** | 4. In these circumstances, future policy adjustments will depend on the evolution of the outlook for both inflation and economic growth, as implied by incoming information. | Nonetheless, the Committee judges that some inflation risks remain. The extent and timing of any additional firming that may be needed to address these risks will depend on the evolution of the outlook for both inflation and economic growth, as implied by incoming information. | [Same as A] | The extent and timing of any additional firming that may be needed to foster a moderation in inflation pressures will depend on the evolution of the outlook for both inflation and economic growth, as implied by incoming information. |
| | 5. [None] | [None] | [None] | [None] |