

Prefatory Note

The attached document represents the most complete and accurate version available based on original files from the FOMC Secretariat at the Board of Governors of the Federal Reserve System.

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March 14, 2008

CURRENT ECONOMIC AND FINANCIAL CONDITIONS

Supplemental Notes

Prepared for the Federal Open Market Committee
by the staff of the Board of Governors of the Federal Reserve System

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The Domestic Nonfinancial Economy

Consumer Sentiment

After a sharp decline in February, the Reuters/University of Michigan index of consumer sentiment held steady in early March at a low level. Households' assessment of business conditions during the next twelve months was even more pessimistic in March than in February, but their longer-term view of the economy improved somewhat. While respondents' appraisal of buying conditions for large household goods improved slightly, their views of buying cars and homes slipped. More than 50 percent of households now expect the unemployment rate to rise over the next year.

Households' median expectation for year-ahead inflation jumped almost 1 percentage point in March to 4.5 percent from 3.6 percent in February. This is highest level recorded since the month after Hurricane Katrina. In contrast, the median expectation for inflation over the next five years edged down to 2.9 percent.

Consumer Prices

The consumer price index (CPI) was essentially unchanged in February, as energy prices fell ½ percent and core prices were unchanged. February's flat core CPI reflected a moderation in a few of the categories with high inflation recently. Prices for apparel fell after seasonal adjustment following sizable increases in recent months; lodging away from home dropped back, reversing its significant rise in January; and increases in the indexes for medical services and tenants' and owners' equivalent rent were a good bit lower than in recent months. The twelve-month increase in the core CPI stood at 2.3 percent in February, 0.4 percentage point less than the rise over the previous twelve months.

Based on our translation of the February CPI data, we estimate that both overall PCE prices and core PCE prices rose 0.2 percent last month.¹ Lodging away from home and tenants' and owners' equivalent rent receive a lower weight in PCE than they do in the CPI, and the estimate of medical services in the PCE index comes largely from the producer price index (PPI) instead of the CPI. These differences, along with other weighting differences between the CPI and PCE prices, suggest core PCE inflation in February will moderate substantially less than the CPI.

Last month's decline of ½ percent in the CPI for energy reversed only a small portion of the substantial jump in energy prices since the end of last summer. A sharp increase in natural gas prices in February was more than offset by falling prices for other energy components, particularly a decline of 2 percent in gasoline prices. However, the fall in gasoline prices appears to have been short-lived as survey data from late February and early March suggest a considerable rise in gasoline prices in the March CPI, and futures

¹ The translation from CPI prices to PCE prices is less certain than usual this month because the February PPI has not yet been released.

prices suggest further near-term price increases. For the twelve months ending in February, energy prices in the CPI increased 19 percent, compared with a decline of 1 percent over the previous twelve month period.

Despite declines in prices for meats and for fruits and vegetables, CPI food prices continued their upward climb—rising 0.4 percent in February. Prices of dairy products increased 0.8 percent, and the index for food away from home rose 0.4 percent. Food away from home, one of the least volatile indexes in the CPI, has increased at roughly a 4 percent rate for much of the past year. Overall, the CPI for food was up 4.6 percent over the twelve months ending in February, 1.5 percentage points more than over the preceding year.

The Domestic Financial Economy

March 14, 2008

Reuters/University of Michigan Survey of Consumers
Indexes of consumer sentiment
 (Not seasonally adjusted)

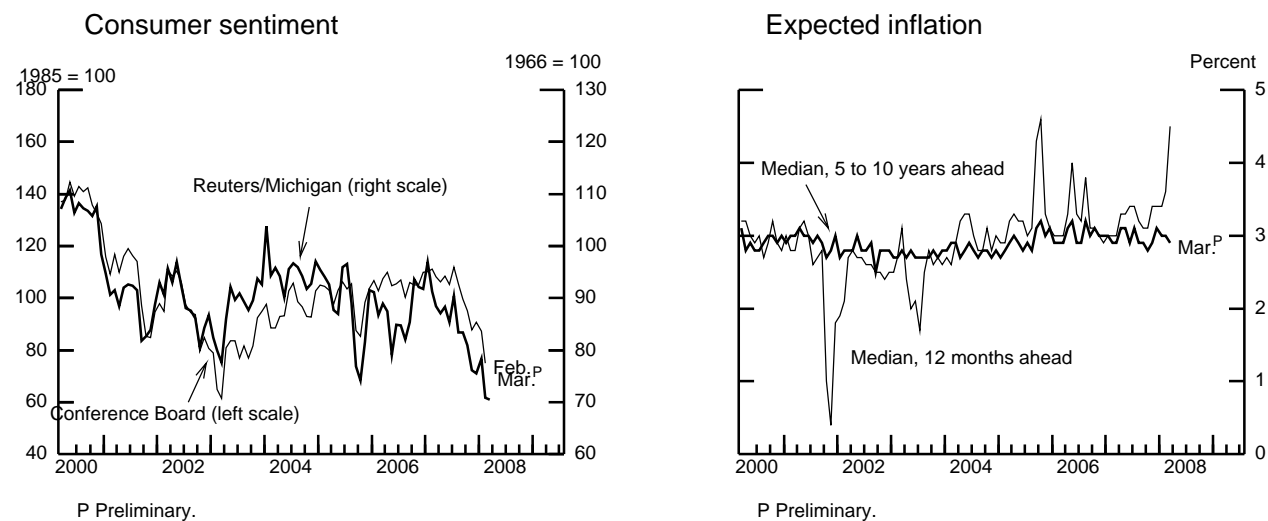
| Category | 2007 | | | | | 2008 | | |
|---|------|-------|------|------|------|------|------|-------------------|
| | Aug. | Sept. | Oct. | Nov. | Dec. | Jan. | Feb. | Mar. ^P |
| Composite of current and expected conditions ¹ | 83.4 | 83.4 | 80.9 | 76.1 | 75.5 | 78.4 | 70.8 | 70.5 |
| Current conditions ¹ | 98.4 | 97.9 | 97.6 | 91.5 | 91.0 | 94.4 | 83.8 | 84.6 |
| Expected conditions ¹ | 73.7 | 74.1 | 70.1 | 66.2 | 65.6 | 68.1 | 62.4 | 61.4 |
| Personal financial situation | | | | | | | | |
| Now compared with 12 months ago ² | 103 | 109 | 111 | 101 | 98 | 98 | 94 | 94 |
| Expected in 12 months ² | 120 | 119 | 119 | 115 | 112 | 116 | 112 | 110 |
| Expected business conditions | | | | | | | | |
| Next 12 months ² | 87 | 82 | 78 | 73 | 68 | 68 | 54 | 48 |
| Next 5 years ² | 88 | 96 | 84 | 76 | 81 | 88 | 83 | 87 |
| Appraisal of buying conditions | | | | | | | | |
| Cars | 133 | 139 | 128 | 117 | 117 | 119 | 119 | 115 |
| Large household appliances ² | 152 | 144 | 142 | 136 | 137 | 146 | 123 | 125 |
| Houses | 118 | 123 | 131 | 122 | 128 | 124 | 140 | 130 |
| Expected unemployment change - next 12 months | 131 | 127 | 130 | 128 | 139 | 141 | 141 | 145 |
| Prob. household will lose a job - next 5 years | 24 | 21 | 21 | 19 | 23 | 21 | 24 | 21 |
| Expected inflation - next 12 months | | | | | | | | |
| Mean | 4.0 | 4.0 | 3.7 | 4.3 | 4.4 | 4.0 | 3.9 | 4.6 |
| Median | 3.2 | 3.1 | 3.1 | 3.4 | 3.4 | 3.4 | 3.6 | 4.5 |
| Expected inflation - next 5 to 10 years | | | | | | | | |
| Mean | 3.4 | 3.4 | 3.1 | 3.4 | 3.5 | 3.4 | 3.4 | 3.3 |
| Median | 2.9 | 2.9 | 2.8 | 2.9 | 3.1 | 3.0 | 3.0 | 2.9 |

Note. Figures on financial, business, and buying conditions are the percent reporting 'good times' (or 'better') minus the percent reporting 'bad times' (or 'worse'), plus 100. Expected change in unemployment is the fraction expecting unemployment to rise minus the fraction expecting unemployment to fall, plus 100.

P Preliminary.

1. Feb. 1966 = 100.

2. Indicates the question is one of the five equally-weighted components of the index of sentiment.



Recent Changes in Consumer Price Indexes
(Percent change)

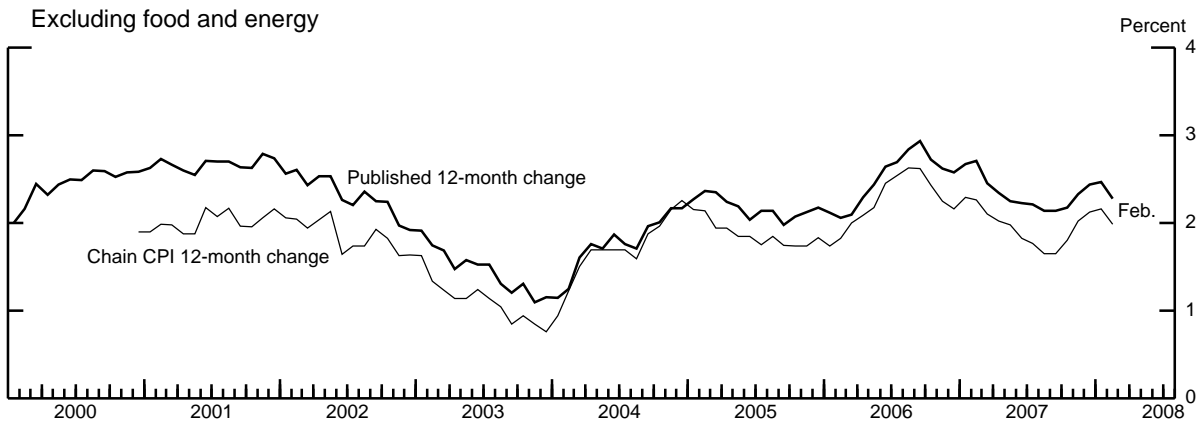
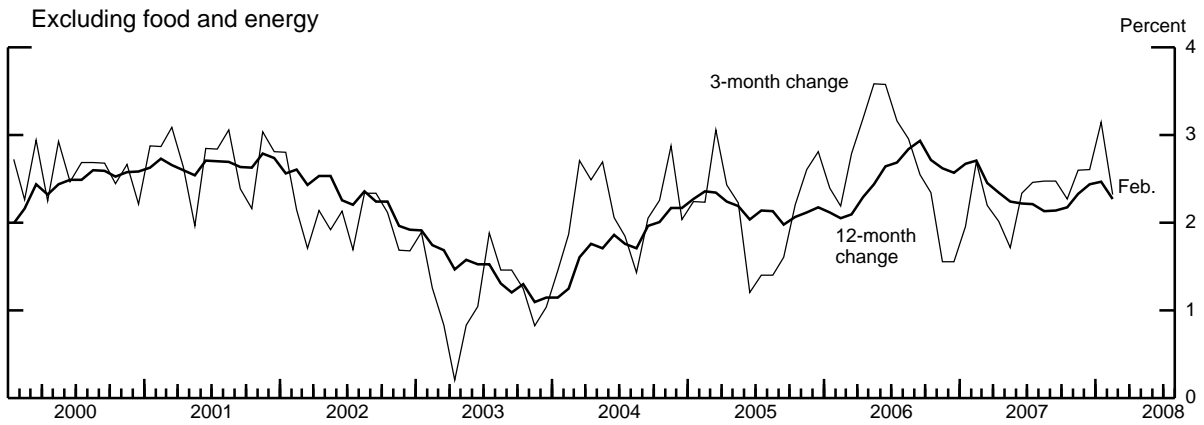
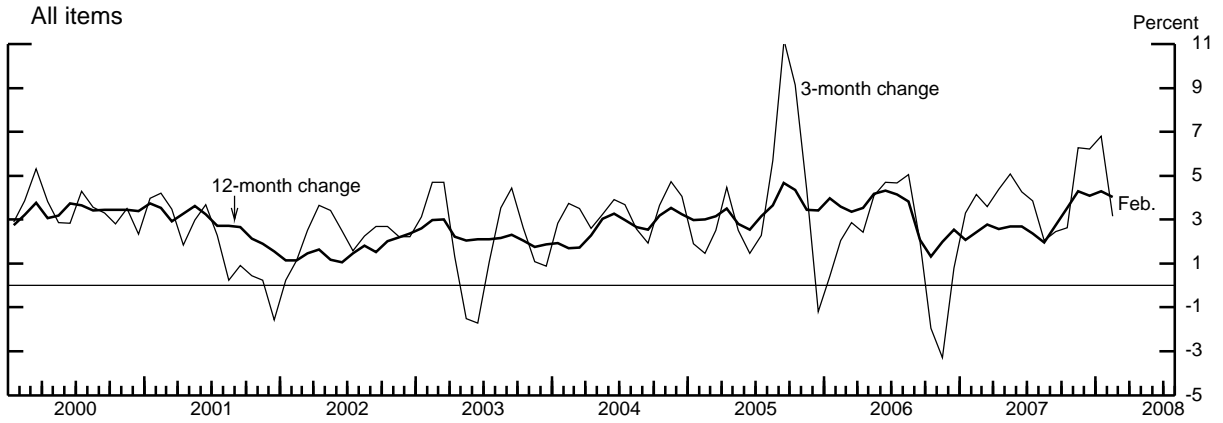
| Item | Weights ¹ | 12-month change ² | | 3-month change | | 2007 | | 2008 | |
|--------------------------------------|----------------------|------------------------------|------------|----------------|------------|--------------|-----------|-----------|-----------|
| | | Feb. 2007 | Feb. 2008 | Nov. 2007 | Feb. 2008 | Nov. | Dec. | Jan. | Feb. |
| | | | | Annual rate | | Monthly rate | | | |
| Total CPI | 100.0 | 2.4 | 4.0 | 6.3 | 3.1 | .9 | .4 | .4 | .0 |
| Food | 13.8 | 3.1 | 4.6 | 4.3 | 4.7 | .4 | .1 | .7 | .4 |
| Meats, poultry, fish, and eggs | 1.8 | 2.7 | 4.8 | 2.5 | 2.3 | .0 | -.1 | .8 | -.1 |
| Fruits and vegetables | 1.2 | 6.0 | 1.3 | 10.9 | 2.2 | 2.0 | -.3 | 2.2 | -1.3 |
| Other | 10.9 | 2.8 | 4.9 | 3.9 | 5.4 | .3 | .2 | .5 | .6 |
| Energy | 9.7 | -1.0 | 18.9 | 43.6 | 7.6 | 6.9 | 1.7 | .7 | -.5 |
| Motor Fuel | 5.5 | -1.4 | 32.7 | 77.6 | 7.8 | 11.8 | 2.8 | 1.1 | -2.0 |
| Heating oil | .4 | .6 | 33.0 | 72.4 | 21.3 | 8.9 | 2.5 | 3.7 | -1.2 |
| Natural gas | 1.1 | -9.7 | 3.5 | .2 | 21.9 | .5 | .2 | -2.2 | 7.2 |
| Electricity | 2.8 | 3.7 | 3.4 | 9.5 | -1.2 | .6 | .1 | -.1 | -.3 |
| CPI excluding food and energy | 76.5 | 2.7 | 2.3 | 2.6 | 2.3 | .2 | .2 | .3 | .0 |
| Goods ex. food and energy | 21.6 | .0 | .0 | .5 | .4 | .1 | .0 | .2 | -.1 |
| Nondurables ex. food and energy | 10.8 | 2.0 | 1.0 | 1.9 | 2.3 | .2 | .1 | .4 | .1 |
| Apparel | 3.7 | 2.1 | -1.0 | 3.4 | .8 | .6 | .1 | .4 | -.3 |
| Tobacco | .7 | 6.4 | 4.8 | 5.0 | 9.8 | .2 | .8 | 1.1 | .4 |
| Other nondurables | 6.3 | 1.4 | 1.8 | .7 | 2.4 | -.1 | .0 | .3 | .3 |
| Durables | 10.8 | -1.8 | -1.0 | -.9 | -1.4 | .1 | -.1 | -.1 | -.2 |
| New vehicles | 4.6 | -1.4 | -.8 | -.9 | -2.5 | .0 | -.1 | -.3 | -.3 |
| New cars | | -.5 | -.6 | -1.1 | -1.8 | .0 | .0 | -.3 | -.1 |
| New trucks | | -2.3 | -.7 | -.2 | -2.5 | .1 | -.1 | -.2 | -.3 |
| Used cars and trucks | 1.8 | -3.5 | 2.0 | -1.5 | 1.9 | -.2 | .2 | .2 | .0 |
| Computers | .2 | -11.5 | -11.7 | -22.2 | 1.8 | -4.1 | -.1 | 1.0 | -.5 |
| Audio/Video Equipment | .7 | -8.2 | -5.3 | -1.6 | -4.2 | -.1 | .1 | -.3 | -.9 |
| Other Durables | 3.5 | .1 | -1.4 | .9 | -1.3 | .5 | -.2 | .0 | -.2 |
| Services excluding energy | 54.9 | 3.8 | 3.2 | 3.4 | 3.1 | .3 | .3 | .4 | .1 |
| Rent of shelter | 32.3 | 4.3 | 2.9 | 3.0 | 2.7 | .3 | .3 | .4 | .0 |
| Owners' equivalent rent | 23.9 | 4.2 | 2.6 | 3.2 | 2.6 | .3 | .3 | .3 | .1 |
| Rent of primary residence | 5.8 | 4.6 | 3.7 | 4.5 | 3.6 | .4 | .4 | .3 | .2 |
| Lodging away from home | 2.6 | 4.3 | 3.5 | -.9 | 1.0 | -.2 | .3 | 1.1 | -1.2 |
| Services ex. energy and shelter | 22.6 | 3.0 | 3.5 | 3.8 | 3.6 | .3 | .3 | .4 | .1 |
| Medical services | 4.6 | 5.1 | 5.0 | 5.8 | 3.9 | .4 | .3 | .6 | .1 |
| Tuition and other school fees | 2.7 | 6.0 | 5.5 | 6.1 | 5.8 | .5 | .5 | .6 | .3 |
| Air fares | .7 | 1.4 | 7.6 | 18.8 | 7.4 | 1.9 | 1.2 | .8 | -.3 |
| Other services | 14.5 | 1.9 | 2.5 | 2.1 | 3.0 | .2 | .3 | .3 | .1 |
| Memo: | | | | | | | | | |
| Chained CPI | 100.0 | 2.2 | 3.7 | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| All items less food and energy | 77.6 | 2.3 | 2.0 | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |

1. Relative importance weights for December 2007, which are based on 2005-2006 expenditure weights.

For the chained CPI, the 2005-2006 expenditure weights are shown.

2. Not seasonally adjusted.

Consumer Price Index (Percent change at annual rate)



Commercial Bank Credit

(Percent change, annual rate, except as noted; seasonally adjusted)

| Type of credit | 2006 | H1 2007 | Q3 2007 | Q4 2007 | Jan. 2008 | Feb. 2008 ^p | Level ¹ Feb. 2008 ^p |
|---------------------------|------|------------|------------|------------|--------------|---------------------------|--|
| Total | 9.6 | 9.4 | 12.4 | 8.9 | 4.1 | 6.7 | 8,797 |
| <i>Loans²</i> | | | | | | | |
| Total | 10.9 | 10.2 | 12.6 | 11.8 | 12.4 | 4.4 | 6,745 |
| To businesses | | | | | | | |
| Commercial and industrial | 16.5 | 10.0 | 24.3 | 29.2 | 12.6 | 1.6 | 1,428 |
| Commercial real estate | 13.7 | 9.6 | 12.4 | 8.2 | 5.9 | 10.7 | 1,601 |
| To households | | | | | | | |
| Residential real estate | 7.0 | 10.7 | 2.6 | 1.0 | 5.3 | 4.5 | 1,890 |
| Revolving home equity | 1.4 | 2.0 | 6.7 | 11.9 | 10.9 | 5.9 | 489 |
| Other | 9.1 | 13.6 | 1.3 | -2.6 | 3.3 | 4.0 | 1,401 |
| Consumer | 5.9 | 6.4 | 10.5 | 7.6 | 12.7 | 1.3 | 813 |
| Originated ³ | 6.9 | 5.2 | 10.3 | 7.4 | 16.0 | 4.9 | 1,222 |
| Other ⁴ | 11.8 | 14.1 | 19.6 | 18.9 | 35.5 | .7 | 1,014 |
| <i>Securities</i> | | | | | | | |
| Total | 6.1 | 6.9 | 11.7 | .2 | -22.5 | 14.4 | 2,052 |
| Treasury and agency | 1.9 | -4.2 | 5.6 | -22.3 | -21.7 | 4.7 | 1,085 |
| Other ⁵ | 13.2 | 23.8 | 19.9 | 29.3 | -23.6 | 25.6 | 967 |

Note. Yearly annual rates are Q4 to Q4; quarterly and monthly annual rates use corresponding average levels. Data have been adjusted to remove the effects of mark-to-market accounting rules (FIN 39 and FAS 115), the consolidation of certain variable interest entities (FIN 46), the adoption of fair value accounting (FAS 159), and the effects of sizable thrift-to-bank and bank-to-thrift structure activity in October 2006, March 2007, and October 2007. Data also account for breaks caused by reclassifications.

1. Billions of dollars. Pro rata averages of weekly (Wednesday) levels.

2. Excludes interbank loans.

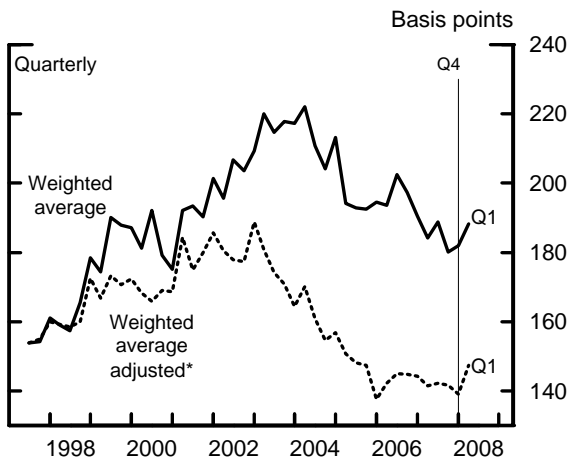
3. Includes an estimate of outstanding loans securitized by commercial banks.

4. Includes security loans and loans to farmers, state and local governments, and all others not elsewhere classified. Also includes lease financing receivables.

5. Includes private mortgage-backed securities, securities of corporations, state and local governments, foreign governments, and any trading account assets that are not Treasury or agency securities, including revaluation gains on derivative contracts.

p Preliminary.

C&I Loan Rate Spreads

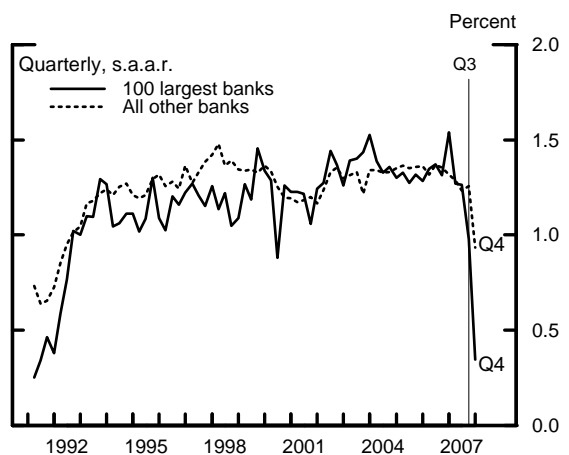


Note. Spreads over market interest rate on an instrument of comparable maturity on loans less than \$25 million (2006\$).

*Adjusted for changes in nonprice loan characteristics.

Source. Survey of Terms of Business Lending.

Return on Assets for Commercial Banks



Source. Call Report.

III-T-1
Selected Financial Market Quotations
(One-day quotes in percent except as noted)

| Instrument | 2006 | 2007 | 2008 | | Change to Mar. 13 from selected dates (percentage points) | | |
|---|---------|----------|---------|---------|---|------------------|-----------------|
| | June 29 | Sept. 17 | Jan. 29 | Mar. 13 | 2006 June 29 | 2007 Sept. 17 | 2008 Jan. 29 |
| <i>Short-term</i> | | | | | | | |
| FOMC intended federal funds rate | 5.25 | 5.25 | 3.50 | 3.00 | -2.25 | -2.25 | -.50 |
| Treasury bills ¹ | | | | | | | |
| 3-month | 4.88 | 4.05 | 2.23 | 1.33 | -3.55 | -2.72 | -.90 |
| 6-month | 5.06 | 4.15 | 2.29 | 1.47 | -3.59 | -2.68 | -.82 |
| Commercial paper (A1/P1 rates) ² | | | | | | | |
| 1-month | 5.27 | 5.23 | 3.08 | 2.61 | -2.66 | -2.62 | -.47 |
| 3-month | 5.37 | 5.25 | 3.02 | 2.80 | -2.57 | -2.45 | -.22 |
| Large negotiable CDs ¹ | | | | | | | |
| 3-month | 5.47 | 5.52 | 3.22 | 2.78 | -2.69 | -2.74 | -.44 |
| 6-month | 5.59 | 5.36 | 3.17 | 2.82 | -2.77 | -2.54 | -.35 |
| Eurodollar deposits ³ | | | | | | | |
| 1-month | 5.33 | 5.55 | 3.30 | 2.80 | -2.53 | -2.75 | -.50 |
| 3-month | 5.49 | 5.60 | 3.30 | 2.85 | -2.64 | -2.75 | -.45 |
| Bank prime rate | 8.25 | 8.25 | 6.50 | 6.00 | -2.25 | -2.25 | -.50 |
| <i>Intermediate- and long-term</i> | | | | | | | |
| U.S. Treasury ⁴ | | | | | | | |
| 2-year | 5.26 | 4.12 | 2.25 | 1.66 | -3.60 | -2.46 | -.59 |
| 5-year | 5.15 | 4.18 | 2.89 | 2.52 | -2.63 | -1.66 | -.37 |
| 10-year | 5.28 | 4.58 | 3.88 | 3.79 | -1.49 | -.79 | -.09 |
| U.S. Treasury indexed notes ⁵ | | | | | | | |
| 5-year | 2.51 | 2.04 | .78 | .31 | -2.20 | -1.73 | -.47 |
| 10-year | 2.61 | 2.15 | 1.39 | 1.18 | -1.43 | -.97 | -.21 |
| Municipal general obligations (Bond Buyer) ⁶ | 4.71 | 4.46 | 4.29 | 4.94 | .23 | .48 | .65 |
| Private instruments | | | | | | | |
| 10-year swap | 5.81 | 5.17 | 4.26 | 4.19 | -1.62 | -.98 | -.07 |
| 10-year FNMA ⁷ | 5.59 | 5.01 | 4.26 | 4.57 | -1.02 | -.44 | .31 |
| 10-year AA ⁸ | 6.20 | 6.05 | 5.66 | 6.16 | -.04 | .11 | .50 |
| 10-year BBB ⁸ | 6.74 | 6.46 | 6.39 | 6.75 | .01 | .29 | .36 |
| 10-year high yield ⁸ | 8.74 | 8.95 | 9.85 | 10.40 | 1.66 | 1.45 | .55 |
| Home mortgages (FHLMC survey rate) | | | | | | | |
| 30-year fixed | 6.78 | 6.34 | 5.68 | 6.13 | -.65 | -.21 | .45 |
| 1-year adjustable | 5.82 | 5.65 | 5.05 | 5.14 | -.68 | -.51 | .09 |

| Stock exchange index | Record high | | 2007 | 2008 | | Change to Mar. 13 from selected dates (percent) | | |
|----------------------|-------------|---------|----------|---------|---------|---|------------------|-----------------|
| | Level | Date | Sept. 17 | Jan. 29 | Mar. 13 | Record high | 2007 Sept. 17 | 2008 Jan. 29 |
| Dow Jones Industrial | 14,165 | 10-9-07 | 13,403 | 12,480 | 12,146 | -14.25 | -9.38 | -2.68 |
| S&P 500 Composite | 1,565 | 10-9-07 | 1,477 | 1,362 | 1,315 | -15.95 | -10.91 | -3.44 |
| Nasdaq | 5,049 | 3-10-00 | 2,582 | 2,358 | 2,264 | -55.16 | -12.32 | -4.01 |
| Russell 2000 | 856 | 7-13-07 | 776 | 705 | 680 | -20.57 | -12.39 | -3.61 |
| Wilshire 5000 | 15,807 | 10-9-07 | 14,839 | 13,740 | 13,267 | -16.07 | -10.60 | -3.44 |

1. Secondary market.
2. Financial commercial paper.
3. Bid rates for Eurodollar deposits collected around 9:30 a.m. eastern time.
4. Derived from a smoothed Treasury yield curve estimated using off-the-run securities.
5. Derived from a smoothed Treasury yield curve estimated using all outstanding securities and adjusted for the carry effect.
6. Most recent Thursday quote.
7. Constant-maturity yields estimated from Fannie Mae domestic noncallable coupon securities.
8. Derived from smoothed corporate yield curves estimated using Merrill Lynch bond data.

NOTES:

June 29, 2006, is the day the most recent policy tightening ended.
September 17, 2007, is the day before the most recent policy easing began.
January 29, 2008, is the day before the most recent FOMC announcement.