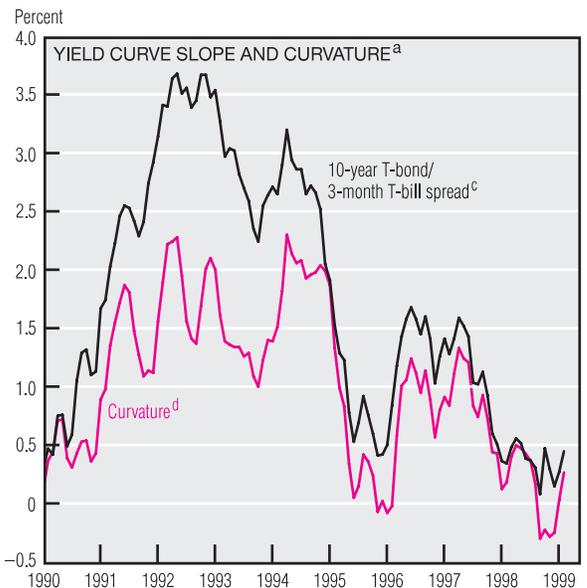
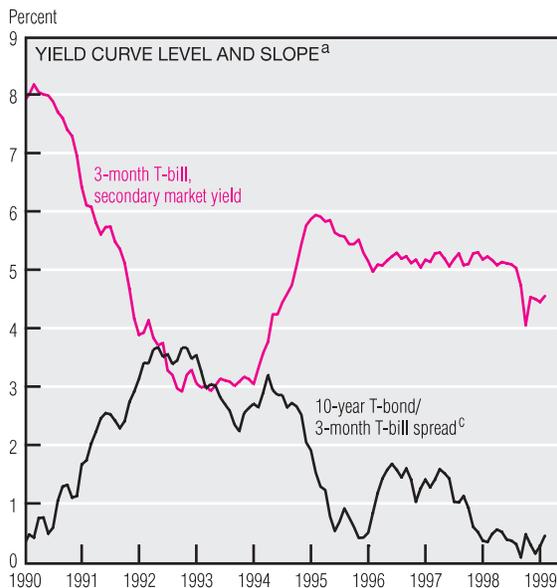
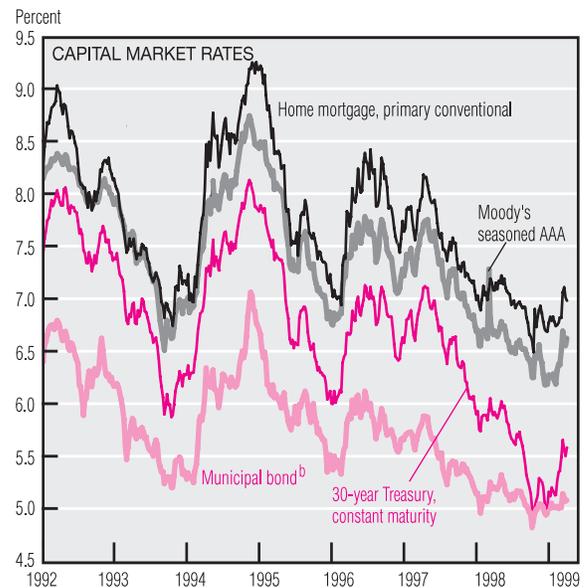
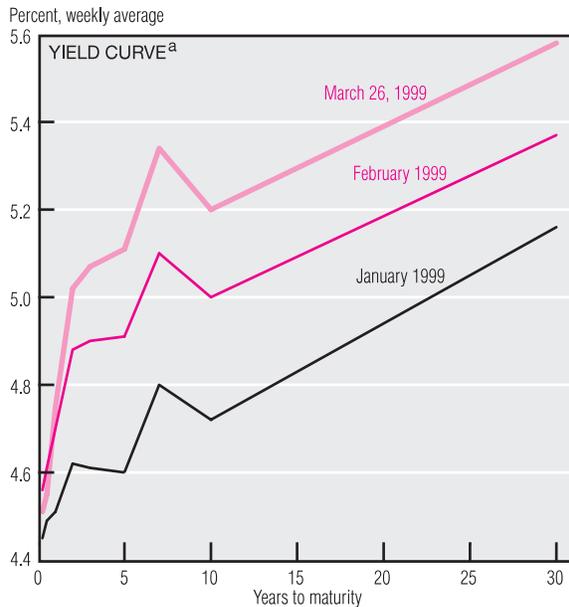


# Interest Rates



a. All instruments are Treasury constant-maturity series.

b. Bond Buyer Index, general obligation, 20 years to maturity, mixed quality.

c. 10-year Treasury bond yield minus secondary market 3-month Treasury bill yield.

d. Curvature equals the spread between the 5-year Treasury note yield and the secondary market 3-month Treasury bill yield, minus the spread between the 10-year Treasury bond yield and the 5-year Treasury note yield.

SOURCE: Board of Governors of the Federal Reserve System, "Selected Interest Rates," *Federal Reserve Statistical Release*, H.15.

The yield curve has steepened since last month, as 3- and 6-month rates fell and all others rose. The 3-year, 3-month spread increased from 34 to 56 basis points; the 10-year, 3-month spread grew from 44 to 69 basis points. Some have attributed the steepening to anticipation of a Federal Reserve hike in the federal funds rate. However, it is hard to see how such anticipation would accord with the drop in short rates, since Fed hikes usually flatten the curve. Long rates have risen in sync; the spread between 30-year and 10-year rates has barely nudged up, from 37 to 38 basis points.

Since the beginning of the year, longer-term capital market rates have moved broadly upward. The exception seems to be municipals, which have changed very little. All have shown a gradual decrease in spread over 30-year Treasuries. This trend becomes even more pronounced if taken back to October, when spreads peaked during the flight-to-quality episode that followed the ruble's collapse. Spreads have not returned to their precrisis level, perhaps because of a rational market assessment that crises are still possible.

Three factors account for much of the movement in the yield curve: level, slope, and curvature. Compared with the past decade, the current level is high, though the slope and curvature are relatively low. Level and slope show an inverse relationship: Rates move together, but long rates move up and down less than short ones. Slope and curvature show a more positive relationship. A given decrease in short rates, for example, decreases 5-year rates, but not as far, and leads to an even smaller drop in 10- and 30-year rates.