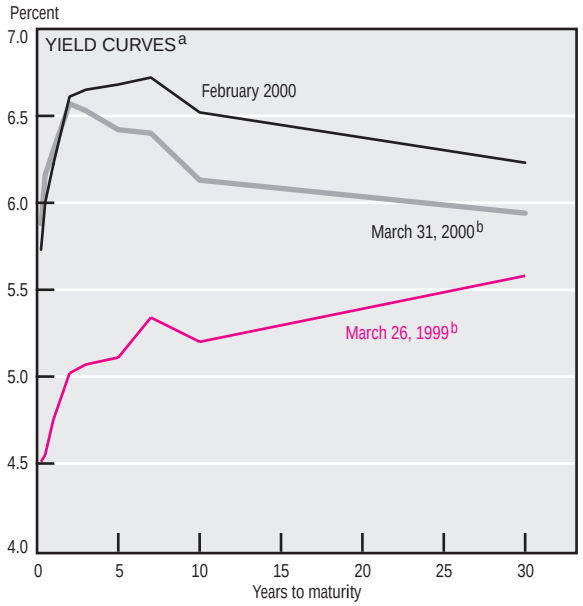
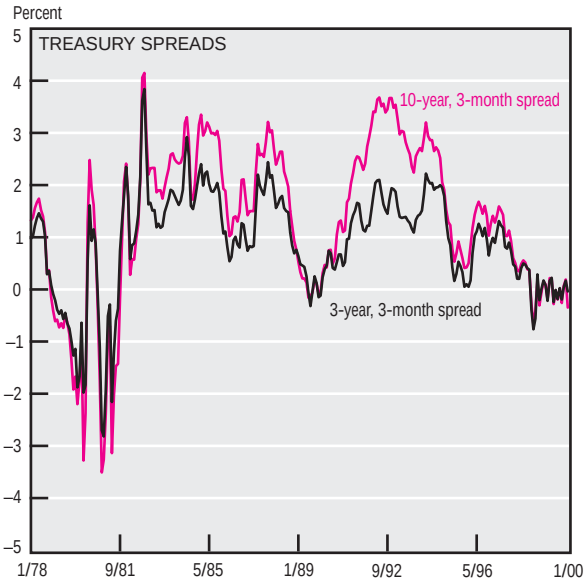
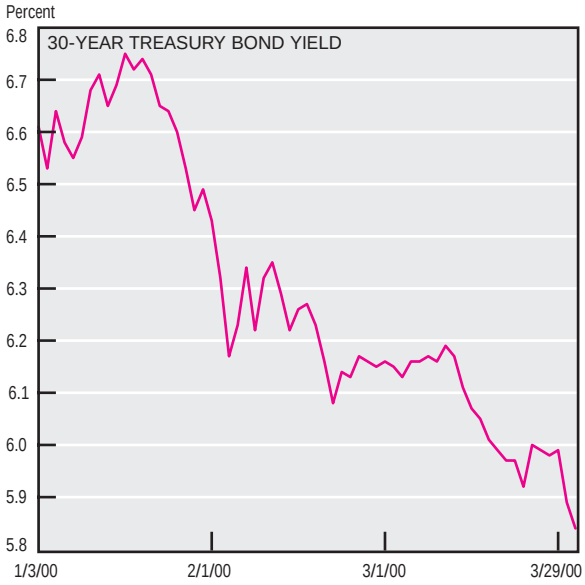
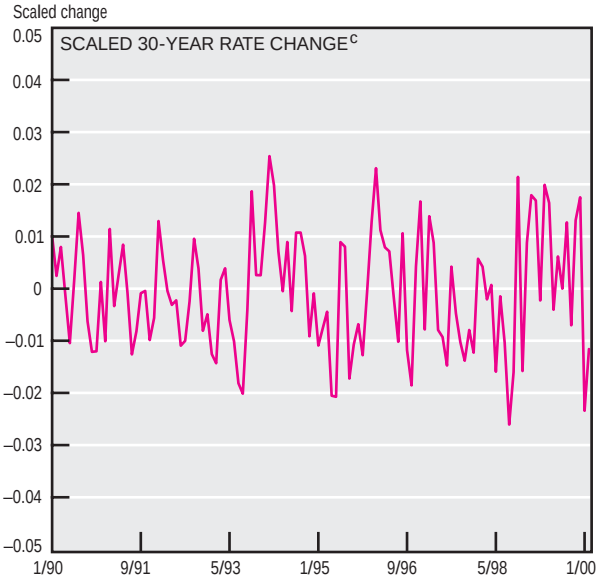
Interest Rates









a. All yields are from constant-maturity series.
b. Weekly averages.
c. Monthly change in rate, scaled by level raised to the 1.5^{th} power.
SOURCES: Board of Governors of the Federal Reserve System, "Selected Interest Rates," *Federal Reserve Statistical Releases,* H.15.

The yield curve continues to show a humped shape, with long rates falling since last month. The peak of the curve has moved toward a shorter maturity, to the two-year yield from last month's peak at seven years. It is interesting to see that the spreads that historically have predicted recessions most accurately remain positive, at least for the Treasury constant-maturity series. The 3-year, 3-month spread stands at 65 basis points (bp) and the 10-year, 3-month spread at 25 bp.

Recent moves—the Federal Open Market Committee raising the federal funds rate and the Treasury retiring longer-term bonds—have caused some apprehension about increased volatility in the fixed-income markets. Indeed, the recent plunge of 90 bp in the 30-year yield does look impressive. Placed in a historical context, however, the evidence for increased volatility is less overwhelming. A look at spreads indicates that recent movements have been in a relatively narrow range, nothing at all like the movements of the late 1970s, or even the tightening of 1994–95.

Interest-rate volatility depends on the level of interest rates because high rates show larger fluctuations than low ones (for example, low rates cannot fall below zero). Consequently, scaling those measures can provide a better measure of the changeability of interest rates. Furthermore, because the relation between levels and changes can be nonlinear, the scaling should be nonlinear as well. Scaled changes in 30-year rates over the past decade show slight evidence that rates have entered a more volatile period, at least relative to the early 1990s.