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- 3 To Conclude: Keep Inflation Low and, in Principle, Eliminate It
Thomas C. Melzer

The U.S. economy performed well across the board in 1997, with low unemployment, robust economic growth, and the lowest sustained inflation in decades. Nevertheless, the current framework for monetary policymaking does not ensure that inflation is down for the count, says Federal Reserve Bank of St. Louis president Thomas C. Melzer in a speech reprinted here. In this speech, Melzer argues that the Federal Reserve ought to secure the best environment for economic growth by adopting multi-year inflation targets to reduce the trend rate of inflation and keep inflation low.

- 9 The New Risk Management: The Good, the Bad, and the Ugly
Philip H. Dybvig and William J. Marshall

At one time, risk management was limited to insurance and the avoidance of lawsuits and accidents. The new risk management also includes using tools developed for pricing financial options for the management of financial risks within the firm. Trading in financial markets based on these tools can insulate companies from the risk of changes in interest rates, input prices, or currency fluctuations. In this article Philip H. Dybvig and William J.

Marshall introduce the new risk management and the policy choices firms should be considering.

- 23 Recent Developments in Wholesale Payments Systems
William R. Emmons

Wholesale payments and settlement systems in G-10 countries have undergone significant change in recent years. Notably, central banks have sought to increase the safety and reliability of these systems. In this article, William R. Emmons describes two approaches that have been pursued. Significant progress has been achieved in strengthening (or "securing") many existing payments system arrangements based on net settlement. In addition, many new gross settlement systems have been created, and existing ones have been improved. The article also explores why private-sector financial institutions often prefer to upgrade and secure existing net settlement systems rather than moving to gross settlement systems, despite central bank preferences for the latter.

- 45 Using Federal Funds Futures Rates to Predict Federal Reserve Actions
John C. Robertson and Daniel L. Thornton

The federal funds futures rate naturally embodies the market's expectation of the average behavior of the federal funds rate. But, as John C. Robertson and Daniel L. Thornton explain, analysts cannot attempt to identify Fed policy from the behavior of the federal funds futures rate without making somewhat arbitrary additional assumptions. The authors investigate the predictive accuracy of a rule based on the federal funds futures rate from October 1988 through

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August 1997 using an assumption that is sufficient for partially identifying when the market is expecting a Fed action but not for predicting the magnitude of the action. Their forecasting rule correctly predicts a target change at the one-month horizon only about one-third of the time. They conclude that more research is needed, especially in light of the FOMC's recent practice of disclosing policy decisions immediately after FOMC meetings.

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