



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The System Open Market Account's domestic securities holdings totaled \$2,457.5 billion as of April 20, 2011, up \$21.7 billion from the prior release on April 13. The portfolio remained concentrated in Treasury coupon securities, which stood at \$1,320.8 billion, alongside \$933.2 billion in agency mortgage-backed securities and a comparatively small \$18.4 billion in Treasury bills. The week-over-week increase was consistent with the ongoing asset purchase program running through the second quarter of 2011. It should be noted that this account covers SOMA securities holdings only — total size, composition, and the change from the prior release — and does not encompass repo or reverse-repo operation results, for which no point-in-time-safe data source is currently available.

STAFF REVIEW OF THE ECONOMIC SITUATION

Underlying inflation remained well below the Committee's longer-run objective. Core PCE prices rose 0.69 percent over the prior twelve months, far short of the 2.0 percent target. Labor market slack was pronounced: the unemployment rate stood at 8.8 percent against an estimated natural rate of 5.2 percent, and initial jobless claims at 412,000 remained elevated. The Chicago Fed National Activity Index at -0.48 pointed to growth running below its historical trend. The Employment Cost Index reading of 114.7 gave no indication of accelerating labor compensation.

The Beige Book material for the Seventh District described continued expansion in February and March, though contacts' optimism was tempered by elevated uncertainty tied to recent global events. Consumer and business spending both increased, manufacturing production expanded, and hiring rose, with contacts adding temporary and permanent workers and manufacturers reiterating difficulty finding appropriately skilled labor. Against these gains, construction remained subdued, and single-family homebuilders anticipated a slower-than-expected spring building season with a drop in the contract conversion rate. Credit conditions 'continued to improve.' The report flagged 'some further pass-through of higher commodity prices to downstream prices,' with a few contacts building raw-material inventories in anticipation of further price increases, and noted that potential production disruptions stemming from events in Japan and the effect of rising gas prices on demand added considerable uncertainty, particularly for the auto sector.

STAFF REVIEW OF THE FINANCIAL SITUATION

Financial conditions were benign and showed no sign of stress. The financial stress index stood at 0.1251, a low reading, and the VIX at 15.07 indicated subdued equity volatility. Credit risk premia were contained, with the Baa corporate spread at 2.55, consistent with the Beige Book's account of improving credit conditions. The Treasury yield curve was steeply positive, with the 10-year/2-year



spread at 2.74, giving no recession signal. At the short end, the 3-month T-bill spread relative to the current policy rate was -0.055, essentially flat and consistent with market participants pricing no near-term change in the target range.

STAFF ECONOMIC OUTLOOK

The forward-looking indicators available to the staff pointed to conditions consistent with maintaining the current policy stance rather than moving off it. The estimated neutral real rate (r^*) of 0.844, combined with core inflation running near 0.7 percent, implied a neutral nominal rate barely above zero — leaving the current target range close to appropriately calibrated even before accounting for the effective lower bound. Inflation momentum was essentially flat to slightly negative at -0.07, giving no signal of building price pressure despite the commodity pass-through noted in regional reporting. Unemployment momentum at -0.45 suggested the labor market was improving, but only gradually, and from a level far above the estimated natural rate.

The reference rules cohered around this reading. The Taylor rule, Balanced Approach rule, First-Difference rule, and ELB-adjusted rule each returned 0 basis points, and the framework judged the reference rules reliable this meeting. Taken together, the low neutral rate, the absence of inflation acceleration, the wide but slowly narrowing employment gap, and the uniform rule outputs projected a path in which accommodation remains warranted, with no near-term case for either removing support or, given the lower-bound constraint, adding to it conventionally.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

All five participants entered the discussion favoring an unchanged target range of 0.0 to 0.25 percent, and their reasoning, developed across four rounds, converged on that outcome while reflecting distinct emphases. The participant most attentive to inflation risk framed the central question as whether price pressures justified tightening and concluded they did not: with core PCE at 0.69 percent, this was undershooting rather than overshooting the objective. This participant took seriously the Beige Book's report of commodity pass-through and of firms building raw-material inventories ahead of expected price increases, describing it as a genuine warning to keep on the radar, but judged that the underlying core measure remained subdued and that the enormous slack — 8.8 percent unemployment against a 5.2 percent natural rate, contained ECI readings, and elevated claims — sharply limited any wage-price spiral risk. The inflation momentum reading of -0.07 reinforced the view that no accelerating trend demanded action, and this participant stated that hiking now on commodity fears would risk choking a fragile, below-trend recovery, while pledging to reassess should core measures begin rising.



The participant most focused on the labor market emphasized the 3.6-point shortfall of unemployment from its natural rate as the central concern, one that ordinarily would call for maximum accommodation. This participant stressed that the target range already sat at the effective floor and that the ongoing asset purchase program continued to provide support beyond the policy rate, so that holding represented the maximally accommodative feasible stance rather than complacency. Claims at 412,000 and the Chicago Fed index at -0.48 were cited as evidence that the labor recovery remained fragile and below trend; the unemployment momentum of -0.45 was read as improvement, but slow improvement, such that premature tightening would put that gradual healing at risk. This participant noted that even a rule weighting employment heavily returned 0 basis points at the floor.

The participant attentive to financial stability began from the stress and credit indicators, observing that the stress index at 0.1251, the VIX at 15.07, and the Baa spread at 2.55 all pointed to orderly, non-stressed conditions, and that the Beige Book's finding of improving credit conditions indicated the credit channel was healing rather than deteriorating. This participant saw no financial-stability case for tightening and cautioned that abruptly altering course mid-program could itself widen spreads and destabilize still-fragile conditions without an inflation justification. The participant weighting market-implied pricing pointed to the 3-month T-bill spread of -0.055 as evidence that markets expected no near-term move and to the steep 2.74 curve slope as signaling no recession fear but only gradual eventual normalization, concluding that front-end pricing was anchored and consistent with continued accommodation.

The data-dependent participant read both mandate legs as pointing the same direction — inflation too low, slack too high — and emphasized that all four reference rules returned 0 basis points with the framework judging them reliable. This participant found the Taylor rule's logic most persuasive for disciplining against overreaction to transitory commodity moves, and noted that the low r^* of 0.844 paired with sub-target inflation placed the neutral nominal rate barely above zero, reinforcing the lower-bound constraint. Across the rebuttal exchanges, no participant presented evidence that shifted another's emphasis; several observed that even the participant most inclined toward vigilance on inflation conceded the data did not trigger a hike, which was taken as confirmation that the convergence was genuine rather than forced. Participants generally judged that the current stance was well-calibrated: neither too tight nor too loose given subdued core inflation, wide labor slack, calm markets, and the effective lower bound. Several identified watch items for future meetings — any widening of the Baa spread, spikes in volatility, acceleration in core PCE or the ECI, and the evolving effects of the Japan disruptions and gas prices — while agreeing that none of these warranted action now.

COMMITTEE POLICY ACTIONS



In the predictive round, all five members expected the Committee to maintain the federal funds target range at 0.0 to 0.25 percent, a unanimous 0-basis-point vote (5 of 5 for no change). On the deterministic policy engine's recommendation of 0 basis points, the Committee was in full agreement: all five members endorsed the recommendation as-is, with no members declining and none registering partial agreement. The predictive expectation and the optimal-side outcome thus coincided, with each member — the inflation hawk, the labor market dove, the financial stability voice, the data-dependent centrist, and the market signal realist — endorsing the recommendation to hold.