



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The desk reported that System Open Market Account holdings of domestic securities totaled \$2,595.2 billion as of November 30, 2011, the most recent release available at the point-in-time-safe cutoff. Within that total, Treasury notes and bonds accounted for \$1,575.4 billion, Treasury bills for \$18.4 billion, and agency mortgage-backed securities for \$827.1 billion. Holdings declined by \$7.3 billion relative to the prior release of November 23. The staff noted that this account covers SOMA securities holdings only — total size, composition, and week-over-week change — and does not encompass repo or reverse-repo operation results, for which no point-in-time-safe data source is presently available; accordingly, the review of open market operations here is confined to the securities portfolio.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reviewed indicators pointing to continued but modest expansion. Core PCE inflation stood at 1.56 percent on a year-over-year basis, below the 2.0 percent objective. The unemployment rate was 8.6 percent, well above the estimated natural rate of 5.2 percent, leaving a gap of roughly 3.4 percentage points. Initial jobless claims were near 402,000, and the Employment Cost Index registered 115.6. The Chicago Fed National Activity Index came in at -0.13, consistent with growth somewhat below trend. M2 stood at \$9,607.5 billion.

The Beige Book described overall activity as increasing at a slow to moderate pace across all Districts except St. Louis, which reported a decline. Consumer spending rose modestly on balance, with several Districts noting gains in retail sales, increases in motor vehicle sales, and signs of strength in tourism; a few Districts noted that colder weather had spurred apparel sales. Manufacturing expanded at a steady pace across most of the country, and activity in energy and mining increased. Residential real estate remained sluggish and commercial real estate lackluster, with single-family home construction weak and commercial construction slow, even as home refinancing grew more rapidly. Hiring was generally subdued, though some firms with open positions reported difficulty finding qualified applicants. Wages and salaries remained stable, overall price increases remained subdued, and some cost pressures were reported to have eased.

STAFF REVIEW OF THE FINANCIAL SITUATION

Financial conditions were characterized as strained but functioning. The financial stress index stood at 0.297, described as elevated but not extreme, and the VIX was 28.13, reflecting persistent market anxiety consistent with lingering global financial strains. The Baa corporate spread of 3.26 pointed to meaningful credit-cost stress, with borrowers still facing elevated financing costs. The 10-year/2-year Treasury spread was 1.83, remaining clearly upward-sloping and not signaling an imminent recession.



The 3-month T-bill spread relative to the current target rate was -0.105, with the bill yielding below the current range midpoint, suggestive of flight-to-safety in the short end and consistent with market pricing of no near-term tightening. With the federal funds target range already at 0.0 to 0.25 percent, there was little conventional room to ease further through the policy rate.

STAFF ECONOMIC OUTLOOK

The staff projection drew on the reference-rule framework and the small set of forward-looking quantities available. The estimated neutral rate (r^*) used in the analysis was 0.262, a very low figure implying that even a target range of 0.0 to 0.25 percent is only modestly accommodative in real terms and that the scope for additional conventional easing is effectively exhausted. Inflation momentum was estimated at a modest 0.165 and unemployment momentum at -0.05, the latter indicating only glacial improvement in the labor market. Taken together, these figures suggest a path in which inflation remains near but below the 2.0 percent objective without accelerating, and in which the unemployment gap narrows only very slowly from its current wide level.

All four reference rules — the Taylor rule, the Balanced Approach rule, the First-Difference rule, and the ELB-adjusted rule — pointed to a policy rate of 0 basis points, and the framework judged the rules reliable for this meeting. The convergence of rules with differing structures, combined with a very low neutral rate and a binding effective lower bound, implies that unconstrained prescriptions would call for rates near or below zero, floored at the current range. The projection therefore points to a continuation of accommodative conditions, with no near-term impetus toward tightening implied by the momentum terms or the credit and volatility readings, and no feasible avenue for further conventional easing given the floor.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their initial predictive positions, all five participants arrived independently at no change to the target range, though the reasoning behind that common conclusion varied considerably by lens. The member most attentive to inflation risk emphasized that core PCE at 1.56 percent sits clearly below the 2.0 percent objective rather than above it, that cost pressures were reportedly easing, and that wage data — stable wages and salaries across Districts and a benign ECI reading of 115.6 — offered no sign of wage-push inflation. From that vantage there was simply no inflation case demanding tightening, and no room and no reason to cut further from the floor.

The participant weighting labor-market conditions most heavily stressed the scale of remaining slack: unemployment at 8.6 percent against a 5.2 percent natural rate, elevated claims near 402,000, and subdued hiring. This member's instinct favored maximum accommodation and expressed sympathy



with a prior dissent that had favored additional support. The operative constraint, however, was the effective lower bound: with the range already at 0.0 to 0.25 percent, that desire could not be expressed through the funds rate itself. The financial-stability voice reached the same hold from a third direction, citing the Baa spread of 3.26, the VIX at 28.13, and the stress index at 0.297 as evidence of fragile conditions in which any tightening would risk widening spreads, while the negative T-bill spread and upward-sloping curve indicated markets already priced near-zero rates with no imminent recession. The data-dependent centrist read both mandate legs — below-target inflation and elevated unemployment — as pointing the same way, and the market-signal realist observed that the T-bill spread of -0.105 and the positively sloped curve were consistent with holding rather than a move in either direction.

In the rebuttal round, no participant was moved off the initial position; several noted that the convergence itself, reached from distinct starting points, strengthened confidence in the hold. A recurring theme was the distinction between comfort and constraint: the labor-market participant was explicit that a vote to hold reflected the binding floor, not any acceptance of 8.6 percent unemployment, and that whatever additional support might be warranted would come through existing programs and the guidance already committed through the previously stated horizon rather than through the target range.

Turning to the optimal-framework reasoning, participants engaged directly with the reference-rule outputs and the loss-function terms. All four rules printed 0 basis points and were judged reliable, and members drew on different rules to make the same point. The inflation-focused member found the Taylor rule most persuasive, noting that with inflation near target and the lower bound binding, holding is optimal, while maintaining a caution against cutting into below-target inflation lest policy overshoot once slack recedes. The labor-market and market-signal members leaned on the ELB-adjusted rule, reading the very low r^* of 0.262 as confirmation that rate-based easing is exhausted and that 0 to 0.25 percent is only modestly accommodative in real terms. The financial-stability member emphasized that any tightening would be the wrong direction given visible credit-cost stress, and the centrist read the complete convergence of rules, framework output, and data as an unambiguous literal case for holding.

Across the final rebuttal, participants reaffirmed these views without changing emphasis. The small momentum terms — inflation momentum of 0.165 and unemployment momentum of -0.05 — were read as signaling no abrupt shift demanding action in either direction. The labor-market participant continued to frame the hold as a constrained optimum driven by the floor rather than by satisfaction with the current stance, and the inflation-focused member reiterated that below-target inflation is not below-anchor inflation and did not, in its view, yet warrant easing. No participant indicated an intention



to dissent for additional accommodation, and all judged steady policy at 0.0 to 0.25 percent to be the loss-minimizing choice available given the effective lower bound, subdued inflation, wide labor-market slack, and elevated but manageable financial stress.

COMMITTEE POLICY ACTIONS

In the predictive vote, all five participants supported maintaining the target range for the federal funds rate at 0.0 to 0.25 percent, a unanimous 5-to-0 outcome for no change. On the deterministic framework's recommendation of 0 basis points, the Committee was likewise in full agreement: all five members — the inflation hawk, the labor-market dove, the financial-stability voice, the data-dependent centrist, and the market-signal realist — endorsed the recommendation as-is, with no members declining and none registering partial agreement. Participants concurred that continued accommodation, alongside the existing supportive programs and the guidance for low rates over the previously committed horizon, remained appropriate given below-target inflation, substantial labor-market slack, and financial conditions that were strained but not at crisis levels.