

**Appendix 1: Materials used by Mr. Dudley**

**(1) Correlation of Daily Price/Yield Changes**

January 01, 2007 – February 26, 2007

<i>Variables</i>	2YR Yield	10YR Yield	S&P	USD/JPY	Swap Spreads	VIX	Merrill-HY
2YR Yield							
10YR Yield	0.94						
S&P	-0.24	-0.21					
USD/JPY	0.39	0.41	-0.26				
Swap Spreads	0.41	0.41	-0.33	0.17			
VIX	0.00	0.00	-0.82	0.16	0.22		
Merrill-HY	-0.71	-0.71	0.10	-0.37	-0.40	0.13	

Source: Bloomberg

Blue boxes denote correlations greater than 0.50 or less than -0.50

**(2) Correlation of Daily Price/Yield Changes**

February 27, 2007 – March 21, 2007

<i>Variables</i>	2YR Yield	10YR Yield	S&P	USD/JPY	Swap Spreads	VIX	Merrill-HY
2YR Yield							
10YR Yield	0.97						
S&P	0.67	0.69					
USD/JPY	0.83	0.83	0.86				
Swap Spreads	-0.49	-0.50	-0.81	-0.66			
VIX	-0.79	-0.78	-0.95	-0.84	0.78		
Merrill-HY	-0.82	-0.80	-0.78	-0.86	0.64	0.80	

Source: Bloomberg

Blue boxes denote correlations greater than 0.50 or less than -0.50

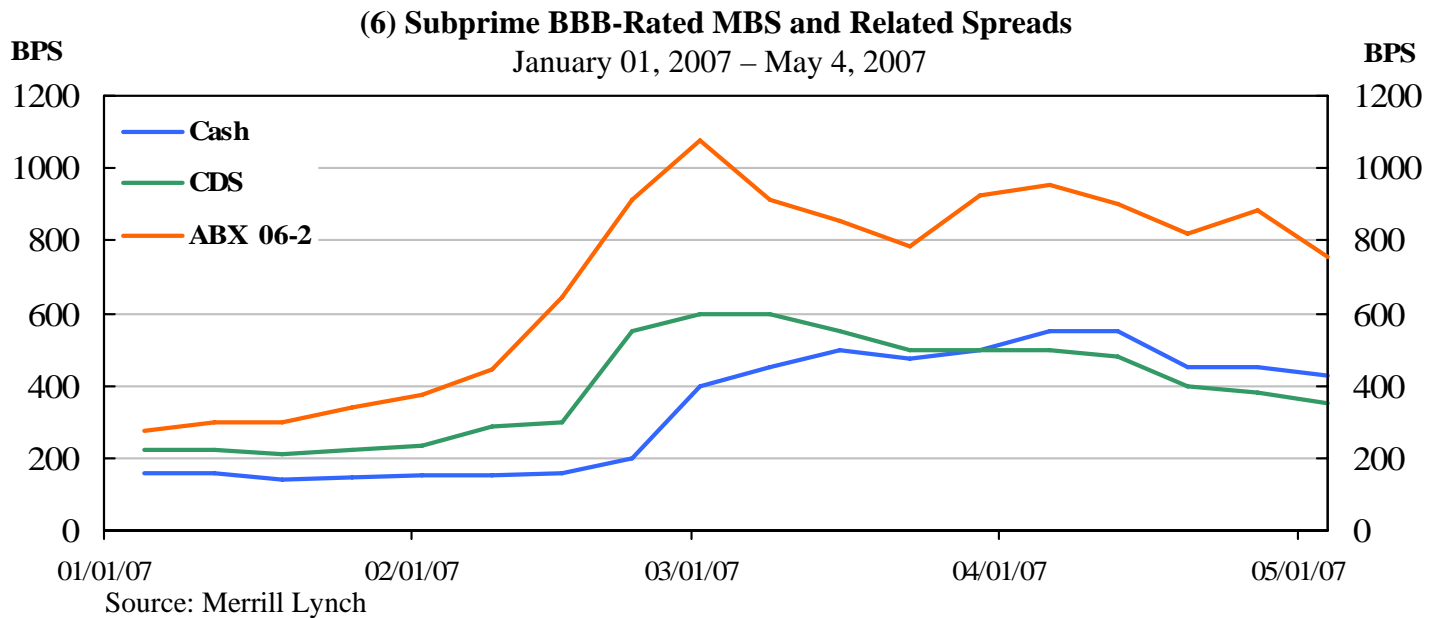
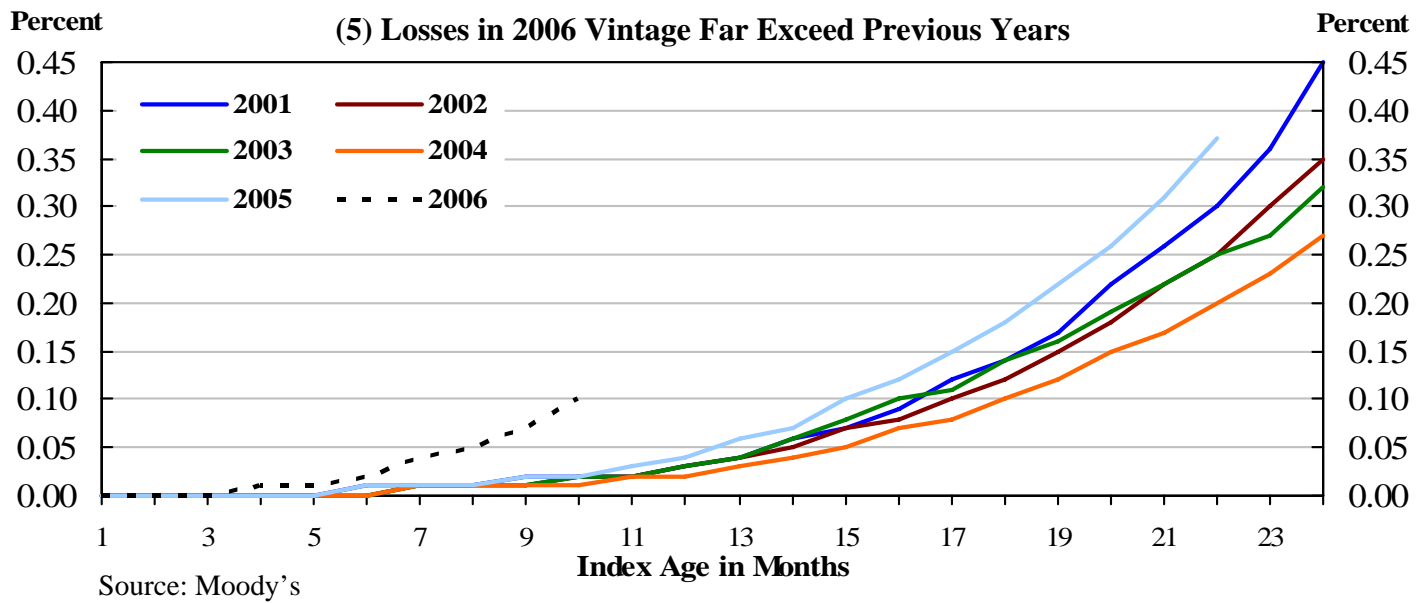
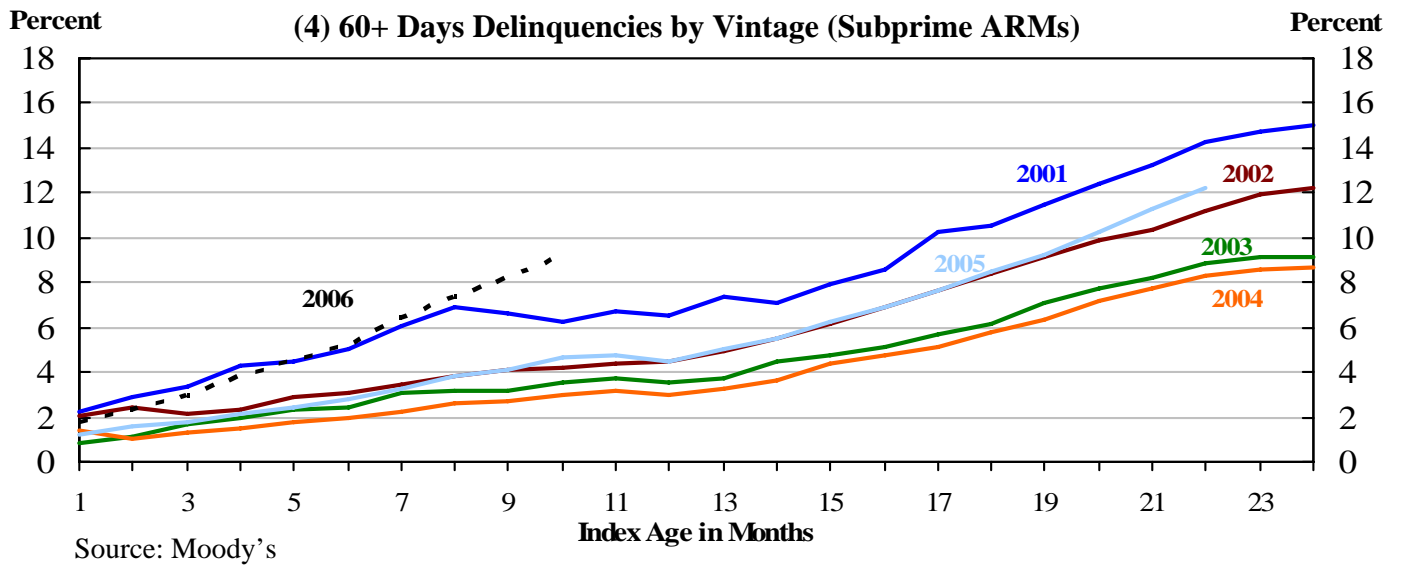
**(3) Correlation of Daily Price/Yield Changes**

March 22, 2007 – May 7, 2007

<i>Variables</i>	2YR Yield	10YR Yield	S&P	USD/JPY	Swap Spreads	VIX	Merrill-HY
2YR Yield							
10YR Yield	0.92						
S&P	0.26	0.14					
USD/JPY	0.65	0.49	0.40				
Swap Spreads	0.11	0.19	-0.11	0.10			
VIX	-0.30	-0.27	-0.70	-0.30	0.11		
Merrill-HY	-0.57	-0.69	-0.30	-0.37	0.01	0.30	

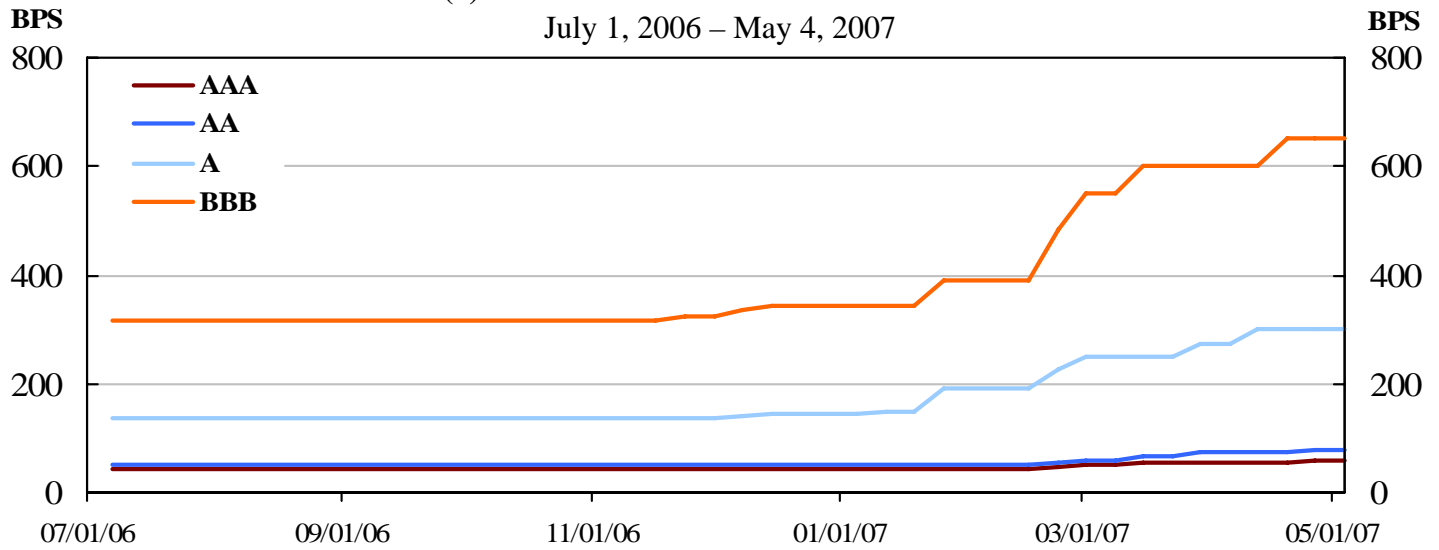
Source: Bloomberg

Blue boxes denote correlations greater than 0.50 or less than -0.50



**(7) Mezzanine Structured Finance CDO**

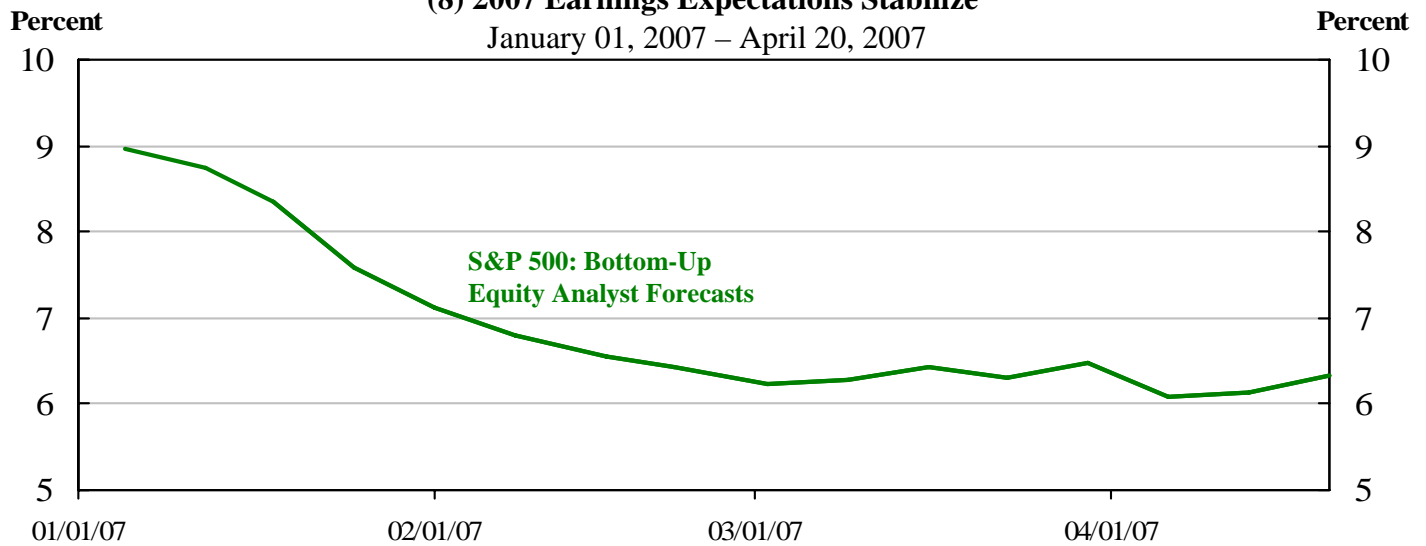
July 1, 2006 – May 4, 2007



Source: Merrill Lynch

**(8) 2007 Earnings Expectations Stabilize**

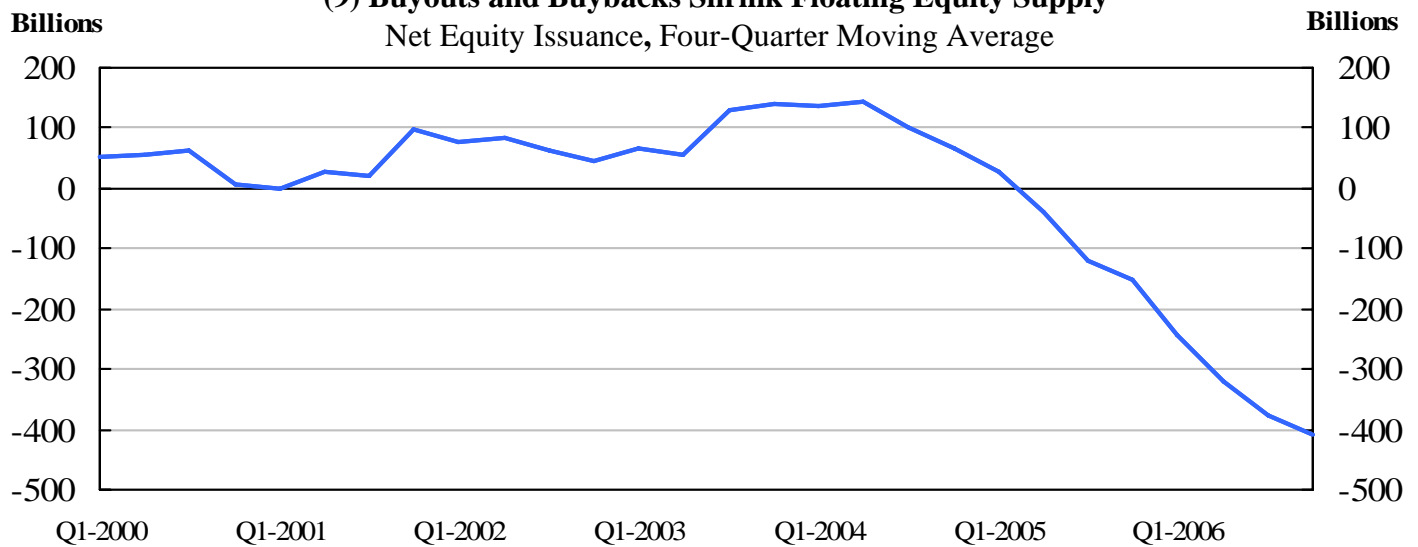
January 01, 2007 – April 20, 2007



Source: Thompson Financial

**(9) Buyouts and Buybacks Shrink Floating Equity Supply**

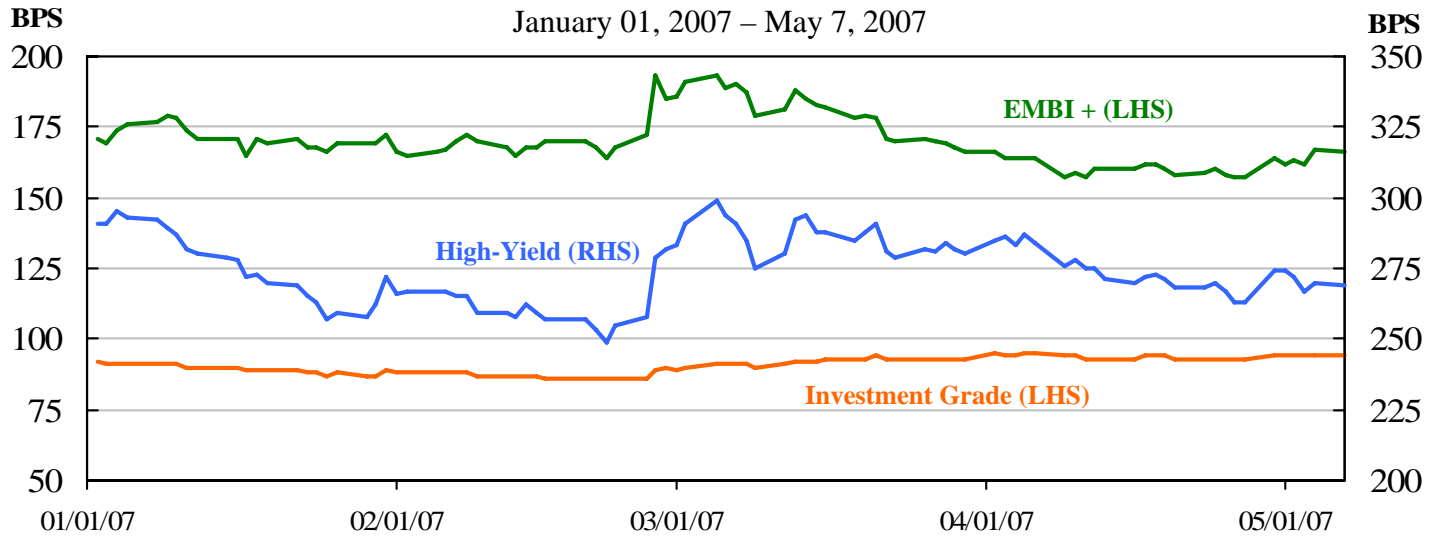
Net Equity Issuance, Four-Quarter Moving Average



Source: Federal Reserve Board Z.1 Release - Flow of Funds Accounts of the United States

### (10) Debt Spreads

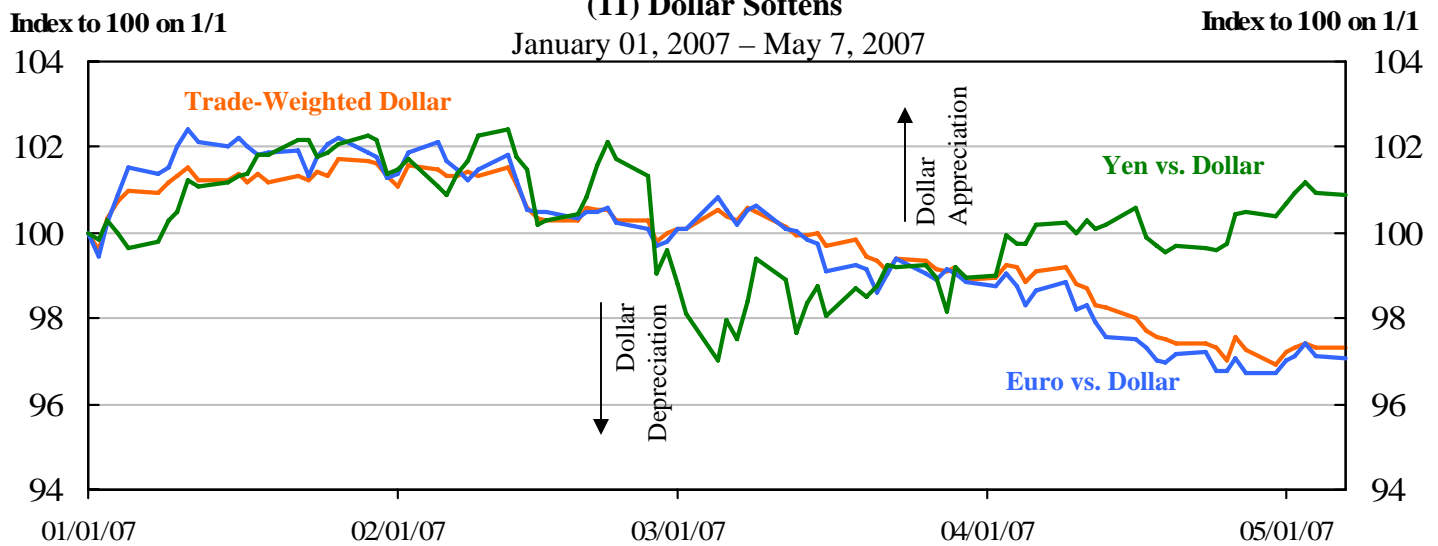
January 01, 2007 – May 7, 2007



Source: Bloomberg

### (11) Dollar Softens

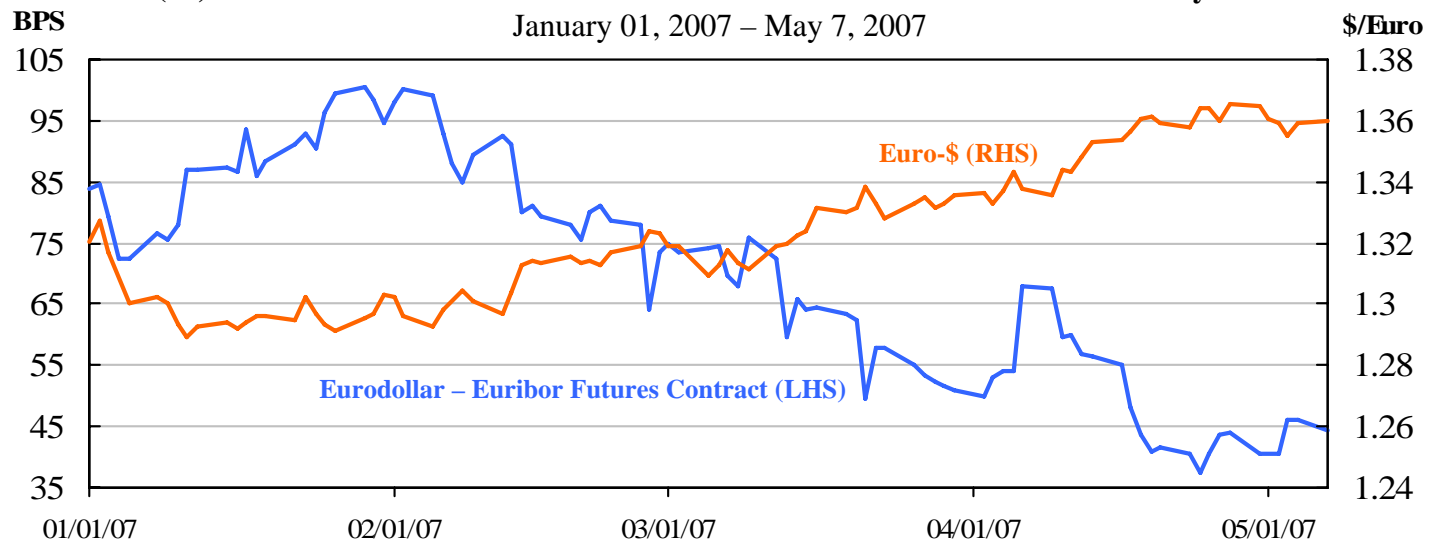
January 01, 2007 – May 7, 2007



Source: Bloomberg

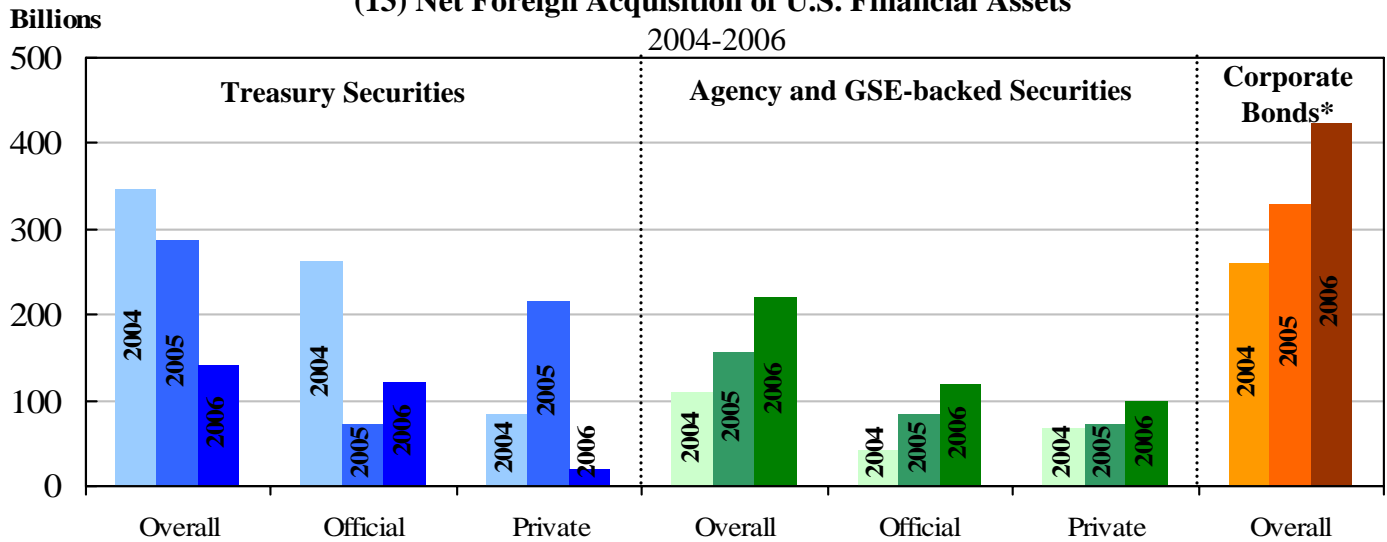
### (12) June 2008 Eurodollar and Euribor Contracts and Euro-Dollar Currency Pair

January 01, 2007 – May 7, 2007



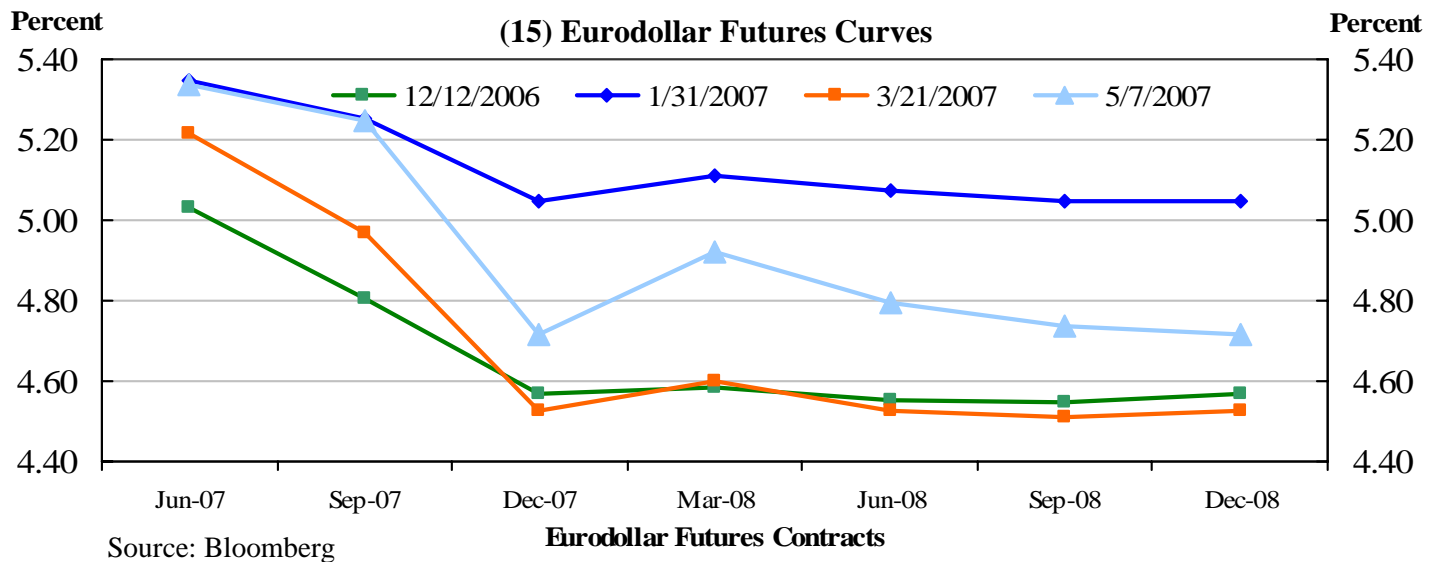
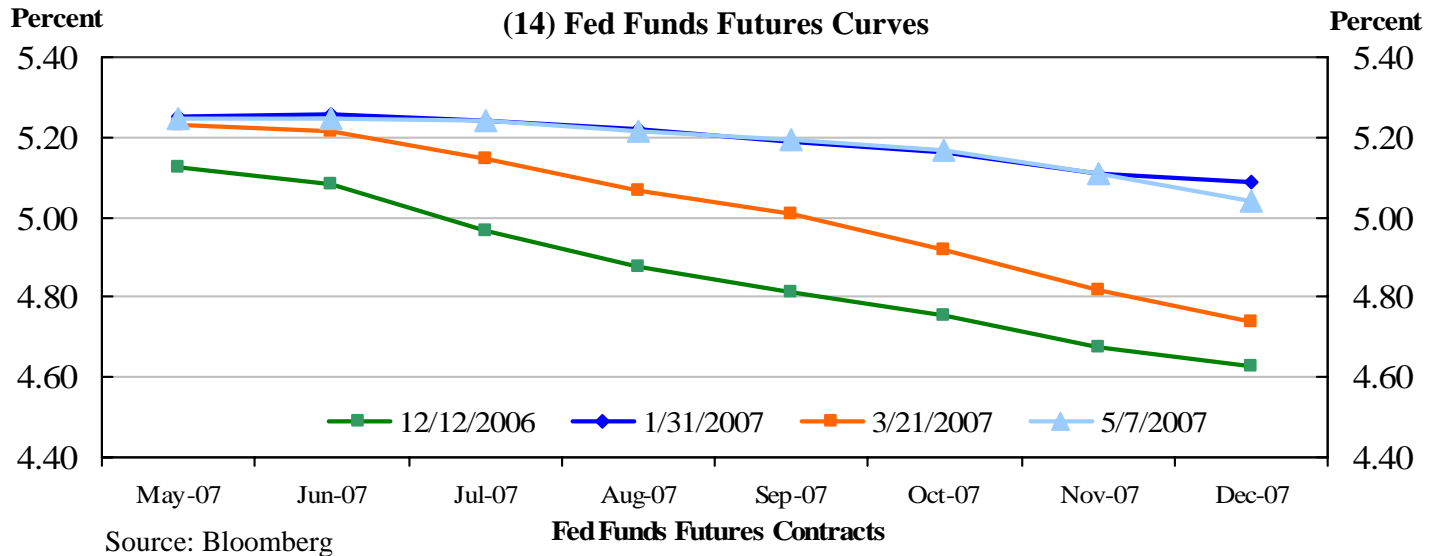
Source: Bloomberg

**(13) Net Foreign Acquisition of U.S. Financial Assets**

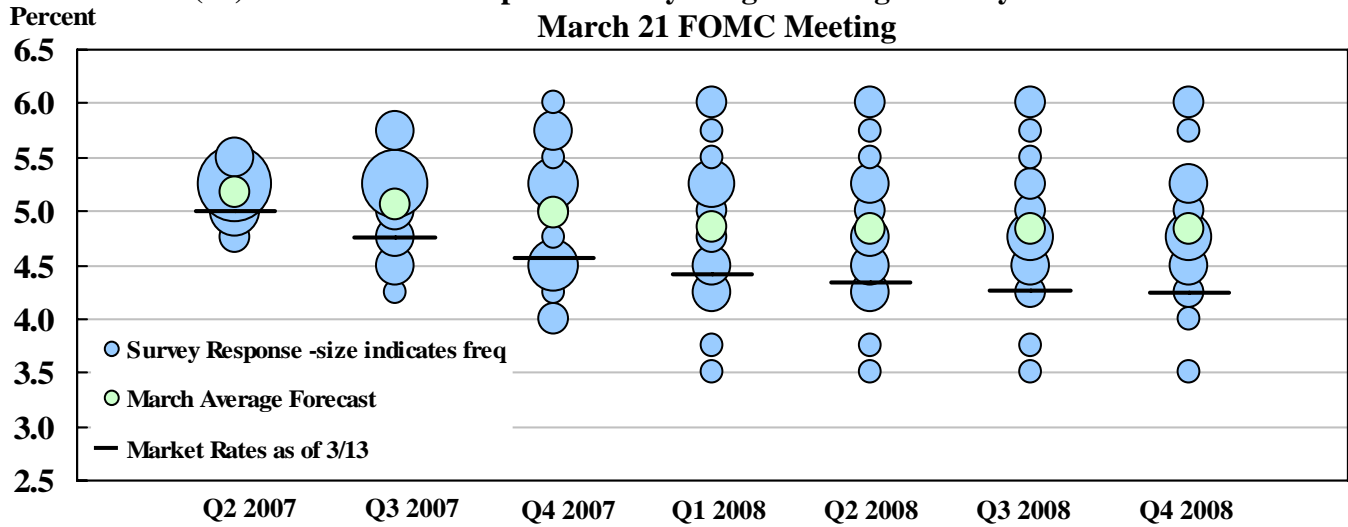


\* Includes private asset-backed securities

Source: Federal Reserve Board Z.1 Release - Flow of Funds Accounts of the United States

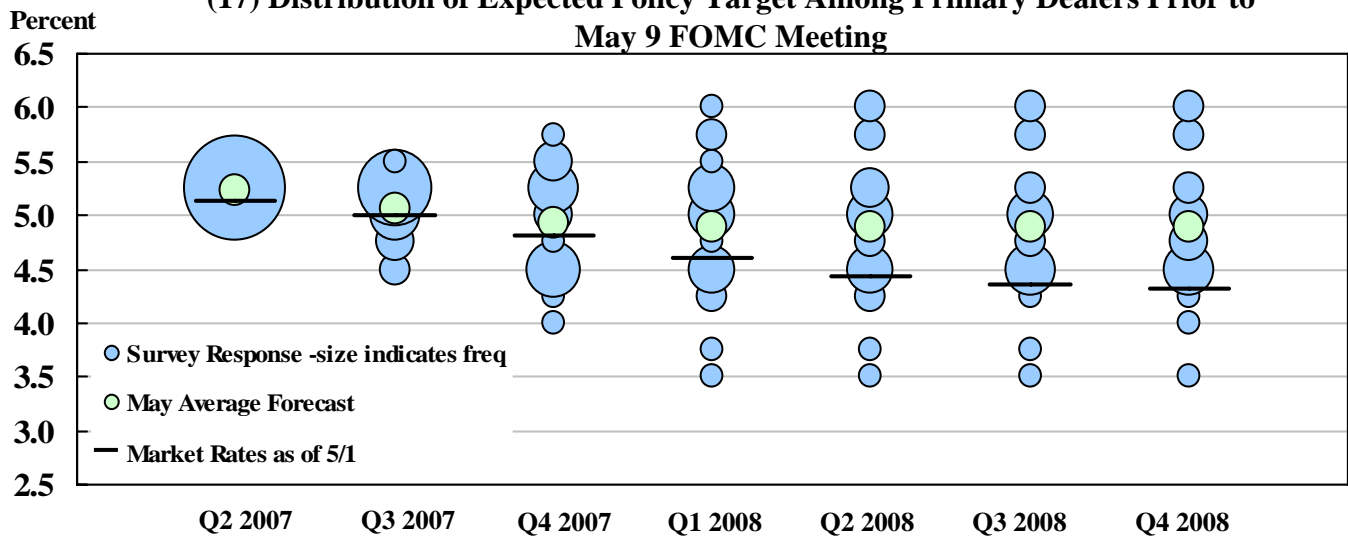


### (16) Distribution of Expected Policy Target Among Primary Dealers Prior to March 21 FOMC Meeting



Source: Dealer Policy Survey

### (17) Distribution of Expected Policy Target Among Primary Dealers Prior to May 9 FOMC Meeting



Source: Dealer Policy Survey

**Appendix 2: Materials used by Mr. Reinhart**



Class I FOMC - Restricted Controlled (FR)

**BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM**  
**FOMC SECRETARIAT**

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**Date:** May 8, 2007  
**To:** Federal Open Market Committee  
**From:** Deborah J. Danker  
**Subject:** Draft Tables and Charts for Projections Trial Run

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Attached are tables and histograms summarizing the projections submitted for the trial run. Please note that hard copies of these will also be available at tomorrow's meeting.

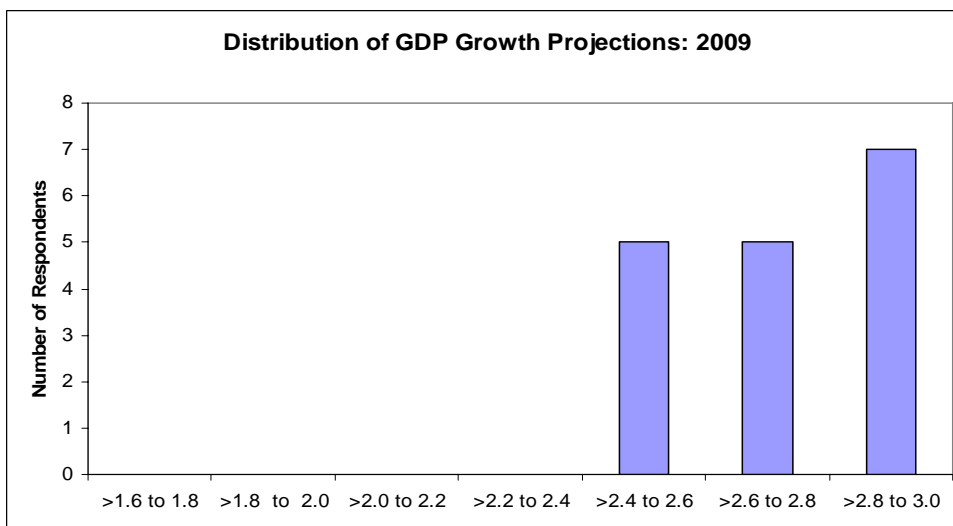
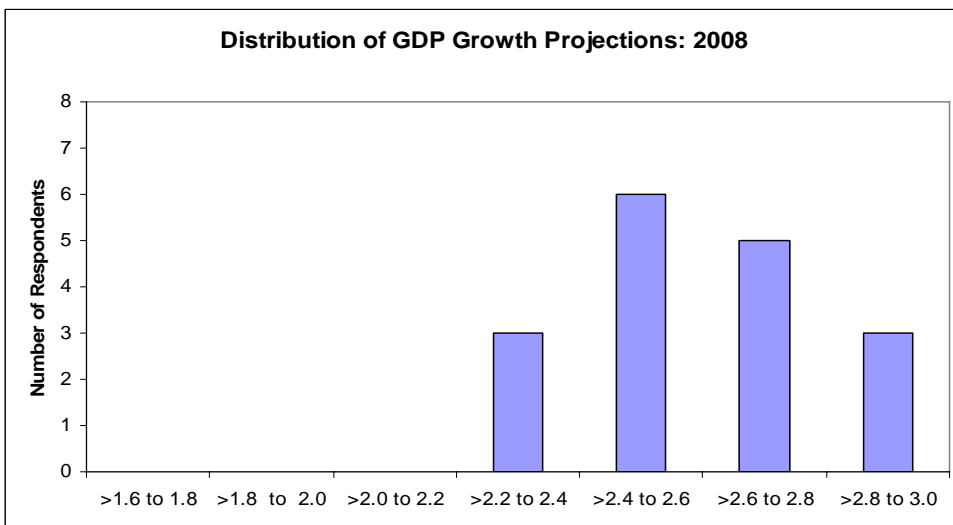
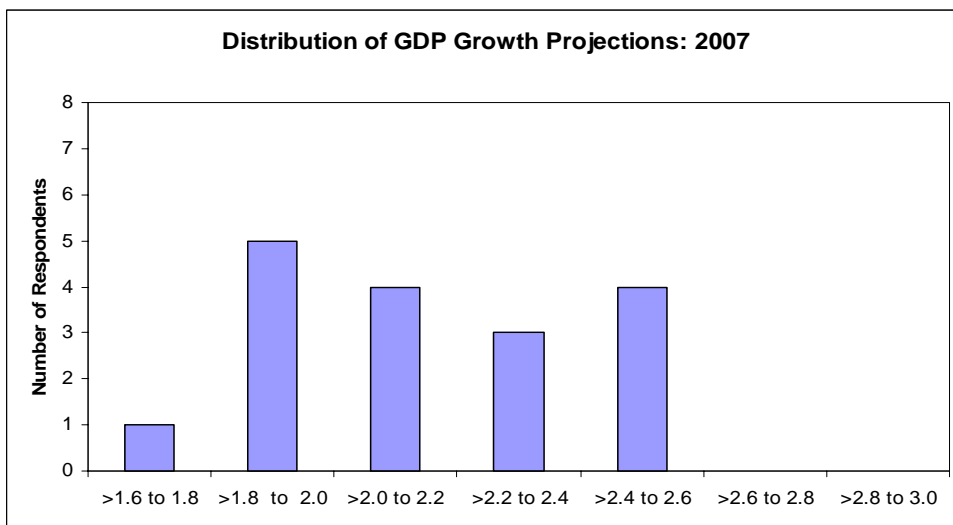
## Class I FOMC - Restricted Controlled (FR)

**Summary of Trial Run Economic Projections****Table 1: Economic Projections of Board Members and Reserve Bank Presidents**

	<b>2007</b>	<b>2008</b>	<b>2009</b>
<b>GDP Growth</b>			
<b>Central Tendency</b>	2.0 to 2.5	2.5 to 2.8	2.5 to 3.0
<i>Memo: Central Tendency at January 2007 Meeting</i>	(2.5 to 3.0)	(2.8 to 3.0)	
<b>Range</b>	1.8 to 2.6	2.4 to 3.0	2.5 to 3.0
<b>Width of Median 70 Percent Confidence Band</b>	2.2	3.0	3.4
<b>Core PCE Inflation</b>			
<b>Central Tendency</b>	2.1 to 2.3	1.8 to 2.1	1.6 to 2.0
<i>Memo: Central Tendency at January 2007 Meeting</i>	(2.0 to 2.3)	(1.8 to 2.0)	
<b>Range</b>	2.0 to 2.3	1.8 to 2.4	1.5 to 2.3
<b>Width of Median 70 Percent Confidence Band</b>	0.9	1.3	1.4
<b>Unemployment Rate</b>			
<b>Central Tendency</b>	4.7 to 4.8	4.7 to 4.9	4.7 to 5.0
<i>Memo: Central Tendency at January 2007 Meeting</i>	(4.6 to 4.8)	(4.6 to 4.8)	
<b>Range</b>	4.5 to 4.9	4.6 to 5.0	4.6 to 5.1
<b>Width of Median 70 Percent Confidence Band</b>	0.7	1.2	1.6

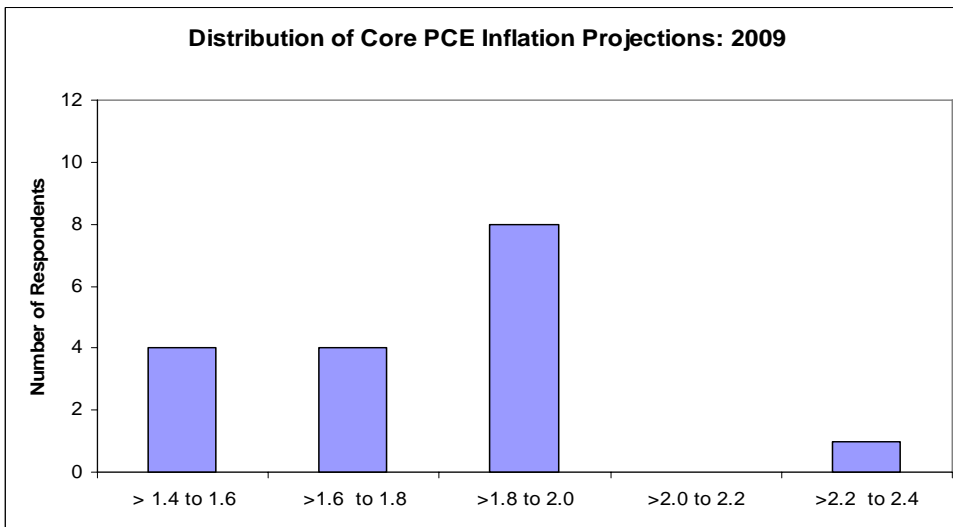
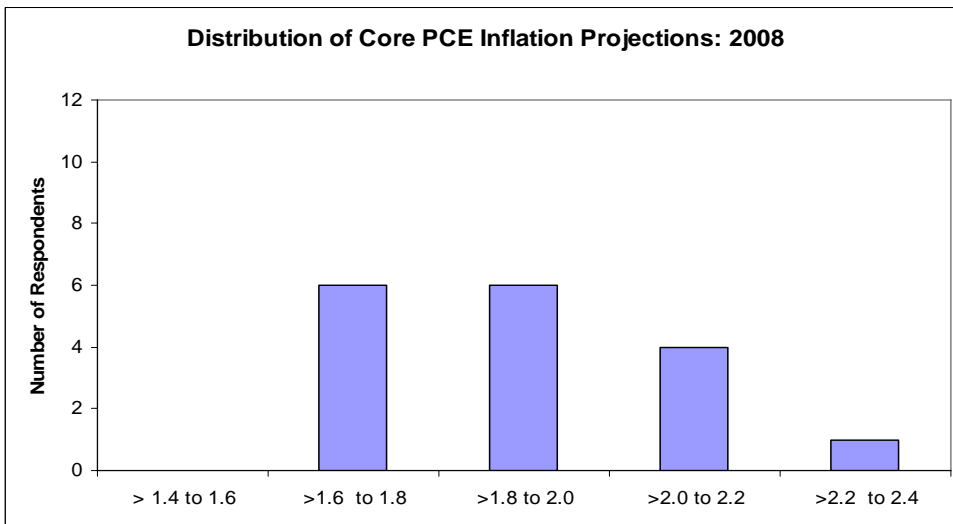
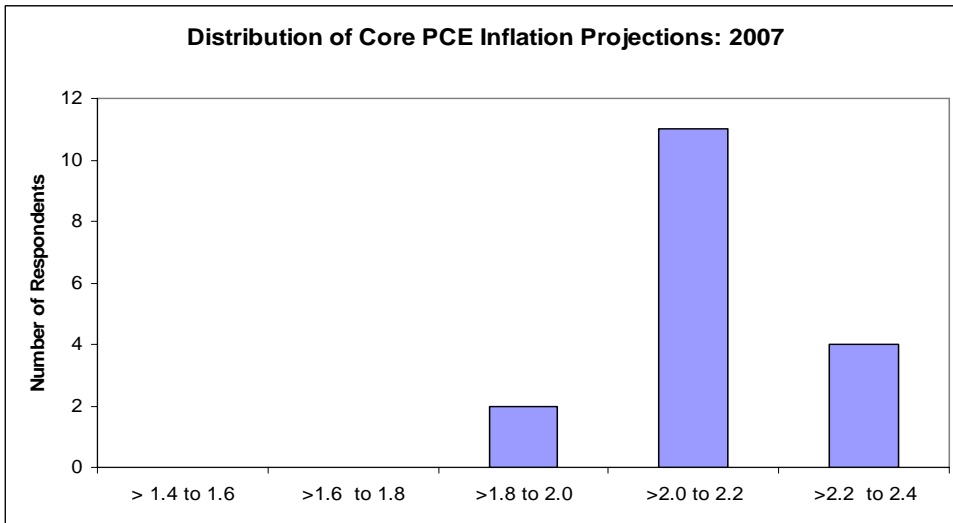
Class I FOMC - Restricted Controlled (FR)

**Histograms of GDP Growth Projections: 2007-2009**



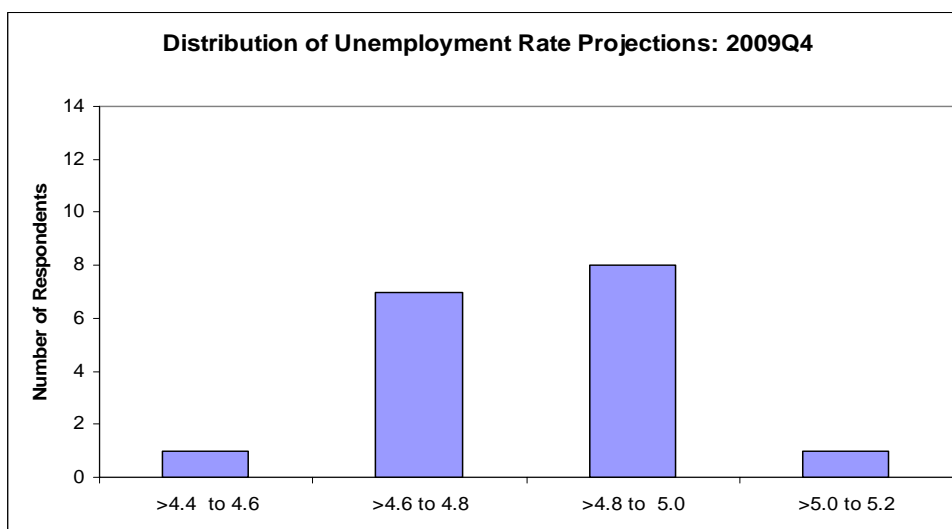
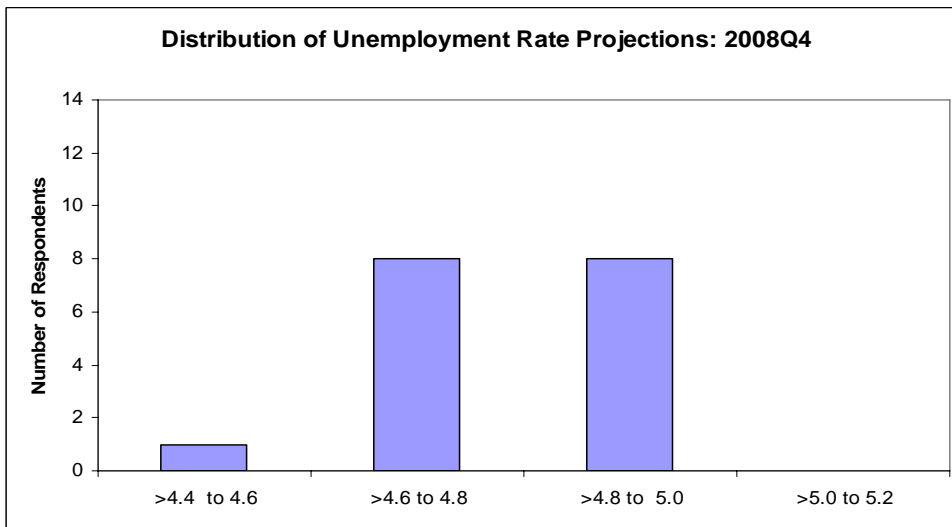
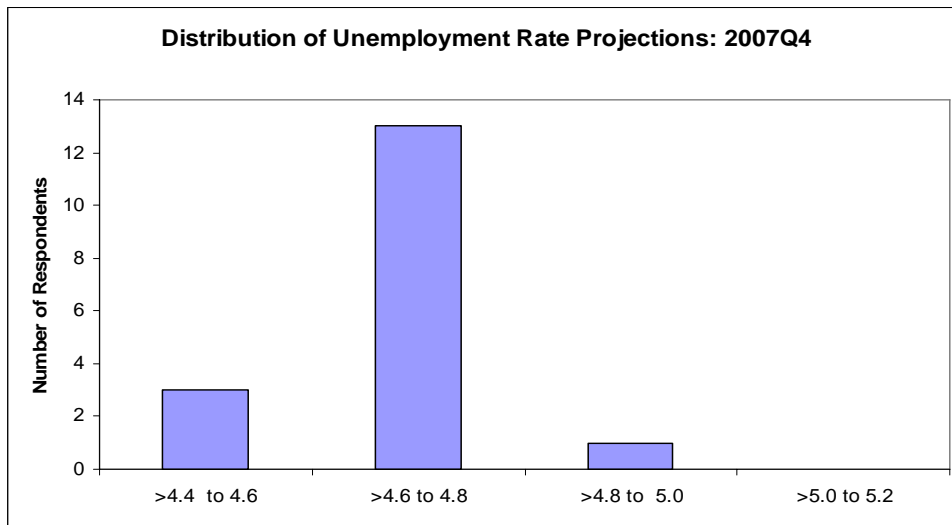
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**Histograms of Projections for Core PCE Inflation: 2007-2009**



Class I FOMC - Restricted Controlled (FR)

**Histograms of Projections for Unemployment Rate: 2007Q4, 2008Q4, 2009Q4**



**Appendix 3: Materials used by Mr. Reinhart**

**Class I FOMC - Restricted Controlled (FR)**

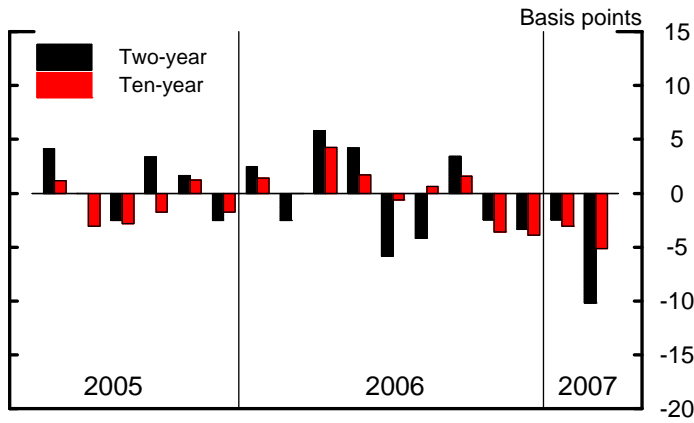
*Material for*

**FOMC Briefing on Monetary Policy Alternatives**

**Vincent R. Reinhart**  
**May 9, 2007**

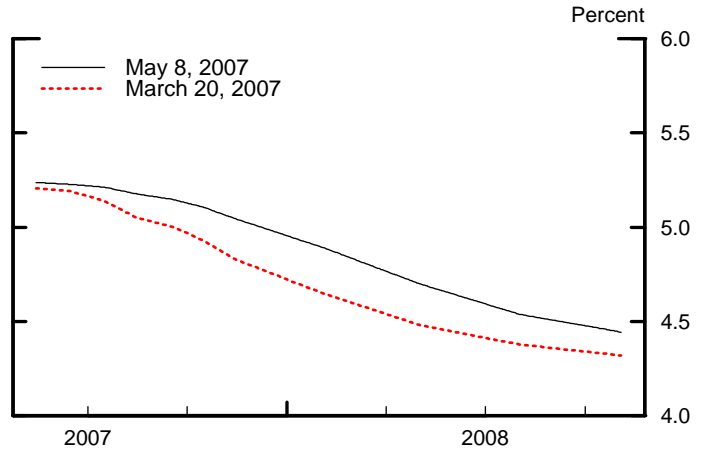
**Exhibit 1  
Market Developments**

Announcement effects\*



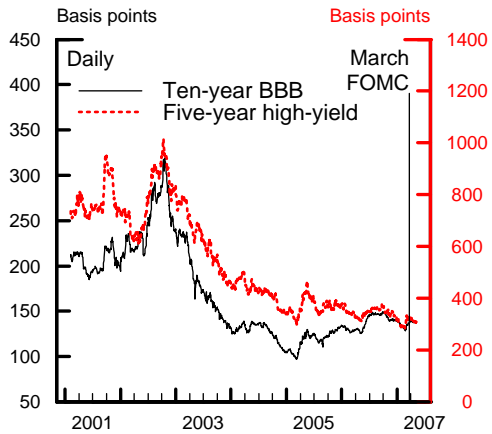
\* Change in the on-the-run two-year and ten-year Treasury yields from 15 minutes before to 1 hour after the release of an FOMC statement.

Expected federal funds rates\*



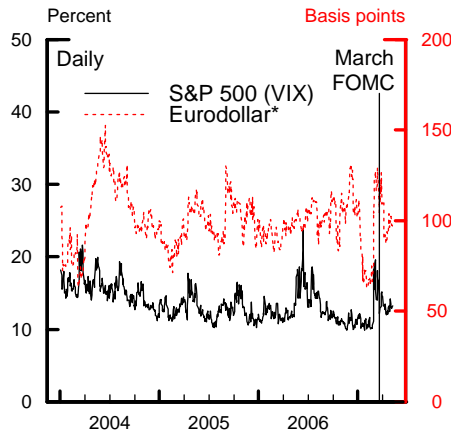
\*Estimates from federal funds and Eurodollar futures, with an allowance for term premiums and other adjustments.

Corporate bond spreads\*



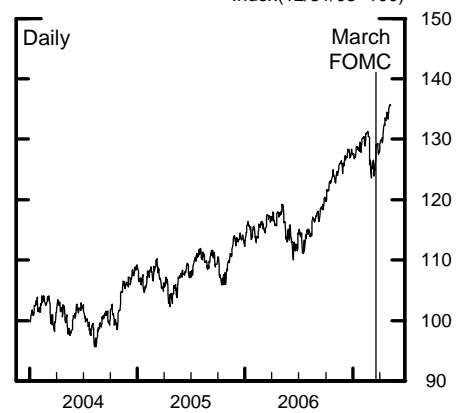
\*Measured relative to an estimated off-the-run Treasury yield curve.

Implied volatilities



\*Six months ahead.

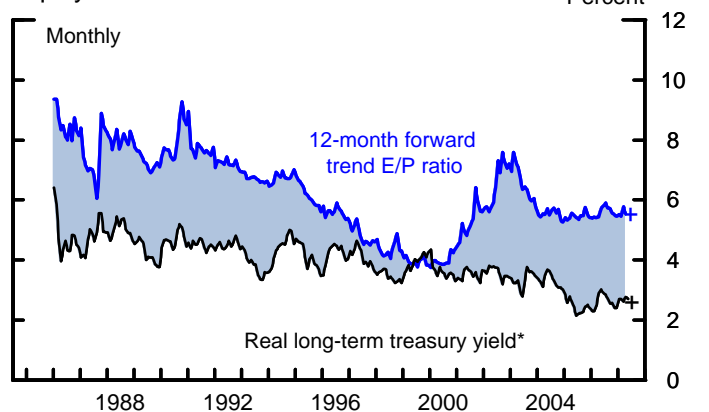
S&P 500



Reasons for higher stock prices

- A. Earnings were solid.
- B. Equity premium narrowed a bit.
- C. Downside risks to the outlook appeared to ease.
- D. All of the above.

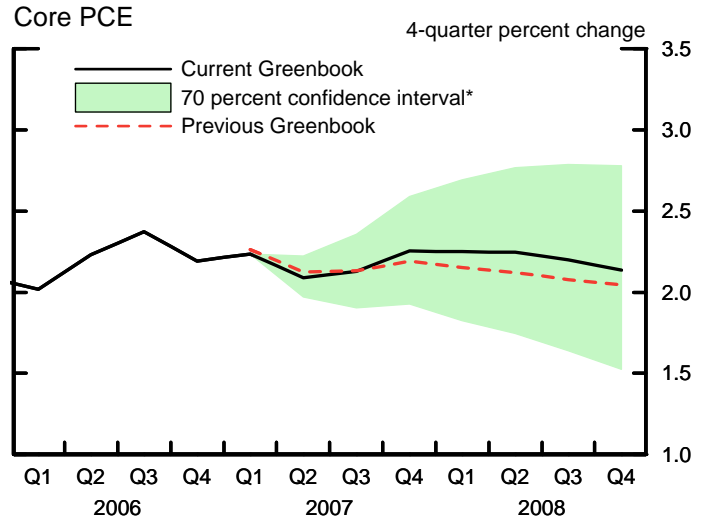
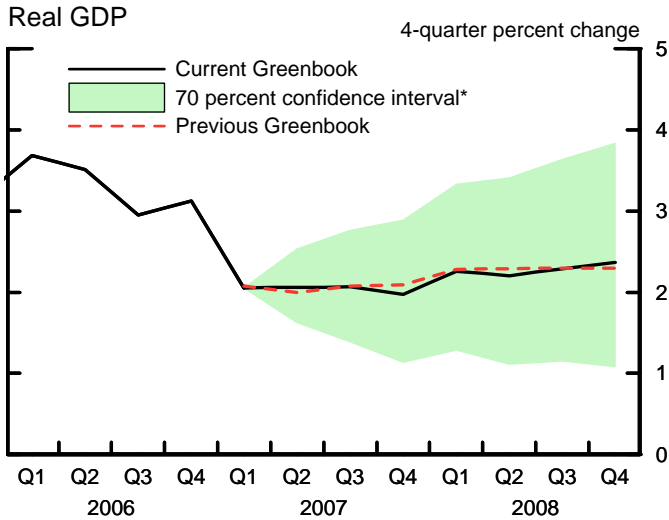
Equity valuation



\*Perpetuity Treasury yield minus Philadelphia Fed 10-year expected inflation. Note. + Denotes the latest observation using daily interest rates and stock prices and latest earnings data from I/B/E/S.

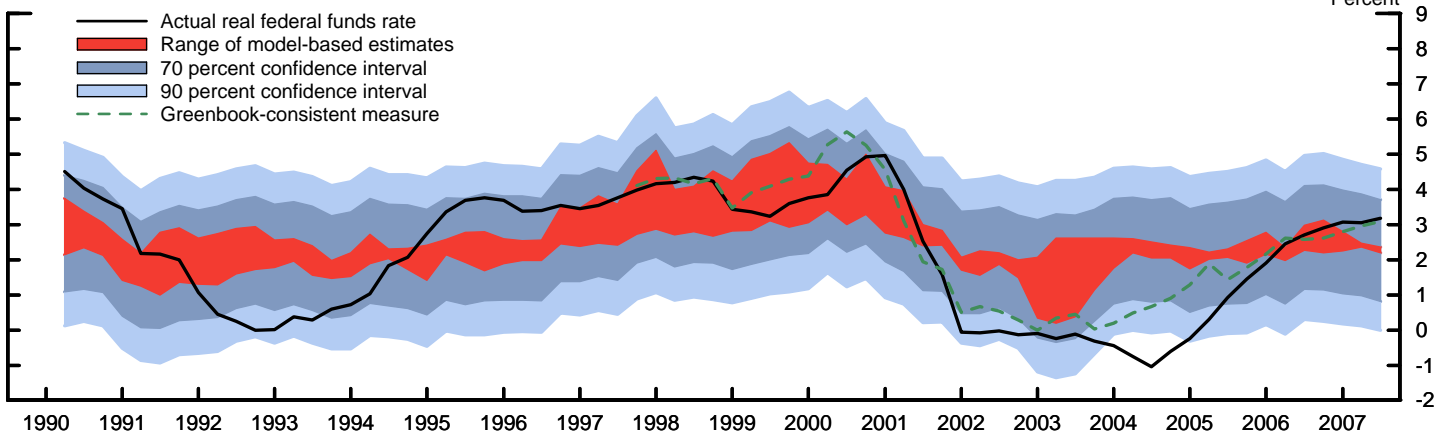


**The Case for Alternative B**

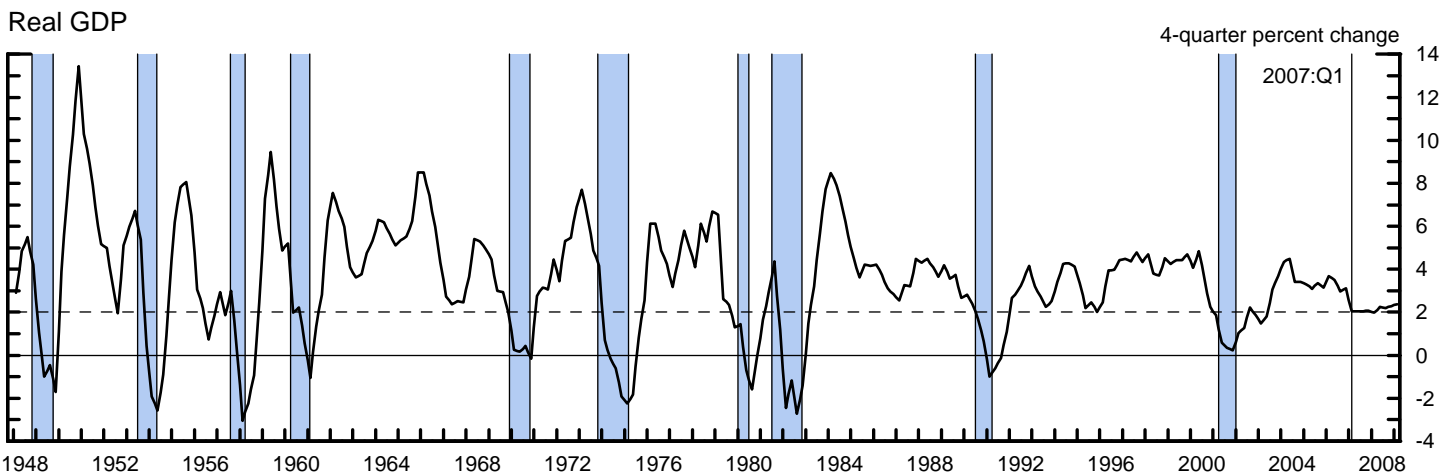


\*Confidence intervals based on FRB/US stochastic simulations.

Equilibrium real federal funds rate\*  
Short-run estimates with confidence intervals



\*Explanatory notes are provided in appendix A of the Bluebook.



### Exhibit 3 Why Might You Change Policy?

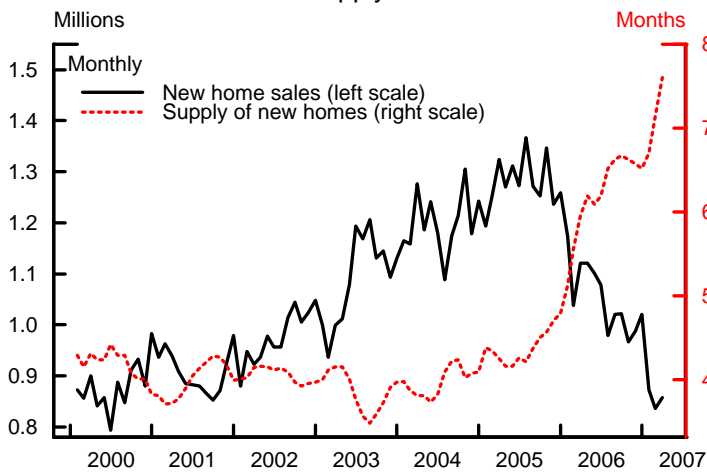
The case for alternative A

- Housing sector adjustment and possible spillovers.
- Investment spending weakness.
- Financial markets could correct.

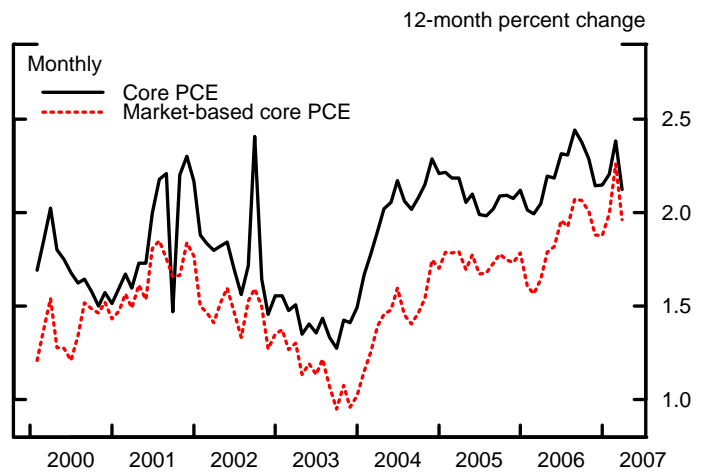
The case for alternative C

- Inflation not clearly on a downward trend.
- Oil and other commodity prices higher.
- Inflation expectations could drift up.

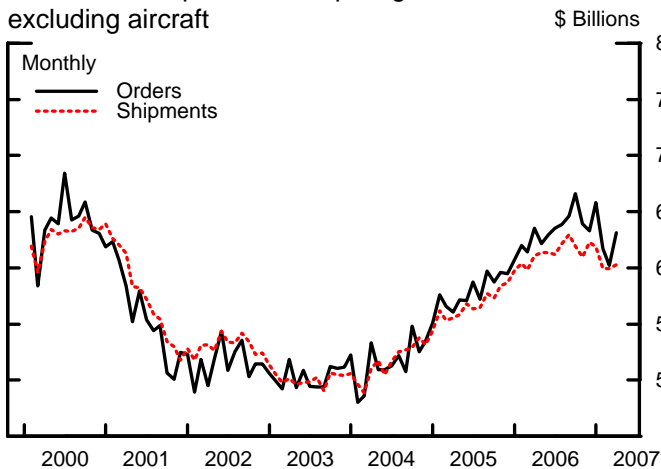
New home sales and supply of new homes



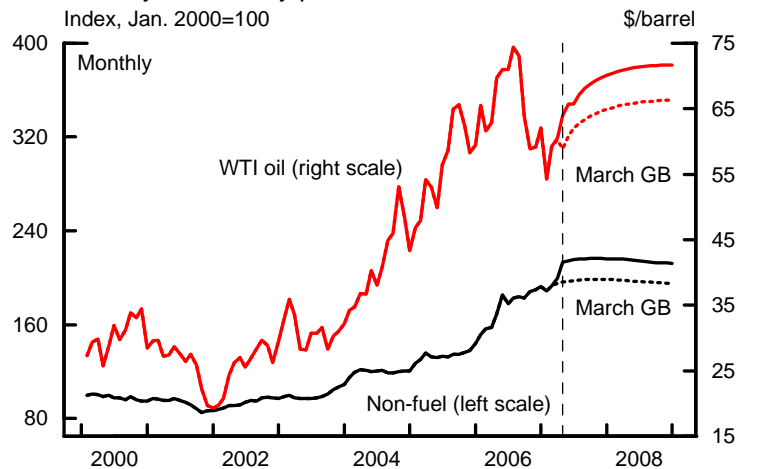
Core PCE



Orders and shipments of capital goods excluding aircraft



Primary commodity prices



**Table 1: Alternative Language for the May 2007 FOMC Announcement**

	<b>March FOMC</b>	<b>Alternative A</b>	<b>Alternative B</b>	<b>Alternative C</b>
<b>Policy Decision</b>	1. The Federal Open Market Committee decided today to keep its target for the federal funds rate at 5¼ percent.	The Federal Open Market Committee decided today to <b>lower</b> its target for the federal funds rate <b>25 basis points to 5</b> percent.	The Federal Open Market Committee decided today to keep its target for the federal funds rate at 5¼ percent.	The Federal Open Market Committee decided today to <b>raise</b> its target for the federal funds rate <b>25 basis points to 5½</b> percent.
<b>Rationale</b>	2. Recent indicators have been mixed and the adjustment in the housing sector is ongoing. Nevertheless, the economy seems likely to continue to expand at a moderate pace over coming quarters.	The economy seems <b>most</b> likely to expand at a moderate pace over coming quarters. <b>But weakness in housing and capital spending imply a significant risk that economic activity might grow more slowly than anticipated.</b>	<b>Economic growth slowed in the first part of this year</b> and the adjustment in the housing sector is ongoing. Nevertheless, the economy seems likely to expand at a moderate pace over coming quarters.	<b>Despite the ongoing</b> adjustment in the housing sector, the economy seems likely to expand at a moderate pace over coming quarters.
	3. Recent readings on core inflation have been somewhat elevated. Although inflation pressures seem likely to moderate over time, the high level of resource utilization has the potential to sustain those pressures.	<b>Core inflation remains</b> somewhat elevated <b>on balance</b> . <b>Although the high level of resource utilization has the potential to sustain inflation pressures, those pressures seem likely to moderate over time.</b>	<b>Core inflation remains</b> somewhat elevated <b>on balance</b> . Although inflation pressures seem likely to moderate over time, the high level of resource utilization has the potential to sustain those pressures.	<b>Core inflation remains</b> somewhat elevated <b>on balance</b> . Inflation pressures seem likely to moderate over time, <b>but considerable uncertainty surrounds that judgment</b> . <b>Moreover</b> , the high level of resource utilization, <b>in combination with the recent increases in energy and other commodity prices</b> , has the potential to sustain those pressures.
<b>Assessment of Risk</b>	4. In these circumstances, the Committee’s predominant policy concern remains the risk that inflation will fail to moderate as expected. Future policy adjustments will depend on the evolution of the outlook for both inflation and economic growth, as implied by incoming information.	In these circumstances, <b>future</b> policy adjustments will depend on the evolution of the outlook for both inflation and economic growth, as implied by incoming information.	[Unchanged]	<b>Even after this action</b> , the Committee’s predominant policy concern remains the risk that inflation will fail to moderate as expected. Future policy adjustments will depend on the evolution of the outlook for both inflation and economic growth, as implied by incoming information.