



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

No System Open Market Account holdings data was available from a point-in-time-safe source on or before the cutoff for this meeting. Accordingly, the Committee is unable to report the total size of SOMA holdings, their composition across security types, or any change from the prior release. This absence pertains specifically to SOMA portfolio holdings; it should be noted that this section in any case covers SOMA holdings only and does not encompass the results of temporary open market operations such as repurchase and reverse repurchase agreements, for which no point-in-time-safe data source currently exists. Members proceeded on the understanding that portfolio detail could not inform the present discussion.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reviewed incoming data indicating that solid economic growth continued through April and May, though with accumulating evidence of some deceleration from the rapid pace observed earlier in the year. The Chicago Fed National Activity Index stood at 0.12, consistent with growth near trend. The labor market remained very tight: the unemployment rate was 4.1%, well below the estimated natural rate of 5.11%, and initial jobless claims at 294,000 showed no sign of labor-market deterioration. Core PCE inflation, measured year over year, was 1.74%, below the 2.0% level often cited as an objective. M2 stood at \$4,759.1 billion.

The Beige Book, prepared before June 6, reinforced this picture. Districts characterized growth as solid, with Minneapolis reporting activity 'remains hot' and Chicago and Richmond describing growth as strong, while most other Districts reported moderate or steady expansion. All Districts but Minneapolis noted scattered signs of cooling or a slowing pace. Labor markets were tight across all twelve Districts, but the staff noted the tightness did not appear to have intensified since the prior report; several Districts indicated shortages were constraining output growth, and a number reported that conditions would be more severe absent inflows of immigrants and students. Base wages of permanent employees were generally not accelerating, though seasonal and temporary workers, and certain occupations facing acute shortages, commanded sizable raises. Retail sales exceeded year-earlier levels in every District, but half reported a recent slowdown in the rate of growth, and a majority noted weaker sales of autos and durable goods accompanied by rising inventories of some big-ticket items.

STAFF REVIEW OF THE FINANCIAL SITUATION

The staff reported that financial conditions reflected a policy stance that markets read as restrictive, alongside contained but non-trivial market anxiety. The 10-year/2-year Treasury yield curve spread was inverted at -0.39, and the 3-month T-bill stood 0.85 percentage point below the current 6.5%



funds rate, a configuration consistent with market expectations of no further tightening and, potentially, easing ahead. The Baa corporate spread of 2.35 indicated moderate borrowing-cost pressure in credit markets without acute dislocation. The VIX at 20.61 reflected elevated but not extreme equity volatility, and the broader financial stress index at 0.3084 pointed to conditions that were contained yet not benign. Taken together, these readings suggested the tightening cycle had bitten and that markets judged policy to be at or near its peak.

STAFF ECONOMIC OUTLOOK

The staff outlook drew on the forward-looking quantities available. The estimated neutral real rate (r^*) of 3.737, combined with core PCE inflation of 1.74%, implies a neutral nominal rate in the vicinity of 5.5%, roughly 100 basis points below the prevailing 6.5% funds rate. On this reading, the current stance sits meaningfully above estimated neutral, which would tend to restrain activity going forward and is broadly consistent with the inverted yield curve and the sub-funds T-bill rate. Momentum measures were small in magnitude: inflation momentum registered +0.09 and unemployment momentum -0.1, indicating that neither price pressures nor labor-market tightness were accelerating sharply, even as both remained in territory suggesting an economy still running above trend.

The reference rules spanned a wide range and did not point in a single direction. The Taylor rule prescribed +50 basis points and both the Balanced Approach and ELB-adjusted rules +75 basis points, each leaning heavily on the large gap between the 4.1% unemployment rate and the 5.11% natural rate. The First-Difference rule, which responds to changes rather than levels, prescribed 0 basis points, consistent with the near-zero momentum readings. With the reference rules assessed as reliable, the loss-minimizing framework output was -25 basis points, reflecting below-target inflation, the restrictive gap between the funds rate and estimated neutral, and the accumulating signs of cooling — a projection that the appropriate path tilts toward modest accommodation rather than the further tightening implied by the levels-based rules.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their independent opening assessments, all five participants arrived at the same near-term judgment: hold the funds rate at 6.5%. The reasoning behind that convergence, however, drew on distinct lenses. The participant most attentive to inflation risk emphasized that labor markets were tight across all twelve Districts, that several Districts reported scattered signs of worsening price inflation, and that unemployment at 4.1% represented a substantial overshoot below the 5.11% natural rate. Yet this participant judged that core PCE at 1.74% remained below target and that the widespread signs of slowing argued for patience over an additional hike; a cut was viewed as clearly inappropriate with labor this tight.



The participant weighting employment risk most heavily examined whether the data showed rising unemployment or slowing job growth and found neither — jobless claims at 294,000 were low, and labor-market tightness, though not intensifying, had not eased. On that basis a cut was deemed premature, while restrictive policy at 6.5% argued against any hike. The financial-stability voice and the market-signal participant reinforced one another: the inverted 10-year/2-year spread at -0.39 and the 3-month T-bill 0.85 point below the funds rate were read as evidence that prior tightening had bitten and that markets saw policy near its peak, so that hiking into an inverted curve would risk destabilizing credit conditions. The data-dependent centrist synthesized these strands, noting cooling in nearly all Districts, softening autos and durables, and rising inventories, while judging inflation contained and growth near trend at a CFNAI of 0.12. In the rebuttal round, no participant was moved off the hold; several observed that the convergence from different lenses strengthened confidence in it. The final predictive tally was unanimous at 0 basis points.

When the discussion turned to the framework's loss-minimizing recommendation of -25 basis points, genuine disagreement emerged. The participant focused on employment risk endorsed the cut, arguing that momentum, not levels, should govern: cooling in eleven of twelve Districts, softening demand, and an inverted curve pointed toward a turn that a 25-basis-point move would insure against before slowing hardened into rising unemployment. This participant characterized the Taylor and Balanced Approach rules, at +50 to +75 basis points, as backward-looking anchors on the low unemployment level that ignored the forward signals the mandate prioritized.

The market-signal participant likewise endorsed -25 basis points, stressing that the estimated r^* of 3.737 with core PCE at 1.74% implied neutral near 5.5%, roughly 100 basis points below the current rate — corroborating the market's own read that the stance had become too tight. The financial-stability voice endorsed the direction and magnitude as well, treating the inversion and the Baa spread of 2.35 as warnings of tightening-into-slowdown that justified a small precautionary ease while below-target inflation removed any constraint; this participant emphasized that with no acute distress evident, a single 25-basis-point step, not aggressive action, was the right size.

The dissenting reasoning came from two participants who declined the cut. The inflation-focused participant held that risk skewed to the upside, that three of four reference rules argued for higher rather than lower rates, and that positive inflation momentum of +0.09 and still-negative unemployment momentum meant pressures were building, not reversing; in this view the inverted curve signaled future slowing rather than present price relief, and easing should wait until inflation momentum clearly turned negative. The centrist declined on the ground that momentum near zero pointed to the First-Difference rule's 0 basis points, that labor remained very tight at 4.1% against a



5.11% natural rate, and that with financial stress moderate and no crisis at hand, a cut against below-target-but-firm data was premature — allowing that the easing direction was plausible but not yet warranted this meeting.

COMMITTEE POLICY ACTIONS

On the near-term policy decision, the Committee's predictive vote was unanimous to hold the target federal funds rate at 6.5%, five members in favor and none opposed. On the framework's loss-minimizing recommendation of -25 basis points, the Committee was divided: three members endorsed the recommendation as-is — the participant weighting employment risk, the financial-stability voice, and the market-signal participant — while two members declined it, the inflation-focused participant and the data-dependent centrist, the latter allowing that the easing direction was plausible but judging a move premature at this meeting. There were no partial positions.