



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The System Open Market Account's domestic securities holdings stood at \$4,062.5 billion as of June 11, up \$7.6 billion from the prior release on June 4. The portfolio remained concentrated in two components: Treasury notes and bonds of \$2,274.3 billion and agency mortgage-backed securities of \$1,648.0 billion. The week-over-week increase was modest and consistent with the ongoing maintenance of the account. It should be noted that this review covers SOMA holdings only — total size, composition, and the change from the preceding release. It does not encompass repurchase or reverse-repurchase operation results, for which no point-in-time-safe data source currently exists; those operations are therefore outside the scope of what the staff can report here.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reviewed indicators pointing to continued moderate expansion. Core PCE inflation stood at 1.13 percent on a year-over-year basis, well below the Committee's 2 percent objective. The unemployment rate was 6.3 percent, above the 5.5 percent estimate of the natural rate, indicating that some slack remained in the labor market. Initial jobless claims were 312,000, a relatively low reading. The Chicago Fed National Activity Index at -0.32 was consistent with growth somewhat below its historical trend. The Employment Cost Index registered 120.5, and M2 money supply stood at \$11,214.8 billion.

Beige Book material for the Second District described activity continuing to grow at a moderate pace since the prior report. Manufacturers reported that business activity had picked up considerably in recent weeks, while service-sector firms indicated mixed performance. Labor market conditions showed signs of firming across a broad range of industries, with scattered reports of labor shortages. Prices of finished goods and services remained generally stable, and businesses reported only modest upward pressure on input prices. General merchandise retailers described sales as rebounding strongly in April and early May, with same-store sales at two major chains running roughly 10 percent ahead of comparable 2013 levels, although cold and rainy weather continued to restrain shopper traffic in parts of upstate New York. Auto dealers reported strong new-vehicle sales, with Rochester-area April sales up 17 percent from a year earlier and Buffalo-area gains of about 5 percent. Tourism strengthened as harsh weather eased, housing markets showed further improvement, and commercial real estate was generally steady. Banks reported fairly widespread increases in loan demand, especially for mortgages, with little-changed credit standards and delinquency rates steady to down modestly.

STAFF REVIEW OF THE FINANCIAL SITUATION



Financial conditions were notably calm and accommodative. The financial stress index was near zero at 0.009, and the VIX stood at 11.6, a compressed level indicating very low expected volatility. The Baa corporate spread was 2.21, historically tight and showing no sign of widening credit-market strain. The 10-year to 2-year Treasury yield spread was a comfortably positive 2.21, offering no recession signal from the term structure. The 3-month T-bill spread relative to the current policy rate was -0.085, indicating that market participants were not pricing any near-term move in the policy rate. Taken together, these readings described an orderly environment in which accommodation was being absorbed without evident imbalance, though the staff noted that the combination of very low volatility and tight spreads could reflect elevated risk appetite.

STAFF ECONOMIC OUTLOOK

The staff's outlook drew on several forward-looking quantities. The estimated neutral real rate (r^*) was -0.5 percent, implying that even with the nominal policy rate at its effective floor, the current stance was not markedly restrictive relative to neutral and remained accommodative. Inflation momentum was mildly positive at 0.11, suggesting that prices were firming only gradually rather than accelerating toward the 2 percent objective; on this trajectory, core inflation would be expected to close the gap to target slowly. Unemployment momentum was zero, consistent with a labor market that was neither deteriorating nor rapidly tightening, and pointing toward continued gradual absorption of the remaining gap between the 6.3 percent unemployment rate and the 5.5 percent natural rate.

All four reference rules — the Taylor rule, the Balanced Approach rule, the First-Difference rule, and the ELB-adjusted rule — pointed to no change in the policy rate, and the framework judged these rules reliable in the current environment. With below-target inflation, a persistent unemployment gap, and a deeply negative neutral rate, the rule-based projection implied that maintaining the present stance would be broadly consistent with a gradual return of conditions toward the Committee's objectives, without the near-term pressures that would call for a move in either direction.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

Participants generally agreed that the incoming data described an economy expanding at a moderate pace with subdued inflation and a labor market that was improving but not yet tight. With core PCE inflation at 1.13 percent, well below the 2 percent objective, no participant saw a case for tightening at this meeting. The member most attentive to inflation risk observed that the conditions triggering his caution — inflation above target or elevated inflation risk — were simply not present; the Beige Book's firming labor markets, scattered labor shortages, and modest input-price pressure were the kinds of early signals he watches closely, but finished-goods prices remained generally stable and the pressures were described as modest rather than accelerating. This warranted vigilance, he judged, not action



now, and he indicated he would advocate moving first if inflation momentum accelerated past target.

The member most focused on employment emphasized that the direction of the labor market mattered more than its level for his concern. Unemployment at 6.3 percent left a gap above the 5.5 percent natural rate, which would normally incline him toward accommodation, but jobless claims at 312,000 and the broad firming reported in the Beige Book indicated the recovery was intact rather than reversing. He also stressed a mechanical point that several participants found decisive: with the target range already at 0 to 0.25 percent, there was no meaningful room to cut further, so easing was not a feasible tool even had the data called for it. Given the still-incomplete recovery and the absence of inflation pressure, he judged that holding kept policy maximally supportive of employment.

The participant attentive to financial stability scanned for stress signals and found none that would push the Committee off its path: a stress index near zero, a Baa spread at 2.21 showing no credit widening, and delinquencies steady to down modestly. His one lingering concern was the compressed VIX at 11.6 and the reach-for-yield complacency that ultra-low volatility can seed, but he characterized this as a medium-term instability worry rather than an immediate trigger. He added that a rate move in either direction would itself be a destabilizing surprise, given that markets were pricing continuity. The member weighting market signals most heavily reinforced this reading, noting that the T-bill spread at -0.085 showed no near-term hike priced in and that the positive 10-year to 2-year spread gave no recession signal; in his view market pricing and fundamentals both pointed to holding steady. The data-dependent member took the indicators at face value and arrived at the same literal consensus reading — below-target inflation and persistent slack argued for maintaining accommodation, and nothing in the data created urgency to deviate.

When participants turned to the framework's recommendation, the discussion reinforced rather than reopened these positions. Several noted that the estimated neutral real rate of -0.5 percent meant the current floor was not overly accommodative, and all four reference rules converging on no change lent discipline to the hold. The inflation-focused member found the Taylor rule most persuasive, observing that its inflation gap already leaned easy; the employment-focused member and the financial-stability voice each found the ELB-adjusted rule most directly relevant to a situation in which rates could not go meaningfully lower. Inflation momentum of 0.11 and unemployment momentum of zero were cited as evidence of no dynamic pressure forcing a change. Participants generally judged that the agreement between their own reasoning and the framework indicated the stance was appropriately calibrated: accommodative but not requiring further easing, and not yet warranting any withdrawal of support.

Across the rounds, no participant offered an argument for a move in either direction, and none was persuaded to revise. The remaining differences were ones of emphasis rather than direction — the



degree of vigilance owed to firming labor markets and input prices, and the weight to place on compressed volatility as a future rather than present risk. Participants agreed to continue monitoring these developments, with particular attention to any acceleration in inflation momentum or any reversal in job growth.

COMMITTEE POLICY ACTIONS

In the predictive vote, all five members supported maintaining the current federal funds target range at 0.0 to 0.25 percent, a unanimous 5-to-0 outcome with no dissents. On the optimal-policy 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 none declining and none registering partial agreement. The predictive and optimal-side outcomes were therefore fully aligned.