



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The System Open Market Account held \$4,222.9 billion in domestic securities as of the December 9 release, essentially unchanged from the December 2 release, a reported change of zero. The composition was split between \$2,346.6 billion in Treasury notes and bonds and \$1,744.8 billion in agency mortgage-backed securities. The staff noted that this account remained flat over the week, with no additions or runoff registered in the point-in-time data. It should be emphasized that these figures cover SOMA securities holdings only — total size, composition, and week-over-week change — and do not encompass the results of repo or reverse-repo operations, for which no point-in-time-safe data source is currently available.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reported that labor market conditions continued to firm. The unemployment rate stood at 5.0 percent, essentially at the estimated natural rate of 5.05 percent, and initial jobless claims remained low at 269,000. The Beige Book for the Second District described labor markets as showing 'some further signs of tightening,' with service-sector firms reporting ongoing upward pressure on input prices and wages. The Employment Cost Index reading was 124.5. Against this firming in labor conditions, price pressures remained subdued: core PCE inflation ran at 1.19 percent on a twelve-month basis, well below the Committee's 2 percent objective, and District contacts characterized selling prices as generally stable.

Broader activity indicators pointed to growth near trend but with several soft spots. The Chicago Fed National Activity Index registered -0.04 , consistent with roughly trend growth. The Beige Book described District activity as having 'leveled off' since the prior report. Consumer spending was 'mixed but somewhat weaker, on balance,' with retailers reporting sluggish October and early-November results; one major chain reported sales below plan and below 2014 levels in both months. Contacts attributed some softness to the strong dollar's effect on tourism, particularly in New York City, and to mild weather dampening seasonal merchandise. Tourism remained sluggish and manufacturers continued to report weakening activity. Offsetting these, housing markets continued to improve, commercial real estate was mostly stronger, and banks reported a pickup in demand for commercial loans and mortgages along with some improvement in delinquency rates for commercial borrowers.

STAFF REVIEW OF THE FINANCIAL SITUATION

Financial conditions were described as calm. The financial stress index stood at 0.099, a very low reading, and the VIX at 19.61 was moderate rather than elevated. The Baa corporate spread at 3.19 was somewhat wide, which the staff flagged as a mild indication of credit-cost pressure worth monitoring,



though not a sign of systemic stress. The Treasury yield curve remained positively sloped, with the 10-year/2-year spread at 1.29, giving no inversion or recession signal from the term structure. The 3-month T-bill spread relative to the current rate stood at 0.145, a level that exceeded the width of the current target range and suggested that market participants were pricing in a near-term move. M2 money supply was reported at \$12,201.4 billion.

STAFF ECONOMIC OUTLOOK

The staff's projection took as a starting point that the estimated neutral real rate (r^*) was around -0.5 percent, implying that the current 0.0 to 0.25 percent target range was already close to neutral in real terms rather than substantially accommodative. On this reading, the degree of stimulus provided by the present stance was more limited than the level of nominal rates alone might suggest. Inflation momentum was estimated at a barely positive 0.055 and unemployment momentum at -0.1, indicating slow, gradual improvement rather than acceleration on either front. Taken together, these figures pointed to conditions likely to evolve only slowly: no near-term inflation pickup that would force restraint, and no rapid tightening of labor markets beyond an already largely closed gap.

Consistent with this, all four reference rules — the Taylor rule, the Balanced Approach rule, the First-Difference rule, and the ELB-adjusted rule — prescribed a 0 basis point move, and all were judged reliable for this meeting. The staff noted that the below-target inflation shortfall, weighted against an unemployment gap near zero, netted to a prescription to hold under each rule; even the ELB-adjusted rule, which accounts for the proximity to the lower bound, returned the same result. The projection therefore implied that, absent a change in the incoming data, current policy settings were broadly aligned with what the rules would optimally require, with inflation expected to return toward target only gradually.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In the initial round of predictive discussion, all five participants indicated they expected a 25 basis point increase, moving the target range from 0.0 to 0.25 percent up to 0.25 to 0.50 percent. The reasoning converged around a shared reading that the labor-market precondition for liftoff had been met: unemployment at 5.0 percent essentially at the natural rate, low jobless claims, and Beige Book evidence of further tightening and upward wage pressure in services. Participants generally judged that although core PCE at 1.19 percent remained well below the 2 percent objective, prior guidance had conditioned a move on 'reasonable confidence' that inflation would return to target over the medium term rather than on inflation already being at target.



The member weighting inflation risk most heavily framed the case as a hedge against forward inflation pressure as slack disappeared, while conceding that immediate price pressure was modest. The participant focused on the employment mandate observed that the conditions ordinarily prompting a dovish stance — rising unemployment or slowing job growth — were simply absent, and so found no basis to resist a small, gradual move. The financial-stability voice emphasized that the calm backdrop, with the stress index at 0.099 and a moderate VIX, meant a well-telegraphed move was unlikely to shock placid markets, while the participant weighting market signals noted that the 3-month T-bill spread of 0.145 implied markets had already priced a near-certain hike. The centrist read the literal, consensus interpretation of the data as supporting a first step. In the rebuttal round, no participant was moved from this position; several noted that the soft inflation reading argued against anything larger than 25 basis points, and each characterized the convergence as coherent rather than merely coincidental.

The character of the discussion shifted when participants turned to the loss-minimizing framework, which recommended holding at 0.0 to 0.25 percent. Here a genuine gap opened between what participants expected the Committee to do and what the data alone appeared to require. The participant focused on inflation risk acknowledged this as a rare case in which the usual bias toward hiking lost its footing: with core PCE well below target and inflation momentum barely positive at 0.055, no acceleration signal justified preemptive tightening, and the Beige Book's stable selling prices and weak consumer spending offered no demand-driven price pressure to counter. That member found the Balanced Approach rule, with its heavy weighting of the inflation shortfall, most persuasive on the framework's own terms.

Other participants reinforced the case for holding from their distinct vantage points. The employment-focused member stressed that unemployment momentum of -0.1 indicated decelerating rather than robust improvement, and that with r^* estimated at -0.5 percent the near-zero stance was barely accommodative — leaving little to be gained from adding restraint into softening demand. The financial-stability voice returned to the somewhat wide Baa spread of 3.19, arguing that tightening into that credit backdrop and the fragile demand described in the Beige Book carried destabilization risk without inflation cover; that member found the ELB-adjusted rule most telling, since it prescribed a hold even after accounting for the lower bound. The market-signal participant drew the sharpest distinction, noting that market pricing reveals what the Committee is expected to do, not what fundamentals optimally require, and that the convergence of all four reference rules at 0 basis points was the more authoritative guide to the latter.



Across the final rebuttal, participants explicitly reconciled the divergence between their predictive votes and the framework's recommendation. Several described their anticipated 25 basis point move as reflecting the Committee's normalization impulse and forward-looking read of the medium-term return to 2 percent, while conceding that the current mandate readings — a clear inflation shortfall, momentum near zero, and labor at but not beyond its natural rate — did not by themselves supply a data-grounded case for tightening. The centrist summarized this as an honest gap: the predictive hike was driven by normalization intent, whereas the literal reading of the data and the reliable reference rules counseled patience. No participant identified an argument that overturned the framework's 0 basis point prescription.

COMMITTEE POLICY ACTIONS

In the predictive vote on the policy action, all five participants supported a 25 basis point increase in the target range, from 0.0 to 0.25 percent to 0.25 to 0.50 percent, a unanimous tally of 5 for the increase. Separately, on the deterministic optimal policy framework's recommendation to hold at 0.0 to 0.25 percent — grounded in the convergence of the Taylor, Balanced Approach, First-Difference, and ELB-adjusted rules at 0 basis points — all five members endorsed the recommendation as-is, with none declining and none registering partial agreement. The Committee thus recorded a genuine and openly acknowledged divergence between its predictive expectation of a near-term move and its unanimous judgment that, on the current data alone, holding was the loss-minimizing course.