



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The manager reported on the System Open Market Account, which as of the June 5 release stood at \$6,701.1 billion in total domestic securities holdings. Composition was concentrated in Treasury notes and bonds at \$3,791.5 billion, with Treasury bills accounting for a comparatively small \$195.2 billion and agency mortgage-backed securities at \$2,346.5 billion. Total holdings declined by \$28.7 billion from the prior release of May 29, continuing a gradual reduction in the portfolio's size. It should be noted that this review covers SOMA holdings only — total size, composition, and the week-over-week change — and does not encompass repo or reverse-repo operation results, for which no point-in-time-safe data source is currently available.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reviewed incoming data as pointing to an economy that had cooled modestly while remaining fundamentally solid. Core PCE inflation stood at 2.28 percent on a twelve-month basis, above the Committee's 2 percent objective but well down from earlier peaks. The unemployment rate was 3.9 percent, still below the estimated natural rate of 4.41 percent, and initial jobless claims at 219,000 gave no indication of emerging labor-market stress. The Employment Cost Index registered 164.0. The Chicago Fed National Activity Index at -0.23 indicated growth somewhat below trend, consistent with an economy expanding but losing some momentum. M2 stood at \$20,867.3 billion.

The Beige Book characterized economic activity as about flat on balance, with prices increasing modestly and wage growth described as slow-to-moderate amid stable employment. Real estate activity, both commercial and residential, had weakened slightly after showing signs of improvement earlier in the year. Across Districts the tone was mixed but cautiously optimistic: New York and Philadelphia reported slight growth with better balance between labor demand and supply, while Cleveland noted a slowdown that some contacts attributed to interest rates staying 'higher for longer' than anticipated, and reported a modest decline in consumer spending. Richmond described moderate consumer spending driven by higher-income households as lower-income individuals pulled back or traded down. Atlanta reported easing wage pressures and generally healthy consumer demand. Several Districts flagged that expectations for future growth had edged down even as they remained positive.

STAFF REVIEW OF THE FINANCIAL SITUATION

The staff described financial conditions as calm and broadly accommodative relative to the stance of policy. The financial stress index at 0.1385 was low, and the VIX at 12.63 was very low, pointing to little market anxiety and, by some readings, a degree of complacency. Credit conditions appeared healthy,



with the Baa corporate spread at 1.49 remaining tight and showing no sign of borrowing-cost distress. The 10-year/2-year Treasury spread was inverted at -0.43 , a configuration consistent with market expectations of eventual easing alongside recession risk, while the 3-month T-bill spread of -0.125 relative to the current target range suggested markets leaned slightly toward lower rates ahead but were not pricing an imminent move. The current target range for the federal funds rate was 5.25 to 5.50 percent.

STAFF ECONOMIC OUTLOOK

The staff outlook drew on the forward-looking quantities embedded in the reference-rule framework. The estimated neutral rate was negative at -0.436 , implying that the current 5.25 to 5.50 percent range sits well above neutral and is therefore meaningfully restrictive. Inflation momentum was slightly negative at -0.055 , suggesting that disinflation was continuing rather than reversing, while unemployment momentum was modestly positive at 0.05 , a mild signal of labor-market cooling. Taken together, these figures pointed to conditions in which price pressures were likely to keep easing gradually and labor slack to build slowly rather than abruptly.

The reference rules that the framework judged reliable spanned a wide range. The Taylor rule, the Balanced Approach rule, and the ELB-adjusted rule each pointed to -75 basis points, reflecting the gap between the current range and the low estimated neutral rate together with inflation near target. The First-Difference rule, which responds to the change in conditions rather than the level gap, pointed the other way at $+25$ basis points. The framework's loss-minimizing recommendation of -25 basis points fell between these poles, implying that the likely path of conditions would support a measured initial reduction in restrictiveness rather than either a large move or continued holding, provided inflation momentum stays contained.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their initial predictive discussion, participants converged on holding the target range at 5.25 to 5.50 percent, though they reached that judgment from distinct vantage points. The participant most focused on inflation risk emphasized that core PCE at 2.28 percent remained above the 2 percent objective and that the prior meeting had demanded greater confidence in sustained disinflation before any cut — confidence not yet established. This participant read the Beige Book's modest price increases and slow-to-moderate wage growth as some progress but not decisive, and saw no urgency to move given a labor market still tight at 3.9 percent unemployment, below the 4.41 percent natural rate.



The participant attentive to employment risk framed the hold as conditional. With unemployment below the natural rate and claims low at 219,000, no realized labor deterioration justified a cut this meeting, but this participant flagged the inverted 10-year/2-year spread and the below-trend Chicago Fed index as forward risks worth taking seriously and stated a readiness to move promptly should unemployment rise or claims break higher. The participant focused on financial stability observed that no stress indicator was flashing alarm — the stress index at 0.1385, the VIX at 12.63, and the Baa spread at 1.49 all pointed to calm, even complacent, markets — and judged that cutting into such conditions with above-target inflation risked re-igniting price pressures. The data-dependent participant and the market-signal participant read the incoming data as most literally supporting a hold, with the latter noting that the T-bill spread of -0.125 implied markets expected eventual easing but were not pricing a move at this meeting. In the rebuttal round no participant was persuaded to revise, and the predictive vote was unanimous.

The discussion shifted materially when participants turned to the framework's loss-minimizing recommendation of -25 basis points. Here the convergence loosened into genuine debate. Several participants found the case for a measured first cut persuasive. Those weighing employment and stability risks pointed to the negative estimated neutral rate of -0.436 as evidence that the current range was deeply restrictive, and read the Beige Book's weakening real estate and the contacts citing 'higher for longer' rates as the slow credit-channel and demand strain that restrictive policy was already imposing. The employment-focused participant characterized -25 basis points as front-loaded insurance — beginning to remove excess restriction before labor damage became visible in the hard data, on the view that waiting for unemployment to actually rise risks acting too late.

Participants supporting the recommendation generally agreed on its magnitude as much as its direction. The market-signal participant argued that the T-bill spread justified roughly one quarter-point cut and no more, so that the -75 basis points implied by the Taylor, Balanced Approach, and ELB-adjusted rules would front-run market pricing, while the +25 of the First-Difference rule ignored the inverted curve and below-trend activity. The framework's -25 was seen as threading these signals. The financial-stability participant made a parallel point: a full -75 could jar calm markets and appear panicked absent any stress justification, whereas a small preemptive cut would relieve gradual credit tightening before it built into future instability. The data-dependent participant likewise judged that near-target inflation with negative momentum, combined with a range far above neutral, supported a measured first step.

The inflation-focused participant, however, declined to support the recommendation. While acknowledging that the direction toward eventual easing was defensible and that the framework's



tempering of the aggressive rules to -25 itself reflected inflation caution, this participant judged the timing premature. Core PCE remained above target, inflation momentum at -0.055 amounted to one soft reading rather than sustained progress, and the prior statement's concern that inflation was 'relatively broad based' had not been resolved. This participant stressed that the estimated neutral rate and recession signals were model estimates, not realized labor damage, and that with claims low and unemployment below the natural rate there was no labor emergency. Cutting while inflation sat above target, on this view, risked an embarrassing reversal should prices reaccelerate; holding until confidence was greater cost little given calm markets and only modest market-implied easing.

COMMITTEE POLICY ACTIONS

On the predictive question of the policy decision at this meeting, the Committee voted unanimously, 5 to 0, to maintain the target range for the federal funds rate at 5.25 to 5.50 percent. On the separate question of the framework's loss-minimizing recommendation of -25 basis points, the Committee did not reach full agreement: four members — the labor-market participant, the financial-stability participant, the data-dependent participant, and the market-signal participant — endorsed the recommendation as-is, while one member, the inflation-focused participant, declined to support it on the grounds that a cut was premature with inflation still above target. There were no partial positions.