



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

System Open Market Account holdings of domestic securities totaled \$6,400.1 billion as of the January 22, 2025 release, the most recent available on or before the point-in-time-safe cutoff. Of that total, Treasury notes and bonds accounted for \$3,647.3 billion, Treasury bills for \$195.3 billion, and agency mortgage-backed securities for \$2,221.8 billion. Holdings declined by \$3.3 billion from the prior release on January 15. The manager noted that this review covers SOMA securities 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 currently exists.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reported that core PCE inflation stood at 2.12 percent on a twelve-month basis, modestly above the Committee's 2.0 percent objective. The unemployment rate was 4.1 percent, below the estimated natural rate of 4.32 percent, and initial claims for unemployment insurance remained low at 217,000. The Chicago Fed National Activity Index registered -0.12, consistent with growth near trend, and the Employment Cost Index reading came in at 166.8. M2 money supply stood at \$21,447.6 billion. The current target range for the federal funds rate was 4.25 to 4.50 percent, with the Committee's most recent set of projections having shown a median projected federal funds rate of 3.9 percent.

Drawing on the Beige Book, the staff observed that economic activity had increased slightly to moderately across the twelve Districts in late November and December. Consumer spending moved up moderately, with most Districts reporting strong holiday sales that exceeded expectations, while vehicle sales grew modestly. Construction activity decreased overall as high materials and financing costs weighed on growth, and manufacturing decreased slightly on net, with a number of Districts noting that manufacturers were stockpiling inventories in anticipation of higher tariffs. Residential real estate activity was unchanged on balance as high mortgage rates continued to hold back demand. On labor, employment ticked up on balance, with six Districts reporting a slight increase and six reporting no change; layoffs remained rare and contacts across multiple sectors noted difficulty finding skilled workers, though some Districts expressed greater uncertainty about future staffing needs. Wage growth picked up to a moderate pace in most Districts, though some reports indicated easing pressures. Prices increased modestly overall, with an avian flu outbreak reducing egg supplies and lifting prices. More contacts were optimistic about the outlook for 2025 than pessimistic, but several Districts flagged concern that changes in immigration and tariff policy could weigh on the economy.

STAFF REVIEW OF THE FINANCIAL SITUATION



The staff characterized financial conditions as calm and accommodative. The financial stress index stood at 0.1118, a low reading indicating well-functioning markets with no acute strain, and the VIX at 15.1 reflected subdued equity-market volatility. The Baa corporate spread of 1.46 percentage points was tight, consistent with healthy corporate borrowing conditions. The 10-year/2-year Treasury yield curve spread was positive at 0.31 percentage point, an un-inverted configuration that removed the recession signal that an inversion would carry. The 3-month Treasury bill yielded 15.5 basis points below the current federal funds rate midpoint, a modest negative spread suggesting that market participants anticipated some easing over time rather than an imminent move. Financial service providers reported modest growth in lending and little change in asset quality overall, though lenders and community organizations voiced concerns about delinquencies among small businesses and lower-income households.

STAFF ECONOMIC OUTLOOK

The staff outlook took as its point of departure several forward-looking quantities embedded in the policy framework. The estimated neutral real rate (r^*) was placed at -0.227 , an unusually low value that, when fed through the level-based reference rules, implied substantial room for accommodation: the Taylor rule, the Balanced Approach rule, and the ELB-adjusted rule each pointed to a 75 basis point reduction. The First-Difference rule, which responds to the change in conditions rather than to an estimated level of neutral, indicated no change. Inflation momentum was mildly positive at 0.17, while unemployment momentum was flat at 0.0, and the reference rules were flagged as reliable in the current configuration.

Taken together, these figures projected an economy operating close to both mandate objectives, with no deterioration in labor markets to pull policy toward easing and a small but positive drift in inflation that argued against it. The gap between the level rules and the First-Difference rule was largely attributable to the very low r^* estimate; the staff noted that such neutral-rate estimates carry considerable uncertainty and that placing full weight on them would imply a far more restrictive characterization of current policy than the momentum-based reading supported. On balance, the loss-minimizing recommendation from the framework was for no change to the target range, reflecting a judgment that current policy is roughly appropriate given near-target inflation, positive inflation momentum, and steady employment, with tariff and immigration policy uncertainty representing an unresolved upside risk to prices over the projection horizon.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their discussion of current conditions, participants generally judged that the economy was close to both of the Committee's objectives and that there was no urgent case for adjusting the target range



this meeting. Core PCE inflation at 2.12 percent was seen as slightly above the 2.0 percent goal, and several participants stressed that disinflation had visibly slowed over the course of 2024, with recent readings coming in higher than expected. The member most focused on inflation risk emphasized that the fight was not yet finished and that back-to-back easing, following the prior meeting's 25 basis point cut, would risk re-accelerating prices while there was little offsetting benefit. This participant pointed to the Beige Book's observation that wage growth had 'picked up to a moderate pace' in most Districts and that selling prices were rising modestly, as well as to reports that manufacturers were stockpiling inventories ahead of anticipated tariffs — a signal of coming price pressure rather than one already visible in the data.

The member whose mandate weighted employment risk most heavily approached the question from the labor side and reached the same conclusion. With unemployment at 4.1 percent below the 4.32 percent natural rate, initial claims low at 217,000, and layoffs rare, this participant saw no deterioration that would justify a defensive cut to protect jobs. The Beige Book note that some Districts expressed greater uncertainty about future staffing needs was flagged as a watch item, but current signals were judged inconsistent with softening that would demand preemptive easing. This participant observed that because the labor market was firm, there was no need to 'spend a cut' now, and that holding preserved the capacity to move promptly and more forcefully should employment weaken later.

The participant attentive to financial stability noted that core stability indicators were benign across the board: the financial stress index at 0.1118, the VIX at 15.1, a tight Baa spread of 1.46 percentage points, and a positive 10-year/2-year curve. The lone genuine watch item from this perspective was the Beige Book's mention of delinquency concerns among small businesses and lower-income households, but this was characterized as a concern rather than a materializing stress, with financial service providers reporting little change in asset quality overall. This participant cautioned that cutting into calm, well-anchored conditions would risk re-loosening financial conditions and reigniting inflation without any offsetting stability benefit. The market-focused participant reinforced this reading from the pricing side: the 3-month bill sitting 15.5 basis points below the current rate midpoint implied roughly a gradual path of easing over time rather than an imminent January move, and the un-inverted curve carried no recession alarm. The data-dependent member summarized the balance as an economy near both mandate goals simultaneously, where patience allowed the Committee to assess whether disinflation would resume amid tariff uncertainty.

When the discussion turned to the framework's loss-minimizing recommendation of no change, participants engaged directly with the divergence between the reference rules. Several participants noted that the Taylor, Balanced Approach, and ELB-adjusted rules each pointed to a 75 basis point cut,



but attributed those signals primarily to an implausibly low estimated neutral rate of -0.227 . A number of participants expressed distrust of placing weight on so uncertain an r^* estimate and found the First-Difference rule's reading of no change more persuasive, since it responded to inflation momentum of 0.17 and flat unemployment momentum rather than to a noisy level of neutral. Participants generally interpreted the gap between the -75 basis point level rules and the 0 basis point decision as evidence that current policy, though restrictive on paper, was in fact only mildly restrictive and roughly appropriate — not loose enough to overheat and not so tight as to strain credit.

In the concluding exchanges, participants agreed that no argument raised had shifted their positions, and that the convergence of the inflation-focused and employment-focused members on holding, arrived at through different mandate lenses, constituted a genuine consensus signal rather than mere coincidence. Participants broadly concurred that holding at 4.25 to 4.50 percent preserved optionality against the unresolved upside inflation risks flagged in the Beige Book — tariff stockpiling and immigration policy uncertainty — while leaving the Committee well positioned to respond should credit conditions deteriorate or employment soften. The Committee reaffirmed its intention to remain data-dependent as it assessed incoming information.

COMMITTEE POLICY ACTIONS

In the predictive round, all five participants supported maintaining the target range for the federal funds rate at 4.25 to 4.50 percent, a unanimous vote of 5 to 0 for no change. On the deterministic optimal policy framework's recommendation of 0 basis points, the Committee's recorded stance was likewise unanimous: 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 decision and the optimal-side outcome were thus in full alignment.