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THE SEMIANNUAL MONETARY POLICY REPORT TO THE CONGRESS

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BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED EIGHTEENTH CONGRESS

SECOND SESSION

ON

OVERSIGHT ON THE MONETARY POLICY REPORT TO CONGRESS PURSU-
ANT TO THE FULL EMPLOYMENT AND BALANCED GROWTH ACT OF 1978

JULY 9, 2024

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C O N T E N T S

TUESDAY, JULY 9, 2024

	Page
Opening statement of Chair Brown	1
Prepared statement	42
Opening statements, comments, or prepared statements of:	
Senator Scott	3
Prepared statement	43

WITNESS

Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System ..	6
Prepared statement	45
Responses to written questions of:	
Chair Brown	47
Senator Scott	49
Senator Van Hollen	58
Senator Hagerty	59

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

Monetary Policy Report to the Congress dated July 5, 2024	61
Documents submitted for the Record	135

THE SEMIANNUAL MONETARY POLICY REPORT TO THE CONGRESS

TUESDAY, JULY 9, 2024

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10 a.m., via Webex and in room 216, Hart Senate Office Building, Sherrod Brown, Chair of the Committee, presiding.

OPENING STATEMENT OF CHAIR SHERROD BROWN

Chair BROWN. The Committee on Banking, Housing, and Urban Affairs will come to order.

Welcome, Chair Powell. Nice to have you back. Good to have you first this time of year.

Ohioans know, Americans know, that our economy fundamentally is not a fair playing field. Instead, we have a David-and-Goliath economy where the largest corporations use their power to funnel all the gains in the economy to the top, aided and abetted by too many people in this room. Corporations squeeze every last penny from Americans' pocketbooks and workers' paychecks.

They don't even try to hide it anymore. The biggest corporations are charging more for less. Americans are frustrated. No. Actually, Americans are pissed off. They have fewer and fewer choices. Those choices cost more and more. Keeping prices down is part of the Fed's mandate. But as many of us have made clear, the Fed's main tool to combat inflation—raising interest rates—does nothing to address the biggest causes of rising prices right now, corporate greed.

Keeping rates too high for too long threatens workers' paychecks while keeping other costs high, particularly housing costs. Housing prices and rents continue to go up. It's no surprise that since the Fed began raising rates the amount of income families need to qualify for a mortgage has nearly doubled. Home ownership has long been a bedrock of our middle class, but today fewer and fewer middle class families can afford to buy a home.

Higher interest rates are making our country's housing supply shortage worse, not better. We need more housing construction of all types. Higher rates lead to the opposite and particularly make it harder for multifamily construction to work financially. Higher interest rates make borrowing more expensive for working families, whether it's for a mortgage or a car or anything else.

Most people don't have the luxury of paying for everything in cash. And for the millions of Americans feeling their budgets

stretched by higher prices, taking on credit card debt to pay for groceries and other essentials has become an option of last resort.

But as more people struggle to pay down their debts, credit card interest rates are reaching all-time highs. Last month, Director Chopra testified in front of this Committee and explicitly stated that credit card issuers are charging higher rates far beyond what they need to cover their costs, corporate greed rearing its head again.

Banks are making record profits at the expense of cash-strapped Americans. Every month that the Fed keeps rates high, Mr. Chair, it costs Americans money by making it more expensive to buy a house and to borrow money. Higher borrowing costs stifle future economic growth, leading to fewer homes being built, leading to businesses making fewer investments in the economy, and eventually, if the Fed doesn't stop, leading to workers losing their jobs.

As they set economic policy, I urge the Fed to weigh these trade-offs and remember whose jobs and futures are at stake. It's why I have worked with my colleagues to hold corporations accountable and will continue to do that. For instance, we fought to cap insulin prices for senior citizens. We'll continue to fight to extend this price gap—this price cap—on lifesaving drugs for all Americans, and why my colleagues and I on this Committee are working—it's why we're working to lower housing costs for more Americans.

The Fed also continues its work to keep the banking system stable and ensure consumers' money is safe. Last year, the Fed and other bank regulators issued a proposal to update bank capital requirements, strong capital standards, and you've heard in this Committee overwhelming support for strong capital standards.

They are critical for the economy. It's our way of making sure that if Wall Street's bets go poorly, which they often do, investors, executives, and shareholders should pay for it, not taxpayers. The biggest banks have spent—have spent obscene amounts of money attacking this Fed proposal. But you, the Fed, don't work for big banks. You work for the American people. Your concern should be developing capital rules that protect Americans' money, not protect bank CEO's stock portfolios. The Fed needs to look past these shameless lobbying efforts and finalize a rule in the best interest of taxpayers.

Another dangerous piece of the Wall Street business model that makes our banking system less safe is incentive-based compensation. This compensation model rewards risky behavior that enriches Wall Street executives in the short term but banks—makes banks more likely to fail.

We saw the results of that model in 2008. We saw it again last year with the failure of Silicon Valley Bank and Signature. Other regulators have moved forward with a proposal to rein in these reckless incentives, but the rule, Mr. Chair, can't move forward without your and the Fed's moving on it. This rule is long overdue. The Fed must join the statutorily required effort as soon as possible.

The Fed also has the important job of reviewing mergers and acquisitions between and among banks. Over the last several decades, we've seen the largest banks grow into massive, literally trillion-dollar companies, while thousands of small banks in rural com-

munities in northwest and southeast Ohio, in small towns in those areas, and all across America, have disappeared. Consumers have lost trust at local banks. Small businesses have lost long-time reliable banking partners.

Regulators like the Fed have the crucial job of guarding against mergers that reduce or eliminate competition and lead to bank closures or layoffs.

I recently sent comment letters to the OCC and the FDIC on their current efforts. I expect the Fed to take the proper steps to ensure that its merger review process is robust and that it protects consumers and communities.

Finally, Mr. Chair, you must ensure the Fed has high ethical standards. Fed officials should never again be able to profit from their positions by using confidential plans about Fed monetary policy and emergency programs to pad their investment portfolios.

The Board's latest update to its trading rules is simply not good enough. It still fails to establish the clear penalties needed for Federal Reserve officials who make investments in violation—in violation of the public trust. A rule with no consequences is really not much of a rule at all.

The American people need to be able to trust that the Federal Reserve works for them in a time of deep cynicism that people have about the Federal Government overall, and the American people need to know that officials aren't abusing their positions for personal gain.

As chair, you have an important role to play to make sure the economy works for everyone, not just for Wall Street. The Fed's regional banks must do their part to hear from people and other stakeholders in their 12 districts to understand their needs.

I look forward to hearing today how the Fed will balance its dual mandate, how it will protect Americans' money, how it will foster an economy that upholds the dignity of work.

Senator Scott.

OPENING STATEMENT OF SENATOR TIM SCOTT

Senator SCOTT. Thank you, Mr. Chairman.

Thank you, Chair Powell, for being with us this morning. Welcome, and welcome back.

Joe Biden broke this economy, and it has been very difficult to fix it. That's the bottom line. I want to start with the end in mind. Joe Biden broke our economy, and it is very difficult for anyone to fix it.

Everyday families are struggling to put food on the table. Real wage growth is being eaten away by rising prices and runaway inflation. Think about the fact that for 52 consecutive weeks under Joe Biden, wages were eclipsed by inflation. For 52 consecutive paychecks.

I remember back in December 2020, in South Carolina gas was \$1.99 per gallon. Today it's still \$3.19 per gallon, a 50 percent increase in just a few years. So, it's devastating to the average American family, particularly families like the one I grew up in, a single-parent household mired in poverty.

When you see your gas prices up 50 percent, your food up 30 percent, your cost of keeping your house cool or warm up 25 percent,

it's not a challenge. It's not unfortunate. It's an absolute crisis. And too many households in America today are living paycheck to paycheck, and they fear the challenges that are coming our way, the headwinds brought to us by the Biden administration.

Those headwinds, of course, are seen through the prism of inflation. Inflation hasn't been this high since the Jimmy Carter years, and that devastation is being felt and measured in the households by too much money at the end of the month. And that devastation is real for the vast majority of Americans.

And the finger pointing—I'll tell you what, whether—it's the Biden administration throwing the Fed under the bus or any other way they can deflect from the real problem. I've seen it committee hearing after committee hearing after committing hearing. My friends on the left want to point their fingers at anyone other than the real culprit at 1600 Pennsylvania Avenue.

The progressive wish list spending projects and out-of-control regulations of this Administration continues to eat away at American paychecks, and they continue to blame—whether it's shrinkflation, greedflation, skimpflation—they are looking for someone to blame except for Bidenflation. The devastation of Joe Biden's economic policy continues to impact everyday Americans.

The American people see through the facades, and they want real solutions. It doesn't take a Ph.D. economist to understand what the average American is experiencing under this Administration.

When President Biden and my Democratic colleagues pumped trillions of dollars into our economy, those dollars increased the demand and pushes prices higher. It's that simple. The American people see and feel it every single time, and they see it, as I said earlier, at the grocery stores, the gas stations, at the doctor's office. It's just undeniable the impact that is happening.

Just last week we celebrated the birth of our country, the birth of this notion of freedom and liberty. But American families got slapped with the most expensive July 4th on record with a cookout this year costing on average 30 percent more than it did just a few years ago. I call that hogwash.

What's worse is that this Administration doesn't want to learn a lesson in economics. Instead of reducing the push for more spending and more regulation, they only simply double down. Let's take, for example, the tens of billions of dollars of student loan forgiveness, constant new plans to forgive more money, regardless of the constitutionality of their decisions.

So, it's important to ask, who are these billions of dollars of forgiveness actually benefiting? Well, the answer is simple. This forgiveness scheme will result in debt relief for 750,000 individuals from households with an average income of 300,000 or more. And just don't forget the fact that the average American family has a household income around \$74,000.

So, what we're doing with this unconstitutional student loan forgiveness is actually asking the median household of \$74,000 per household to bear the burden of forgiving debt for students who live in households of over \$300,000. And the actual cost of this, somewhere between \$870 billion and \$1.4 trillion.

So, why do I have to even ask the question? Why do we continue to punish American families struggling paycheck to paycheck with a new scheme to relief households over \$300,000 of student loan debt? Well, the answer is pretty simple. Politics. It's one way to buy vote after vote after vote for November's election. It's just hard to imagine.

So, while I appreciate your measured words outlining the Fed's work to cool inflation, I think it's past time we all recognize what is truly going on: political pandering from the left. I strongly believe that our economy cannot handle any more of this wasteful spending. And if you disagree, I would love to hear your thoughts on that.

But it's not just spending policies that stifle growth. It's also overregulation, and I can't think of a better example of overregulation than parking more capital on the sidelines through Basel III endgame. That proposal itself would cost millions of Americans their chance to own a home, start a small business, and have access to the credit and the capital necessary to make their American dreams come true.

For those who are actually watching this hearing today on C-SPAN, Basel III capital requirements are like taking your star quarterback, Dak Prescott, and telling him to sit on the sidelines because he just might get injured during the season. It's just plain ridiculous. But these proposed capital requirements would just do that, forcing more money to the sidelines of the greatest economy on the planet and out of the hands of first-time homebuyers, business owners, and folks trying to achieve the American dream.

The stakes are high, and that is why we have to get this right. You've heard me say this a number of times, but it bears repeating. We need transparency in your rulemaking process as this enormous proposal lacks any form of clear justification.

Chairman Powell, it is essential that you and your fellow governors and the other agencies join in this rulemaking, following the law, do the homework, and then let the public check the work. That's why I believe that it is absolutely necessary to have a complete re-proposal of Basel III endgame. Give the stakeholders an opportunity to take a look at it, and then recalibrate what is necessary going forward.

Any increases in capital that are not quantitatively justified harm the American people who need it most. Our farmers, homebuyers, small businessowners, need and deserve access to credit.

Therefore, I'll repeat it one more time, you need to restore confidence in this rulemaking process, pull the existing proposal, and have a complete restart. And then, when the data has been analyzed and is available for the public scrutiny, reissue an appropriate proposed rule following the requirements of the APA.

I look forward to your opening statement and having a chance to have a conversation afterwards.

Chair BROWN. Thank you, Senator Scott.

Mr. Chair, welcome. Thank you for your service and for your testimony today. Please proceed.

**OPENING STATEMENT OF JEROME H. POWELL, CHAIR, BOARD
OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM**

Mr. POWELL. Chairman Brown, Ranking Member Scott, and other Members of the Committee, I appreciate the opportunity to present the Federal Reserve's semiannual *Monetary Policy Report*.

The Federal Reserve remains squarely focused on our dual mandate to promote maximum employment and stable prices for the benefit of the American people. Over the past 2 years, the economy has made considerable progress toward the Fed's 2 percent inflation goal, and labor market conditions have cooled while remaining strong. Reflecting these developments, the risks to achieving our employment and inflation goals are coming into better balance.

I will review the current economic situation before turning to monetary policy.

Recent indicators suggest that the U.S. economy continues to expand at a solid pace. Gross domestic product growth appears to have moderated in the first half of this year following impressive strength in the second half of last year. Private domestic demand remains robust, however, with slower but still-solid increases in consumer spending. We have also seen moderate growth in capital spending and a pickup in residential investment so far this year. Improving supply conditions have supported resilient demand and the strong performance of the U.S. economy over the past year.

In the labor market, a broad set of indicators suggests that conditions have returned to about where they stood on the eve of the pandemic: strong, but not overheated. The unemployment rate has moved higher but was still at a low level of 4.1 percent in June. Payroll gains averaged 222,000 per month in the first half of the year.

Strong job creation over the past couple of years has been accompanied by an increase in the supply of workers, reflecting increases in labor force participation among individuals aged 25 to 54, so-called workers in their prime working years, and a strong pace of immigration.

As a result, the jobs-to-workers gap is well down from its peak and now stands just a bit above its 2019 pre-pandemic level. Nominal wage growth has eased over the past year. The strong labor market has helped narrow long-standing disparities in employment and earnings across demographic groups.

Inflation has eased notably over the past couple of years but remains above the Federal Open Market Committee's longer-run goal of 2 percent. Total personal consumption expenditures prices rose 2.6 percent over the 12 months ending in May. Core PCE prices, which exclude the volatile food and energy categories, also increased 2.6 percent.

After a lack of progress toward our 2 percent inflation objective in the early part of this year, the most recent monthly readings have shown modest further progress. Longer-term inflation expectations appear to remain well anchored, as reflected in a broad range of surveys of households, businesses, and forecasters, as well as measures from financial markets.

Our monetary policy actions are guided by our dual mandate to promote maximum employment and stable prices for the American people. In support of these goals, the committee has maintained

the target range for the Federal funds rate at $5\frac{1}{4}$ to $5\frac{1}{2}$ percent since last July, after having tightened the stance of monetary policy significantly over the previous year-and-a-half. We have also continued to reduce our securities holdings. At our May meeting, we decided to slow the pace of balance sheet runoff starting in June, consistent with the plans released previously. Our restrictive monetary policy stance is helping to bring demand and supply conditions into better balance and to put downward pressure on inflation.

The committee has stated that we do not expect it will be appropriate to reduce the target range for the Federal funds rate until we have gained greater confidence that inflation is moving sustainably toward 2 percent. Incoming data for the first quarter of this year did not support such greater confidence. The most recent inflation readings, however, have shown some modest further progress, and more good data would strengthen our confidence that inflation is moving sustainably toward 2 percent. We continue to make decisions meeting by meeting. We know that reducing policy restraint too soon or too much could stall or even reverse the progress that we have seen on inflation. At the same time, in light of the progress we have made both in lowering inflation and in cooling the labor market over the past 2 years, elevated inflation is not the only risk we face. Reducing policy restraint too late or too little could unduly weaken economic activity and employment.

In considering adjustments to the target range for the Federal funds rate, the committee will continue its practice of carefully assessing incoming data and their implications for the evolving outlook, the balance of risks, and the appropriate path of monetary policy.

Congress has entrusted the Federal Reserve with operational independence that is needed to take a longer-term perspective in the pursuit of our dual mandate of maximum employment and stable prices. We remain committed to bringing inflation back down to our 2 percent goal and to keeping longer-term inflation expectations well anchored. Restoring price stability is essential to achieving maximum employment and stable prices over the long run. Our success in delivering on these goals matters to all Americans.

I will conclude by emphasizing that we understand that our actions affect communities, families, and businesses across the country. Everything we do is in service to our public mission.

Thank you. I look forward to your questions.

Chair BROWN. Thank you, Mr. Chair. The senior Member of the Committee will begin the questioning. Senator Reed.

Senator REED. Thank you very much, Mr. Chairman. Former President Trump has indicated that he would propose, if elected, a substantial increase in tariffs of between 10 and 60 percent, and by doing, thus, eliminate the Federal income tax.

First, the question, though, what would be the impact of tariff increases on prices, consumers, and the economy?

Mr. POWELL. Thank you, Senator Reed. So, I am going to say that we go very far out of our way not to comment on campaign-type information. We just—we just don't do that. And we also don't comment on trade policy. We have really specific and important jobs, and we try to stick to those.

Senator REED. Well, I'm glad I allowed you to establish that principle up front, Mr. Chair.

[Laughter.]

Senator REED. But let me opine a bit. Ten percent increases in tariffs is going to have an effect on prices in the shop aisle. It's going to increase them, because they will be passed on likely. Sixty percent tariff increases are significant. And, in fact, I have been told that to replace the income tax we would have to raise tariffs across the board over 70 percent to make up for the loss of the income tax, which would I think create huge economic problems.

I respect your impartiality and your neutrality, but the numbers don't seem to add up to anything that would help the country.

Let me switch to something else that might be more within your line of response. You said in your opening statement that the labor markets appear to be in a better balance, and that's one of the key factors to judge whether interest rates can be lowered.

I must say, I am concerned a bit that we are not on a very fast track to decreasing interest rates from the Fed. And because of the better balance you cite, could you comment on that, Mr. Chairman?

Mr. POWELL. Sure. So, the most recent labor market data do send, to your point, a pretty clear signal that labor market conditions have cooled considerably compared to where they were 2 years ago. This is no longer an overheated economy. This is an economy, as I mentioned in my opening remarks, that is more or less back, by most measures, to where it was before the pandemic. And that was a strong labor market, but it was not an overheated labor market.

So, I think the upshot of that really is that we are—we are well aware that we now face two-sided risks and have for some time, but now it—you know, the labor market appears to be fully back in balance. We know that if we move too quickly we risk—we risk, you know, unnecessarily hampering economic activity and possibly interfering with the ongoing expansion.

We know that if we move too slowly that we may undo the good we've done. Well, actually, it's the other way. If we—if we loosen policy too late or too little, we could—we could hurt economic activity. If we loosen policy too much or too soon, then we could undermine the progress on inflation. So, we are very much balancing those two risks, and that's really the essence of what we're thinking about these days.

Senator REED. But the direction seems to be going toward lowering interest rates at some point, we would hope. That might be a wish rather than a direction.

Mr. POWELL. I think if you look at the last summary of economic projections, I guess I would say it this way. It doesn't seem likely that the next policy move would be a rate increase. We don't take things like that off the table, but that does not seem the likely direction.

The likely direction does seem to be in—as we make more progress on inflation, and as the labor market remains strong, we begin to loosen policy at the right moment.

Senator REED. Thank you. Two weeks ago the Supreme Court handed down two decisions that impact every Federal regulatory agency, including the Federal Reserve. They overturned the Chev-

ron case, which had eliminated judicial deference to agency decisionmaking for many, many decades. And they also dramatically extended the statute of limitations under the Administrative Procedure Act.

What, in your judgment, is the cumulative effect of these decisions on the Federal Reserve? More broadly, what does it mean to the economy if virtually any regulatory decision the Fed makes can be second-guessed by a judge? What position are we in now?

Mr. POWELL. So, we are—you know, we are, as an institution, very focused on reading the actual letter and intent of the law and following it carefully. This is a—this is a strong institutional value that we have. Those are brand-new decisions that just came down, and we're really in the process of just studying. So, I don't have anything for you on them, but we will of course follow the law as the Supreme Court—as the Supreme Court has read it, because that's their job.

Senator REED. Thank you. I concur with compliance with the law. But when you do your analysis, and if it is detrimental to your ability to regulate the banking interests of the United States, I think you have an obligation to make that public.

Thank you, Mr. Chair.

Chair BROWN. Thank you.

Senator Scott from South Carolina is recognized.

Senator SCOTT. Thank you, Mr. Chairman.

Chair Powell, we've heard a steady stream of commentary that there will be changes to Basel III endgame proposal. That can be seen certainly as good news. Some reports say it could be finalized as soon as August. Others say you are circulating a term sheet for a revised proposal.

Through it all, this proposal will have outsized impacts on our banking system from big to regional to our U.S.-based foreign institutions, as well as impeding access to credit for consumers. So, even though you yourself have said there will be broad and material changes, I believe this proposal is flawed, both in process and in substance, and should be withdrawn.

Do you agree? And will you commit to withdrawing the existing proposal and issuing a new proposal with a robust notice and comment process?

Mr. POWELL. Well, let me update everyone on the——

Senator SCOTT. Please.

Mr. POWELL. ——status of all that. So, over the past several months, we have had—in fact, Vice Chair for Supervision Barr has held a series of discussions with the other bank regulatory agencies around potential changes to the original proposal. I am pleased to say that we have made quite a bit of progress on those and are very close to agreeing on the substance of those changes.

And I can't really be specific because nothing is agreed until everything is agreed, so I won't have a lot of specifics for you today.

The question where we're continuing to try to make progress is that of process. So, it is—it is—my view is the strongly held view of the—of members of the Board that we do need to put a revised proposal out for comment for some period. And the reason is, you know, when there are broad and material changes, that has been our practice. We don't see a reason to deviate from that practice.

It seems to be consistent with past practice and with the Administrative Procedure Act.

So, that's very much what we think, and we're working through that question with the FDIC and the OCC. We haven't reached agreement on that, but I'm very hopeful that we will. You know, we're prepared to move forward at that—when we do reach agreement on that.

Senator SCOTT. I appreciate most of your response there. I do want to discuss one aspect more of Basel before we move on to another topic. I find it very concerning with how much of this proposal and this process appears to have been done behind closed doors. The Fed, the FDIC, OCC proposed Basel III endgame last July.

Then, in October, the Fed began the collection of data to conduct a quantitative impact study on the cost of Basel III proposal, a study which I will note should have been conducted before any proposal was ever issued. Move forward to January of this year, Vice Chair Barr committed to a public comment period once results of the study were published. We are still waiting to view the results.

Keep in mind, all the while we are hearing rumors that the Fed is working on revising its proposal and moving toward an updated version. Please help me understand, how will the Fed revise or re-issue a capital proposal before receiving public comments? Basically my question.

Mr. POWELL. As you know, we have received extensive public comments, and we have also evaluated the quantitative impact survey that you mentioned.

Senator SCOTT. Yes.

Mr. POWELL. And so the idea would be, when we—when we do reach agreement with the other agencies fully, that we would publish the—you know, the proposed changes, and also the quantitative impact survey, and also the effects that the QIS suggest that the changes would have. So, we put all of that out for comment again for a period of time.

And then, having had yet another round of comment and we can then move toward finalizing. That's basically the broad strokes of how I would see this moving forward.

Senator SCOTT. And how long do you see that opportunity for public comments?

Mr. POWELL. So, it would be meaningful. I mean, it might be 60 days. We don't need to make it—it doesn't need to be a long one. But, you know, before we do that, we'd need—there's a lot of work that needs to take place, you know, before you actually put out the revised proposal. Quite a bit of work.

So, it will take some time, and then we would put it out, and then there would be—I mean, I'm just taking that number, 60 days of comment, and then we would get the comments back, and it would be another period of evaluating the comments, and only then would you go final. So, it—there is a number of steps here.

Senator SCOTT. Thank you. Just a final point as I am running out of time here. I think Senator Reed made the comment about the Chevron case and the impact that it could have certainly on curtailing, from our perspective, the regulatory State.

The necessity of a cost-benefit analysis on new regulations that will impact the economy I think is quite helpful. In the thousands—thousand-plus pages of Basel III, I think there were about 20 pages that reflected some kind of cost-benefit analysis approach. I really hope that we see more of that going forward.

Mr. POWELL. Thank you.

Chair BROWN. Senator Tester from Montana is recognized.

Senator TESTER. Well, thank you, Mr. Chairman. Thank you for the courtesy.

Chairman Powell, good to see you here today. Appreciate your work. Look, regardless of where I go in the State of Montana, housing is a big issue. Whether it's Billings or Butte or Bozeman or Busby or Big Sandy, it doesn't matter, larger towns to medium-sized towns to small towns, housing is a huge issue.

And I think it's a huge issue all over the country, and correct me if I'm not correct in that. And I was wondering how the housing challenges fit into the overall economic picture that you're seeing.

Mr. POWELL. So, we do pay a lot of attention, and I would agree with you, we have significant housing issues in the country, and we had them before the pandemic. Certainly, the pandemic has created new distortions, and, you know, monetary policy works through interest-sensitive spending. There is no more interest-sensitive spending than, you know, buying a house and having a mortgage.

So, for sure our tighter policy is having an effect on economic activity in the housing sector. And you—but I would also say the best thing we can do for housing is to succeed in getting inflation down to 2 percent on a sustainable basis, so that rates can come down, so that the housing market can get back to what was the pre-pandemic normal, which is to say still a housing shortage but not dealing with the kinds of specific things we're dealing with now.

Senator TESTER. So, let me drill down a little bit. I'm speaking not necessarily from a housing cost interest—and you're correct on the things you just brought up. I'm speaking more from a standpoint of economic growth and that there are plenty of small businesses, schools, hospitals, Main Street businesses, that can't hire people. They can't expand because there simply is no place for them to live.

How does that fit into your economic outlook metrics? Because I think it's—from my perspective at least, I think it's limiting the opportunity for expansion. It's limiting the opportunity for entrepreneurs, business startups. And does that fit into the economic picture that you look at?

Mr. POWELL. So, our mandate is for stable prices and maximum employment. And, again, I think for the—for housing supply, the best thing we can do is get inflation under control so that rates can come back down, so that we can have a more normalized set of rates and a more normalized housing system.

But I think policies to increase housing supply are really not so much in the hands of the Fed. They are in the hands of legislatures, you know, State and Federal.

Senator TESTER. So, do you believe that if we were to put forth some housing incentives, whatever they may be, that could have a positive—if it resulted, if those incentives resulted in more afford-

able workforce housing on the market, that it would have positive impacts on the economy?

Mr. POWELL. You know, these are—these are questions for you, but I would say this, that I'm aware that we—that housing is in short supply, and that for many it's a critical need for the workforce, and so more of it is better. But as to where the fiscal policy should—how you should prioritize that, that's not up to us.

Senator TESTER. Look, I want to talk about the independence of the Fed for a second, because I know that you are a strong supporter of independence, as am I, and political influence I don't think helps with monetary policy in the country. And so give me—give me your perspective at least on why the central bank independence is so critically important.

Mr. POWELL. Thank you. I'd be glad to. So, essentially all advanced economies have adopted a policy of central banking operational independence, and that just means that when we make our decisions we are instructed to make them without taking in extraneous factors, one of which would be politics. And the record is pretty clear that that's a good—it's a good institutional arrangement that serves the public well.

And, you know, we just want to stress, as we do periodically, that this is an institutional choice that we make as a country, and that as long as it is seen to serve the public well, it's a good choice. We think so.

Senator TESTER. OK. On advanced economies, there is some that talk about the economy of this country not being in very good shape. From your perspective, tell me how the economy of this country is doing compared to other advanced economies that have central banks.

Mr. POWELL. You know, so I'm in lots and lots of international discussions as part of my job, and the story for the last 2 years has been just how exceptional the performance of the U.S. economy has been. And that's not a secret. You know, there's—clearly, the U.S. economy has performed very well compared to sort of our advanced economy colleagues.

Senator TESTER. Is there any country in the world with a central bank—any advanced economy that's performing better?

Mr. POWELL. Better as a central bank?

Senator TESTER. No. Any economy that's an advanced economy that has a central bank that performs better than us.

Mr. POWELL. You know, none comes to mind. As I think of the majors, the answer would be no.

Senator TESTER. OK. Thank you.

Chair BROWN. Thank you, Senator Tester.

Senator Rounds of South Dakota is recognized.

Senator ROUNDS. Thank you, Mr. Chairman.

Mr. Chairman, first of all, thanks for coming in again and visiting with us. I just want to focus on two specific items, and I'm going to start with the Basel III endgame discussion. I think Senator Scott did an excellent job of kind of laying out the concerns that many of us have had with it.

I would like to go back to just one particular issue, which I think a lot of folks out there that follow this—and I know it's technical

in nature, but let me just ask a specific question and you can kind of pick it apart for me, please.

Both you and Vice Chair Barr have confirmed that there will be material changes to every risk type outlined in the proposal. Since there will be significant changes, do you believe where the agencies have landed now would be considered a logical outgrowth of the original proposal from last summer?

Mr. POWELL. For those people who are not familiar with, that's the legal test for—that determines that to be, if it's a logical outgrowth. If it's not a logical outgrowth, that would require—legally require re-proposal. And I don't want to make the legal judgment.

I will just say, again, from my standpoint, my view, and strongly held view of my—some of my colleagues on the Board is that it will be appropriate for us to put out the changes again for a period of comment, just because it's the right thing to do. It's what we would do typically in a situation where there are, you know, material changes to a proposed rule.

Senator ROUNDS. Do you feel that you have a consensus on the Board to allow that to move forward in terms of an additional comment period?

Mr. POWELL. Yes. But, of course, we have to get the—the FDIC and the OCC, you know, we're in discussions with them to work—to work on something that would meet that need, and we have to get their agreement, too.

Senator ROUNDS. Assuming—it sounds like that's the path that you would like to go down.

Mr. POWELL. Yes.

Senator ROUNDS. And if that were the case, would it be fair to say that we probably would be looking at final determinations or recommendations for a Basel III endgame proposal probably into next year, before it would become anything of a final determination?

Mr. POWELL. I think that may be right. You know, it's—something like that could be right, yeah. I mean, it's hard to be precise. You know, we would put it out. It takes some time to write this stuff up. Then you put it out for comment. Then you get the comments. Then you read the comments. Then you write the final rule. You know, beginning part of next year is a good guesstimate.

Senator ROUNDS. The only reason why I push is because there are so many folks directly involved with this and the impact on our economy here. And with a lot of our financial institutions, this is a significant change, and it's one that a lot of people are following. So, I'm trying to get you to get into the depth of this as much as possible, and I thank you for that.

I also want to go into one other area. And, once again, this is something that you and I have had visits about in front of this group before. But I want to talk about what the parts of inflation are and what parts you can control and what parts, as the Fed, you really can't control.

The demand side of the equation on inflation is a part that you have the tools to work with. But there is the supply side of the equation, which is still out there. And I want to just lay this out because as we do this in this setting, it naturally becomes political in nature, because one of the starting points that we talk about is

when this Administration took office and what happens with supply side issues at that time.

And as I work my way through this, I just want to share the concern that I've got. And then I recognize you don't want to be political in it, but I want to lay this out, and then I want to talk about what you can control and what you can't control with regard to making changes on inflation through the processes that you have.

When President Biden took office, gasoline prices—since President Biden took office, gasoline prices have risen over 54 percent. Energy prices have risen 41 percent. Fuel oil prices have risen 37 percent.

Now, I can go on and on, but you understand what I'm saying is is energy has increased substantially. And I think one of the reasons for this has been additional demand as we have come out of a pandemic, but the other part of this has been whether or not investors really want to go back in and invest in traditional energy resources after the President made the specific determination to cancel the Keystone XL pipeline on the day that he stepped into office.

When he did that, he sent one heck of a message to investors about traditional energy and investing in traditional energy in the United States, and the fact that a multibillion-dollar contract or contract could be canceled with the stroke of a pen.

Now, my question to you is, what percent or has there been a discussion about what percent or what amount of the inflation that we've seen—over 20 percent increase in terms of affordability for a lot of our products, how much of that is attributable to the demand side and how much of it really is attributable to supply side challenges that we've seen in this country?

Mr. POWELL. That's a question that we've thought about a lot, and you—any attempt to reduce that to a precise number would be inappropriate, because it's so uncertain. But I think we can say—I believe strongly there is a significant demand element, and there's a significant supply element. And we've seen the supply side heal so much over the course of the last year, so—and we clearly see that that's contributing to lower inflation.

We also see cooling demand, for example, in the labor market, so the two forces are working together. I can't really break it down. It wouldn't be—it would be such an imprecise estimate I just—

Senator ROUNDS. Just simply a—just simply an acknowledgment, though, that it is both demand—

Mr. POWELL. It's both. It's definitely both.

Senator ROUNDS. —and it is supply.

Mr. POWELL. It is both, yeah.

Senator ROUNDS. Thank you.

Mr. POWELL. For sure.

Senator ROUNDS. Thank you, Mr. Chairman. My time has expired.

Chair BROWN. Thank you, Senator Rounds.

Chair Powell, unemployment has risen by half a percentage point over the past year. The number of jobs—job openings has dropped almost 50 percent. The hiring and quit rates are now below pre-pandemic levels. I'm concerned that if the Fed waits too long to

lower rates, the Fed could undo the progress we made on creating good-paying jobs.

Full employment is part of the mandate, as you say over and over. How are you assessing the risk of higher interest rates on the labor market?

Mr. POWELL. So, I completely agree with your characterization that the latest data do show that we've had considerable cooling in the labor market, and we do—we're very much aware that we have two-sided risks now, as I mentioned earlier. And we're determined to balance those as best we can. We want to see more good inflation data, and we also want to continue to see a strong labor market.

And we—those two things are equal under the law. We have this challenging thing to balance them, but we're very much conscious that that is our job, and we're trying to do that.

Chair BROWN. Well, and you know that if unemployment trends upward, you must act immediately to protect Americans' jobs. Workers have too much to lose if the Fed overshoots the inflation target and causes a completely unnecessary recession. We will say that over and over and over again. I think you understand that.

Housing. Higher interest rates are making housing more unaffordable. Higher rates are supposed to lower costs, yet housing prices continue to soar. By keeping rates high, the Fed ignores the economic reality of millions of Americans struggling to make ends meet and get ahead.

Let me ask you three quick yes or no questions. If you would answer that way. Since late 2022 when the Fed began raising rates, has the volume of housing sales decreased?

Mr. POWELL. I believe it has, yes.

Chair BROWN. Since late 2022, has the median home price increased?

Mr. POWELL. I believe it has.

Chair BROWN. Since late 2022, have monthly mortgage payments become more affordable or less affordable for homebuyers?

Mr. POWELL. Less affordable.

Chair BROWN. OK. Thank you. In short, despite housing sales declining, the median price for a single home—single-family home has increased by nearly \$20,000. People are spending a greater share of their income and mortgage payments. So, in sum, higher rates it's clear—from your answers and data, it's clear higher rates are not bringing down housing costs. The cost of home ownership is going—only going up.

Let me shift to the Synapse bankruptcy. Since mid-May, tens of thousands of people, including many Ohioans, have lost access to their money due to the bankruptcy of this fintech middleman. Reports indicate that as much as \$95 million may have gone missing. The Fed oversees one of Synapse's former partner banks, Evolve Bank & Trust. As a regulator, it's your job to make sure that banks protect the people whom they serve.

What's the Fed doing to help customers who felt the impact by the Synapse collapse? What are you doing to regain access to their money?

Mr. POWELL. So, we're—we do supervise the bank. We don't supervise Synapse or let alone the fintechs that feed into Synapse.

And we're strongly encouraging Evolve to do whatever it can to help make money available to those depositors.

We also, as you may know, did an enforcement action against—before this all happened, we did an inspection or looked at—looked at Evolve, and we hit them with an enforcement action around these very risk management issues, again, before the—before the current situation developed.

Chair BROWN. It's critical that consumers are made whole as soon as possible. We will continue to talk to you about that. We will watch. We will let you know we're watching. The Fed needs to use its supervisory authority to ensure that Evolve is committing the resources necessary to return those funds to the account holders.

Last comment. I want to note one last thing. Last year's Fed report on the failure of Silicon Valley Bank noted how incentive-based compensation encouraged the excessive risk-taking that led to the bank's failure. You either watched or had reports of when those bank CEOs testified in front of this Committee.

The report—the incentive-based compensation that led to the bank's failure I mentioned had said that SVB managers, quote, "Had a financial incentive to focus on short-term profit over sound risk management." That's what a number of us—Senator Smith, Senator Butler, Senator Warren, and I—Warner and I have said over and over, that the short-term profit over sound risk management causes significant problems to our financial system.

Compensation practices still pose a threat to our banking system. Urge you to move quickly to join your colleagues in the long-overdue rulemaking on executive compensation. I mean, you know. You read the reports about the outrage of the public about executive compensation continuing to go up and up and up and up. You have a role, a significant role, a legal role, to deal with that.

Thank you.

Senator Tillis is recognized.

Senator TILLIS. Thank you, Mr. Chair.

Chairman, thank you for being here. I want to be real quick on Basel III endgame, and I want to be mindful of time. Just simply, can I get a commitment from you on releasing the results of the QIS?

Mr. POWELL. We plan to release the results of the QIS, not just—

Senator TILLIS. What timeframe?

Mr. POWELL. Well, first, we have to get agreement with the other banking agencies, but as soon as possible.

Senator TILLIS. Can you imagine any agencies having a concern with—any other banking agencies having a concern with releasing it? Or is it just a matter of—

Mr. POWELL. Not at all.

Senator TILLIS. —put a formal—OK.

Mr. POWELL. No. It's just a matter of the bigger picture of getting agreement on the revisions to Basel III and also how to proceed.

Senator TILLIS. That's great. And I really appreciate the feedback that I have received from you. I should have started by thanking you again for your continued accessibility and discussions outside

of the Committee. They are very productive, and I appreciate that and your leadership at the Fed.

I grew up in the 1970s, got my Social Security number in 1973 when I was 12 years old. That's when I made my first payment. So, I've been following the economy even as a youngster, and that was a really lousy time to enter in the workforce.

Tell me—and I'm hearing discussions among some of our Members now that would almost be reminiscent of discussions with prior Fed members saying, look, we've got to lower interest rates, and we've got inflation—we've got unemployment out of control.

So, it sounds like we're taking plays—some suggestions from some of my colleagues are plays from a playbook that didn't prove to be very effective back in the 1970s. What can we learn—what would—I'm not going to ask you about where you go from here.

But if we look back and do a postmortem on some of the decisions that were made when we had consistently high unemployment, what lessons can we learn there? Or what mistakes should we not necessarily repeat?

And I know every—this is a fingerprint of a challenge. It's not exactly like the stressors that we had back in the 1970s, but what can we learn from the decisions of what I think are arguably the wrong decisions made back then when we were dealing with high unemployment and high inflation? What have we learned?

Mr. POWELL. I think the number one thing we learned was that it's up to the central bank to take it on and stick with it until it's done. And that doesn't sound controversial now, but it actually was back then. And so people didn't really get in there and get it done and it kept—inflation kept coming back.

I also think there are significant differences this time to the questions a minute ago. This is a combination of a supply side that we have very significant supply shocks along with big demand shocks from the reopening of the economy and from all the other things that happened. So, I think we have to—each one of these things is different in its own way. We try to learn the lessons of history, though.

Senator TILLIS. Do you agree or disagree any disconnect between inflation and inflation expectations from the 2 percent target should be addressed now and not at a later time?

Mr. POWELL. Absolutely.

Senator TILLIS. I like that answer. I want to go to something different. I'm trying to go into a lightning round now and finish on time. We have seen the 2024 stress test results for the banking—U.S. banking system. It looks like to me by every objective measure we've got a strong—we've got a banking system that's on strong financial footing. Do you agree?

Mr. POWELL. Yes.

Senator TILLIS. One last thing. As the Fed considers making broad and material changes to the Basel III proposal—back on that one—can I urge you not to overlook the second-order issues, important FBOs, and certain regionals, to ensure the bank—that banks are not unduly influenced?

The current proposal, for the example, the outsized operational risk costs were high. Are we going to take care of that in any sort of re-proposal?

Mr. POWELL. Let me just say we're very conscious of the comments across the spectrum, foreign banks, domestic banks, small-, medium-sized banks. You know, everyone is going to get heard carefully as part of this process. That is our obligation.

Senator TILLIS. And I think in response to Senator Rounds' question you did indicate that probably because of the nature of the likely changes from what Mr. Barr expected to what may ultimately come we are going to open it up to comment again?

Mr. POWELL. That's the strong view of the Federal Reserve. We are working with—on that question with the FDIC and the OCC to try to find a path to do that.

Senator TILLIS. Very good.

Mr. POWELL. But from our standpoint, that's essential.

Senator TILLIS. I think that's the strong view from at least several Members on this side of the dais. I hear that would be very—very, very important because I think it's going to materially change.

Thank you, Mr. Chair.

Chair BROWN. Thank you, Senator Tillis.

Senator Warner of Virginia is recognized.

Senator WARNER. Thank you, Mr. Chairman.

Chairman Powell, it's good to see you again. Coming this late in the questioning, I'm going to at least hit a couple of the items that my colleagues have otherwise already hit, because I want to make sure it's noted that I raised them as well.

First of all, I agree with the chairman. You know, I probably hear more on housing and housing affordability than any other issue. And I agree with the chairman, and we've discussed this around a rate cut. And I understand most of your answer, but I still want to add my two cents here. We've got to find a way to start bringing mortgage rates down and let people get—unlock that housing market.

And, again, we've discussed the rate cut issue, and I know you've got to navigate that. But I hope it's sooner than later.

I will not recap what I've done in the last couple of hearings with you, but I do think the discount window proposal that I've gotten that I know you are working on—you know, before we think about additional regulations that we do need in some cases, I think the discount window is an underused tool, was one of the initial original tools for the Fed.

A lot of my colleagues have talked about quantitative easing or, I mean, Basel III endgame. I do hope when we get the revisions that we'll see the quantitative analysis that, again, Senator Tillis already raised and other colleagues have raised.

I also hope that one of the questions I raised in my March letter to you was, you know, making sure any new regulatory structure, how it intersects with existing regulatory structure in terms of market risk, credit risk, and I, again, hope that we will have that as the revisions come out.

I think one of the things that this debate around Basel III raised was that—it is my understanding at least looked at—you may be all looking at revisions to liquidity standards as well, and wanted to see what you could say about that and whether that part of those standards are under review and what your thinking is.

Mr. POWELL. Yeah. And I think that actually connects to the Silicon Valley Bank questions as well, where I think we—there seems to be a need to update assumptions about liquidity. And that's a separate proposal that we're also working on, and, you know, very important. I think we saw how fast that run was. It was just exponentially faster than prior runs. That's the new world, and, you know, that's some estimate of what that world is is baked into things like the—you know, the liquidity coverage ratio, for example, and other—

Senator WARNER. And wasn't that the case, you know, if you had 25 cents on every depository dollar leave in 6 hours, no matter what the capital standards are?

Mr. POWELL. Yeah.

Senator WARNER. And one of the things I guess, you know, there was a lot of talk after SVB that we need to think about internet-driven runs. A lot of us raised concerns. Candidly, I'm not sure I've heard any good proposals. So, whether it comes from you guys or from folks listening, how we think about this new internet-driven world.

And, frankly, I think some of the irresponsible behavior by some of the folks that were major depositors in SVB who in many ways shouted fire in the crowded theater, and we've not seen any action there. So, I would welcome additional ideas as well.

And that kind of brings me to my last questions around supervisory reform. I know that GAO criticized the Fed's supervisory procedures and the role they played in the 2023 failures. It is a whole brand new world. Are we going to look at—will your changes to supervisory standards be comprehensive? Will they be one-off? How do you think about that in light of the GAO report? And also, in light of just the SVB and a few of the other failures we saw last year.

Mr. POWELL. Vice Chair Barr, who is Vice Chair for Supervision, is leading a process of looking at our—at the way we supervise banks and thinking about how we can be faster whenever it's appropriate, more forceful where it's appropriate. And I think, you know, they've taken a pretty deep dive and tried to learn these lessons and then implement them in a way that is appropriate. So, that's a big project going on at the Fed right now, which really the Vice Chair for Supervision leads.

Senator WARNER. I think I remember lots of conversations with the chairman, with you, with the FDIC, on that Thursday through Sunday, and I think the solution you guys came up with, the Administration came up with, by Sunday night was a good one. But they were pretty scary 3 or 4 days there, and it did seem like the process—I don't know completely how you get fully ahead of that, but I firmly believe that there should have been a clearer early warning system and trying to make sure that we wouldn't be in that kind of crisis situation going forward.

And, again, I would strongly encourage any additional thoughts on this technology risk and how we get that right.

Thank you, Mr. Chairman.

Thank you, Chairman.

Chair BROWN. Thank you, Senator Warner.

Senator Kennedy of Louisiana is recognized.

Senator KENNEDY. Thank you, Mr. Chairman.

Mr. Chairman, our economy is slowing, is it not?

Mr. POWELL. Yes. Although still growing at a solid pace.

Senator KENNEDY. Our unemployment rate is rising, is it not?

Mr. POWELL. Yes, it is. Although the labor market is still strong.

Senator KENNEDY. Our labor market is slowing, is it not?

Mr. POWELL. Yes. But I'd say unemployment is still—you know, is still low by historical standards, but, yes, it is—we've seen cooling, yes.

Senator KENNEDY. And I was looking at some recent jobs numbers. I know you've glanced at them, too. About three-quarters of the net new jobs that were created in June were in Government, health care, and social assistance. What does that tell you?

Mr. POWELL. That's a concentration. You'd rather see broader job creation than that. Those three areas have—in some reports, they have been—as it was this time, they have been the predominant creators of jobs. That tells you that job creation is becoming less broad in the economy and narrower. It's narrowing.

Senator KENNEDY. It tells you that Government is creating those jobs, doesn't it?

Mr. POWELL. Well, it's Government, it's also in-person services, it's also—some of it's Government.

Senator KENNEDY. Manufacturing has been flat.

Mr. POWELL. Yes. Manufacturing is not creating a lot of—a lot of new jobs these days.

Senator KENNEDY. Information technology shed jobs over the past 2 years, hasn't it?

Mr. POWELL. I don't know.

Senator KENNEDY. Leisure and hospitality jobs have slowed to almost a trickle.

Mr. POWELL. That's a place where there were—there was a desperate worker shortage, and they've done quite a bit of hiring, but they're catching up now.

Senator KENNEDY. I mean, three-quarters of the jobs that are being created in our economy can be related directly or indirectly to our spending deficits, can't they?

Mr. POWELL. In this report, in this single report, I don't know that health care is really Government spending. That's something people are consuming.

Senator KENNEDY. Where do you think these hospitals get their money?

Mr. POWELL. They may—they may get it, but, I mean, people are not—the spending on—the spending on health care is not necessarily directly related to deficits is my point.

Senator KENNEDY. I would disagree with you. I mean, here is my point. We talk a lot about expectations in terms of inflation, how if we expect there to be inflation we'll get inflation. It seems to me that consumer expectations play a role—a bigger role in the economy than we cede to them. Most of our economy in America is consumer-driven, is it not?

Mr. POWELL. Yes.

Senator KENNEDY. Unlike, say, China, which is manufacturing driven.

Mr. POWELL. Very much so.

Senator KENNEDY. And I listened to you cite the statistics about the economy, but most Americans—most Americans don't feel good about the economy, do they?

Mr. POWELL. No. And we don't—we don't tell people how to feel about the economy.

Senator KENNEDY. I mean, isn't it a fact that most people, if you—if you ask them to define "Bidenomics," they would say, "That's easy. We get to pay more to live worse"?

Mr. POWELL. I wouldn't touch—

Senator KENNEDY. You don't want to answer that one.

Mr. POWELL. —a sentence with that word in it.

Senator KENNEDY. Yeah. Yeah. I mean, we can pretty this up all we—I guess my point is, and I know you're going to do this anyway, but I'd be really careful with this economy. I mean, people just don't feel better off today. And one can marshal a persuasive argument that, well, you should compared to Europe or compared to China, compared to Canada, but they—you know, feelings are feelings. People don't feel good about this economy, and it's primarily because of inflation.

Let me use my final 30 seconds to ask you—I listened to my good friend, the Chairman, give his opening statement. Do you think inflation was caused by corporate greed?

Mr. POWELL. I'd hate to comment on something the Chairman was speaking about.

Senator KENNEDY. Oh, go ahead.

Mr. POWELL. Well—

[Laughter.]

Mr. POWELL. So, I would just say we see—at the Fed, we see inflation as when there's an imbalance between supply and demand, and we use our tools to work on the demand side of that and bring it back into line with supply.

Senator KENNEDY. I've got 2 seconds. So, when are you going to lower interest rates?

Mr. POWELL. I'm today not going to be sending any signals about the timing of any future actions.

Senator KENNEDY. Thank you, Mr. Chairman.

Chair BROWN. Senator Smith of Minnesota is recognized.

Senator SMITH. Thank you, Mr. Chair. Welcome, Chair Powell. It's good to see you again. I want to follow-up on kind of the line of questioning that Senator Tester was on a bit ago. He was talking about how the U.S. economy has been outperforming other advanced economies around the world in terms of growth rates, in terms of unemployment, in terms of inflation, getting inflation under control, though I think we obviously can all agree that we are not—at least from my perspective, we are not done yet. And we don't want to rest on our laurels.

But I am wondering if you could share what you think that we have learned from this experience? What have we done right? And why is it that we are doing better than some of the other advanced economies in the world?

Mr. POWELL. I think that it's down to the fundamental strengths of our economy. So, as you may know, European economic officials are very, very focused on this question. And they really—it comes up in all of our discussions.

Europe has seen productivity increases of about 1 percent a year for 40 years. We have seen 2 percent. If, you know, you take a number and compound it at 1 percent and compound it at 2 percent, the difference is just enormous after 40 years in terms of incomes and living standards. And their question is why is that? Why is that?

And the standard answer that Americans tend to give, and that I would give, is it's down to, you know, more flexible labor markets. In the pandemic, people were—they kept—they stayed in their existing jobs. In the United States, we had people changing jobs at record levels. And, you know, that's the kind of thing that adds to productivity and contributes to rising living standards, going back to school and getting skills and things like that.

Another one is our financial sector. We don't just have banks. You know, we have a highly developed ecosystem of financing sources that will fund early stage investments. Banks are really not set up to do that. You know, they are prudentially regulated.

So, those are some of the things. I think we just have these natural strengths as a—you know, as an innovative, more flexible economy we can grow faster.

Senator SMITH. I appreciate that. You know, I think sometimes there is a tendency to sort of trash our economy and just sort of say we suck. And actually, I think that there is a great resilience in our economy. I would argue that it has also to do a lot with the incredible resilience of our workers and their creativity and their talent and the training and the education that they have.

And I think I would also argue, though I wouldn't expect you to make this case, that the way in which our Federal Government responded to the pandemic in order to make sure that people weren't evicted. That they still had money to pay their bills even when they weren't able to work meant that overall our economy, you know, survived and was ready to kind of be off to the races when we emerged from the pandemic.

But, Chair Powell, I would like to ask you a question, something that you and I have talked about, I continue to be thinking a lot about, which is the commercial real estate risk that we have in this country.

I think particularly for office space, we know that that has been under strain the last several years. The sector has remained largely stable. But we are hearing about some additional default risk. And one thing that I am noting is that there is some expectation or concern that that may fall disproportionately on smaller banks.

I think that commercial and regional banks hold an estimated two-thirds of all the commercial real estate loans in the country. And so unlike larger banks, these smaller institutions might find it a little harder to deal with this.

So, could you discuss this with us? Could you tell us a little bit about how you see this risk and particularly whether this poses some additional risk that we might be seeing more concentration in the banking sector as these smaller banks are maybe under more pressure?

Mr. POWELL. Yes. So, this, to your point, this is a risk that has been with us and will be with us for some time, probably for years. And banks need to be honestly assessing what their risk is. They

need to be assured that they have the capital and the liquidity and the systems in place to manage this risk.

The stress test that we apply to the largest institutions stressed commercial real estate pretty hard. And, again, the conclusion is that the large banks can manage this problem. And most small banks can, too. But it is in some smaller banks that tend to have that local concentration in commercial real estate.

And, you know, we are in touch with those banks. The supervisors and regulators are in touch with those banks and making sure that they can manage them. And it is going to be an issue for many banks. But it is one that we are trying to work through. One that we are very much aware of, and, again, it will be with us for some time.

Senator SMITH. Thank you. I think so much about the importance of these small regional community banks in small towns, even big towns in Minnesota, and how important it is that, in my book, that they can stay independent and better serve their communities in that way. So, I worry about this risk.

Thank you, Mr. Chair.

Chair BROWN. Thank you, Senator Smith. Senator Butler of California is recognized.

Senator BUTLER. Thank you, Mr. Chairman. Chairman, good to see you. And I am going to make you do the whole last 5 minutes since I am the last one for today. You will recall the first time that we spoke, I tried to engage you around three specific areas. One was how the monetary policy impacts the quality of life for young Americans in the future in the work that you are doing there.

The space of climate risk, and what I see as potentially a future challenge down the road, and that is the state of commercial real estate. You and I have had that conversation before. And no surprises today, I am going to stick to those three topics, somewhat related to questions that you have been asked before relative to the housing market, housing affordability, and interest rates.

I want to narrow the scope just a little bit to ask about those—how those issues and challenges impact again the quality of life for America's next generation. Given the severe shortage of affordable and available homes to buy, coupled with high interest rates, young Americans are continually unable to afford homes and are pushed into a rental market driving rental costs up.

So, there is sort of trickle-down impact here. A recent *Washington Post* analysis showed that Gen Z is spending 31 percent more on housing than their millennial counterparts were 10 years ago after adjusting for inflation.

How do you view—that was a long lead in to just ask the question, how do you envision or view the interest rates of today and the monetary balancing and policy balancing that the Fed is doing on contributing to the future generation predicament if we are to extrapolate the conditions of today.

Mr. POWELL. Our job, of course, is the whole economy and inflation for the whole economy. And the absolute best thing we can do for younger people is to restore price stability so that as we benefited from—you know, I graduated from college in 1975 near the end of the big inflation period.

So, during most of my adult life, inflation has just been not a factor. And that means, you know, stable interest rates, relatively low interest rates. We want to get back to that. And that is what the Fed's job is, is that we are not supposed to look at the housing market as separate from the overall economy.

In the meantime though, there is no question that higher interest rates are making it harder to buy homes in the short term, but in the longer term this is the best thing, particularly for younger people who are not yet in the housing market.

Senator BUTLER. Let me, sort of in line with that community, constituency, population and definitely aligned with the concerns of my State that actually faces some severe climate impacts, just as we speak with wild fires and our colleagues and fellow Americans in Texas and the impact of the hurricane, I wanted to pull in your sort of thoughts about the Fed pilot, the Climate Scenario Exercise.

In May, the Fed conducted a pilot, a Climate Scenario Exercise, and asked the six largest U.S. banks to examine their balance sheets and how it would be affected if a large hurricane hit the Northeast. They reported facing data gaps on property characteristics, their counterparties and insurance coverage.

How does the Federal Reserve intend to invest in expanding the modelling resources for banks that are implementing climate-related financial disclosures?

Mr. POWELL. So, we haven't made any decisions on what to do with that information or whether to repeat that exercise. To your point, it was really a learning exercise, you know, how are banks thinking about this, and how are they modelling it, and how does it work really? It is a very, very challenging thing to model. And so that was really the nature of this exercise.

In terms of disclosures, you know, we don't really have a—that is not really our job. That is really the SEC. But, you know, we don't have a big job on climate, but what it really is is to make sure that the institutions we regulate are aware of and understand the risks that they run, including risks from climate.

Senator BUTLER. And that they are prepared and learning how to—as would be the point of a pilot, learning how to mitigate those risks over time. So, what criteria will you use to evaluate whether or not you would run the exercise again and/or share more broadly the results of that exercise?

Mr. POWELL. I think we did publish, well, most of the results of that exercise. So, I don't know what to say about that. We are looking at it, and we are asking ourselves what did we learn, what do we need to learn next time. So, you know, I am not exactly sure what factors we will be looking at, but we will be doing a careful assessment of what more we need to do.

Senator BUTLER. Thank you, Mr. Chairman.

Chair BROWN. Senator Hagerty is recognized.

Senator HAGERTY. Thank you, Mr. Chairman. Chairman Powell, welcome.

Chairman, last week in Portugal you said that you wanted to be, quote, more confident that inflation is moving sustainably down before you begin to cut rates. You also said in your testimony that you need greater confidence and more good data before lowering rates.

Can you give us any color as to what it is you are looking for in the data and how long it might take us to get there?

Mr. POWELL. We need just to see more good inflation data; that is all. We had 7 months of good inflation data at the end of last year. And then we had a quarter, really a month or so, where inflation went up. And now we had one really good inflation rating and one pretty good one. We just need to see more so that confidence rises. I'm not——

Senator HAGERTY. In terms of—so are we weeks away, months away? Can you give us——

Mr. POWELL. I am going to try to avoid sending any really specific signals about time today because it is going to depend on the data. It also matters what is going on in the labor market though. You know, we have also said that if the labor market weakens unexpectedly, that could be a case for loosening policy as well. Really, we are weighing both of those factors.

Senator HAGERTY. Here is one of my concerns; I'm sure you probably share it. But we are coming off of a 40 year high in inflation. We have seen the rate of inflation coming down, but we haven't gotten to the 2 percent target. And my concern, for lack of a better term, is whether or not this might be transitory in terms of the data that we are seeing right now.

Mr. POWELL. That is exactly why we are approaching this question carefully.

Senator HAGERTY. I thought that might be your answer. Thank you, Mr. Chairman.

Can we shift now to the issue of the Treasury debt? The Fed is the largest holder of Treasury debt. In February you and I talked about the pressures that our fiscal deficit is exerting on interest rates, which by extension makes your job more difficult.

I would like to talk this time about how Treasury issuance is impacting our economy and our monetary policy. First just a basic question. If Treasury issuance were to shift drastically, either to the long end or the short end of the curve, would that affect interest rates? Or maybe more simply, did changes in supply across maturities impact interest rates on the yield curve?

Mr. POWELL. I mean, I think in theory they can.

Senator HAGERTY. I agree. As you know, the Treasury Borrowing Advisory Committee recommends that T-bills comprise between 15 and 20 percent of total U.S. debt. But right now the Treasury is issuing T-bills significantly above that recommended range.

Some people, including myself, believe that this is being done to artificially stimulate markets in the run up to the election. And it is shocking how little attention this is getting. Any manipulation of debt management of this nature stimulates inflationary pressures and increases taxpayer burden because it is higher cost to issue these bills.

So, given that Treasury is issuing an excess of short-term debt, which pulls down longer term rates, isn't it working at cross-purposes with your monetary policy goals of taming inflation?

Mr. POWELL. So, we take Treasury's debt management decisions. We don't comment on them. We just do our jobs. So, I am not going to——

Senator HAGERTY. I am not asking for a comment on their decision, but just as a simple mathematical truth. If they are pulling down demand on the long end of the curve, doesn't that—

Mr. POWELL. I wouldn't say that that has important inflation implications, no.

Senator HAGERTY. You know, it just feels to me, the same way that the Biden administration drains the Strategic Petroleum Reserve, that undermines our ability to respond to energy shocks.

When the Treasury manages its debt in this manner, it constrains our ability to respond to future economic shocks. And that opens our nation up to very real risk, whether it be amplifying the effects of the Fed's balance sheet reduction, flooding the supply of one of the most important short-term debt instruments. The risks seemed to me to be mounting for Treasury market disruption.

I would like to know what your thoughts are, Mr. Chairman, about how the Fed will navigate this and whether you have had discussions with the Treasury about this growing dangerous dynamic.

Mr. POWELL. No, we don't have a seat at the table on Treasury debt management. Treasury makes those decisions. And they don't have a seat at our table on monetary policy.

Senator HAGERTY. I just think the risk is very obvious here, though, where we are headed with this type of poor—

Mr. POWELL. Honestly, it is completely out of bounds for me to comment on Treasury debt management in any way.

Senator HAGERTY. I think you have been dealt a very difficult hand here, Mr. Chair. The Biden administration's policy is aimed to gin up the economy ahead of the election. These efforts directly undermine your policy goals at the Fed. That includes excessive issuance of short-term debt, think about it, Freddie Mac's backstop of second mortgages, unlawful student debt loan cancellations, the draining of the Strategic Petroleum Reserve to suppress fuel prices, and President Biden's own jawboning of the FOMC to lower rates.

As you know, the Federal Reserve was structured to shield monetary policy from political influence, and that independence has given the Fed unique credibility in executing its mission. If the FOMC were influenced in any way by political calculation rather than economic data, it would severely damage the Fed's credibility as an independent institution. It would increase uncertainty in our markets. And it would jeopardize the dollar status as the global reserve currency.

Thank you, Mr. Chair.

Chair BROWN. Senator Warren of Massachusetts is recognized.

Senator WARREN. Thank you, Mr. Chairman. When the CEOs of giant banks can boost their bonuses by getting the banks to take on more risk, they run the risk that they will end up running their banks into the ground. It happened in 2008, and it happened again in 2023.

Back in 2010 though, Congress passed the Dodd-Frank Act. Section 956 told financial regulators solve this problem. Two months ago, regulators put forward a proposal, but the Fed refused to join.

Now in 2018, you told this Committee, Mr. Chairman, that you, quote, expect that banks will have in place compensation plans that do not provide incentives for excessive risk taking. In other

words, you trusted the banks to write their own rules. So, let's see if they actually have.

One thing the proposal would do is require big banks to delay bonuses for a broad group of critical employees who are able to gamble with the bank's finances like the head of a trading desk, for example.

Chair Powell, in the 6½ years since you said trust the banks to regulate themselves, how many of the 10 biggest banks have put policies in place to delay annual bonuses for this broader group of critical employees whose risk taking could endanger the bank?

Mr. POWELL. I don't know specifically. My guess is all of them since the financial crisis.

Senator WARREN. So, you are the regulator who said trust banks to self-regulate so we can avoid another financial meltdown or another bailout, and you don't know if they did or didn't do that?

Mr. POWELL. Well, you make a—it is a very, very specific narrow question you are asking about—

Senator WARREN. Yes, it is a very specific thing because it is something a regulator should do. You think the answer is 10 out of 10. The answer is zero out of 10.

Mr. POWELL. I doubt that.

Senator WARREN. Well, go back and look because we have looked at their statements on this.

Another thing the proposed rule would do is require the banks to consider flat out banning bonuses and bonus pay for executives who took risks that threatened the stability of the bank.

So, let me ask you this one, Chair Powell. In the 6½ years since you said trust the banks to regulate themselves, how many of the ten biggest banks now have policies that would require them to flat out deny bonuses to executives that have engaged in inappropriate risk taking?

Mr. POWELL. I don't know the answer to that. By the way, I never said trust the banks to regulate themselves.

Senator WARREN. I'm sorry. Do you want me to go back and quote you again exactly?

Mr. POWELL. Trust the banks to regulate themselves?

Senator WARREN. When you say I expect that the banks will have in place compensation plans that do not provide incentives for excessive risk taking.

Mr. POWELL. Right. Pursuant to the—

Senator WARREN. I take that as to—

Mr. POWELL. —guidance that we issued in 2010, which is quite detailed.

Senator WARREN. And you have not issued a guidance since you made these comments, since you became chair. And how many banks have actually put in place the regulations that you said I expect the banks will have in place. The answer is out of 10, zero.

Mr. POWELL. It was covered by the 2010 guidance actually.

Senator WARREN. No. You said in 2018 that they would put these in place.

Mr. POWELL. I said they would have in place.

Senator WARREN. No, that is not what you said. So, look, Chair Powell, the last guidance on this subject, as you say, was in 2010, which is before you were at the Fed. The Fed has now refused to

join the other financial regulators in finalizing a rule implementing Section 956 as Congress directed.

So, my question has been, how many of the 10 biggest banks have done this, and the answer is zero. Dodd-Frank was passed 14 years ago. There are still no rules to stop banks from rewarding executives' risky behavior. When you were asked about these Section 956 rules or lack of rules, in March of this year, you said, quote, that you wanted to understand the problem we're solving before proposing a rule.

Chair Powell, the law does not say Jerome Powell in his infinite wisdom should decide if we have a problem with executive compensation. The law passed 14 years ago says executive pay is a problem that threatens the stability of our economy, so write the rules to rein them in.

Finally, finally, the other financial regulators have proposed such a rule, but the Fed has not joined. Chair Powell, I understand why the ten biggest banks in the country like your approach. You let them do whatever they want. But you don't work for the giant banks. You work for the American people. I urge you to do your job.

Thank you, Mr. Chairman.

Chair BROWN. Senator Vance from Ohio is recognized.

Senator VANCE. Thank you, Mr. Chairman. And thanks, Chair Powell, for being here. I appreciated you coming by our office last week to discuss some of these issues.

I would ask something I imagine most of my colleagues are not asking, which is the relationship between immigration, particularly extremely high illegal immigration levels under the Biden administration, and the persistence of the inflation problem. And I recognize this is not your policy focus. But you are the Federal Reserve chairman, so I just want to get your views on this.

And in particular, I would read you a quote from Miki Bowman, who is one of your governors. And this says, quote, there is a risk that increased immigration and continued labor market tightness could lead to persistently high core services inflation. Given the current low inventory of affordable housing, the inflow of new immigrants in some geographic areas could result in upward pressure on rents as additional housing supply may take time to materialize. With labor markets remaining tight, wage growth has been elevated at around or above 4 percent, still higher than the pace consistent with our 2-percent inflation goal given trend productivity growth.

The Bank of England, I believe, produced a recent report on this issue in the United Kingdom, obviously, a different economy and a different country. But what do you see as the relationship, in particular given that housing is such a big driver of the inflation that we have seen over the last few years—as Senator Hagerty said, the highest in 40 years—what role do you see illegal immigration playing in driving up housing costs which, of course, is the main driver of inflation for American citizens.

Mr. POWELL. Let me quickly start by echoing your first comment, which is we don't comment on immigration policy, but we do comment on inflation.

So, I would say this. Many people came into the country over the last couple of years, many of them through asylum requests and went to work. Labor supply increased a great deal. There is no clear answer, but my sense is that in the long run, immigration is kind of neutral on inflation. In the short run, it may actually have helped because the labor market got looser because there were more people.

But you are talking about housing specifically. There will be—I am sure there are places in the country where new people coming into the country—I am sure you can find places that will have contributed to an already tight housing market.

But overall in terms of aggregate inflation, I wouldn't say it's a driver one way or the other.

Senator VANCE. So, I want to follow up on that thread. But just on that topic of particular areas that have been affected, Chairman Brown, I would like to ask unanimous consent to submit a letter for the record from the city of Springfield in our State, the southwestern part of our State, which I think highlights a very real example of this particular concern straight from the horse's mouth itself.

Now this letter, I want to quote from it. Springfield has seen a surge in population through immigration that has significantly impacted our ability as a community to produce enough housing opportunities for all. Springfield's Haitian population has increased 15,000 to 20,000 over the last 4 years in a community of under 60,000 previous residents, putting a significant strain on our resources and the ability to provide ample housing for all of our residents. And end quote there.

Chair BROWN. Without objection, so ordered.

Senator VANCE. Thank you. In my conversations with folks in Springfield, it is not just housing. They are trying to build 5,000 new housing units, which is a very Herculean task in a town of about 55,000 people. But it is also hospital services. It is school services. It is—there is a whole host of ways in which this immigration problem, I think, is having very real human consequences.

Could we go back to just one other question, Chair Powell, on this immigration and labor supply question. So, one of the euphemistic ways in which economists, I think, sometimes talk about labor supply and immigration, is that they will say something to the effect of, well, an increase in labor supply has put downward pressure on labor prices.

What they are effectively saying is that increased immigration has put downward pressure on the wages of American workers.

I wonder, you know, when you hear sort of your colleagues and other economists outside of the Fed talk about the influx of immigration and the fact that I think it admittedly has put downward pressure on wages, OK, obviously, that has put some downward pressure on inflation, but it also puts downward pressure on the wages that people earn to pay for their families.

Why do we see that as a good thing? Or maybe that's wrong. Maybe the premise is fundamentally incorrect. But why do so many economists treat an influx of new labor as a good thing? If labor is constrained, labor supply is constrained, doesn't that lead to rising wages for American workers?

Mr. POWELL. I am certainly not trying to put a value judgment on it. I will say though this is all happening over the last couple of years in a context of an extremely tight labor market, now a little bit less tight, significantly less tight, but you have got a worker shortage. You have got businesses who have jobs that are open. You have, you know, more than one job opening for every unemployed person.

So, you have got a very tight labor market, and it is addressing that. And we are having—wage increases are still very high, but they are coming down to a more sustainable level.

Senator VANCE. And, Mr. Chair, can I—I know I am over time. But can I just ask one more question on this? Thank you.

I understand your point, Chair Powell, and again, I am not ascribing value judgments to you. But if we say we have a really tight labor market, and we say that there are more than one job opening per worker, there are two ways that you could plausibly solve that, probably more than that, but two obvious ways you can plausibly solve that.

One is through a new influx of workers via the immigration system. Another way is by raising wages and bringing some of the workers that are on the side lines, I think specifically of the 7 million prime-age men that have dropped out of the labor force. Why isn't that more the focus of policymakers rather than—you know, you see a labor shortage. Rather than bringing in a large number of new immigrants, why not try to boost wages in a way that brings some of those workers off the side lines. That seems to be a much better focus from my perspective.

Mr. POWELL. Certainly, that's a very constructive focus. I would agree. I don't think it has to be one or the other.

Senator VANCE. Thank you, Mr. Chairman.

Chair BROWN. Senator Van Hollen from Maryland is recognized.

Senator VAN HOLLEN. Thank you, Mr. Chairman. Chairman Powell, it is good to see you. And let me first applaud you and your team at the Fed for at least so far being on track to bring down inflation without so far triggering a surge uptick in unemployment.

But you know very well that is a risk if the Fed does not act with full awareness of that danger. When you were here in March, you said that you were, quote, well-aware, end quote, of the risk to unemployment of waiting too long to cut rates and, quote, very conscious of avoiding it, end quote.

Since then, we have seen a slowing in the economy and a rise in unemployment. I am just reading something today in analysis with Diane Swonk, KPMG's chief economist, who summed it up by saying, quote, the ice is thinning. Red flags are emerging for the U.S. economy, end quote.

The engine of the economy, the labor market, is cooling faster than previously known. The unemployment rate is above 4 percent for the first time since 2021. It is taking workers longer to find jobs. Economic activity in the service sector, which is responsible for two-thirds of economic growth, slowed in June.

So, my question, Mr. Chairman, is, how do you take all of these factors into account? Do you share my concern that as of today there is a real risk of an increase in unemployment larger than is currently on your radar screen?

Mr. POWELL. Yeah, I mean, absolutely. I do, even more so than in March when we were here, see that. So, we have seen, and I think the latest data show, that labor market conditions have now cooled considerably from where they were 2 years ago. And I wouldn't have said that until the last couple of readings.

And I would say also that, you know, for a long time the risks were more that we would fail to hit our inflation target. I think the risks as to the two statutory targets we have, price stability and maximum employment, I think those are coming much more into balance.

My colleagues and I are looking at that, and we fully understand that we have to manage this process of administering the Federal funds rate and deciding what to do with it in a way that manages both of those risks. And, you know, the two mandates are equal under the law. And so, yes, we do get that.

Senator VAN HOLLEN. Well, I appreciate that. And I appreciate the fact that you have seen that sort of calculation change since you were last here. Because I think the data indicates that we are at risk now of not acting soon enough to curb the increase in unemployment. And if we allow that to go too long, we may see a real uptick there.

And so I am pleased that is very, very much on your radar screen and hope that that would be a really deciding factor as you and your other Fed colleagues determine what to do with respect to interest rates.

And has been said in the housing sector, we are seeing a continuing drag created by high interest rates. So, that has been a—I think all of our colleagues, as you probably heard today, are really hearing from our constituents understandably about the very high housing prices. And it has slowed investment in other sectors, like manufacturing as well.

In my final minute, I would like to turn to the question that Senator Warren asked because I asked your colleague, Vice Chair Barr, about exactly this, a question of implementing Section 956 of Dodd-Frank when he was before the Committee just a short time ago, May 16 of this year.

And I asked him about why the Fed had not moved forward along with other agencies with respect to implementing what the law is and what the law has been for 10 years.

NCUA has signalled their intent to propose a rule. The SEC has indicated that they are moving forward. I said to Vice Chair Barr that I have not seen any notice of proposed rule from the Fed. And can I get the commitment that the Fed will quickly begin to process implementing this law by issuing a notice of proposed rule?

His answer was, and I am quoting, in discussions with my colleagues, it became apparent that at the board, we believe we need to conduct some further analysis before deciding what steps to take. We are committed to following the law to implementing Section 956, but we have further work to do.

Count me among those who are very frustrated that we are now 10 years after this law has passed. Vice Chair Barr committed to following the law. I am sure, Mr. Chairman, that you would commit to following the law. But why is it how that it is taking the Fed so long to move forward with implementation of 956.

Mr. POWELL. So, I would like to look at the actual language of the statute. What it says is it calls on the regulators to make determinations about specific incentive compensation practices that cause excessive risk taking. And we haven't done that.

So, we did—you know, we put in place pretty serious guidance back in 2010. After putting it up for comment, we looked at all these questions. It has been in place for 14 years. We supervise on it. And, you know, so the question I am asking is, OK, let's go ahead and look at what the practices are that are happening now, not that are happening before the global financial crisis when it was obvious that things needed to be changed. And we put the guidance in place.

It seems to have largely worked, certainly as it relates to the large firms. And then let's design something that is designed to the residual risk as opposed to just taking something off the shelf from 15 years ago and doing that. So, we are working on that at the Fed now.

And, again, I am—the statute requires us to prescribe regulations or guidelines to prohibit those things. And, you know, I want to do that since we have them.

Senator VAN HOLLEN. Just very briefly, is it your testimony that the Fed has already met the requirements?

Mr. POWELL. No.

Senator VAN HOLLEN. OK.

Mr. POWELL. No.

Senator VAN HOLLEN. I just want to make that clear. And we do look forward to the Fed moving forward.

Thank you, Mr. Chairman.

Chair BROWN. Thank you, Senator Van Hollen. Senator Britt from Alabama is recognized.

Senator BRITT. Thank you, Mr. Chairman. Chair Powell, thank you for being with us today. My colleague from Maryland actually just touched on something. But as I was listening to the exchange from my colleague from Massachusetts in her closing remarks, particularly about Dodd-Frank and 956, there was also a comment at the end where she mentioned you working for giant banks versus the American people.

Now, I have a long list of questions I want to talk to you about, but I did want to get you to respond to that.

Mr. POWELL. That is completely untrue. You know, the things that we are doing are consistent with our international obligations, and they are meant to be the best thing for the American economy. And that is really our only consideration.

We have policy differences across various things. But, you know, we are all trying to achieve the best results we can for the people that we serve.

Senator BRITT. Absolutely. Thank you. Chair Powell, I have repeatedly talked about my concern with long-term debt proposal. And I just think that it has not been well thought through.

First, I have concerns that it blatantly undermines the tailoring requirement. And on that note, do you believe that 2155 will be applicable to the long-term debt requirement?

Mr. POWELL. I think it applies to everything. And on the long-term debt requirement, you know, we have voluminous comments

that we are looking at carefully and thinking through the process of what to do about them.

Senator BRITT. I appreciate that because I do believe that currently it lacks a real cost/benefit analysis. And I think it really does need serious reconsideration.

And additionally, when you take a look at it and its overlapping nature with Basel III, it seems inappropriate that we would move forward with a new long-term debt proposal finalizing that rule when we don't even really understand what Basel III is going to mean for capital requirements for banks and obviously financial institutions.

So, my question for you is just that. Would it be inappropriate to move forward with the long-term debt proposal finalizing that rule prior to Basel III being finalized as well?

Mr. POWELL. I don't know that I would—I can't give you a clear answer on that. It will depend. I mean, Basel III won't be finally finalized for some time. But that is not to say that we wouldn't reach a place where people understand and accept and support what it is that we are doing. And then I think at that point we would certainly move forward with other rules.

Senator BRITT. I heard you mention to one of my other colleagues that probably by the time this all took place, it would be the beginning of next year. I would just say my concern, the Fed has said that the long-term debt rule will directly be impacted by the final Basel product.

And so, you know, why would it be inappropriate or appropriate to move forward with that before banks can fully understand what they are facing from Basel? So, I would just that you all are thoughtful about that.

These are a lot of things that people are dealing with and trying to really understand the implications of. And I think we have seen consistently that people are not taking a look at the cumulative impact of these things and not really taking a look at the trickledown effect.

And on that, on Basel, when you testified in March, you said the Fed was aware and fully considering the potential impacts of a proposal on our commodities markets. And I do want to talk about that. The commodities market, our agriculture industry, is one in five jobs. In the State of Alabama, it is 20 percent of our economy. I am a big believer in food security is national security.

And the proposal would increase hedging cost by 80 percent, meaning banks would be far less likely and are inclined to offering clearing services. So, this could have a detrimental effect to our agriculture community and increase other costs providing food and fiber for our Nation.

When you look at inputs such as feed, seed, fertilizer prices, those have skyrocketed. And prices have ended up just getting passed down to the consumer, and grocery prices are up 21 percent since January.

So, do you believe that the revised Basel proposal will alleviate these concerns that our farmers and our ag community have had about Basel III and has the Fed done anything specifically to take a look at this and if not, will you commit to doing so?

Mr. POWELL. I don't want to get into the specific changes that we are going to make. I will just say that we are very well aware of and very focused on that particular set of changes and paying close attention to the issues you have raised.

Senator BRITT. I appreciate that. And I also hope that the Fed, when you craft these types of regulation, you really consider the relationship between economic impact and the ability of community banks to serve their communities as well. I have heard you mention that to another one of my colleagues. So, I know that you are committed to doing that. But that is incredibly important to Alabamians and our Main Streets all across the State.

In my last few seconds, I want to touch on one more topic. So, finding solutions to expanding affordable childcare is a top priority of mine. And it is something that I know a number of my colleagues on the other side of the aisle share an interest in and believes is an important issue as well.

So, Chair Powell, do you believe that increasing access to affordable childcare would positively impact labor participation in our county?

Mr. POWELL. I do believe that.

Senator BRITT. Thank you.

Chair BROWN. Thank you, Senator Britt. Senator Cortez Masto of Nevada is recognized.

Senator CORTEZ MASTO. Thank you. Excuse me. Chairman Powell, thank you for joining us. And I always appreciate visiting with you in my office as well and your comments.

Let me start by a comment you made in the opening. Over the past 2 years, you said the economy has made considerable progress toward the Federal Reserve's 2 percent inflation goal. Labor market conditions have cooled, while remaining strong, reflecting these developments. The risk to achieving our employment and inflation goals are coming into better balance.

And what we know is that since Biden came into office, the United States has added over 15 million jobs. Under President Biden, we had 41 consecutive months of job growth. And you just said it again here today that wages are up as well. The average U.S. wages and salaries grew by nearly, what 16,700 between January 2021 and April 2024.

So, would you agree with the statement by a Ranking Member earlier today that the U.S. has the greatest economy on the planet?

Mr. POWELL. I certainly would.

Senator CORTEZ MASTO. Let me ask you this. Jumping around, and there has been talks today about the Fed's independence and how important the Fed's independence is. *The Wall Street Journal* recently reported former Trump administration officials drafted policy options to weaken the independence of the Federal Reserve. If President Trump were to be elected in November, allegedly former Administration officials discussed policy options to erode the Fed's independence to make it easier for a President to impact interest rate decisions or fire the Fed chair at will.

Chairman Powell, how important is it that the Fed has independence to provide economic stability and anchor inflation expectations?

Mr. POWELL. So, I think it is actually essential. It is literally essential. And the good news is I think that is pretty broadly understood and particularly on Capitol Hill on both sides of the aisle. I believe that people do understand that we need to do our work in a way that is outside of the political process to the maximum extent possible.

Of course, we need to be accountable and tremendously transparent. If you look at the box in the monetary policy report on Central Bank independence, it is really a box about transparency. That is the other side.

So, I think it is really important. I think it is an institutional arrangement that has served the public well. And I do believe that there is pretty wide support for it.

Senator CORTEZ MASTO. And you said that it has been intentional and institutional arrangement over the years for this very reason, correct?

Mr. POWELL. Yes. This is a choice that we make. And I think countries around the world, advanced economies, have all made this choice effectively. And the results are clear that you now have independent central banks, and you have better anchored inflation expectations. And you have better performance on inflation and better performance in the economy generally, which isn't to say there won't be shocks and crises and that kind of thing.

Senator CORTEZ MASTO. And then let me touch on a subject that one of my colleagues just talked about because I was going to ask about this, which is our immigration.

In Nevada, immigrants are extremely important for our economy. They are essential workers, doctors, nurses, and teachers in my community. Can you, without getting into other ancillary issues that don't impact what you do, can you talk about and elaborate on how immigration affects the employment rate and why you look at it, and for what reason you look at the immigration issue?

Mr. POWELL. So, again, we don't—just to make the point that you made, we don't take a position. We don't comment on immigration policy. We have no responsibility for it. It's not our job. So, we just look at the numbers, and we sort of try to assess the economic consequences of immigration.

And over the last 2 years—two years ago, we had an economy where we really had a labor shortage. And what has happened is we have had a wave of immigration. And many of those people have gone to work and gone to work legally through the asylum process. Not all of them. There is also a group that has not been legally processed. But many of this latest group have sought asylum and then gotten—gone through the process of getting a work permit.

So, what that means is that employers wanted workers, and there were more job openings than there were people actively seeking work or working. And so now you have a new supply of workers, and they filled those jobs. So, we have a bigger economy. But it is not a tighter economy because labor supply has increased the economic capacity. That is just the arithmetic. That is not saying it is a good thing or a bad thing. There are other policy choices that could be made, and they are not for us to make.

Senator CORTEZ MASTO. When you say greater economy—

Mr. POWELL. Larger economy.

Senator CORTEZ MASTO. In other words, it has improved the growth of our economy.

Mr. POWELL. The economy grew three-point-something percent—3.4 percent, believe—last year. And some part of that was that, as Congressional Budget Office analysis showed, and to many a surprise, there had been a really significant uncounted group of workers coming into the country who had gone to work.

And that is part of the story of how the economy managed to grow that much while inflation was coming down pretty sharply. Inflation came down two full percentage points during 2023 while the economy was growing at 3.4 percent and while these people were coming.

And so that is part of the explanation for why we had such an interesting and pretty good year in 2023.

Senator CORTEZ MASTO. Thank you.

Mr. POWELL. Senator Cramer of North Dakota is recognized.

Senator CRAMER. Hi, Mr. Chairman. Thank you, Chairman. As always, all of my prep goes out the window with the last question. So, on the legal immigration workforce front, and I know this isn't your bailiwick, but the issue of workforce is important to the economy.

I would submit to my colleagues, beyond even the people who come here seeking asylum suddenly being available for the workforce, we have a million plus people who we welcome in legally every year, the vast majority of whom don't come in with a job or even a skill set. And we have so much work to do, colleagues, on the legal immigration front to create a connection between economic demands for workers and the skill set and education that our immigrants bring to us.

So, most every other country requires some sort of skill set useful in the economy. We don't do much of that. So, that is just my speech for the moment.

I know, Mr. Chairman, you have gotten already lots of very specific questions. And I have heard a couple of them on Basel III. So, I am just going to make an illustration, and you can comment on it if you would like. But there is a large generation and transmission utility in North Dakota, Rural Electric Cooperative, Basin Electric, a very large G&T members all over the Upper Midwest.

And they recently testified in front of the CFTC on Basel III, and they expressed concern about how operations would be impacted if lending was curtailed or limited in any way. And they gave a real-world example. And I wanted to just give you that example.

Now, remember this is electricity supply that we are talking about. It is critical that it remains reliable. It is critical that it remains affordable. And part of an electric cooperative's risk management program, of course, is how it buys the fuel that generates the electricity, in this case, natural gas. They may buy natural gas in advance at a fixed price, realizing that natural gas is one of those commodities that goes up and down in pretty big swings at times.

But they can hedge by buying it at a fixed price for a power plant. And it protects the cooperative financially since electricity prices, again, follow those spot prices generally. So, spot prices spike. So, do electricity prices. However, with a natural gas hedge,

the cooperative can generate electricity at a lower fixed fuel cost, protecting itself and its consumers from high prices. It is an upfront cost on the balance sheet between the cooperative and its bank. But it protects the reliability and affordable supply of electricity.

I give you that very specific example, not to even mention that the cooperative model itself has some unique qualities. But if you would like to comment on it. You have already stated that there are going to have to be changes. I just throw that into your box of things to think about. And you are welcome to comment if you like.

Mr. POWELL. I'll just say we are well aware of that issue, and I appreciate you bringing it up.

Senator CRAMER. Thank you, Mr. Chairman. With that, then, I am just going to speak to this independence issue. I think that the senators who have questioned you on it are correct. I share that concern. As you know, the independence of the Fed is essential. I have resisted moves within my own party to change it. But those moves are very narrow and not very, I don't think, very realistic.

And I appreciate you pointing out that from what you can tell, at least on Capitol Hill, we are all pretty much united on that front. Perception does matter. It matters a great deal. And you and I have had discussions over the years on you were very—you admonished us strongly as Congress to spend what we needed to spend to get through the pandemic and to maintain the economy. I think you were right to do that.

You were just as aggressive in not responding to calls to rein it in a little when Democrats brought the Inflation Reduction Act and the American Rescue Plan to the forefront. And I think it really basically hijacked the economy and put fuel on the inflation. But perception matters.

And so I would just submit to you, and you haven't said you are going to do this. I don't have any reason to believe you will do this. But any move to lower interest rates or move interest rates either direction before November 5 could certainly be a bad perception even if there is a strong push to do that.

I know you understand that. But I just want you to know that as long as you remain independent, I will be on your side. I think neutral is a good place to be.

And by the way, you have one of those jobs where being boring is one of the noble things you can be. So, great job. Thank you.

Mr. POWELL. We do our best.

Chair BROWN. Thank you, Senator Cramer. Senator Warnock is recognized, who is decidedly not boring.

Senator WARNOCK. Thank you very much, Mr. Chairman. The latest monetary policy report shows inflation and housing costs is gradually easing. That is good news. But many Georgians still feel the sting of unaffordable homes and mortgages. And one reason for this, and you and I have discussed this, is that we aren't building enough houses.

A 2022 study published in the *Journal of Economic Geography* found that for every 10 percent increase in the housing stock, rents decreased by 1 percent.

We have discussed this issue, particularly the effects of housing supply on housing costs, and we agree that while the Federal Re-

serve does not control housing supply, it can help create the environment that encourages the construction of new housing, particularly affordable housing.

Chair POWELL, how has the Fed been working to foster an environment that encourages home construction. And what, in your view, are the challenges that remain?

Mr. POWELL. So, in the long run, the absolute best thing we can do for the housing market and for the economy is to sustainably bring inflation back down so that people aren't talking about it anymore. And it's just assumed by everybody in their daily lives that inflation will be around 2 percent, so we don't need to talk about it, which is where we were for a long time. We want to get back to that.

Interest rates can come down then. And the housing market can return to the state it was in before the pandemic, which was to say really tight. We don't have enough housing. And that's not really a monetary policy issue.

In the short-term though, you know, I would say tight monetary policy weighs on the housing market. You know, the policy works through interest-sensitive spending, and housing is definitely at the top of the list of interest-sensitive spending.

So, we understand that, you know, we are suppressing—not suppressing, but our higher interest rates, you know, have led to lower housing starts and lower activity in the housing market. But we are doing that to get back to 2 percent inflation for the whole economy so that the housing market can be on a better foundation.

Senator WARNOCK. Yeah, and related to that, when you have these high interest rates, of course, you see across the country, but particularly in a State like Georgia, these institutional investors who are coming into the space and they are buying houses in all cash, boxing out first-time, first-generation homebuyers and, of course, the conditions for them doing that improve to their favor with higher interest rates. Would you agree with that assessment?

Mr. POWELL. I know that some of that is happening. I don't know that higher interest rates make it—I mean, some of that is—they are working with—

Senator WARNOCK. You have got higher interest rates, and you have got institutional buyers who can purchase it all cash. Doesn't that further—

Mr. POWELL. But they have to borrow the money at higher interest rates. I am just saying higher interest rates doesn't make their investment any cheaper.

Notwithstanding, I understand it is a sensitive issue. And in most markets, it is still a pretty small portion of the outstanding housing stock. But it is not an issue for us. You know, they are a legal buyer of housing. Our job is really the whole economy. I mean, it is more of a question for legislatures.

Senator WARNOCK. So, how can the Fed better use its monetary tools to ensure that we are meeting key inflation objectives like housing affordability?

Mr. POWELL. You know, I think the best thing we can do is kind of what we think we have been doing, which is to move carefully as we think about loosening policy and make sure that we do that

when we have got greater confidence that inflation is moving sustainably down to our 2 percent target.

We are also keeping a close eye on the labor market. And if we see unexpected weakening there, then we could respond to that too. But that is really the best thing we can do for the whole economy and very specifically for the housing market, too.

Senator WARNOCK. I will point that you are limited in terms of your influence there. And there is a role for Congress to be sure, which is one of the reasons I wanted to be on this Committee to introduce a Down Payment Toward Equity Act with my colleague, Senator Butler. This bill would help first generation homebuyers compete with Wall Street institutional investors by helping with down payment costs, closing costs, and costs to reduce interest rates.

I look forward to continuing productive conversations with you and looking at how we can make housing more affordable for all Americans.

I am running out of time here, but one of the other concerns I maintain with respect to reducing the racial wealth gap is this issue around home appraisals. And the Fed as part of their agency task force on property appraisal and valuation equity, what expertise and perspective has the Fed brought to this task force and how are you responding to this issue of home appraisals?

Mr. POWELL. So, as you know, we have been an active participant in that task force. And, you know, we bring all of the expertise we have in the housing market as well as regulatory, supervisory, and economic expertise generally as we look at that.

And I will also say that our strongly held view is that discrimination has no place in the banking system and that includes appraisals and other valuations.

Senator WARNOCK. I agree with that. And quickly, I was glad to see that CFPB and other agencies recently finalized a rule that creates strong anti-discrimination standards for automated home valuations.

The Fed has not yet approved this rule. Why not and does the Fed plan to do so?

Mr. POWELL. I'm sorry. Why do we?

Senator WARNOCK. You have not yet approved the rule that was made—that was suggested by the CFPB. They finalized the rule.

Mr. POWELL. But do we—I am sorry. I am not aware that it is a rule that we have to finalize too. Is that the case?

Senator WARNOCK. That is my understanding.

Mr. POWELL. Let me follow up with you on that. I am not aware of that.

Senator WARNOCK. Thank you.

Chair BROWN. Senator Daines of Montana is recognized.

Senator DAINES. Chairman, thank you. Chairman Powell, thanks for being here today. Certainly, it is not lost on anybody here, election season is in full swing. And so from now until election day, my Democratic colleagues in Congress as well as the Biden-Harris administration will waste no time attempting to sell a fairy tale to the American people that financially and economically they are better off now than they were almost 4 years ago.

When President Biden took office, inflation was at 1.4 percent. His failed policies drove us to the highest inflation we have seen in 40 years. I can tell you the folks back home in Montana aren't fooled because in every part of their lives, inflation is not some kind of hypothetical. They see the everyday impacts of the decades-high inflation brought on by the policies of the Biden administration and facilitated by congressional Democrats.

The cost of most goods and services across the economy are more expensive than they were in 2020, and that is a fact that no amount of political spin or mental gymnastics can make go away. Here are a couple of examples. Breakfast cereal, prices have increased 28 percent since January of 2020. Gas prices increased 36 percent from the national average of \$2.63 a gallon to \$3.58 per gallon. Egg prices, egg prices have jumped \$3 per dozen in 2024, double the cost of \$1.45 in February of 2020.

And this dishonesty doesn't stop with inflation. On the labor market, while President Biden and Senate Democrats are celebrating a victory lap in light of the recent jobs report, showing 206,000 new jobs last month, they are willfully ignoring the fact that more than a third of these job gains came from the Government sector.

Mr. Chairman, I commend you for the job you have done thus far in trying to rein in inflation, and I encourage you to continue the fight despite the political pressures you may face. I am also encouraged by the comments you made earlier this month about the dire need for Washington to address its fiscal imbalance. I couldn't agree more.

I have said many times and continue to believe that Washington's culture of reckless spending, of excessive borrowing is leading us down a very dangerous path by leaving future generations with mountains of debt. And I am happy to hear you agree with that assessment.

Mr. Chairman, given that it is an election year, you are undoubtedly facing immense political pressure to lower rates. Thus far, you have done an admirable job in using the tools at your disposal to fight inflation, and I urge you to continue to be led by data and not calendars or political influence.

You said as recently as last week that while things are trending in the right direction, you would need to see further evidence before cutting rates.

So, here is my question, Mr. Chairman. What specifically are you looking at and looking for as we head into the next FOMC meeting, and how do you factor in this recent labor data and certainly the significant part of that being Government jobs?

Mr. POWELL. So, we are looking for two things really. One is just more good inflation data. And we had quite a lot of good inflation data the last 7 months of last year. Then we had kind of a bump in inflation in the first quarter. And now we have had one good and one very good inflation reading.

And we need more good data so that we can be confident that what we are seeing is really—that is where inflation is going. That it is going back down toward 2 percent. We don't need to see it at 2 percent. Right now we are at 2.6 percent. So, that is on inflation.

On the labor market, to your question, we have seen that the labor market has cooled really significantly across so many measures and a number of people here today have pointed them out. And the unemployment rate has moved up. You see a labor market that is now pretty much in balance, pretty much where it was in 2019. It is not a source of broad inflationary pressures for the economy now, but it is still a strong labor market.

You know, 4.1 percent unemployment is a very good and historically low unemployment rate. So, we want to—we have a mandate to support maximum employment. And we also are paying close attention. And if we see that the labor market was weakening unexpectedly, which is to say, you know, more than what we have seen in a material way, unexpectedly, then we could also respond to that because we have a dual mandate. And we now see the two mandates as more in balance than they were a year ago. Really the focus had to be, and was on, inflation. Now we need to be focusing on both goals.

Senator DAINES. Chairman, thank you. I want to get one question on Basel III and then we will—in March, this Committee agreed that it was seriously flawed and needed to be completely rewritten. I was encouraged to see reports last month that the Federal Reserve had provided other financial regulation to possible changes to the proposal. My question is I continued to believe the proposal should be scrapped altogether. But could you share what changes you are planning to make and the status of the ongoing development of the updated proposal?

Mr. POWELL. So, we have had extensive discussions led by Vice Chair for Supervision Barr with the FDIC and the OCC. We have made a lot of progress in getting close to an agreement on a set of proposed changes. The work that remains is to agree on a process forward. How are we going to move forward? It is our view institutionally that we need to put the changes out for comment for some period of time so that the public, all members of the public who want to comment, can see them again and comment on them again and see them in the context of the quantitative impact survey that we did. And that is the right way to proceed. That is how we would ordinarily proceed. And we don't see why we would deviate from that. And this is the conversation we are now having with the leadership of the FDIC and the OCC. And my hope is it will be able to come together around a way to proceed forward, you know, very soon. I would hope we would have done so by now. But I believe we will do so very soon.

Chair BROWN. Thank you for joining us today, Chair Powell. I look forward to working with you strengthen this economy.

For Senators who wish to submit questions for the hearing record, they are due 1 week from today, July 16, to Chair Powell. Please submit your responses to questions for the record 45 days, no more than 45 days from the day you receive them.

Thank you for your testimony. The Committee is adjourned.

[Whereupon, at 12:12 p.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF CHAIR SHERROD BROWN

Welcome Chair Powell.

Ohioans know and Americans know that our economy fundamentally is not a fair playing field.

Instead, we have a David and Goliath economy, where the largest corporations use their power to funnel all the gains in the economy to the top—aided and abetted by too many people in this town. Corporations squeeze every last penny from Americans' pocketbooks and workers' paychecks.

They don't even try to hide it anymore.

The biggest corporations are charging more for less. Americans are frustrated—no, actually, they're pissed off. They have fewer and fewer choices and those choices cost more and more.

Keeping prices down is part of the Fed's mandate. But as many of us have made clear: the Fed's main tool to combat inflation, raising interest rates does nothing to address the biggest causes of rising prices right now—corporate greed.

Keeping rates too high for too long threatens workers' paychecks while keeping other costs high—particularly housing.

Housing prices and rents continue to go up.

It is no surprise that since the Fed began raising rates, the amount of income families need to qualify for a mortgage has nearly doubled.

Home ownership has long been a bedrock of our middle class, but today, fewer and fewer middle-class families can afford to buy a home.

And higher interest rates are making our country's housing supply shortage worse, not better. We need more housing construction, of all types. Higher rates lead to the opposite, and particularly make it harder for multifamily construction to work financially.

Higher interest rates make borrowing more expensive for working families—whether it's for a mortgage or a car or anything else. Most people do not have the luxury of paying for everything in cash.

And for the millions of Americans feeling their budgets stretched by higher prices, taking on credit card debt to pay for groceries and other essentials has been an option of last resort.

But as more people struggle to pay down their debts, credit card interest rates are reaching all-time highs. Last month Director Chopra testified in front of the Committee and he explicitly stated that credit card issuers are charging higher rates far beyond what they need to cover their costs.

Banks are making record profits at the expense of cash-strapped Americans.

Every month that the Fed keeps rates high, it costs Americans money by making it more expensive to buy a house and borrow money.

Higher borrowing costs stifle future economic growth, leading to:

Fewer homes being built.

Businesses making fewer investments in the economy.

And eventually, if the Fed doesn't stop, workers losing their jobs.

As they set economic policy, I urge the Fed to weigh these tradeoffs and remember whose jobs and futures are at stake.

This is why I have worked with my colleagues to hold corporations accountable, and will continue to.

I have fought hard to cap insulin prices for senior citizens and will continue to fight to extend this price cap on life-saving drugs to all Americans.

And why my colleagues and I on this Committee are working to lower housing costs for more families.

The Fed also continues its work to keep the banking system stable and ensure consumers' money is safe.

Last year, the Fed and the other banking regulators issued a proposal to update bank capital requirements. Strong capital standards are critical for the economy—it's our way of making sure that if Wall Street's bets go poorly, investors and executives and shareholders pay for it, not taxpayers.

The biggest banks have spent obscene amounts of money attacking this proposal. But the Fed doesn't work for big banks—it works for the American people. Your concern should be developing capital rules that protect Americans' money—not bank CEOs' stock portfolios.

The Fed needs to look past these shameless lobbying efforts and finalize a rule that's in the best interests of taxpayers.

Another dangerous piece of the Wall Street business model that makes our banking system less safe is incentive-based compensation. This compensation model rewards risky behavior that enriches Wall Street executives in the short term, but makes banks more likely to fail.

We saw the results of that model in 2008 and again last year with the failures of SVB and Signature.

Other regulators have moved forward with a proposal to rein in these reckless incentives, but the rule can't move forward without the Fed.

Chair Powell, this rule is long overdue and the Fed must join this statutorily required effort as soon as possible.

The Fed also has the important job of reviewing mergers and acquisitions between banks.

Over the last several decades, we've seen the largest banks grow into massive, trillion-dollar companies, while thousands of small banks in rural communities and small towns and all across America have disappeared. Consumers have lost trusted local banks, and small businesses have lost longtime banking partners.

Regulators like the Fed have the crucial job of guarding against mergers that reduce or eliminate competition and lead to branch closures or layoffs.

I recently sent comment letters to the FDIC and OCC on their current efforts, and I expect the Fed to take the proper steps to ensure that its merger review process is robust and protects consumers and communities.

Finally, you must ensure that the Fed has the highest ethical standards.

Fed officials should never again be able to profit from their positions by using confidential plans about Fed monetary policy and emergency programs to pad their investment portfolios.

The Board's latest update to its trading rules is simply not good enough.

It still fails to establish the clear penalties needed for Federal Reserve officials who make investments in violation of the public trust. A rule with no consequences isn't much of a rule at all.

The American people need to be able to trust that the Federal Reserve works for them, and that officials aren't abusing their positions for personal gain.

As Chair of the Federal Reserve, you have an important role to play to make sure our economy works for everyone, not just for Wall Street. And the Fed's regional banks must do their part to hear from people and other stakeholders in their districts to understand their needs.

I look forward to hearing today how the Fed will balance its dual mandate, protect Americans' money, and foster an economy that upholds the dignity of work.

PREPARED STATEMENT OF SENATOR TIM SCOTT

Thank you, Mr. Chairman. Thank you, Chair Powell, for being with us this morning. Welcome back.

Joe Biden broke this economy and it's been very difficult to fix it. That's the bottom line. I want to start with the end in mind. Joe Biden broke our economy and it is very difficult for anyone to fix it.

Everyday families are struggling to put food on the table. Real wage growth is being eaten away by rising prices and runaway inflation.

Think about the fact that for 52 consecutive weeks in the Joe Biden [administration] wages were eclipsed by inflation for 52 consecutive paychecks. I remember back in December of 2020, in South Carolina, gas was a dollar and 99 cents per gallon. Today, it's still \$3.19 per gallon. A 50 percent increase in just a few years.

So, it's devastating to the average American family, particularly families like the one I grew up in—a single parent household mired in poverty. When you see your gas prices up 50 percent, your food up 30 percent, your cost of keeping your house cool or warm up 25 percent. It's not a challenge. It's not unfortunate. It's an absolute crisis.

And too many households in America today are living paycheck to paycheck, and they fear the challenges that are coming our way—the headwinds brought to us by the Biden administration.

The headwind, of course, is seen through the prism of inflation. Inflation hasn't been this size since the Jimmy Carter years, and that devastation is being felt in measured households by too much [money] at the end of the [month]. And that devastation is real for the vast majority of Americans.

And the pointing finger—I tell you what, whether it's the Biden administration throwing the Fed under the bus or any other way they can deflect from the real problem. I've seen it in committee hearing after committee hearing after committee hearing. My friends on the left want to point their fingers at anyone other than the real culprits at 1600 Pennsylvania Avenue.

The progressive wish list, spending projects, and out of control regulations of this Administration continues to eat away at American paychecks. And they continue to

blame—whether it’s “shrinkflation,” “greedflation,” and “skimplation.” They’re looking for someone to blame except for Bideninflation.

The devastation of Joe Biden’s economic policy continues to impact everyday Americans. The American people see through the facades, and they want real solutions. It doesn’t take a Ph.D. economist to understand what the average American is experiencing under this Administration. When President Biden and my Democratic colleagues pumped trillions of dollars into our economy, those dollars increase the demand and pushes prices higher.

It’s that simple. The American people see and feel it every single time, and they see it, as I said earlier, the grocery stores, the gas stations, at the doctor’s office. It’s just undeniable the impact is happening.

Just last week, we celebrated the birth of our country, the birth of this Nation of freedom and liberty. But American families got slapped with the most expensive July 4th on record, with a cookout this year costing on average 30 percent more than it did just a few years ago. I call that hogwash.

What’s worse is that this Administration doesn’t want to learn a lesson in economics. Instead of reducing the push for more spending and more regulations, they only simply double down.

Let’s take, for example, the tens of billions of dollars of student loan forgiveness—constant new plans to forgive more money regardless of the constitutionality of their decisions.

So, it’s important to ask, who are these billions of dollars of forgiveness actually benefitting? Well, the answer simple. This forgiveness scheme will result in debt relief for 750,000 individuals from households with an average income of \$300,000 or more.

And just don’t forget the fact that the average American family has a household income around \$74,000. So, what we’re doing with this unconstitutional student loan forgiveness is actually asking the median household of \$74,000 per household to bear the burden of forgiving debt for students who live in households of over \$300,000. And the actual cost of this? Somewhere between \$870 billion to \$1.4 trillion dollars.

Why do I have to even ask the question? Why do we continue to punish American families struggling paycheck to paycheck with the new scheme to relieve households over \$300,000 of student loan debt? Well, the answer is pretty simple. Politics. It’s one way to buy vote after vote after vote for November’s election. It’s just hard to imagine.

So, while I appreciate your measured words outlining the Fed’s work to cool inflation, I think it’s past time we all recognize what is truly going on. Political pandering from the left. I strongly believe that our economy cannot handle any more of this wasteful spending. And if you disagree, I would love to hear your thoughts on that. But it’s not just spending policies that stifle growth, it’s also overregulation.

And I can’t think of a better example of overregulation than parking more capital on the sidelines through Basel III Endgame. That proposal itself would cost millions of Americans their chance to own a home, start a small business, and have access to the credit and the capital necessary to make their American Dreams come true.

For those who are actually watching this hearing today on C-SPAN, Basel III capital requirements are like taking your star quarterback Dak Prescott and telling him to sit on the sidelines because he just might get injured during the season.

It’s just plain ridiculous. But these proposed capital requirements would just do that. Forcing more money to the sidelines of the greatest economy on the planet and out of the hands of first-time homebuyers, business owners, and folks trying to achieve the American Dream. The stakes are high, and that is why we have to get this right.

You’ve heard me say this a number of times, but it bears repeating, we need transparency in your rulemaking process, as this enormous proposal lacks any form of clear justification.

Chairman Powell, it is essential that you and your fellow governors, and the other agencies join in this rulemaking, follow the law, do the homework, and then let the public check the work.

That’s why I believe that it is absolutely necessary to put to have a complete re-proposal of Basel III Endgame.

Give the stakeholders an opportunity to take a look at it and then recalibrate what is necessary going forward.

Any increases in capital that are not quantitatively justified harmed the American people who need it most. Our farmers, homebuyers, small business owners need and deserve access to credit.

Therefore, I’ll repeat it one more time. You need to restore confidence in this rule-making process. Pull the existing proposal and have a complete restart. And then

when the data has been analyzed and is available for the public scrutiny, reissue an appropriate proposed rule following the requirements of the APA.

I look forward to your opening statement and having a chance to have a conversation afterwards.

PREPARED STATEMENT OF JEROME H. POWELL
CHAIR, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

JULY 9, 2024

Chairman Brown, Ranking Member Scott, and other Members of the Committee, I appreciate the opportunity to present the Federal Reserve's semiannual *Monetary Policy Report*.

The Federal Reserve remains squarely focused on our dual mandate to promote maximum employment and stable prices for the benefit of the American people. Over the past 2 years, the economy has made considerable progress toward the Federal Reserve's 2 percent inflation goal, and labor market conditions have cooled while remaining strong. Reflecting these developments, the risks to achieving our employment and inflation goals are coming into better balance.

I will review the current economic situation before turning to monetary policy.

Current Economic Situation and Outlook

Recent indicators suggest that the U.S. economy continues to expand at a solid pace. Gross domestic product growth appears to have moderated in the first half of this year following impressive strength in the second half of last year. Private domestic demand remains robust, however, with slower but still-solid increases in consumer spending. We have also seen moderate growth in capital spending and a pick-up in residential investment so far this year. Improving supply conditions have supported resilient demand and the strong performance of the U.S. economy over the past year.

In the labor market, a broad set of indicators suggests that conditions have returned to about where they stood on the eve of the pandemic: strong, but not overheated. The unemployment rate has moved higher but was still at a low level of 4.1 percent in June. Payroll job gains averaged 222,000 jobs per month in the first half of the year. Strong job creation over the past couple of years has been accompanied by an increase in the supply of workers, reflecting increases in labor force participation among individuals aged 25 to 54 and a strong pace of immigration. As a result, the jobs-to-workers gap is well down from its peak and now stands just a bit above its 2019 level. Nominal wage growth has eased over the past year. The strong labor market has helped narrow long-standing disparities in employment and earnings across demographic groups.¹

Inflation has eased notably over the past couple of years but remains above the committee's longer-run goal of 2 percent. Total personal consumption expenditures (PCE) prices rose 2.6 percent over the 12 months ending in May. Core PCE prices, which exclude the volatile food and energy categories, also increased 2.6 percent. After a lack of progress toward our 2 percent inflation objective in the early part of this year, the most recent monthly readings have shown modest further progress. Longer-term inflation expectations appear to remain well anchored, as reflected in a broad range of surveys of households, businesses, and forecasters, as well as measures from financial markets.

Monetary Policy

Our monetary policy actions are guided by our dual mandate to promote maximum employment and stable prices for the American people. In support of these goals, the committee has maintained the target range for the Federal funds rate at 5¼ to 5½ percent since last July, after having tightened the stance of monetary policy significantly over the previous year-and-a-half. We have also continued to reduce our securities holdings. At our May meeting, we decided to slow the pace of balance sheet runoff starting in June, consistent with the plans released previously. Our restrictive monetary policy stance is helping to bring demand and supply conditions into better balance and to put downward pressure on inflation.

The committee has stated that we do not expect it will be appropriate to reduce the target range for the Federal funds rate until we have gained greater confidence that inflation is moving sustainably toward 2 percent. Incoming data for the first quarter of this year did not support such greater confidence. The most recent infla-

¹ A box in our latest *Monetary Policy Report*, "Employment and Earnings Across Demographic Groups", discusses differences in labor market outcomes among segments of the population.

tion readings, however, have shown some modest further progress, and more good data would strengthen our confidence that inflation is moving sustainably toward 2 percent.

We continue to make decisions meeting by meeting. We know that reducing policy restraint too soon or too much could stall or even reverse the progress we have seen on inflation. At the same time, in light of the progress made both in lowering inflation and in cooling the labor market over the past 2 years, elevated inflation is not the only risk we face. Reducing policy restraint too late or too little could unduly weaken economic activity and employment. In considering adjustments to the target range for the Federal funds rate, the committee will continue its practice of carefully assessing incoming data and their implications for the evolving outlook, the balance of risks, and the appropriate path of monetary policy.

Congress has entrusted the Federal Reserve with the operational independence that is needed to take a longer-term perspective in the pursuit of our dual mandate of maximum employment and stable prices. We remain committed to bringing inflation back down to our 2 percent goal and to keeping longer-term inflation expectations well anchored. Restoring price stability is essential to achieving maximum employment and stable prices over the long run. Our success in delivering on these goals matters to all Americans.

Let me conclude by emphasizing that we understand that our actions affect communities, families, and businesses across the country. Everything we do is in service to our public mission.

Thank you. I am happy to take your questions.

QUESTIONS SUBMITTED FOR THE RECORD

Question for The Honorable Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System, from Chair Sherrod Brown:

1. Chair Powell, since FedNow's launch, 800 financial institutions have signed up to participate on the FedNow network.[1] Vice Chair Barr, in recent remarks, commented on FedNow's essential role in advancing financial inclusion, stating that FedNow "will enable banks to offer customers the ability to send and receive money immediately, which can help customers weather income disruption and unexpected expenses. By reducing payment delays and the high costs for consumers associated with those delays, FedNow can over time improve access to the financial system and lower costs." [2] While it is promising to see the widespread interest among financial institutions who have joined the FedNow service, many of these financial institutions have joined the FedNow Service as receive-first participants with plans to enable send when they are ready. To make instant payments more widely accessible, participating financial institutions must be able to send and receive payments on the network.

[1] <https://explore.fednow.org/explore-the-city?id=3&building=news-center&postId=64&postTitle=in-the-news:-here’s-how-the-fednow-service-answers-the-need-for-fast,-safe-and-reliable-instant-payments>.

[2] <https://www.federalreserve.gov/newsevents/speech/barr20240709a.htm>.

- a. Currently, how many of the participating financial institutions on the FedNow network can receive and send payments? What percentage of FedNow participants can only receive payments on the network?

As of early September 2024, over 950 banks and credit unions from across the country have joined the FedNow Service[®]. The majority are in "receive-first" mode, which from a risk management perspective can be a prudent first step that institutions take in adapting to a new payment service. We expect to see institutions gradually shift away from receive-first as they adjust operations and respond to growing customer demand for sending instant payments.

- b. Since its launch, how many payments have been transacted across the FedNow network? What is the total dollar amount of payments transacted on the FedNow network?

For the banks and credit unions that have joined the FedNow Service in send-and-receive mode, a smaller subset of those institutions is generating most of the volume at this time. Others are still in the early stages of implementing new instant payment services for their customers, with limited transactions. Accordingly, the number of transactions and dollar amounts sent on the FedNow Service since July 2023 is modest, which is in line with what we expected for a new service. Our intention is to publish volume and value information in the future for the FedNow Service as we do for our other payment services. From a longer-term perspective, we expect transaction volumes will follow the typical trajectory of a new payment service and grow steadily over time.

Question for The Honorable Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System, from Chairman Sherrod Brown:

2. Chair Powell, at the most recent Humphrey-Hawkins hearing before the Senate, you noted that the Federal Reserve supervises financial institutions according, in part, to its 2010 guidance on incentive-based compensation. The Review of the Federal Reserve's Supervision and Regulation of Silicon Valley Bank ("Silicon Valley Report") noted that, "Compensation packages of senior management through 2022 were tied to short-term earnings and equity returns and did not include risk metrics. As such, managers had a financial incentive to focus on short-term profit over sound risk management." In his letter accompanying the Silicon Valley Report, Vice Chair Barr stated that, "We should consider setting tougher minimum standards for incentive compensation programs and ensure banks comply with the standards we already have."

The Silicon Valley Report also states that, "the [Federal Reserve's] 2010 Incentive Compensation Guidance was designed to help ensure that incentive compensation policies do not encourage irresponsible risk-taking and are consistent with safe and sound banking practices."

Has the Fed revised its supervisory approach to incentive-based compensation in response to the Silicon Valley Report's findings? If so, can you please describe how the Fed has revised its supervisory approach to incentive-based compensation and how the Fed believes those changes will enhance the supervision of incentive-based compensation plans going forward.

Incentive compensation practices before the global financial crisis were flawed and an important post-crisis lesson was that compensation programs should provide incentives for employees to act in the long-term interest of the firm. Senior management should be held accountable for managing risks in a manner consistent with the long-term health of the organization. To this end, the Federal Reserve Board (Board), among other federal banking agencies, provided robust supervisory guidance for banks on incentive compensation to assist them in improving their compensation practices.

Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requires six agencies—the Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the National Credit Union Administration, and the Securities and Exchange Commission—to jointly issue regulations or guidelines implementing prohibitions on certain incentive compensation arrangements at supervised financial institutions and requiring firms to disclose relevant information related to incentive compensation arrangements. The Board is committed to implementing section 956. However, further work on this issue should be based on updated analysis to reflect current banking conditions and practices. We are focused on conducting this analysis to determine the best path forward.

Question for The Honorable Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System, from Ranking Member Tim Scott:

6. As of May 31, 2024, the Federal Reserve's Master Account and Services Database confirms that Numisma Bank has access to Reserve Bank financial services. Numisma is now the first bank without deposit insurance to have been granted master account access under the 2022 framework.

- a. Can you explain why Numisma was granted a master account?
- b. What makes Numisma different than other tier 3 applicants?
- c. Please provide any documentation provided to Numisma relating to their application approval.

The Federal Reserve generally does not comment on, or disclose documentation relating to, individual institutions. Under the Federal Reserve Act, master account and financial services access decisions are made by the Reserve Banks. Reserve Banks evaluate requests for accounts and financial services using the Account Access Guidelines published by the Federal Reserve Board (Board) in August 2022.¹

8. In advance of this hearing, several of my questions for the record from your prior testimony in March of this year were not yet responded to, despite nearly 4 months passing. Responses provided to several other questions were insufficient and duplicative.

- a. Why have my questions for the record gone unanswered?
- b. Do you believe that responsiveness to Congressional oversight is important?
- c. Will you commit to answering questions for the record in a timelier fashion going forward?

I recognize the importance of transparency and accountability to both Congress and the public. My responses to your Questions for the Record following the March 7, 2024, Monetary Policy Report hearing were fully completed and submitted to the Committee on May 23, 2024.

9. A Federal Reserve study found that access to free checking accounts declined as a result of the reduction of debit interchange,[3] while GAO has also concluded that "debit card interchange fee regulations increased the cost of checking accounts." [4] A George Mason University study found that debit interchange fee caps increased the unbanked population by approximately one million, primarily low-income Americans.[5]

[3] <https://www.federalreserve.gov/econres/feds/the-impact-of-price-controls-in-two-sided-markets-evidence-from-us-debit-card-interchange-fee-regulation.htm>.

¹ See <https://www.federalreserve.gov/newsevents/pressreleases/files/other20220815a1.pdf>.

[4] <https://www.gao.gov/assets/gao-22-104468.pdf>.

[5] https://www.law.gmu.edu/pubs/papers/14_18.

a. Have you considered the impact that further reduction of debit interchange will have on access to free checking and other critical consumer financial services?

Section 1075 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requires the Board to prescribe standards for assessing whether the amount any interchange fee received by a debit card issuer is reasonable and proportional to the cost incurred by the issuer with respect to the transaction. The Board fulfilled this statutory mandate in 2011 when it adopted the interchange fee cap in Regulation II.

Regulation II's current interchange fee cap is based on the costs incurred by large debit card issuers with respect to transactions performed in 2009. Since that time, the Board has continued to collect data from large debit card issuers on a biennial basis, as required by section 1075. These data show that the costs incurred by large debit card issuers have changed significantly since 2009. As a result, the current interchange fee cap may no longer be effective for assessing whether the amount of any interchange fee is reasonable and proportional to the cost incurred by the issuer with respect to the transaction, as required by statute.

Last year, the Board proposed to update the interchange fee cap for the first time based on the latest data reported to the Board by large debit card issuers concerning transactions performed in 2021. In addition, the Board proposed to update the interchange fee cap every other year going forward by directly linking the interchange fee cap to data from the Board's biennial survey of large debit card issuers. Under the proposed approach, any changes in the costs incurred by large debit card issuers would be reflected in the interchange fee cap as quickly as practicable.

The Board requested comment on all aspects of the proposal. The public comment period closed on May 12, 2024, and the Board is currently in the process of reviewing the public feedback received.

Questions for The Honorable Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System, from Ranking Member Tim Scott:

3. During the hearing, we did not have time for you to fully respond to my comments regarding the impacts of the Supreme Court's Loper decision on the Federal Reserve. I am a firm believer in cost-benefit analysis, and in light of this decision, believe thorough cost-benefit analysis for any rulemakings or guidance is necessary to reach the "best" outcome.
 - a. Please explain how will this decision impact the Federal Reserve's pending and future rulemakings?
 - i. Do you believe this decision will spur increased cost-benefit analyses in the Federal Reserve's rulemaking process?
 - ii. Will you commit to requiring Federal Reserve proposals to have more rigorous cost-benefit analyses?
 - iii. What other changes do you foresee for the Federal Reserve in light of recent supreme court decisions, including Loper?
 - iv. Do you anticipate this decision impacting litigation on the final rule implementing the Community Reinvestment Act Rule? If so, how?

At the Federal Reserve, we take seriously our obligation to follow the laws enacted by Congress, as interpreted by the Supreme Court. I want to assure you that we will continue to do so.

The independence accorded to our institution by Congress demands that the institution take great care to approach statutory interpretation in a studied, deliberate, and nonpartisan manner. This institutional value has guided our interpretations of the law as we consider regulatory actions.

Congress has charged the Federal Reserve with a number of important responsibilities by statute. We will continue to seek the best and most faithful reading of any grant of authority from Congress and will deploy its expertise within those confines.

7. During your testimony before the House Financial Services Committee on July 10, you appeared to indicate your belief that Section 956 of Dodd-Frank does not require a rulemaking, but rather requires a rulemaking or guidance to be issued. During your testimony before the Senate Banking Committee on July 9, you spoke multiple times about the 2010 executive compensation guidance.

- a. Do you believe the 2010 guidance is sufficient to fulfill the requirements of Section 956? Please answer "yes" or "no."
 - i. If "no", please explain why.

Incentive compensation practices before the global financial crisis were flawed and an important post-crisis lesson was that compensation programs should provide incentives for employees to act in the long-term interest of the firm. Senior management should be held accountable for managing risks in a manner consistent with the long-term health of the organization. To this end, the Federal Reserve Board (Board), among other federal banking agencies, provided robust supervisory guidance for banks on incentive compensation to assist them in improving their compensation practices.

Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requires six agencies—the Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the National Credit Union Administration, and the Securities and Exchange Commission—to jointly issue regulations or guidelines implementing prohibitions on certain incentive compensation arrangements at supervised financial institutions and requiring firms to disclose relevant information related to incentive compensation arrangements. The Board is committed to implementing section 956. However, further work on this issue should be based on updated analysis to reflect current banking conditions and practices. We are focused on conducting this analysis to determine the best path forward.

Question for The Honorable Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System, from Ranking Member Tim Scott:

4. During the hearing, you reiterated that the FOMC remains data driven and data focused when considering any changes to the Federal Funds Rate. On Friday July 5, the Bureau of Labor Statistics (BLS) revised the number of job gains in April and May of 2024 lowered by a combined 111,000 jobs.[1] This trend is not new and was seen throughout 2023 in which employment gains were reduced by an average of 55,000 a month from January to October.[2]

[1] The Employment Situation - June 2024 (bls.gov)

[2] <https://www.bls.gov/web/emp/sit/cesnaicsrev.htm#2023>

- a. Given the consistent revisions of BLS data, do you believe the FOMC currently has accurate economic data?
- b. Are you concerned that these revisions could result in the FOMC making a mistake?
- c. Do you have any idea why the data is so frequently being revised down?
- d. Are you concerned other economic data may be flawed?

Policy decisions at the Federal Reserve are data dependent. Because we know that no single indicator is perfect, those decisions are made in light of analysis of a broad range of labor market indicators. For example, to assess labor market conditions we look at the Bureau of Labor Statistics's (BLS) payroll employment figures, together with data from the Current Population Survey, the payroll processing firm ADP, the Quarterly Census of Employment and Wages, job vacancies data from the BLS's Job Openings and Labor Turnover Survey and from Indeed, unemployment insurance claims, and layoff announcements, among a number of other indicators.

As you note, over the past year and a half there has been a clear tendency for monthly payroll employment gains to revise down from their initial to their third estimate. In 2023, the average monthly revision was -30,000, and so far in 2024 it has been -44,000 per month.¹ Moreover, on August 21, 2024, the BLS released its preliminary estimate of the annual benchmark revision to the payroll data, which will be implemented in February 2025. The preliminary estimate indicates a downward adjustment of 818,000 to the March 2024 level of nonfarm payroll employment.² This estimate suggests that monthly payroll gains from April 2023 to March 2024 will be revised down further by about 68,000 per month on average when the BLS incorporates its final benchmark revision early next year.

¹ As of early October, the latest month for which the third estimate was available was July 2024.

² See <https://www.bls.gov/web/emp/sit/cesprelbnk.htm>.

There are a number of possible factors contributing to these revisions. As for the expected downward revision from the annual benchmarking process, this issue could be related to the adjustments made to payroll gains to account for establishment births and deaths.³ Another likely contributing factor is that the BLS seasonally adjusts the data using concurrent seasonal adjustment, which can result in downward revisions to the seasonally adjusted data when the pace of payroll growth is slowing.⁴ In addition, survey response rates have declined in recent years, including in the establishment survey that underpins the payrolls data, which might help explain a larger magnitude of revisions.⁵

We will continue to make our policy decisions meeting by meeting, based on the totality of the data, the outlook, and the balance of risks. I remain confident that those assessments are based on the best available data.

³ The birth-death adjustment is an adjustment made to survey-based employment growth estimates to account for the net employment effect of establishments opening and going out of business (since these establishments are not captured immediately in the survey). These adjustments are model-based estimates that are calibrated using a few years of past data and therefore can be slow to capture rapid changes in business creation and deaths. When the economy is slowing (resulting in declines in business creation and increases in business deaths), the slow updating of the birth-death model estimates can lead to a temporary overstatement of employment gains.

⁴ Concurrent seasonal adjustment uses the most recent data (up to the latest month) to estimate the seasonal component. When payroll growth is slowing significantly, the seasonal adjustment process can incorrectly interpret some of this slowdown as changes in seasonality. Consequently, the seasonal factor may initially boost the payroll growth figures, leading to an overestimation of seasonally adjusted payroll growth. As more data come in showing weaker growth, the process recognizes that the slowdown is due to a slowing trend rather than to seasonal changes. The seasonal factors are then adjusted to be less supportive, leading to downward revisions to seasonally-adjusted payroll growth.

⁵ See <https://www.bls.gov/osmr/response-rates/#chart2a>.

Questions for The Honorable Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System, from Ranking Member Tim Scott:

1. During the hearing I questioned why so much of the Basel III Endgame proposal appears to be being negotiated behind closed doors and why the public has not yet seen the results of the Fed's quantitative impact study. In response, you stated, "...when we do reach agreement with the other agencies fully, that we would publish the, you know, the proposed changes and also the quantitative impact survey. And also the effects that the QIS suggest that the changes would have."
 - a. Does this mean that you are currently using data submitted as part of the initial QIS to analyze changes to the proposal?
 - i. If so, will you clearly state what changes made in your re-proposal stem from the QIS?
 - ii. Will you commit to publishing the results of the QIS and the calculations undertaken to arrive at such results to allow for public analysis?
 - b. Do you plan to or think there should be another QIS undertaken for any re-proposal?

We have received and reviewed voluminous substantive comments on the capital proposal, as well as data from the quantitative impact studies. As I noted during my testimony, I believe there should be broad and material changes to the original proposal. Further, when there are broad and material changes to a proposal of this importance, I believe the best practice is to put those changes out for public comment. This is consistent with the Federal Reserve's past practice. We continue to work with the Office of the Comptroller of the Currency (OCC) and Federal Deposit Insurance Corporation (FDIC) on next steps with regards to the proposal. Our primary focus is getting this work done right.

2. During your testimony before the House Financial Services Committee on July 10, in response to Congressman Garbarino, you appeared to indicate that the Fed plans to repropose only a portion of the Basel III Endgame proposal. You stated, "[T]here will be additional changes that will be made that won't be re-proposed. That's what we're working on rather than a full, wide proposal."
 - a. Do you stand by your remarks made that there will only be a partial re-proposal?
 - b. If so, please explain why some changes will require re-proposal and others will not. In your explanation, please include any metrics you are using to determine whether a change should be included in the partial re-proposal.
 - c. Do you believe that each portion of the original proposal is interconnected with the other portions? If no, please explain why not.

d. Will this re-proposal be an interagency re-proposal or is the Fed moving forward alone?

i. If the Fed is moving forward alone, please explain the process for interagency finalization?

We have received and reviewed voluminous substantive comments on the capital proposal, as well as data from the quantitative impact studies. As I noted during my testimony, I believe there should be broad and material changes to the original proposal. Further, when there are broad and material changes to a proposal of this importance, I believe the best practice is to put those changes out for public comment. This is consistent with the Federal Reserve's past practice. We continue to work with the OCC and FDIC on next steps with regards to the proposal. Our primary focus is getting this work done right.

5. In response to Senator Britt questioning on the Long-Term Debt proposal, you stated, "That's not to say we wouldn't reach a place where people understand and accept and support what it is we're doing [on bank capital] and at that point we could certainly move ahead with other rules."

a. To clarify, was this a commitment not to move forward with other capital or liquidity proposals until the Basel III Endgame proposal is finalized?

Given how interconnected your regulatory work is, can you commit to not moving forward on proposing/finalizing major proposals until you've announced what is happening on B3E?

Taking an overall perspective and considering the aggregate impact of our regulatory framework is an important part of our work. We have been carefully considering comments on all aspects of the proposals, including how each proposal would interact with other rulemaking proposals and impact the U.S. economy and regulated firms. We will continue to work on the capital proposal, as well as other policy initiatives, in the normal course. Our primary focus is getting this work done right.

10. On June 26, the Federal Reserve released the results of the 2024 Stress Tests, which as Vice Chair stated, "shows that large banks have sufficient capital to withstand a highly stressful scenario and meet their minimum capital ratios." [6]

[6] <https://www.federalreserve.gov/newsevents/pressreleases/barr-statement-20240626.htm>.

a. In light of these results, how does the Federal Reserve justify proposals to increase capital as part of Basel III Endgame?

b. What is the Federal Reserve's plan for resolving the operational risk overlap in the Basel III Endgame proposal with the existing stress testing and models to prevent a double counting of risks?

I am committed to implementing the Basel III endgame in a way that is broadly consistent with the Basel agreement and broadly comparable to what other large jurisdictions are doing.

We have received and reviewed voluminous substantive comments, as well as data from the quantitative impact studies, on all aspects of the capital proposal, including those on operational risk. As I noted during my testimony, I believe there should be broad and material changes to the original proposal. Further, when there are broad and material changes to a proposal of this importance, I believe the best practice is to put those changes out for public comment. This is consistent with the Federal Reserve's past practice. We continue to work with the OCC and FDIC on next steps with regards to the proposal. Our primary focus is getting this work done right.

11. In recent months, we have seen various other jurisdictions delay or consider delaying their Basel III Endgame implementation due to concerns of international competitiveness.[7] As proposed, the Basel III Endgame proposal would result in greater increases to capital than those proposed by other jurisdictions. Given that it is clear that foreign jurisdictions are intent on international competitiveness of their own banking sectors, how does American competitiveness play into your analysis?

[7] <https://www.reuters.com/business/finance/eu-says-delay-core-element-basel-bank-capital-rules-2024-06-18/>.

a. Is this a factor the Federal Reserve is considering as changes are made to the Basel III Endgame proposal?

I am committed to implementing the Basel III endgame in a way that is broadly consistent with the Basel agreement and broadly comparable to what other large jurisdictions are doing. As I noted in my statement during our open meeting, the proposal exceeds what is required by the Basel agreement, and exceeds, as well, what we know of plans for implementation by other large jurisdictions. Our rules should support an effective and efficient regulatory regime that maintains the resiliency of the financial system and protects the American economy, while imposing no more burden than is necessary.

We have received and reviewed voluminous substantive comments on the capital proposal, as well as data from the quantitative impact studies. As I noted during my testimony, I believe there should be broad and material changes to the original proposal. Further, when there are broad and material changes to a proposal of this importance, I believe the best practice is to put those changes out for public comment. This is consistent with the Federal Reserve's past practice. We continue to work with the OCC and FDIC on next steps with regards to the proposal. Our primary focus is getting this work done right.

Questions for The Honorable Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System, from Senator Chris Van Hollen:

Chair Powell, during your testimony to the Committee I asked you why the Federal Reserve was taking so long to move forward with the implementation of Dodd-Frank Section 956, a law that has been in place for 14 years now. In your response, you mention that the Fed *has not* yet done that.

1. Can you explain your answer on why the Federal Reserve has not yet met the legal requirements of Dodd-Frank Section 956?

Incentive compensation practices before the global financial crisis were flawed and an important post-crisis lesson was that compensation programs should provide incentives for employees to act in the long-term interest of the firm. Senior management should be held accountable for managing risks in a manner consistent with the long-term health of the organization. To this end, the Federal Reserve Board (Board), among other federal banking agencies, provided robust supervisory guidance for banks on incentive compensation to assist them in improving their compensation practices.

Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requires six agencies—the Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the National Credit Union Administration, and the Securities and Exchange Commission—to jointly issue regulations or guidelines implementing prohibitions on certain incentive compensation arrangements at supervised financial institutions and requiring firms to disclose relevant information related to incentive compensation arrangements. The Board is committed to implementing section 956. However, further work on this issue should be based on updated analysis to reflect current banking conditions and practices. We are focused on conducting this analysis to determine the best path forward.

2. What is your plan as Chair to get the Fed in compliance with 956?

Please see my response to question 1.

Question for The Honorable Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System, from Senator Bill Hagerty:

1. The Federal Reserve holds more than \$2.3 trillion of mortgage-backed securities (MBS). Has the Fed assessed the direct credit risk of its holdings of GSE MBS in the event that the GSE conservatorships are ended?

The Federal Reserve purchased large volumes of Treasury and agency mortgage-backed securities (MBS) in response to the 2008 financial crisis and again in the wake of the extreme economic and financial disruptions associated with the global pandemic. These purchases provided critical support for the U.S. economy and the flow of credit to households and businesses during times of crisis, and they were an essential tool for the Federal Reserve in promoting its statutory goals of maximum employment and stable prices.

In 2022, with the recovery of the economy well underway, the Federal Open Market Committee (FOMC) announced principles and plans for reducing the size of the Federal Reserve's balance sheet. As detailed in those plans, the Federal Reserve has been reducing its holdings of Treasury and agency MBS since June of 2023. To date, the Federal Reserve's securities holdings have declined by about \$1.8 trillion. The FOMC has indicated that it intends to hold primarily Treasury securities in the longer run. As a result, even when the size of the Federal Reserve's balance sheet has been normalized, the share of agency MBS in the Federal Reserve's securities holdings will continue to decline over time. At present, the Federal Reserve's holdings of agency MBS are running off at a pace of about \$15 billion per month, and the Federal Reserve could consider sales of its agency MBS at some point if it wished to expedite the shift in the composition of the Federal Reserve's securities holdings toward Treasury securities.

Regarding the potential credit risk associated with the Federal Reserve's agency MBS holdings, more than 20 percent of the Federal Reserve's agency MBS holdings are in the form of Ginnie Mae securities, which are full faith and credit obligations of the United States. The credit risk associated with the Federal Reserve's holdings of securities issued by Fannie Mae and Freddie Mac would stem only from the extreme case in which losses on the mortgage pools underlying agency MBS were so large that Fannie and Freddie were not able to honor the guarantee on the securities. On this issue, as the Financial Stability Oversight Council has noted, government-sponsored enterprise (GSE) capital buffers "should be tailored to mitigate the potential risks to financial stability and otherwise ensure that the Enterprises have sufficient capital to absorb losses during periods of severe stress and remain viable going concerns."¹ If post-conservatorship GSEs nonetheless incurred losses that could not be absorbed by capital or other risk mitigants, the credit risk to all holders of agency MBS would depend on the specific details within the economic and financial market backdrop of such an extreme scenario.

¹ See <https://home.treasury.gov/system/files/261/Financial-Stability-Oversight-Councils-Statement-on-Secondary-Mortgage-Market-Activities.pdf>.

Question for The Honorable Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System, from Senator Bill Hagerty:

- 2. How did the Federal Reserve incorporate its prior research on debit interchange fee caps into the formulation of the recently proposed interchange rule? How has the Fed weighed any hypothetical benefits of the proposed rule against its documented drawbacks?**

Section 1075 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requires the Federal Reserve Board (Board) to prescribe standards for assessing whether the amount any interchange fee received by a debit card issuer is reasonable and proportional to the cost incurred by the issuer with respect to the transaction. The Board fulfilled this statutory mandate in 2011 when it adopted the interchange fee cap in Regulation II.

Regulation II's current interchange fee cap is based on the costs incurred by large debit card issuers with respect to transactions performed in 2009. Since that time, the Board has continued to collect data from large debit card issuers on a biennial basis, as required by section 1075. These data show that the costs incurred by large debit card issuers have changed significantly since 2009. As a result, the current interchange fee cap may no longer be effective for assessing whether the amount of any interchange fee is reasonable and proportional to the cost incurred by the issuer with respect to the transaction, as required by statute.

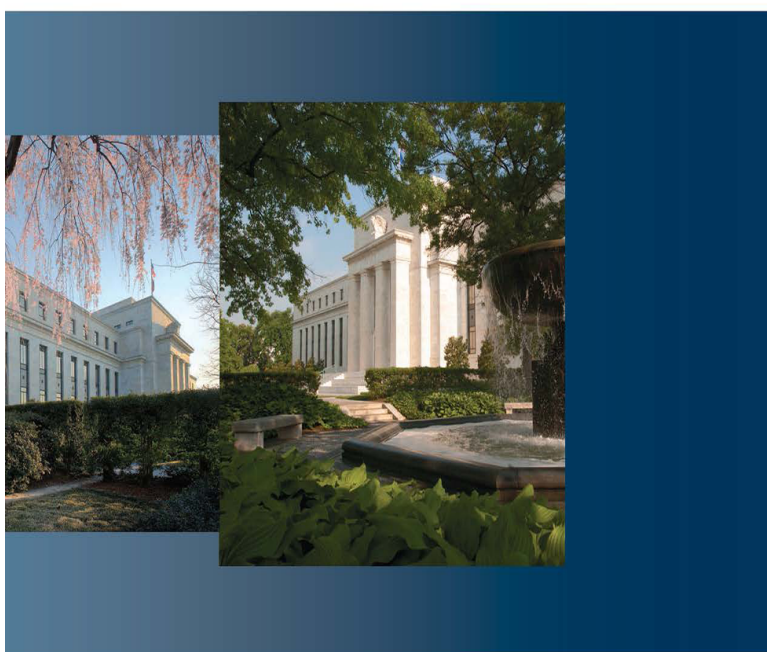
Last year, the Board proposed to update the interchange fee cap for the first time based on the latest data reported to the Board by large debit card issuers concerning transactions performed in 2021. In addition, the Board proposed to update the interchange fee cap every other year going forward by directly linking the interchange fee cap to data from the Board's biennial survey of large debit card issuers. Under the proposed approach, any changes in the costs incurred by large debit card issuers would be reflected in the interchange fee cap as quickly as practicable.

The Board requested comment on all aspects of the proposal. The public comment period closed on May 12, 2024, and the Board is currently in the process of reviewing the public feedback received.

For use at 11:00 a.m. EDT
July 5, 2024

MONETARY POLICY REPORT

July 5, 2024



Board of Governors of the Federal Reserve System

LETTER OF TRANSMITTAL



BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM

Washington, D.C., July 5, 2024

THE PRESIDENT OF THE SENATE
THE SPEAKER OF THE HOUSE OF REPRESENTATIVES

The Board of Governors is pleased to submit its *Monetary Policy Report* pursuant to section 2B of the Federal Reserve Act.

Sincerely,

A handwritten signature in black ink, reading "Jerome H. Powell". The signature is written in a cursive, flowing style.

Jerome H. Powell, Chair

STATEMENT ON LONGER-RUN GOALS AND MONETARY POLICY STRATEGY

Adopted effective January 24, 2012; as reaffirmed effective January 30, 2024

The Federal Open Market Committee (FOMC) is firmly committed to fulfilling its statutory mandate from the Congress of promoting maximum employment, stable prices, and moderate long-term interest rates. The Committee seeks to explain its monetary policy decisions to the public as clearly as possible. Such clarity facilitates well-informed decisionmaking by households and businesses, reduces economic and financial uncertainty, increases the effectiveness of monetary policy, and enhances transparency and accountability, which are essential in a democratic society.

Employment, inflation, and long-term interest rates fluctuate over time in response to economic and financial disturbances. Monetary policy plays an important role in stabilizing the economy in response to these disturbances. The Committee's primary means of adjusting the stance of monetary policy is through changes in the target range for the federal funds rate. The Committee judges that the level of the federal funds rate consistent with maximum employment and price stability over the longer run has declined relative to its historical average. Therefore, the federal funds rate is likely to be constrained by its effective lower bound more frequently than in the past. Owing in part to the proximity of interest rates to the effective lower bound, the Committee judges that downward risks to employment and inflation have increased. The Committee is prepared to use its full range of tools to achieve its maximum employment and price stability goals.

The maximum level of employment is a broad-based and inclusive goal that is not directly measurable and changes over time owing largely to nonmonetary factors that affect the structure and dynamics of the labor market. Consequently, it would not be appropriate to specify a fixed goal for employment; rather, the Committee's policy decisions must be informed by assessments of the shortfalls of employment from its maximum level, recognizing that such assessments are necessarily uncertain and subject to revision. The Committee considers a wide range of indicators in making these assessments.

The inflation rate over the longer run is primarily determined by monetary policy, and hence the Committee has the ability to specify a longer-run goal for inflation. The Committee reaffirms its judgment that inflation at the rate of 2 percent, as measured by the annual change in the price index for personal consumption expenditures, is most consistent over the longer run with the Federal Reserve's statutory mandate. The Committee judges that longer-term inflation expectations that are well anchored at 2 percent foster price stability and moderate long-term interest rates and enhance the Committee's ability to promote maximum employment in the face of significant economic disturbances. In order to anchor longer-term inflation expectations at this level, the Committee seeks to achieve inflation that averages 2 percent over time, and therefore judges that, following periods when inflation has been running persistently below 2 percent, appropriate monetary policy will likely aim to achieve inflation moderately above 2 percent for some time.

Monetary policy actions tend to influence economic activity, employment, and prices with a lag. In setting monetary policy, the Committee seeks over time to mitigate shortfalls of employment from the Committee's assessment of its maximum level and deviations of inflation from its longer-run goal. Moreover, sustainably achieving maximum employment and price stability depends on a stable financial system. Therefore, the Committee's policy decisions reflect its longer-run goals, its medium-term outlook, and its assessments of the balance of risks, including risks to the financial system that could impede the attainment of the Committee's goals.

The Committee's employment and inflation objectives are generally complementary. However, under circumstances in which the Committee judges that the objectives are not complementary, it takes into account the employment shortfalls and inflation deviations and the potentially different time horizons over which employment and inflation are projected to return to levels judged consistent with its mandate.

The Committee intends to review these principles and to make adjustments as appropriate at its annual organizational meeting each January, and to undertake roughly every 5 years a thorough public review of its monetary policy strategy, tools, and communication practices.

CONTENTS

Summary	1
Recent Economic and Financial Developments	1
Monetary Policy	3
Special Topics	3
Part 1: Recent Economic and Financial Developments	5
Domestic Developments	5
Financial Developments	30
International Developments	36
Part 2: Monetary Policy	41
Part 3: Summary of Economic Projections	53
Abbreviations	71
 List of Boxes	
Housing Services Inflation and Market Rent Measures	9
Employment and Earnings across Demographic Groups	16
Developments Related to Financial Stability	33
Monetary Policy Independence, Transparency, and Accountability	42
Developments in the Federal Reserve's Balance Sheet and Money Markets	47
Monetary Policy Rules in the Current Environment	50
Forecast Uncertainty	68

Note: This report reflects information that was publicly available as of noon EDT on July 2, 2024.

Unless otherwise stated, the time series in the figures extend through, for daily data, June 28, 2024; for monthly data, May 2024; and, for quarterly data, 2024:Q1. In bar charts, except as noted, the change for a given period is measured to its final quarter from the final quarter of the preceding period.

For figures 26, 37, and 43, note that the S&P/Case-Shiller U.S. National Home Price Index, the S&P 500 Index, and the Dow Jones Bank Index are products of S&P Dow Jones Indices LLC and/or its affiliates and have been licensed for use by the Board. Copyright © 2024 S&P Dow Jones Indices LLC, a division of S&P Global, and/or its affiliates. All rights reserved. Redistribution, reproduction, and/or photocopying in whole or in part are prohibited without written permission of S&P Dow Jones Indices LLC. For more information on any of S&P Dow Jones Indices LLC's indices, please visit www.spdji.com. S&P® is a registered trademark of Standard & Poor's Financial Services LLC, and Dow Jones® is a registered trademark of Dow Jones Trademark Holdings LLC. Neither S&P Dow Jones Indices LLC, Dow Jones Trademark Holdings LLC, their affiliates, nor their third-party licensors make any representation or warranty, express or implied, as to the ability of any index to accurately represent the asset class or market sector that it purports to represent, and neither S&P Dow Jones Indices LLC, Dow Jones Trademark Holdings LLC, their affiliates, nor their third-party licensors shall have any liability for any errors, omissions, or interruptions of any index or the data included therein.

SUMMARY

Inflation eased notably last year and has shown modest further progress so far this year, but it remains above the Federal Open Market Committee's (FOMC) objective of 2 percent. Job gains have been strong, and the unemployment rate is still low. Meanwhile, as job vacancies continued to decline and labor supply continued to increase, the labor market moved into better balance over the first half of the year. Real gross domestic product (GDP) growth was modest in the first quarter, while growth in private domestic demand remained robust, supported by slower but still-solid increases in consumer spending, moderate growth in capital spending, and a sharp pickup in residential investment.

The FOMC has maintained the target range for the federal funds rate at $5\frac{1}{4}$ to $5\frac{1}{2}$ percent since its July 2023 meeting. In addition, the Committee has continued to reduce its holdings of Treasury securities and agency mortgage-backed securities. The Committee does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2 percent. Reducing policy restraint too soon or too much could result in a reversal of the progress on inflation. At the same time, reducing policy restraint too late or too little could unduly weaken economic activity and employment. In considering any adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks.

The FOMC is strongly committed to returning inflation to its 2 percent objective. The Committee remains highly attentive to inflation risks and is acutely aware that high inflation imposes significant hardship, especially on those least able to meet the higher costs of essentials.

Recent Economic and Financial Developments

Inflation. Although personal consumption expenditures (PCE) price inflation slowed notably last year and has shown modest further progress this year, it remains above the FOMC's longer-run objective of 2 percent. The PCE price index rose 2.6 percent over the 12 months ending in May, down from the 4.0 percent pace over the preceding 12 months and a peak of 7.1 percent in June 2022. The core PCE price index—which excludes food and energy prices and is generally considered a better guide to the direction of future inflation—also rose 2.6 percent in the 12 months ending in May, down from 4.7 percent a year ago and slower than the 2.9 percent pace at the end of last year. On a 12-month basis, core goods price inflation and housing services price inflation continued to ease over the first part of the year, while core nonhousing services price inflation flattened out after slowing notably last year. Measures of longer-term inflation expectations are within the range of values seen in the decade before the pandemic and continue to be broadly consistent with the FOMC's longer-run objective of 2 percent.

The labor market. The labor market continued to rebalance over the first half of this year, and it remained strong. Job gains were solid, averaging 248,000 per month over the first five months of the year, and the unemployment rate remained low. Labor demand has eased, as job openings have declined in many sectors of the economy, and labor supply has continued to increase, supported by a strong pace of immigration. With cooling labor demand and rising labor supply, the unemployment rate edged up to 4.0 percent in May. The balance between labor demand and supply appears similar to that in the period immediately

2 SUMMARY

before the pandemic, when the labor market was relatively tight but not overheated. Nominal wage growth continued to slow in the first part of the year but remains above a pace consistent with 2 percent inflation over the longer term, given prevailing trends in productivity growth.

Economic activity. Real GDP growth is reported to have moderated in the first quarter after having increased at a robust pace in the second half of last year. Much of the slowdown was due to sizable drags in the volatile categories of net exports and inventory investment; growth in private domestic final purchases—which includes consumer spending, business fixed investment, and residential investment—also moved a little lower in the first quarter but remained solid. Real consumption growth slowed in the first quarter from a strong pace in the second half of last year, reflecting a decline in goods spending. Real business fixed investment grew at a moderate pace in the first quarter despite high interest rates, supported by strong sales growth and improvements in business sentiment and profit expectations. Activity in the housing sector picked up sharply in the first quarter as a result of a jump in existing home sales and rising construction of single-family homes.

Financial conditions. Financial conditions appear somewhat restrictive on balance. Treasury yields and the market-implied expected path of the federal funds rate have moved up, on net, since the beginning of the year, while broad equity prices have increased. Credit remains generally available to most households and businesses but at elevated interest rates, which have weighed on financing activity. The pace of bank lending to households and businesses increased in the first five months of the year but continues to be somewhat tepid. Delinquency rates on small business loans stayed slightly above pre-pandemic levels, and delinquency rates for credit cards, auto loans, and commercial real estate loans continued to increase in the first

quarter of 2024 to levels above their longer-run averages.

Financial stability. The financial system remains sound and resilient. The balance sheets of nonfinancial businesses and households stayed strong, with the combined credit-to-GDP ratio standing near its two-decade low. Business debt continued to decline in real terms, and debt-servicing capacity remained solid for most public firms, in large part due to strong earnings, large cash buffers, and low borrowing costs on existing debt. However, there were also signs of vulnerabilities building in the financial system. In asset markets, corporate bond spreads narrowed, equity prices rose faster than expected earnings, and residential property prices remained high relative to market rents. Moreover, in the banking sector, some banks' fair value losses on fixed-rate assets remained sizable, despite most of them continuing to report solid capital levels. Additionally, parts of banks' commercial real estate portfolios are facing stress. Some banks' reliance on uninsured deposits remained high. Even so, liquidity at most domestic banks remained ample, with limited reliance on short-term wholesale funding. Bond mutual funds' exposure to interest rate risk stayed elevated, and data through the third quarter of 2023 show that hedge fund leverage had grown to historical highs, driven primarily by borrowing by the largest hedge funds. (See the box "Developments Related to Financial Stability" in Part I.)

International developments. Foreign economic activity appears to have improved in the first quarter after a soft patch in the second half of last year. In advanced foreign economies, growth rates returned to moderate levels despite the effects of restrictive monetary policy as lower inflation improved real household incomes. In emerging market economies, growth was supported by a recovery in exports and rising global demand for high-tech products, with the rise in activity in China in the first quarter being particularly

outsized. Nonetheless, other factors continued to weigh on economic growth: Data indicated ongoing weakness in China's property sector, and in Europe, energy-intensive sectors continue to struggle, reflecting their ongoing adjustment to past increases in energy prices following Russia's 2022 invasion of Ukraine.

Foreign headline inflation has continued to decline since the middle of last year, but the pace of disinflation has been gradual and uneven across countries and economic sectors. Still, many foreign central banks have noted this progress in lowering inflation, and some have begun to cut their policy rates. A notable exception is Japan, which ended its negative interest rate policy and yield curve control in March amid persistently high inflation. The trade-weighted exchange value of the dollar rose significantly, consistent with widening gaps between U.S. and foreign interest rates.

Monetary Policy

Interest rate policy. The FOMC has maintained the target range for the policy rate at 5¼ to 5½ percent since its July 2023 meeting. The Committee judges that the risks to achieving its employment and inflation goals have moved toward better balance over the past year. The Committee perceives the economic outlook to be uncertain and remains highly attentive to inflation risks. The Committee has indicated that it does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2 percent. Policy is well positioned to deal with the risks and uncertainties the Committee faces in pursuing both sides of its dual mandate. In considering any adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks.

Balance sheet policy. The Federal Reserve has continued the process of significantly reducing its holdings of Treasury and agency

securities in a predictable manner.¹ Beginning in June 2022, principal payments from securities held in the System Open Market Account have been reinvested only to the extent that they exceeded monthly caps. Under this policy, the Federal Reserve has reduced its securities holdings about \$1.7 trillion since the start of balance sheet reduction. The FOMC has stated that it intends to maintain securities holdings at amounts consistent with implementing monetary policy efficiently and effectively in its ample-reserves regime. To ensure a smooth transition from abundant to ample reserve balances, the FOMC slowed the pace of decline of its securities holdings at the beginning of June and intends to stop reductions when reserve balances are somewhat above the level that the Committee judges to be consistent with ample reserves.

Special Topics

Housing services inflation. The PCE price index for housing services started accelerating in 2021, notably increasing its contribution to core PCE inflation. Because this index calculates average rent for all tenants—both new tenants and existing tenants—its changes tend to lag changes in market rent measures for new leases. Therefore, measures of market rent growth for new leases can help predict future changes in the PCE price index. Since mid-2022, market rents have decelerated and returned to a growth rate similar to or below their average pre-pandemic pace, while the PCE index continues to show elevated inflation, reflecting the gradual pass-through of market rates to existing tenants. As this process continues, PCE housing services inflation should gradually decline, though much uncertainty remains about the extent

1. See the May 4, 2022, press release regarding the Plans for Reducing the Size of the Federal Reserve's Balance Sheet, available on the Board's website at <https://www.federalreserve.gov/newsevents/pressreleases/monetary20220504b.htm>.

and timing. (See the box “Housing Services Inflation and Market Rent Measures” in Part 1.)

Employment and earnings across groups. A strong labor market over the past two years has been especially beneficial for historically disadvantaged groups of workers. As a result, many of the long-standing disparities in employment and wages by sex, race, ethnicity, and education have narrowed, and some gaps reached historical lows in 2023 and the first half of 2024. However, despite this narrowing, significant disparities in absolute levels across groups remain. (See the box “Employment and Earnings across Demographic Groups” in Part 1.)

Monetary policy independence, transparency, and accountability. Congress has established a statutory framework that specifies the long-run objectives of monetary policy—maximum employment and stable prices—and gives the Federal Reserve operational independence in conducting monetary policy. In this framework, the Federal Reserve makes determinations about the monetary policy actions that are most appropriate for achieving the dual-mandate goals that Congress has assigned to it. The Federal Reserve recognizes that independence is a trust given to it by Congress and the American people and that with independence comes the need to be transparent about, and accountable for, its monetary policy decisions. Transparency also improves monetary policy’s effectiveness. The Federal Reserve promotes transparency by providing

information about FOMC decisions through policy communications and a variety of publications. The means by which the Federal Reserve informs the American people about its monetary policy decisions include official FOMC statements, monetary policy reports, and Committee meeting minutes and transcripts, as well as speeches, press conferences, and congressional testimony given by Federal Reserve officials. (See the box “Monetary Policy Independence, Transparency, and Accountability” in Part 2.)

Federal Reserve’s balance sheet and money markets. The size of the Federal Reserve’s balance sheet has continued to decrease since February as the FOMC has reduced its securities holdings. Reserve balances, the largest liability on the Federal Reserve’s balance sheet, and usage of the overnight reverse repurchase agreement facility—another Federal Reserve liability—both declined. (See the box “Developments in the Federal Reserve’s Balance Sheet and Money Markets” in Part 2.)

Monetary policy rules. Simple monetary policy rules, which prescribe a setting for the policy interest rate in response to the behavior of a small number of economic variables, can provide useful guidance to policymakers. With inflation easing over the past year, the policy rate prescriptions of most simple monetary policy rules have decreased recently and now call for levels of the federal funds rate that are close to or below the current target range for the federal funds rate. (See the box “Monetary Policy Rules in the Current Environment” in Part 2.)

PART 1

RECENT ECONOMIC AND FINANCIAL DEVELOPMENTS

Domestic Developments

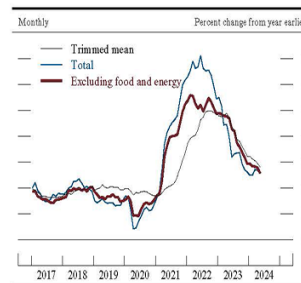
Inflation eased notably last year and has shown modest further progress in recent months

Inflation stepped down markedly last year and has shown modest further progress so far this year. Inflation remains elevated, though, and is still above the Federal Open Market Committee's (FOMC) longer-run objective of 2 percent. The price index for personal consumption expenditures (PCE) rose 2.6 percent over the 12 months ending in May, down from the 4.0 percent pace a year ago but little changed since the end of last year (figure 1). After having slowed markedly in the second half of 2023, monthly core PCE price inflation—which excludes food and energy prices and is generally considered a better guide to the direction of future inflation—firmed in the first quarter of this year and then eased somewhat in April and May. As a result, the 12-month change in core PCE prices declined from the 4.7 percent pace in May of last year to 2.9 percent in December and moved down further this year, to 2.6 percent in May (figure 2). A similar message is evident from the trimmed mean measure of PCE prices constructed by the Federal Reserve Bank of Dallas, which provides an alternative approach to reducing the influence of idiosyncratic price movements. The index increased 2.8 percent over the 12 months ending in May, a pace that is somewhat slower than at the end of last year (as shown in figure 1).

Consumer energy prices have increased, while food price inflation has flattened out

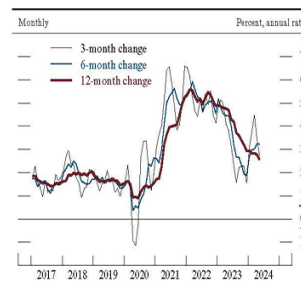
PCE energy prices increased 4.8 percent in the 12 months ending in May after having declined 12.3 percent over the preceding 12 months

1. Personal consumption expenditures price indexes



SOURCE: For trimmed mean, Federal Reserve Bank of Dallas; for all else, Bureau of Economic Analysis; all via Haver Analytics.

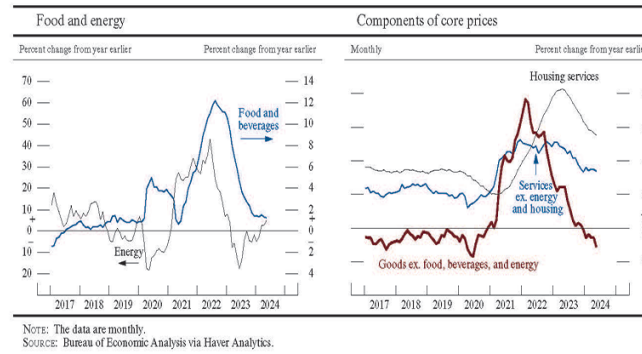
2. Core personal consumption expenditures price index



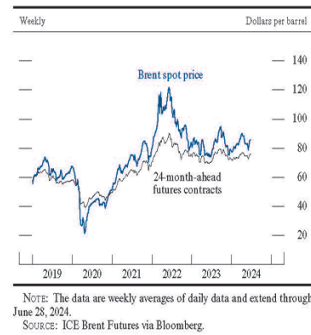
SOURCE: Bureau of Economic Analysis, personal consumption expenditures via Haver Analytics.

6 PART 1: RECENT ECONOMIC AND FINANCIAL DEVELOPMENTS

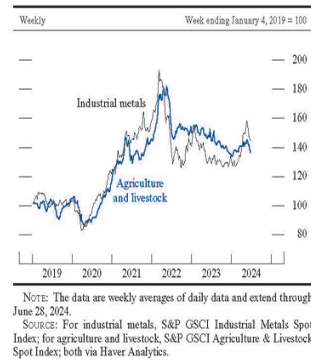
3. Subcomponents of personal consumption expenditures price indexes



4. Spot and futures prices for crude oil



5. Spot prices for commodities



(figure 3, left panel). Oil prices increased, on net, in the first half of this year (figure 4). Prices rose amid concerns about escalation of the conflict in the Middle East, additional costs of rerouting some oil shipping away from the Red Sea, and ongoing production cuts by OPEC (Organization of the Petroleum Exporting Countries) and its allies. Continuing geopolitical tensions, including tensions emanating from the conflicts in the Middle East and Ukraine, pose an upside risk to energy prices.

Prices of agricultural commodities and livestock edged up, on net, over the first half of this year after having come down markedly in 2022 and 2023 from the highs reached at the start of Russia's war on Ukraine in early 2022 (figure 5). As a result of these movements, the 12-month change in PCE food prices slowed substantially from its peak of 12.2 percent in August 2022 to just 1.2 percent in May (as shown in figure 3, left panel).

Prices of both energy and food products are of particular importance for lower-income households, for which such necessities account for a large share of expenditures. Reflecting the sharp increases seen in 2021 and 2022, these price indexes are 25 percent and 32 percent higher than in 2019, for food and energy, respectively.

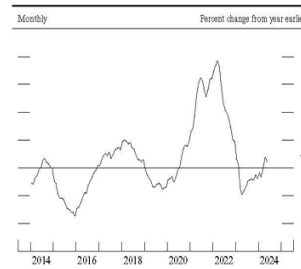
Core goods prices increased modestly this year after having declined sharply in the second half of 2023

In assessing the outlook for inflation, it is helpful to consider three separate components of core prices: core goods, housing services, and core nonhousing services. After posting notable declines in the second half of last year, core goods prices increased modestly, on net, over the first months of this year. This development likely reflects, in part, movements in nonfuel import prices, which turned up in recent months after having declined, on net, over 2023 (figure 6). Smoothing through these monthly movements, prices for core goods over the 12 months ending in May moved down 1.1 percent, similar to their pre-pandemic rate of decline, after having increased 2.5 percent over the previous 12-month period (figure 3, right panel). The progress on inflation for core goods reflects improvements in supply-demand imbalances. Indeed, the supply chain issues and other capacity constraints that had earlier boosted inflation so much continued to ease, though at a more gradual pace this year than over the past two years, and supply-demand conditions in goods markets appear to be relatively balanced. For example, the shares of respondents to the Quarterly Survey of Plant Capacity Utilization citing insufficient supply of labor or materials as reasons for producing below capacity, which had increased considerably during the pandemic, have continued to fall and are now near pre-pandemic levels (figure 7).

Housing services price inflation continued to slow gradually but remains elevated . . .

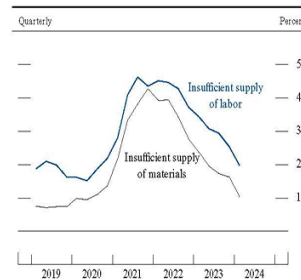
The 12-month change in housing services prices moved down from more than 8 percent in May 2023 to 5.5 percent in May of this year but is still well above its pre-pandemic level (as shown in figure 3, right panel). Market rent inflation, which measures increases in rents for new housing leases to new tenants, has fallen markedly since late 2022 to near pre-pandemic rates, and this slowdown points to continued easing of housing services inflation over the

6. Nonfuel import price index



SOURCE: Bureau of Labor Statistics via Haver Analytics.

7. Reasons for operating below full capacity



NOTE: The series are the share of firms selecting each reason for operating below full capacity.

SOURCE: U.S. Census Bureau: Quarterly Survey of Plant Capacity Utilization.

year ahead. (The box “Housing Services Inflation and Market Rent Measures” provides further details.)

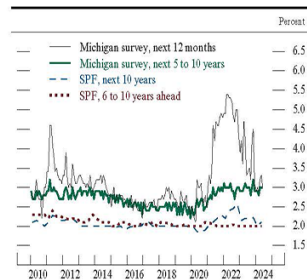
... while core nonhousing services price inflation flattened out so far this year

Finally, price inflation for core nonhousing services—a broad group that includes services such as travel and dining, financial services, and car repair—slowed last year but flattened out, on net, in the first five months of this year. Core nonhousing services prices rose 3.4 percent in the 12 months ending in May, down from 4.7 percent a year ago but little changed since the end of last year (as shown in figure 3, right panel). The lack of further progress this year is due in large part to price increases in volatile categories—for example, portfolio management services, which can be influenced by idiosyncratic factors, such as swings in the stock market, more than supply and demand conditions. Because labor is a significant input to these service sectors, the ongoing deceleration in labor costs—supported by softening labor demand and improvements in labor supply—suggests that disinflation will eventually resume for this category.

Measures of longer-term inflation expectations have been stable; shorter-term expectations have been volatile but are generally lower than a year earlier

The generally held view among economists and policymakers is that inflation expectations influence actual inflation by affecting wage- and price-setting decisions. Survey-based measures of expected inflation over a longer horizon have generally been moving sideways over the past year, within the range seen during the decade before the pandemic, and they appear broadly consistent with the FOMC’s longer-run 2 percent inflation objective. This development is seen for surveys of households, such as the University of Michigan Surveys of Consumers, and for surveys of professional forecasters (figure 8). For example, the median forecaster in the Survey of Professional

8. Measures of inflation expectations



NOTE: The data for the Michigan survey are monthly and extend through June 2024. The Survey of Professional Forecasters (SPF) data are quarterly and extend through 2024:Q2.

SOURCE: University of Michigan Surveys of Consumers; Federal Reserve Bank of Philadelphia, SPF.

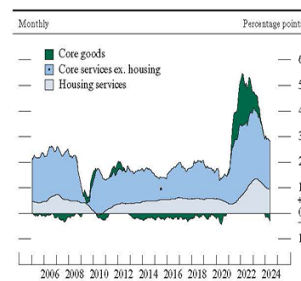
Housing Services Inflation and Market Rent Measures

The price index for housing services includes rents explicitly paid by renters as well as implicit rents that homeowners would have to pay if they were renting their homes known as owners' equivalent rent (OER). This index is an important component of the price index for personal consumption expenditures (PCE), composing about 15.5 percent of the total PCE price index. Housing services prices started accelerating in 2021, and, as figure A illustrates, the contribution of these prices to the 12-month change in the core PCE price index increased notably, reaching a peak of 1.4 percentage points in 2023. In May 2024, the contribution of this component stood at 1.0 percentage point, down from its peak but still well above the 0.5 percentage point that was typical before the COVID-19 pandemic.

The PCE price index for housing services is derived from two components of the consumer price index (CPI): rent of primary residence and OER.¹ The rent of primary residence index measures the average rent paid by tenants. OER estimates the rent that homeowners would pay if they were renting their homes without furnishings or utilities and is derived from rental data for units in the same neighborhood, with an adjustment for structure type.²

Because the price index for housing services measures average rent for all tenants—both new tenants and existing tenants—its changes are more subdued and tend to lag changes in rent measures for new leases, described later. Because rental agreements typically last for 12 months, most renters will not see an immediate increase in their rent even if the rent for new leases increases sharply. Additionally, the Bureau of Labor Statistics, the agency responsible for computing the CPI, reports that when rent increases occur for

A. Contributions to 12-month change in core personal consumption expenditures price index



SOURCE: Bureau of Economic Analysis via Haver Analytics; Federal Reserve Board staff calculations.

units, they are typically smaller for continuing tenants renewing their lease than they are for new tenants.³

This lag implies that measures of rent growth for new leases can help predict future changes in the PCE price index for housing services. Over the past few decades, private firms have started publishing various “market rent” measures that track the average rent for new leases by new tenants.⁴ For example, the

(continued on next page)

1. The sum of the weights of these two components in the total CPI is 34.4 percent, considerably higher than their weight in the total PCE price index.

2. The typical structure type varies significantly across owner- and tenant-occupied units: Owner-occupied homes are mostly single-family units, while renter-occupied homes are roughly evenly divided between single-family and multifamily units. Constructing the OER measure involves reweighting the sample of rent quotes for a given area to reflect the relative importance of owner-occupied housing in that area. See slide 13 of Robert Cane (2019), “Measurement of Owner Occupied Housing in the U.S. Consumer Price Index” (Washington: Bureau of Labor Statistics, November 15), https://www.bea.gov/system/files/2019-11/bea_tac_nov2019_cane.pdf.

3. See Ben Houck (2022), “Housing Leases in the U.S. Rental Market,” *Spotlight on Statistics* (Washington: Bureau of Labor Statistics, September), <https://www.bls.gov/spotlight/2022/housing-leases-in-the-u-s-rental-market/home.htm>.

4. PCE prices for housing services differ from these market rent measures for reasons beyond the fact that market rent measures are limited to new leases to new tenants. In addition, the discrepancy arises from the methodology used for index construction (for example, the rent measures used in the PCE price index sample a given residence only once every six months), the representativeness of the sample, and the way in which the measure controls for quality adjustments. Moreover, market rent measures capture the “asking” prices posted by landlords, while the rent measures used in the PCE price index gauge the rent that tenants actually pay. Among these factors, whether all leases are used (as opposed to only new leases) appears to be the main contributor to this discrepancy. See Brian Adams, Lara Loewenstein, Hugh Montag, and Randal Verbrugge (2024), “Disentangling Rent Index Differences: Data, Methods, and Scope,” *American Economic Review: Insights*, vol. 6 (June), pp. 230–45.

Housing Services Inflation *(continued)*

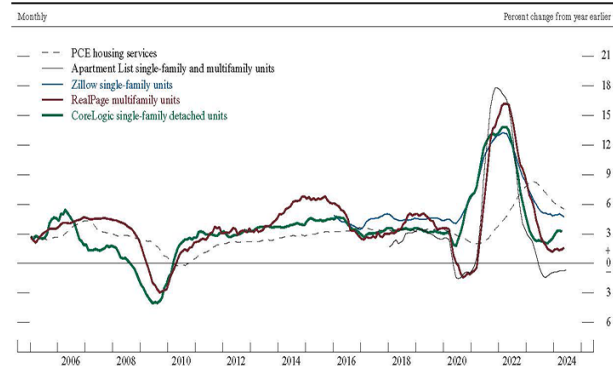
CoreLogic Single-Family Rent Index measures changes in average market rents for single-family homes. Other measures include the Zillow, Apartment List, and RealPage indexes, which vary in terms of the type of unit they cover (single-family versus multifamily), their methodologies, and the representativeness of the national rental market.⁵

5. The Zillow Observed Rent Index for single-family residences, available beginning in 2015, focuses on changes in asking rents for single-family units. The RealPage Rent Index, available beginning in 1996, measures changes in average market rents across professionally managed

multifamily apartment buildings. The Apartment List National Rent Index, available beginning in 2017, measures changes in median market rents across the entire rental market for both single-family and multifamily units. To calculate unit-level rent growth, all these measures, including the CoreLogic index, use the repeat-rent methodology to control for differences in property characteristics among the units listed for rent in different periods.

(continued)

B. Housing rents



NOTE: CoreLogic data extend through April 2024, Zillow data start in January 2016, and Apartment List data start in January 2018 and extend through June 2024. Zillow, CoreLogic, Apartment List, and RealPage measure market-rate rents—that is, rents for a new lease by a new tenant. PCE is personal consumption expenditures.

SOURCE: Bureau of Economic Analysis, PCE, via Haver Analytics; CoreLogic, Inc.; Zillow, Inc.; Apartment List, Inc. via Haver Analytics; RealPage, Inc.; Federal Reserve Board staff calculations.

services prices, with the market rent measure typically leading the PCE measure by one year.⁶ This relationship is particularly evident in the periods following the Great Recession and the COVID-19 pandemic. For example, PCE housing services inflation reached a peak of 8.3 percent in April 2023, exactly one year after the 12-month change for the CoreLogic index reached its peak of 13.8 percent.

Since mid-2022, each of these measures of market rents has decelerated and returned to a growth rate similar to or below its average pre-pandemic pace.⁷ While the PCE price index for housing services also began decelerating in mid-2023, its current rate of increase remains well above the average rate seen in the years before the pandemic. As noted earlier, changes in the PCE price index for housing services tend to lag changes in market rents because rental

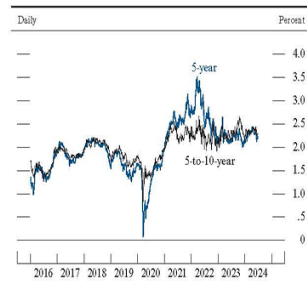
contracts typically last for a year and rents for existing tenants take some time to catch up to the rents charged to new tenants. In particular, the rise in measures of market rents, including the CoreLogic Single-Family Rent Index and the Zillow Observed Rent Index, from the onset of the pandemic until now has been larger than the corresponding increase in the PCE price index for housing services, suggesting that the PCE price measure has not yet fully caught up with the current state of the rental market.⁸ However, as long as market rents continue to increase moderately, PCE housing services inflation should gradually decline and eventually return to its pre-pandemic pace as well. However, significant uncertainty remains regarding the timing of this decline and whether market rent inflation will, in fact, remain moderate.

6. Several studies use market rent measures to predict housing services inflation. See, for instance, Marijn A. Bolhuis, Judd N.L. Cramer, and Lawrence H. Summers (2022), "The Coming Rise in Residential Inflation," *Review of Finance*, vol. 26 (September), pp. 1051–72; and Kevin J. Lansing, Luiz E. Oliveira, and Adam Hale Shapiro (2022), "Will Rising Rents Push Up Future Inflation?" FRBSF Economic Letter 2022-03 (San Francisco: Federal Reserve Bank of San Francisco, February), <https://www.frbf.org/wp-content/uploads/sites/4/el2022-03.pdf>.

7. In addition, the Bureau of Labor Statistics has recently started publishing a quarterly rent index for new tenants (the New Tenant Rent Index). While the New Tenant Rent Index is subject to revision with each release, the year-over-year growth of this index declined from its peak of 12.9 percent in the second quarter of 2022 to 0.4 percent in the first quarter of 2024, the lowest reading since the second quarter of 2010. See Bureau of Labor Statistics (n.d.), "New Tenant Rent Index," webpage, <https://www.bls.gov/pir/new-tenant-rent.htm>.

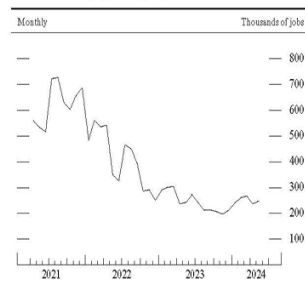
8. Between January 2020 and April 2024, the CoreLogic Single-Family Rent Index and the Zillow Observed Rent Index have increased 32 percent and 38 percent, respectively, while PCE prices for housing services have increased 23 percent. See Christopher D. Cotton (2024), "A Faster Convergence of Shelter Prices and Market Rent: Implications for Inflation," Current Policy Perspectives 2024-4 (Boston: Federal Reserve Bank of Boston, June), <https://www.bostonfed.org/-/media/Documents/Workingpapers/PDF/2024/cpp20240617.pdf>.

9. Inflation compensation implied by Treasury Inflation-Protected Securities



NOTE: The data are at a business-day frequency and are estimated from smoothed nominal and inflation-indexed Treasury yield curves.
SOURCE: Federal Reserve Bank of New York; Federal Reserve Board staff calculations.

10. Nonfarm payroll employment



NOTE: The data shown are a 3-month moving average of the change in nonfarm payroll employment.
SOURCE: Bureau of Labor Statistics via Haver Analytics.

Forecasters, conducted by the Federal Reserve Bank of Philadelphia, continued to expect PCE price inflation to average 2 percent over the five years beginning five years from now.

Inflation expectations over a shorter horizon—which tend to follow observed inflation more closely and tend to be more volatile—have moved down, on net, since the middle of 2022 to near the range seen during the decade before the pandemic. In recent months, the median value for inflation expectations over the next year as measured in the Michigan survey has been generally lower than readings from a year earlier. Similarly, expected inflation for the next year as measured in the Survey of Consumer Expectations, conducted by the Federal Reserve Bank of New York, has also declined, on average, from a year earlier.

Market-based measures of longer-term inflation compensation, which are based on financial instruments linked to inflation such as Treasury Inflation-Protected Securities, are also broadly in line with readings seen in the years before the pandemic and consistent with PCE inflation returning to 2 percent. These measures have been little changed, on net, since the beginning of the year (figure 9).

The labor market remains strong

Payroll employment gains have been strong, averaging 248,000 per month over the first five months of the year. Job gains slowed from the first half to the second half of last year but appear to have picked up, on net, so far this year (figure 10). Recent job gains have been broad based, with over 60 percent of industries expanding their employment, on net, over the three months ending in May. That said, gains have been particularly strong in health care and in state and local governments, where employment remains below the levels implied by pre-pandemic trends.²

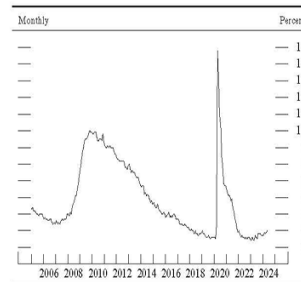
2. Administrative data from the Quarterly Census of Employment and Wages (QCEW) suggest that job growth last year was solid, but not as strong as reported in the Current Employment Statistics (CES). The CES

The unemployment rate has edged up since the middle of 2023 but was still at a historically low level of 4.0 percent in May. Through May, the unemployment rate has remained at or below 4 percent for over two years (figure 11). Unemployment rates among most age, educational attainment, sex, and ethnic and racial groups remain near their respective historical lows (figure 12).

Labor demand has been gradually cooling . . .

Demand for labor remained strong in the first half of 2024 but has continued to cool gradually, on net, from its very elevated levels of early 2022. Job openings, as measured in the Job Openings and Labor Turnover Survey (JOLTS), have continued to fall from their all-time high recorded in March 2022 but are

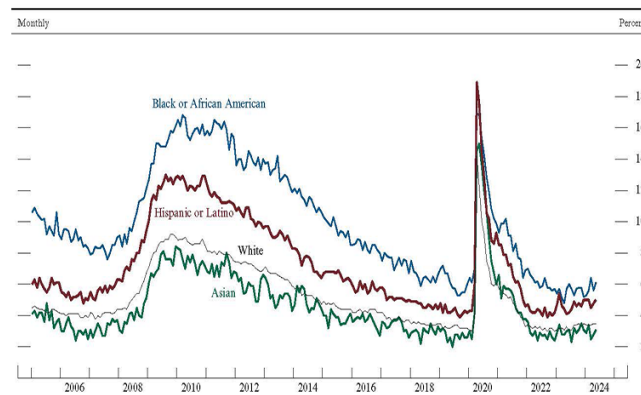
11. Civilian unemployment rate



SOURCE: Bureau of Labor Statistics via Haver Analytics.

payroll data will be revised in early 2025, when the Bureau of Labor Statistics benchmarks these data to employment counts from the QCEW as part of its annual benchmarking process.

12. Unemployment rate, by race and ethnicity



NOTE: Unemployment rate measures total unemployed as a percentage of the labor force. Persons whose ethnicity is identified as Hispanic or Latino may be of any race. Small sample sizes preclude reliable estimates for Native Americans and other groups for which monthly data are not reported by the Bureau of Labor Statistics.

SOURCE: Bureau of Labor Statistics via Haver Analytics.

still slightly above pre-pandemic levels.³ An alternative measure of job vacancies using job postings data from the large online job board Indeed also shows that while vacancies have proceeded to move gradually lower through the first half of 2024, they have remained above pre-pandemic levels.⁴ Consistent with the decline in job vacancies, the National Federation of Independent Business (NFIB) survey indicated that on net, in May, fewer firms planned to add workers over the next three months than was the case at the end of 2023; firms' hiring plans reported in the NFIB survey have been trending down since the middle of 2021.

The cooling in labor demand has been mostly due to reductions in firm hiring, as indicators of layoffs, such as initial claims for unemployment insurance and the rate of layoffs and discharges in the JOLTS report, have remained at historically low levels.

. . . and labor supply has increased further . . .

Meanwhile, the supply of labor has continued to increase on net. While labor force participation has leveled off over the past year, the U.S. population increased strongly because of high levels of immigration.

The labor force participation rate (LFPR)—which measures the share of people either working or actively seeking work—increased solidly from the beginning of 2021 through the middle of 2023 but appears to have

3. Some analysts have noted that the vacancy-posting behavior of firms may have changed since 2019 in ways that lift the number of vacancies. For example, multi-establishment firms may be posting vacancies for a single job opening at several or all of its establishments if the new job allows workers to work remotely from any establishment. These multiple job postings may result in overcounting of job vacancies in establishment-level measures, such as those from JOLTS and Indeed. Alternatively, after having experienced an exceptionally strong labor market in 2022, firms may now be more willing to post vacancies for positions that they are unlikely to fill immediately.

4. Indeed job postings data are available on the company's Hiring Lab portal at <https://data.indeed.com/#/postings>.

flattened out at a relatively high level since then. The LFPR was 62.5 percent in May, a touch below its average level over the past 12 months (figure 13). Notably, the post-pandemic recovery in the LFPR has differed widely across demographic groups, with the participation rate for women aged 25 to 54 reaching all-time highs in recent months and the participation rate for individuals older than 55 exhibiting no signs of recovery. (The box “Employment and Earnings across Demographic Groups” provides further details.)

Labor supply has also been boosted in recent years by relatively strong population growth due to a notable expansion in immigration. Though official estimates by the Census Bureau show a robust increase in population growth in 2022 and 2023, recent estimates by the Congressional Budget Office indicate that actual population growth may have been considerably higher. The most recent data suggest that immigration is somewhat slower than the strong rates seen late last year.⁵

... resulting in a normalization of labor market conditions

With cooling labor demand and rising labor supply, the labor market became gradually less tight over the first half of this year, although it nevertheless remains strong. The balance between demand and supply in the labor market appears similar to that during the period immediately before the pandemic.

5. A recent report from the Congressional Budget Office (CBO) estimates that immigration in 2022 and 2023 was considerably higher than in the Census Bureau's estimates. See Congressional Budget Office (2024), *The Demographic Outlook: 2024 to 2054* (Washington: CBO, January), <https://www.cbo.gov/publication/59697>. Recent studies have put more weight on the CBO estimates, in part because the Census Bureau is using lagged estimates of immigration from the American Community Survey, while the CBO is using more recent, high-frequency data. See Wendy Edelberg and Tara Watson (2024), “New Immigration Estimates Help Make Sense of the Pace of Employment,” Hamilton Project (Washington: Brookings Institution, March), https://www.brookings.edu/wp-content/uploads/2024/03/20240307_Immigration_Employment_Paper.pdf.

13. Labor force participation rate



NOTE: Data are monthly, and values before January 2024 are estimated by Federal Reserve Board staff in order to eliminate discontinuities in the published history.

SOURCE: Bureau of Labor Statistics via Haver Analytics.

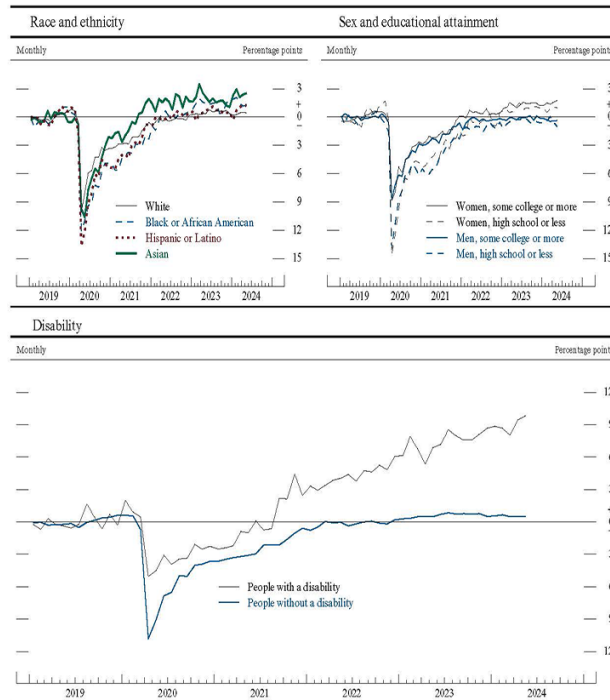
Employment and Earnings across Demographic Groups

At the aggregate level, solid labor demand and improved labor supply, together with ongoing gains in productivity and falling inflation, have resulted in high rates of employment and rising real wages over the past year. This solid labor market performance has been broadly shared and has been especially beneficial for historically disadvantaged groups of workers. As a result, many of the long-standing disparities in employment and wages by sex, race, ethnicity, and education have narrowed, and some gaps reached historical lows in 2023 and the first half of 2024. However, despite this narrowing, significant disparities in absolute levels across groups remain.

Among prime-age people (aged 25 to 54), the employment-to-population (EPOP) ratio for Black or African American workers remained near its historical peak in the first half of 2024, and the gap in the EPOP ratio between prime-age Black and white workers fell to its lowest point in almost 50 years. Similarly, prime-age Hispanic or Latino workers' EPOP ratio has increased notably over the first part of 2024 and is now more than 1 percentage point above its 2019 level (figure A, top-left panel). That improvement has further reduced the EPOP ratio gap between Hispanic or Latino workers and white workers from already

(continued)

A. Prime-age employment-to-population ratios compared with the 2019 average ratio, by group



NOTE: Prime age is 25 to 54. All series are seasonally adjusted by the Federal Reserve Board staff.
SOURCE: Bureau of Labor Statistics; U.S. Census Bureau, Current Population Survey; Federal Reserve Board staff calculations.

historically low levels. Although the EPOP ratio for prime-age Asian workers has moved somewhat lower over the past year, it remains historically high and above its 2019 level.¹

The EPOP ratio for prime-age women has continued to increase steadily, reaching another record high in the first few months of 2024, whereas the EPOP ratio for prime-age men has been mostly flat over the past year, near its level in the year before the pandemic (figure A, top-right panel). As a result, the EPOP ratio gap between prime-age men and women fell to a record low this year. The increase in the female EPOP ratio relative to the pre-pandemic period is (almost) entirely attributable to rising labor force participation, which had also been increasing briskly before the pandemic, consistent with a growing share of women with a college degree.² Other factors, including strong labor market conditions and greater availability of remote-work options, may have also contributed to rising prime-age female labor force participation.³

Among prime-age persons with a disability, the EPOP ratio has surged well above its 2019 level during the past few years (figure A, bottom panel). Some of this increase is likely due to the unique labor market circumstances of the past few years. With tight labor market conditions, employers may have been relatively more likely to hire persons with a disability than in other times. Additionally, the rise of remote work may have enabled persons with a disability to work without the challenges of on-site work. However, some of the increase could stem from a change in the composition of this group, as the number of persons with a disability rose following the pandemic, which may have raised

B. Employment-to-population ratios relative to 2019 average, by age



NOTE: Data before January 2023 are estimated by Federal Reserve Board staff in order to eliminate discontinuities in the published history.
SOURCE: Bureau of Labor Statistics; U.S. Census Bureau, Current Population Survey; Federal Reserve Board staff calculations.

the average employment rate for this group.⁴ For persons without a disability, the EPOP ratio is little changed from its 2019 level.

Although most groups have shown robust employment gains over the past few years, the EPOP ratio for people aged 55 or older remains approximately 2 percentage points below its 2019 level and has changed little since late 2021 (figure B). This shortfall is attributable to a persistent increase in the rate of retirement among this group. Most of the increase in retirement relative to 2019 is due to the continued aging of the baby-boom generation, a trend that was expected to have occurred even without the pandemic.⁵ However, retirements have also been

(continued on next page)

1. As monthly series have greater sampling variability for smaller groups, we do not plot EPOP ratio estimates for American Indians or Alaska Natives.

2. For a discussion of the contribution of educational attainment to prime-age female labor force participation before the pandemic, see Didem Tüzemen and Thao Tran (2019), “The Uneven Recovery in Prime-Age Labor Force Participation,” Federal Reserve Bank of Kansas City, *Economic Review*, vol. 104 (Third Quarter), pp. 21–41, <https://www.kansascityfed.org/Economic%20Review/documents/652/2019-The%20Uneven%20Recovery%20in%20Prime-Age%20Labor%20Force%20Participation.pdf>.

3. For a discussion on access to remote work and participation rates, see Maria D. Tito (2024), “Does the Ability to Work Remotely Alter Labor Force Attachment? An Analysis of Female Labor Force Participation,” FEDS Notes (Washington: Board of Governors of the Federal Reserve System, January 19), <https://doi.org/10.17016/2380-7172.3433>.

4. The increase in the number of persons with a disability may be linked to cases of long COVID, which, while debilitating, might not limit work as much as other types of disabilities. As a result, an influx of relatively higher-employment individuals into the disabled category could have raised employment rates for this group even if no individual’s employment changed.

5. For example, as baby boomers have continued to age, the median age of the population aged 55 or older increased from 66 in 2019 to 67 in the first half of 2024, and the median age of that group is expected to continue increasing into the future. This shift in the composition of the 55-or-older population has naturally lowered the observed EPOP ratio for this group nearly 0.5 percentage point per year, as EPOP ratios are lower at older ages.

Employment and Earnings *(continued)*

elevated above the level expected from aging alone, mostly for individuals aged 65 or older.⁶

While employment disparities across many demographic groups are now within historically narrow ranges, substantial gender, racial, and ethnic gaps remain, underscoring long-standing structural factors. Currently, prime-age women are employed at a rate 10 percentage points less than men, while prime-age Black and Hispanic workers are employed at a rate 3 to 4 percentage points less than white workers.

Similar to employment, a continued strong labor market has supported strong nominal wage growth, and as inflation has come down, that strong nominal wage growth has translated into higher real wage growth. Real wage growth has been comparatively robust for historically disadvantaged groups. As shown in the top-left panel of figure C, real wage growth—as measured

by the Federal Reserve Bank of Atlanta's Wage Growth Tracker and deflated by the personal consumption expenditures price index—was consistently stronger for workers in lower wage quartiles compared with the top quartiles during the pandemic and early recovery, but now all quartiles are experiencing similar growth.⁷

Strong wage growth across the income distribution is reflected in the experiences of different demographic groups. Wage growth for nonwhite workers has been a bit stronger than that for white workers for much of the past year (figure C, top-right panel). Wages for women and men have grown essentially in tandem over the past year (figure C, bottom-left panel).⁸ Real wage growth for workers with a high school diploma or less remains strong and has been rising a bit faster than for workers with more education, on average, over the past few years (figure C, bottom-right panel).

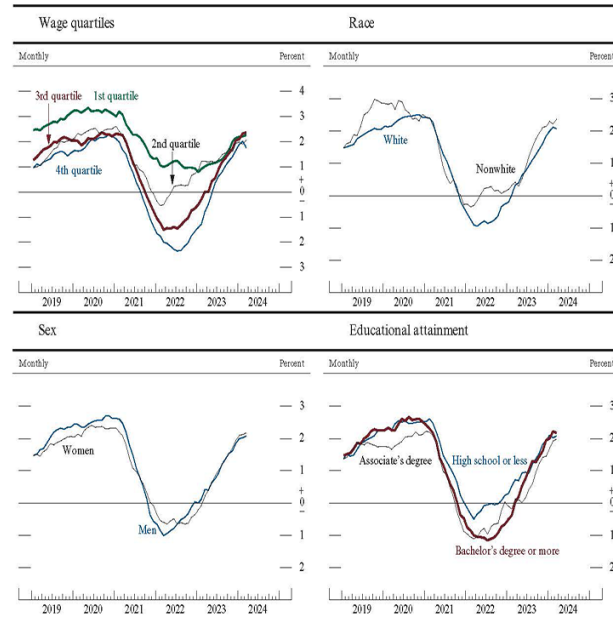
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6. For an analysis on the increase in retirements following the pandemic, see Joshua Montes, Christopher Smith, and Juliana Dajon (2022), “The Great Retirement Boom: The Pandemic-Era Surge in Retirements and Implications for Future Labor Force Participation,” Finance and Economics Discussion Series 2022-081 (Washington: Board of Governors of the Federal Reserve System, November), <https://doi.org/10.17016/FEDS.2022.081>.

7. To reduce noise due to sampling variation, which can be pronounced when considering disaggregated groups' wage changes, the series shown in figure C are the 12-month moving averages of the groups' median 12-month real wage changes. Thus, by construction, these series lag the actual real wage changes. Wage data extend through March 2024 only to avoid complications stemming from changes in the underlying data source.

8. The measure of real wage growth shown in the figure uses the same price index for all groups, but inflation experiences can differ across demographic groups because of differences in what they purchase or where they shop. See Jacob Orchard (2021), “Cyclical Demand Shifts and Cost of Living Inequality,” working paper, February (revised September 2022).

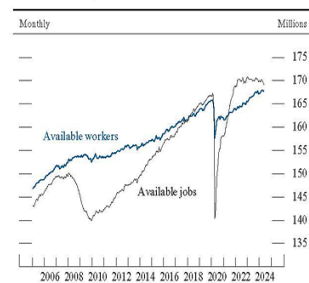
C. Median real wage growth, by group



NOTE: The data extend through March 2024. Series show 12-month moving averages of the median percent change in the hourly wage of individuals observed 12 months apart, deflated by the 12-month moving average of the 12-month percent change in the personal consumption expenditures price index. In the top-left panel, workers are assigned to wage quartiles based on the average of their wage reports in both Current Population Survey outgoing rotation group interviews; workers in the lowest 25 percent of the average wage distribution are assigned to the 1st quartile, and those in the top 25 percent are assigned to the 4th quartile.

SOURCE: Federal Reserve Bank of Atlanta, Wage Growth Tracker; Bureau of Labor Statistics; U.S. Census Bureau, Current Population Survey.

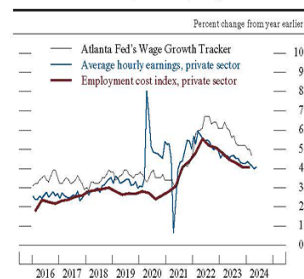
14. Available jobs versus available workers



NOTE: Available jobs are employment plus job openings as of the end of the previous month. Available workers are the labor force. Data for employment and labor force before January 2024 are estimated by Federal Reserve Board staff in order to eliminate discontinuities in the published history.

SOURCE: Bureau of Labor Statistics via Haver Analytics; U.S. Census Bureau; Federal Reserve Board staff calculations.

15. Measures of change in hourly compensation



NOTE: For the private-sector employment cost index, change is over the 12 months ending in the last month of each quarter; for private-sector average hourly earnings, the data are 12-month percent changes; for the Atlanta Fed's Wage Growth Tracker, the data are shown as a 3-month moving average of the 12-month percent change and extend through March 2024.

SOURCE: Bureau of Labor Statistics; Federal Reserve Bank of Atlanta, Wage Growth Tracker; all via Haver Analytics.

A variety of labor market indicators support this assessment. The ratio of job openings to unemployment has fallen notably from its peak of about 2.0 in spring 2022 to 1.2 in May, the same as its average in 2019. Similarly, the gap between the number of total available jobs (measured by employed workers plus job openings) and the number of available workers (measured by the size of the labor force) has also moved down markedly from its peak of 6.1 million in spring 2022 to 1.4 million in May and is only a bit above its 2019 average of 1.2 million (figure 14). The unemployment rate has continued to edge up this year and reached 4.0 percent in May, modestly higher than in 2019. In addition, the percentage of workers quitting their jobs each month, an indicator of the availability of attractive job prospects, has continued to move down this year and, though still elevated, is now modestly below its pre-pandemic level. Similarly, the share of respondents to the Conference Board Consumer Confidence Survey reporting that jobs are plentiful has continued to move down and is somewhat lower than its level in 2019. Furthermore, the NFIB survey indicates that firms' perceptions of labor market tightness have come down from their recent peaks and returned to their pre-pandemic range. Finally, business contacts surveyed for the Federal Reserve's May 2024 Beige Book reported signs of a cooling labor market—including easing in hiring plans, better labor availability, and modest wage growth—and, similar to 2019, cited some difficulty finding workers in selected industries or areas.⁶

Wage growth remains elevated but has slowed

Consistent with the easing in labor market tightness, nominal wage growth continued to slow so far this year, though it remains above its pre-pandemic pace and likely too high, given productivity trends, to be consistent with 2 percent inflation over time (figure 15). Total hourly compensation, as measured by the

6. See the May 2024 Beige Book, available on the Board's website at <https://www.federalreserve.gov/monetarypolicy/beigebook202405.htm>.

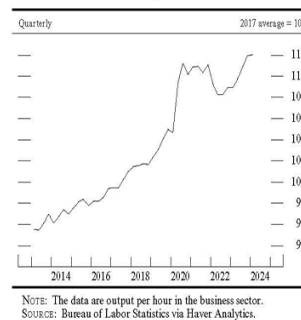
employment cost index, increased 4.1 percent over the 12 months ending in March, a noticeable slowing from the peak increase of 5.5 percent in mid-2022. Other aggregate measures of labor compensation, such as average hourly earnings (a less comprehensive measure of compensation) and the Federal Reserve Bank of Atlanta's Wage Growth Tracker (which reports the median 12-month wage growth of individuals responding to the Current Population Survey), have also continued to slow from their recent peaks in 2022 but remain well above their pre-pandemic growth rates. Wage growth has not normalized to the same extent as the measures of labor market tightness cited earlier, suggesting that there is some persistence in the adjustment process to past shocks. With PCE prices having risen 2.6 percent over the 12 months through May, these nominal wage measures suggest that most workers saw increases in the purchasing power of their wages over the past year.

Labor productivity has increased at a moderate pace with significant volatility

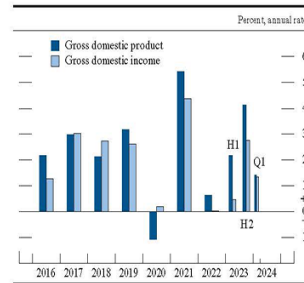
The extent to which nominal wage gains raise firms' costs and act as a source of inflation pressure depends importantly on the pace of productivity growth. Labor productivity in the business sector—the ratio of output to hours worked—has been extremely volatile since the pandemic began. It increased sharply in 2020, moved roughly sideways in 2021, declined strongly in 2022, and then rebounded solidly in 2023 (figure 16). Averaging through these large swings, business-sector productivity has increased at a moderate annual average rate of 1½ percent since the onset of the pandemic, in line with the average rate of growth observed during the previous business cycle (from the fourth quarter of 2007 to the fourth quarter of 2019).

The pace of future productivity growth is highly uncertain. It is possible that productivity growth could remain at around its current moderate pace. However, it is also possible that the rapid adoption of new technologies like artificial intelligence (AI)

16. U.S. labor productivity



17. Change in real gross domestic product and gross domestic income



NOTE: The key identifies bars in order from left to right.
SOURCE: Bureau of Economic Analysis via Haver Analytics.

and robotics, as well as the high rate of new business formation brought about by the pandemic, could boost productivity growth above that pace in coming years.

Growth in gross domestic product moderated in the first quarter, but private domestic demand remained solid

After expanding at a robust pace in the second half of last year despite restrictive financial conditions, real gross domestic product (GDP) decelerated to a moderate annual growth rate of 1.4 percent in the first quarter of this year (figure 17). The step-down was due in large part to sizable drags from net exports and inventory investment; these categories of expenditures tend to be volatile even in normal times and have been even more so since the pandemic. Growth in private domestic final purchases—that is, consumer spending, business fixed investment, and residential investment—also moderated in the first quarter but remained solid.⁷ Among these components of GDP, consumer spending rose strongly in the second half of last year and decelerated in the first quarter as goods spending declined while services spending continued to rise solidly. Business fixed investment increased at a moderate pace in the first quarter as a result of strength in nontransportation equipment spending and intellectual property investment, while nonresidential structures slowed after surging in 2023. Residential investment grew rapidly in the first quarter, reflecting, for the most part, increases in existing home sales and construction of single-family homes.

7. Real gross domestic income (GDI) has been notably weaker than GDP in recent years; both series measure the same economic concept, and any difference between the two figures reflects measurement error in one or both series. GDI is reported to have increased at a pace only slightly slower than GDP in the first quarter but had risen notably less than GDP over the previous three years. As a result, productivity calculated from the income side of the national accounts would be considerably weaker than the published figures over the past three years.

After having returned to pre-pandemic levels in late 2021, manufacturing output has been little changed, on net, since then. While motor vehicle production has continued to rebound from earlier disruptions, factory production outside of motor vehicles has drifted down somewhat. The diffusion indexes of new orders from various national and regional surveys of manufacturers remained mostly soft in June, suggesting continued modest weakness in coming months.

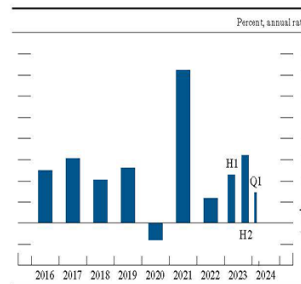
Consumer spending growth has been resilient but eased this year

Consumer spending adjusted for inflation grew at a solid rate of 2.7 percent in 2023 but slowed in the first quarter to a moderate 1.5 percent pace (figure 18). The resilience in consumer spending last year in the face of high interest rates likely reflected strong job gains and rising real wages. Indeed, real disposable personal income increased at a robust 3.8 percent rate in 2023. In addition, last year's spending was bolstered by households drawing down their liquid assets, such as checking accounts, and relying more on credit.

More recently, the easing in consumer spending growth in the first quarter was accompanied by a softening in some household spending fundamentals along with somewhat restrictive financial conditions. Disposable personal income growth moderated in the first quarter after a robust pace last year. While household finances appear healthy in the aggregate, credit card and auto loan delinquencies continued to rise in the first quarter, suggesting that a growing share of households are experiencing some financial stress.

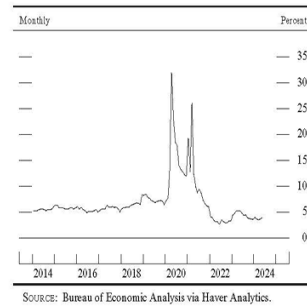
Despite the recent easing in consumer spending growth, households continue to spend more of their income than is typical. The saving rate—the difference between current income and spending, as a share of income—was 3.8 percent in the first quarter and has been well below its pre-pandemic average of over 6 percent for nine consecutive

18. Change in real personal consumption expenditures

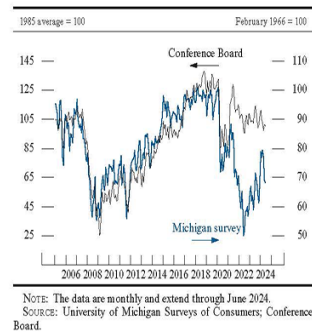


SOURCE: Bureau of Economic Analysis via Haver Analytics.

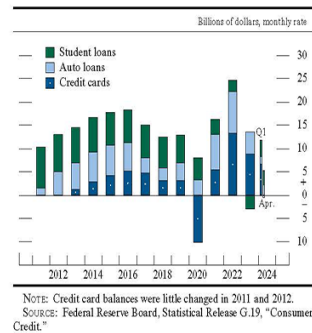
19. Personal saving rate



20. Indexes of consumer sentiment



21. Consumer credit flows



quarters (figure 19). This low saving rate likely reflects in large part the effects of high wealth and still-strong balance sheets of higher-income households.

Consumer spending since the pandemic has been more robust than measures of consumer sentiment would suggest. The indexes of consumer sentiment published by both the University of Michigan and the Conference Board remain well below their pre-pandemic levels. Although the Michigan survey index has improved markedly since spring 2022, it is further below its pre-pandemic level than the Conference Board index, which puts more weight on labor market conditions (figure 20).

Consumer financing conditions remain somewhat restrictive

Consumer financing conditions have been somewhat restrictive, reflecting high borrowing costs and tight bank lending standards. Interest rates for consumer credit products such as new credit cards and auto loans edged down in recent months but remained elevated. In the April Senior Loan Officer Opinion Survey on Bank Lending Practices (SLOOS), conducted by the Federal Reserve Board, banks reported continued tightening of lending standards for consumer loans in the first quarter, likely reflecting increases in delinquency rates. Indeed, credit card and auto loan delinquency rates—measured as the fraction of balances that are at least 30 days past due—have increased from their 2021 lows and are above the levels observed just before the pandemic.

Even so, financing has been generally available to support consumer spending. Consumer credit expanded moderately, on net, during the first four months of the year, driven by still-solid growth in credit card balances and modest growth in auto loans and student loans (figure 21).

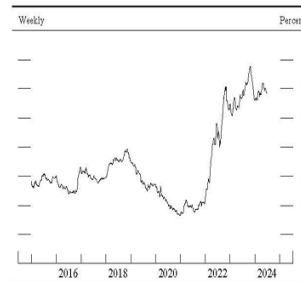
Residential investment turned around and has increased since mid-2023

After rising sharply between early 2022 and late 2023, mortgage interest rates have fallen back some since last fall but, at around 7 percent, remain well above their pre-pandemic peak in 2018 (figure 22). Following the sharp rise in mortgage rates, residential investment declined steeply in 2022 and fell further in the first half of last year but has picked up since mid-2023. Solid income growth and the declines in interest rates late last year have provided support for residential investment demand so far this year. Indeed, residential investment rose sharply in the first quarter.

Sales of existing homes have moved up a touch this year but remain at very low levels. Relatively high mortgage interest rates and house prices have reduced affordability and depressed homebuying sentiment. Moreover, though new listings of existing homes have increased modestly this year, the supply of existing homes for sale remains quite low, as many homeowners are reportedly “rate locked”—unwilling to move and take out a new mortgage while mortgage rates are relatively high. Many households purchased homes or refinanced when fixed mortgage rates were at historically low levels in 2020 and 2021, and, as a result, the majority of outstanding mortgages have interest rates below 4 percent (figure 23).

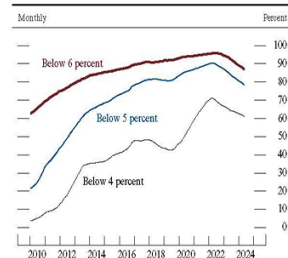
In contrast to existing home sales, sales of new homes declined when mortgage rates first increased, but they bounced back fairly quickly and have remained around their pre-pandemic levels. The new home market has likely been supported by demand from buyers who are unable to find homes in the existing home market and by homebuilder interest rate incentives (figure 24).

22. Mortgage interest rates



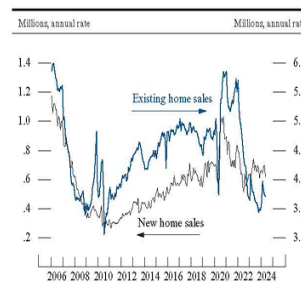
NOTE: The data are contract rates on 30-year, fixed-rate conventional home mortgage commitments and extend through June 27, 2024.
SOURCE: Freddie Mac Primary Mortgage Market Survey via Haver Analytics.

23. Distribution of interest rates on outstanding mortgages



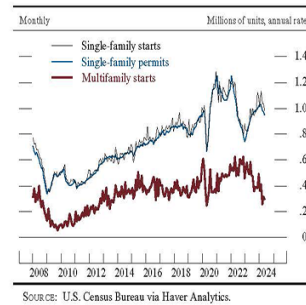
NOTE: The sample only includes outstanding mortgages current on their payments.
SOURCE: ICE, McDash®.

24. New and existing home sales

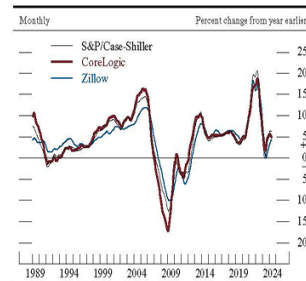


NOTE: The data are monthly. New and existing home sales include only single-family sales.
SOURCE: For new home sales, U.S. Census Bureau; for existing home sales, National Association of Realtors; all via Haver Analytics.

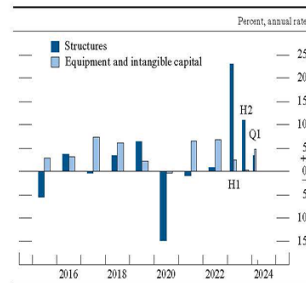
25. Private housing starts and permits



26. Growth rate in house prices



27. Change in real business fixed investment



The relative strength in new home demand encouraged builders to increase housing construction last year, boosting starts and permits for single-family housing (figure 25). In recent months, though, single-family housing starts and permits have drifted back down, likely because of high builder inventories and some easing in new home demand. Reflecting these demand and supply factors, house price growth slowed rapidly in 2022 from a historically high pace and has remained moderate since then (figure 26).

The balance of demand and supply in the multifamily housing market is fundamentally different from that in the single-family housing market, as it is dominated by rental units. Sharp increases in rents in 2021 and 2022 encouraged a dramatic increase in multifamily starts in those years, creating large amounts of new supply. With many units still under construction and weak rental growth since 2022, multifamily starts have been declining since last year (as shown in figure 25).⁸

Capital spending increased at a moderate pace

Business investment spending rose moderately in 2023 and in the first quarter of this year, supported by strong sales growth and improvements in business sentiment and profit expectations—and despite high interest rates (figure 27). However, the sources of strength in business investment shifted recently. Investment in structures—which had surged in early 2023 because of a boom in manufacturing construction, especially for factories that produce semiconductors or electric vehicle batteries—decelerated in the second half of 2023 and has slowed further so far this year, although the level of structures investment remains much higher than in

8. For additional discussion, see the box "Recent Housing Market Developments" in Board of Governors of the Federal Reserve System (2024), *Monetary Policy Report* (Washington: Board of Governors, March), pp. 19–21, https://www.federalreserve.gov/publications/files/20240301_mprfullreport.pdf.

previous years. Starting late last year, growth in business investment in nontransportation equipment and intellectual property stepped up, supported by gains in high-technology equipment spending and software investment.

Business financing conditions are somewhat restrictive, but credit remains generally available

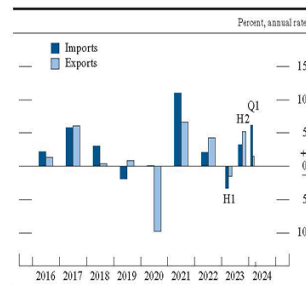
Although businesses face somewhat restrictive financing conditions, as interest rates are still elevated, credit remains generally available to most nonfinancial corporations. Banks continued to tighten lending standards for all business loan types over the first quarter of this year, and even though business loan growth at banks increased in the first five months of the year, it stayed tepid. In contrast, issuance of corporate bonds remained strong so far this year, although well below the levels that prevailed at the beginning of the tightening cycle.

For small businesses, which are more reliant on bank financing than large businesses, credit conditions remained tight but stable over the first half of this year. Surveys indicate that credit supply for small businesses tightened modestly, while interest rates on loans to small businesses were little changed, staying near the top of the range observed since 2008. In addition, while loan default rates have continued to increase, delinquency rates stabilized in the first part of the year at levels that slightly exceeded their pre-pandemic rates. Finally, loan originations have remained stable over the past year and above the range observed before the pandemic, suggesting that credit continues to be available for small businesses.

Net exports were a drag on GDP growth

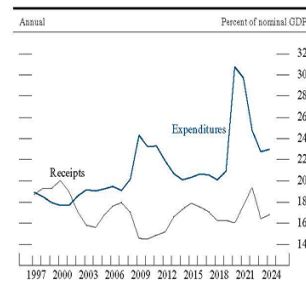
On balance, net exports subtracted 0.7 percentage point from U.S. GDP growth in the first quarter of this year after having contributed about one-tenth to annualized GDP growth in the second half of last year. After moderate growth in the second half of

28. Change in real imports and exports of goods and services



SOURCE: Bureau of Economic Analysis via Haver Analytics.

29. Federal receipts and expenditures



NOTE: Through 2023, the receipts and expenditures data are on a unified-budget basis and are for fiscal years (October to September); gross domestic product (GDP) is for the 4 quarters ending in Q3. For 2024, receipts and expenditures are for the 12 months ending in May; GDP is the average of 2023:Q4 and 2024:Q1.

SOURCE: Department of the Treasury, Financial Management Service; Office of Management and Budget and Bureau of Economic Analysis via Haver Analytics.

last year, real imports of goods and services have stepped up further this year despite some deceleration in U.S. GDP growth. By contrast, real export growth has slowed significantly, as some categories with especially strong growth in the second half of last year declined this year, particularly industrial supplies and materials (figure 28). The current account deficit as a share of GDP widened slightly in the first quarter of 2024 and remains wider than before the pandemic.

Federal fiscal policy actions were roughly neutral for GDP growth last year and so far this year

Federal purchases grew modestly in 2023 and moved sideways in the first quarter of the year. The overall contribution of discretionary federal fiscal policy to real GDP growth appears to have been roughly neutral last year and in the first quarter of this year, as the unwinding of pandemic-related policies offset the boost to consumption and investment from policies enacted after the pandemic.

The budget deficit and federal debt remain elevated

After surging to about 15 percent of GDP in fiscal year 2020, the budget deficit declined through fiscal 2022 as the imprint of the pandemic faded (figure 29). The budget deficit moved up to 6.3 percent of GDP in fiscal 2023 as net interest outlays increased, while tax receipts declined from their elevated level in 2022. Debt service costs have moved up sharply in recent years—as a result of higher interest rates and a higher level of debt—and are at their highest level in over two decades. The primary deficit—the difference between noninterest outlays and receipts—has moved down, on net, since fiscal 2020 and moved sideways in 2022 to 2023, as the effects of a decline in noninterest outlays as a share of GDP were offset by a decline in receipts as a share of GDP.

As a result of the unprecedented fiscal support enacted early in the pandemic, federal debt held by the public jumped roughly 20 percentage

points to close to 100 percent of GDP in 2020—the highest debt-to-GDP ratio since 1947 (figure 30). The debt-to-GDP ratio has moved roughly sideways since then, as upward pressure from large primary deficits has been offset by strong nominal GDP growth.

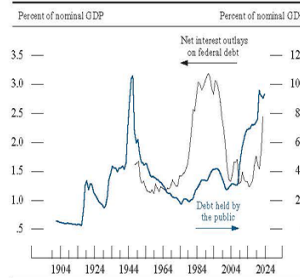
Most state and local government budget positions remained strong . . .

Federal policymakers provided a historically high level of fiscal support to state and local governments during the pandemic; this aid, together with robust state tax collections in 2021 and 2022, left the sector in a strong budget position overall (figure 31). Although state tax revenues weakened in 2023 and early this year—mainly reflecting a normalization of receipts from elevated levels in 2022, as well as the effects of recently enacted tax cuts in some states—taxes as a percentage of GDP remained near recent historical norms. Moreover, states' total balances—that is, including rainy day fund balances and previous-year surplus funds—continued to be near all-time highs. Nevertheless, budget situations varied widely across states, with some states—particularly those that depend heavily on capital gains tax collections—facing tighter budget conditions. At the local level, overall property tax receipts rose briskly in 2023 and continued to increase at an elevated rate in the first quarter.

. . . contributing to brisk growth in employment and construction spending

Employment in state and local governments rose strongly in 2023 and early this year and has now recovered from the drop during the pandemic, though it is still below the level implied by the pre-pandemic trend (figure 32). This surge in state and local employment reflects the waning of pandemic-related headwinds such as a big increase in retirements early in the pandemic and slower wage growth relative to that in the private sector. Similarly, real construction outlays grew at a historically high rate last year, reflecting easing bottlenecks and support from federal grants, and are now somewhat above their pre-pandemic levels.

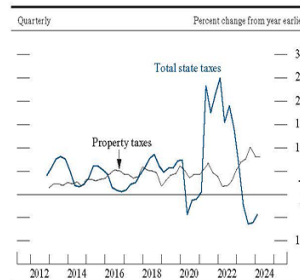
30. Federal government debt and net interest outlays



NOTE: The data for net interest outlays are annual, begin in 1948, and extend through 2023. Net interest outlays are the cost of servicing the debt held by the public, offset by certain types of interest income the government receives. Federal debt held by the public equals federal debt excluding most intragovernmental debt, evaluated at the end of the quarter. The data for federal debt are annual from 1901 to 1951 and a 4-quarter moving average thereafter. GDP is gross domestic product.

SOURCE: For GDP, Bureau of Economic Analysis via Haver Analytics; for federal debt, Congressional Budget Office and Federal Reserve Board, Statistical Release Z.1, "Financial Accounts of the United States."

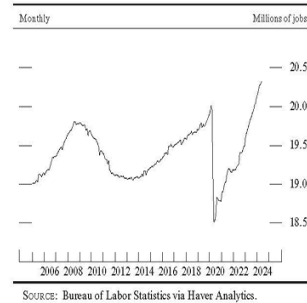
31. State and local tax receipts



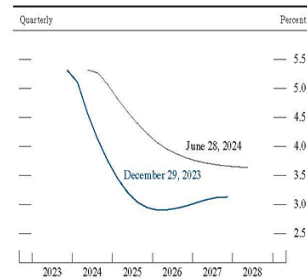
NOTE: Receipts shown are year-over-year percent changes of 4-quarter moving averages and begin in 2012:Q4. Property taxes are primarily collected by local governments.

SOURCE: U.S. Census Bureau, Quarterly Summary of State and Local Government Tax Revenue.

32. State and local government payroll employment



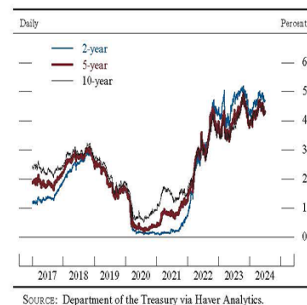
33. Market-implied federal funds rate path



NOTE: The federal funds rate path is implied by quotes on overnight index swaps—a derivative contract tied to the effective federal funds rate. The implied path as of December 29, 2023, is compared with that as of June 28, 2024. The path is estimated with a spline approach, assuming a term premium of 9 basis points. The December 29, 2023, path extends through 2027:Q4 and the June 28, 2024, path through 2028:Q2.

SOURCE: Bloomberg; Federal Reserve Board staff estimates.

34. Yields on nominal Treasury securities



Financial Developments

The expected level of the federal funds rate over the next few years is higher since the beginning of the year

Over the late winter and early spring, the market-implied federal funds rate path moved up, boosted by above-expectations inflation data that prompted market participants to reassess the monetary policy restraint required to return inflation to 2 percent. The rise in the path was partially reversed since late April amid mixed but generally softer-than-expected data on real activity and inflation. Since the beginning of the year, on net, the market-implied federal funds rate path rose substantially (figure 33). Financial market prices currently suggest that investors expect the federal funds rate to decline to about 4.9 percent and 4.0 percent by year-ends 2024 and 2025, respectively. Roughly consistent with market-implied measures, respondents to the Blue Chip Financial Forecasts survey have significantly revised upward their expectations for the path of the federal funds rate, with the average respondent in the July survey expecting the federal funds rate to decline to 5.0 percent in the fourth quarter of 2024—0.6 percentage point higher than anticipated at the end of last year.

Yields on U.S. nominal Treasury securities are higher on net

Consistent with the upward revision in the market-implied federal funds rate path, yields on shorter-term Treasury securities rose notably between mid-February and late April before retracing some of the increase afterward. Yields on longer-term nominal Treasury securities moved similarly with yields on shorter-term nominal Treasury securities. On balance, nominal Treasury yields are moderately higher than at the beginning of the year across the maturity spectrum (figure 34). An increase in real yields—as measured by yields on Treasury Inflation-Protected Securities—accounted for a large portion of the rise in nominal Treasury yields, especially at longer maturities.

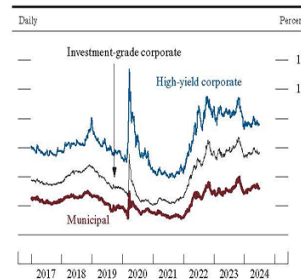
Yields on other long-term debt fluctuated with Treasury yields

Yields on corporate bonds generally followed the movements in longer-term Treasury yields and increased since the beginning of the year for both the investment- and speculative-grade segments of the market (figure 35). Both yield spreads on investment- and speculative-grade corporate bonds over comparable-maturity Treasury securities remain near the low end of their respective historical distributions as corporate bond investors appeared to be pricing in a generally optimistic outlook. Yields on municipal bonds remain at elevated levels relative to rates prevailing before the recent tightening cycle, having increased moderately since January. Meanwhile, spreads of municipal bond yields to yields on comparable-maturity Treasury securities were relatively little changed, on net, and are at compressed levels relative to their historical distribution. Yields on agency mortgage-backed securities (MBS)—an important influence on home mortgage interest rates—increased since the start of the year (figure 36). Agency MBS spreads to Treasury securities remain elevated relative to pre-pandemic levels, due in part to elevated interest rate volatility, which increases the risk of holding MBS.

Broad equity price indexes increased

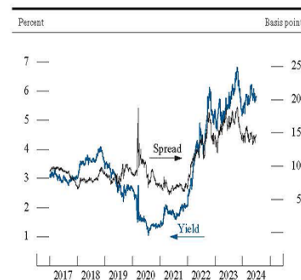
Broad equity price indexes rose substantially since the start of the year, on net, led by large technology firms (figure 37). While equity prices remained sensitive to inflation news, equity investors appeared to be generally sanguine about the prospect of inflation coming down without a sharp downturn in activity. First-quarter corporate earnings releases, which were generally solid, also supported equity valuations. Meanwhile, equity prices for small-cap firms were little changed. Equity prices for large banks increased, on net, while equity prices for regional banks declined, reflecting lingering concerns about the health of these banks related in part to the quality of their commercial real estate loans. One-month option-implied volatility on the S&P 500

35. Corporate bond yields, by securities rating, and municipal bond yield



NOTE: Investment-grade corporate reflects the effective yield of the ICE Bank of America Merrill Lynch (BofAML) triple-B U.S. Corporate Index (C0A4). High-yield corporate reflects the effective yield of the ICE BofAML High Yield Index (H0A0). Municipal reflects the yield to worst of the ICE BofAML U.S. Municipal Securities Index (U0A0). SOURCE: ICE Data Indices, LLC, used with permission.

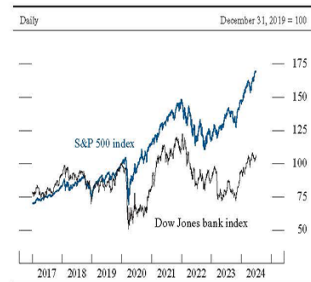
36. Yield and spread on agency mortgage-backed securities



NOTE: The data are daily. Yield shown is for the uniform mortgage-backed securities 30-year current coupon, the coupon rate at which new mortgage-backed securities would be priced at par, or face, value for dates after May 31, 2019; for earlier dates, the yield shown is for the Freddie Mac 30-year current coupon. Spread shown is to the average of the 5-year and 10-year nominal Treasury yields.

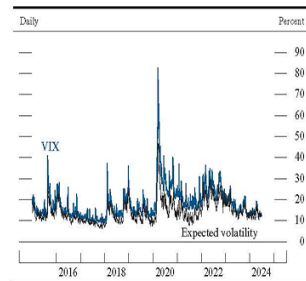
SOURCE: Department of the Treasury; J.P. Morgan. Courtesy of J.P. Morgan Chase & Co., Copyright 2024.

37. Equity prices



SOURCE: S&P Dow Jones Indices LLC via Bloomberg. (For Dow Jones Indices licensing information, see the note on the Contents page.)

38. S&P 500 volatility



NOTE: The VIX is an option-implied volatility measure that represents the expected annualized variability of the S&P 500 index over the following 30 days. The expected volatility series shows a forecast of 1-month realized volatility, using a heterogeneous autoregressive model based on 5-minute S&P 500 returns.

SOURCE: Cboe Volatility Index® (VIX®) via Bloomberg; Refinitiv DataScope; Federal Reserve Board staff estimates.

index—the VIX—fluctuated somewhat, reaching its peak so far this year in early April amid increased inflation concerns and geopolitical tensions, but quickly retraced and ended the period little changed (figure 38). Currently, the VIX stands close to its typical historical level that was observed before the pandemic. (For a discussion of financial stability issues, see the box “Developments Related to Financial Stability.”)

Major asset markets functioned in an orderly manner, despite some indicators pointing to low liquidity

Functioning of the Treasury securities market has continued to be orderly. While a number of measures of Treasury market liquidity remain low by historical standards, some of these measures—such as on-the-run securities market depth, a measure of the availability of securities to transact at the best quoted prices—improved modestly since January. Liquidity in the equity market remained low compared with pre-pandemic levels, and liquidity conditions deteriorated slightly since the beginning of the year. The depth of the S&P 500 futures market decreased a bit, and the price impact increased slightly. Corporate and municipal bond markets continued to function well, and trading conditions remained stable; transaction costs in these markets continued to be fairly low by historical standards.

Short-term funding market conditions remained stable

Conditions in overnight money markets remained stable, with spreads of money market rates to the Federal Reserve’s administered rates roughly unchanged outside of month-end dates. Since the beginning of the year, the effective federal funds rate has stayed 7 basis points below the interest rate on reserve balances, and other unsecured overnight rates have been around similar levels with limited volatility. The Secured Overnight Financing Rate has remained 1 or 2 basis points above the offering rate on the overnight

Developments Related to Financial Stability

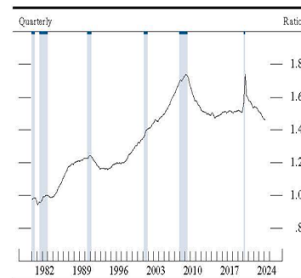
This discussion reviews vulnerabilities in the U.S. financial system. The framework used by the Federal Reserve Board for assessing the resilience of the U.S. financial system focuses on financial vulnerabilities in four broad areas: asset valuations, business and household debt, leverage in the financial sector, and funding risks. All told, the financial system remains sound and resilient. Valuations increased to levels that were high relative to fundamentals across major asset classes, with equity prices growing faster than expected earnings and residential property prices remaining high relative to market rents. Credit to nonfinancial businesses and households relative to gross domestic product (GDP) continued to decline, falling to nearly a two-decade low. Most banks continued to report solid capital levels, but fair value losses on fixed-rate assets remained sizable. In addition, some banks continued to rely significantly on uninsured deposits. Hedge fund leverage grew to historical highs, driven primarily by borrowing by the largest hedge funds.

Valuations rose further to levels that were high relative to fundamentals across major asset classes. Equity prices grew faster than expected earnings, pushing the compensation for equity risk—computed as the difference between the inverse of the forward price-to-earnings ratio and expected real yields on 10-year Treasury securities—to its lowest level since 2007. Corporate bond spreads narrowed and currently stand at levels close to historical lows. Amid limited supply of homes available for sale, residential property prices remained high relative to market rents, standing near their peaks. Conditions in commercial real estate (CRE) markets continued to deteriorate, with declining transaction prices in most segments reflecting weak demand. Nominal long-term Treasury yields increased moderately since the beginning of the year and stayed close to their highest levels over the past decade and a half.

The balance sheets of nonfinancial businesses and households remained strong. The combined debt of both sectors as a share of GDP continued to decline and sat close to its lowest level in two decades (figure A). The decline is due to decreases in both business- and household-sector debt relative to GDP (figure B). Furthermore, business debt continued to decline in real terms, and debt-servicing capacity

(continued on next page)

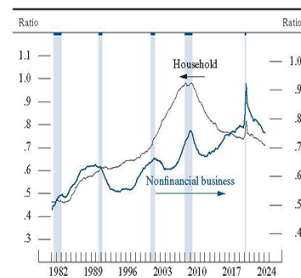
A. Private nonfinancial-sector credit-to-GDP ratio



NOTE: The shaded bars with top caps indicate periods of business recession as defined by the National Bureau of Economic Research: January 1980 to July 1980, July 1981 to November 1982, July 1990 to March 1991, March 2001 to November 2001, December 2007 to June 2009, and February 2020 to April 2020. GDP is gross domestic product.

SOURCE: Federal Reserve Board, Statistical Release Z.1, "Financial Accounts of the United States"; Bureau of Economic Analysis, national income and product accounts; Federal Reserve Board staff calculations.

B. Nonfinancial business and household debt-to-GDP ratios



NOTE: The data are quarterly. The shaded bars with top caps indicate periods of business recession as defined by the National Bureau of Economic Research: July 1981 to November 1982, July 1990 to March 1991, March 2001 to November 2001, December 2007 to June 2009, and February 2020 to April 2020. GDP is gross domestic product.

SOURCE: Federal Reserve Board, Statistical Release Z.1, "Financial Accounts of the United States"; Bureau of Economic Analysis, national income and product accounts; Federal Reserve Board staff calculations.

Developments Related to Financial Stability *(continued)*

stayed solid for most public firms—in large part due to strong earnings, large cash buffers, and low borrowing costs on existing debt. In addition, the pass-through of higher interest rates into debt-servicing costs continues to be muted because the share of long-term, fixed-rate liabilities remained sizable. Corporate bond default rates have returned to their average levels, rising from their low points in 2021 but declining from their peaks in the second half of 2023, suggesting that credit quality is stabilizing with pockets of stress continuing for the riskiest borrowers. Expectations of year-ahead defaults stayed somewhat elevated relative to their history. Household balance sheets are still sound, as most homeowners have ample home equity cushions and strong credit histories. Borrowers with prime credit scores—for whom delinquency rates remained low and stable across credit markets—correspond to more than 60 percent of all borrowers and continued to account for most of household debt outstanding.

Regarding vulnerabilities in the financial sector, most banks continued to report capital levels well above regulatory requirements. However, fair value losses on fixed-rate assets remained sizable for some banks, while parts of banks' CRE portfolios are facing stress. Despite a moderation in deposit outflows, higher funding costs—together with expected increases in loss provisions

for CRE and consumer loans—could put downward pressure on banks' profits and their ability to build capital through retained earnings. Outside the banking sector, hedge fund leverage stayed near historical highs, partly due to funds' substantial positions in the Treasury futures basis trade. Leverage at broker-dealers continued to be near historically low levels, but limited capacity or willingness of broker-dealers to intermediate in Treasury markets during market stress remained a structural vulnerability. Life insurers' leverage increased and stood around its median.

Liquidity at most domestic banks remained ample, with limited reliance on short-term wholesale funding. However, some banks' reliance on uninsured deposits remained high, and bond mutual funds' exposure to interest rate risk continued to be significant. Structural vulnerabilities remained in other short-term funding markets. Prime and tax-exempt money market funds, as well as other cash-investment vehicles and stablecoins, continued to be vulnerable to runs. Bond and loan funds remain susceptible to redemptions during periods of stress, with more severe pressures possible if assets become more illiquid or redemptions become unusually large. In addition, life insurers continued to rely on a higher-than-average share of nontraditional liabilities.

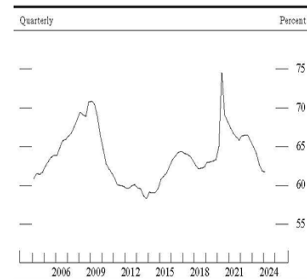
reverse repurchase agreement (ON RRP) facility, except for short-lived upward pressure around month-ends. Take-up at the ON RRP facility declined in the first quarter, reflecting an increase in the net supply of Treasury bills and the associated upward pressure on bill yields relative to the offered rate on ON RRP investments as well as relatively more attractive rates on other short-term investments such as private repurchase agreements. However, the pace of decline in take-up slowed somewhat in the second quarter, primarily because of a decline in net bill supply. (See the box “Developments in the Federal Reserve’s Balance Sheet and Money Markets” in Part 2.)

Assets under management of prime and government money market funds (MMFs), the largest investors in the ON RRP facility, trended up as they continued to offer favorable yields relative to most bank deposits. Prime MMFs increased liquid asset holdings and decreased weighted average maturities to satisfy the Securities and Exchange Commission’s reform requirements that became effective in April. Several institutional prime funds announced conversions to government funds, while a handful announced closures, citing the reform’s liquidity fees starting in October as the main driver behind the decision. However, these announced conversions and closures are unlikely to materially affect the funds’ usage of the ON RRP facility, because only minor additional portfolio changes will be required for conversions and because the decline in money fund assets due to funds closing is likely too small relative to total investments in the facility.

Bank credit continued to expand at a slow pace

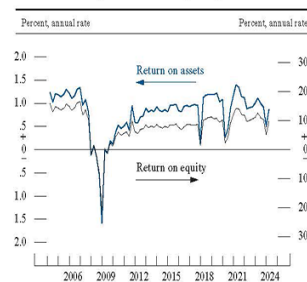
Banks’ total loan holdings grew at about a 2 percent annualized rate in the first five months of the year, modestly up from a 1.3 percent rate in the fourth quarter of 2023. The still-tepid loan growth likely reflects the effects of higher interest rates, tighter credit standards, and economic uncertainty

39. Ratio of total commercial bank credit to nominal gross domestic product



SOURCE: Federal Reserve Board, Statistical Release H.8, "Assets and Liabilities of Commercial Banks in the United States"; Bureau of Economic Analysis via Haver Analytics.

40. Profitability of bank holding companies



NOTE: The data are quarterly.
SOURCE: Federal Reserve Board, Form FR Y-9C, Consolidated Financial Statements for Holding Companies.

(figure 39). Banks in the SLOOS reported generally tighter standards and weaker demand over the first quarter of 2024, extending trends for standards and demand that have been reported since the middle of 2022. Delinquency rates continued to climb to above their longer-run average for commercial real estate and consumer loans in the first quarter of 2024 but remained in ranges observed before the pandemic across most other credit segments. Bank profitability picked up in the first quarter—reversing the dip in the fourth quarter of 2023—mainly driven by recent rising noninterest income and reduced loan loss provisions. Bank profitability levels are still below those that prevailed before the pandemic, reflecting rising funding costs and subdued loan demand (figure 40).

International Developments

Foreign economic growth rose after a soft patch in the second half of 2023

After a soft patch in the second half of 2023, foreign activity appears to have improved in both advanced foreign economies (AFEs) and emerging market economies (EMEs). In AFEs, growth rates returned to moderate levels despite the effects of restrictive monetary policy as lower inflation improved real household incomes. In Europe, energy-intensive sectors continue to struggle amid ongoing structural adjustment to past increases in energy prices following Russia's 2022 invasion of Ukraine.

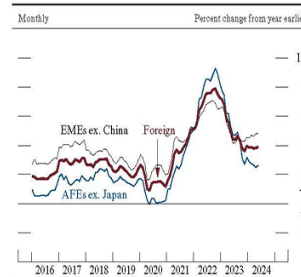
In EMEs, economic growth was supported by a rebound in exports. In addition, industrial production in emerging Asia was supported by rising global demand for high-tech products, driven in part by the AI and electric vehicle sectors. China was a significant contributor to the pickup in foreign aggregate growth, boosted by both strong exports and fiscal policy support, even though household spending expanded only moderately. Notably, activity in China's property sector remained extremely weak and house prices fell sharply,

prompting the authorities to introduce new policy support measures.

Inflation abroad continued to ease but remains above central bank targets in most regions

Foreign headline inflation has continued to stabilize overall since the middle of last year, primarily reflecting disinflation in AFE food and energy prices (figures 41 and 42). That said, the pace of disinflation has proved to be slower than expected and uneven across countries and economic sectors. As in the U.S., the deceleration in goods prices abroad has generally outpaced that in services prices. Inflation remains above target in Europe but has been near zero in China. In many economies, the main risks to continued disinflation include both domestic factors, such as sustained wage pressures, and external geopolitical factors, such as Russia's war against Ukraine and developments in the Middle East, which pose risks for supply chain disruptions, increased trade costs, and higher energy prices.

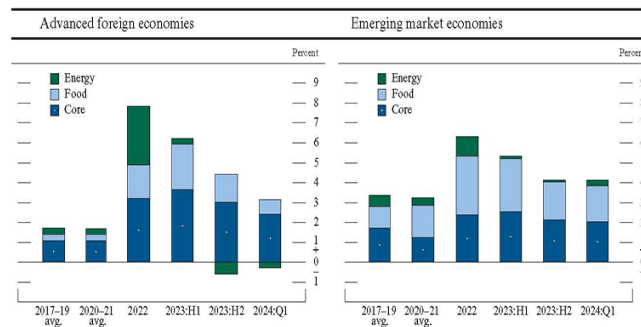
41. Consumer price inflation in foreign economies



NOTE: The advanced foreign economy (AFE) aggregate is the average of Canada, the euro area, and the U.K., weighted by shares of U.S. non-oil goods imports. The emerging market economy (EME) aggregate is the average of Argentina, Brazil, Chile, Colombia, Hong Kong, India, Indonesia, Israel, Malaysia, Mexico, the Philippines, Russia, Saudi Arabia, Singapore, South Korea, Taiwan, Thailand, and Vietnam, weighted by shares of U.S. non-oil goods imports. The foreign aggregate is the import-weighted average of all aforementioned countries. The inflation measure is the Harmonised Index of Consumer Prices for the euro area and the consumer price index for other economies.

SOURCE: Federal Reserve Board staff calculations; Haver Analytics.

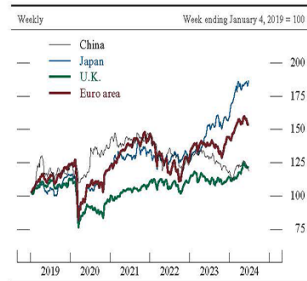
42. Components of foreign consumer price inflation



NOTE: The advanced foreign economy aggregate is the average of Canada, the euro area, and the U.K., weighted by shares of U.S. non-oil goods imports. The emerging market economy aggregate is the average of Argentina, Brazil, Chile, Colombia, Hong Kong, India, Indonesia, Israel, Malaysia, Mexico, the Philippines, Russia, Saudi Arabia, Singapore, South Korea, Taiwan, Thailand, and Vietnam, weighted by shares of U.S. non-oil goods imports, and begins in 2017:Q2. The inflation measure is the Harmonised Index of Consumer Prices for the euro area and the consumer price index for other economies. The data show percent changes from year-ago levels.

SOURCE: Federal Reserve Board staff calculations; Haver Analytics.

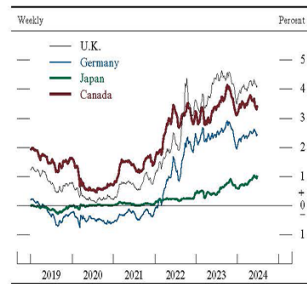
43. Equity indexes for selected foreign economies



NOTE: The data are weekly averages of daily data and extend through June 28, 2024.

SOURCE: For the euro area, Dow Jones Euro Stoxx Index; for Japan, Tokyo Stock Price Index; for China, Shanghai Composite Index; for the U.K., FTSE 100 Index; all via Bloomberg. (For Dow Jones Indices licensing information, see the note on the Contents page.)

44. Nominal 10-year government bond yields in selected advanced foreign economies



NOTE: The data are weekly averages of daily benchmark yields and extend through June 28, 2024.

SOURCE: Bloomberg.

Foreign central banks cut policy rates but remain cautious

Many foreign central banks have noted progress in lowering inflation and easing resource tightness and have indicated that they expect further progress. Some have begun to cut their policy rates while continuing to stress a data-dependent approach.

In EMEs, several central banks began easing monetary policy late in 2023. AFE central banks began to cut rates in the second quarter. The Swiss National Bank, Sweden's Riksbank, the Bank of Canada, and the European Central Bank all cut their policy rates amid easing inflation. Policy rate paths implied by financial market pricing indicate that markets expect other AFE central banks to begin reducing interest rates later this year. Still, most foreign central bank communications have also emphasized upside risks to inflation from persistent core services inflation, currency depreciation, and geopolitical tensions. Japan has been a notable exception: Amid persistently high Japanese inflation, the Bank of Japan (BOJ) ended its negative interest rate policy and yield curve control in March.

Equity prices rose even as sovereign bond yields in advanced foreign economies increased

Foreign equity indexes rose significantly across AFEs and EMEs, consistent with above-expectations economic data and strong corporate earnings in many economies (figure 43). Nevertheless, investors withdrew from EME-focused investment funds as higher advanced-economy yields weighed on their demand for EME assets. In addition, some recent elections abroad contributed to notable movements in equities and other asset prices.

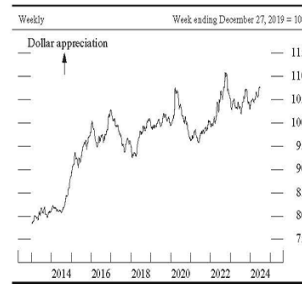
AFE sovereign bond yields increased significantly in early 2024 and are up notably since the start of the year in Germany, Japan, and the U.K. (figure 44). These increases were driven by stronger-than-expected global activity data and spillovers from higher U.S. yields. Relative to late 2023, market-implied

paths for policy rates now indicate a later start to easing and fewer rate cuts by many central banks. In Japan, yields were further supported by three BOJ tightening actions: raising policy rates from negative 0.1 percent to a band of 0 to 0.1 percent, discontinuing the yield curve control framework, and issuing guidance pointing to a potential reduction in sovereign bond purchases.

The exchange value of the dollar rose notably

Since year-end 2023, the broad dollar index—a measure of the exchange value of the dollar against a trade-weighted basket of foreign currencies—increased significantly, on net, reflecting dollar appreciation against both AFE and EME currencies (figure 45). The increase in the dollar index was consistent with a widening of interest rate differentials between the U.S. and the rest of the world.

45. U.S. dollar exchange rate index



NOTE: The data, which are in foreign currency units per dollar, are weekly averages of daily values of the broad dollar index and extend through June 28, 2024. As indicated by the arrow, increases in the data reflect U.S. dollar appreciation and decreases reflect U.S. dollar depreciation.

SOURCE: Federal Reserve Board staff calculations; Federal Reserve Board, Statistical Release H.10, "Foreign Exchange Rates."

PART 2

MONETARY POLICY

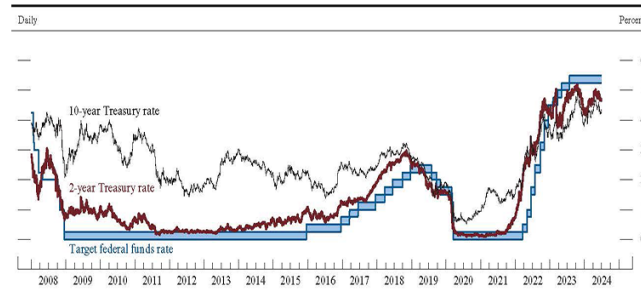
The Federal Open Market Committee has held the federal funds rate steady . . .

The Federal Reserve conducts monetary policy to promote its statutory goals of maximum employment and price stability. (See the box “Monetary Policy Independence, Transparency, and Accountability.”) Inflation has eased over the past year but has remained elevated while the economy has continued to expand at a solid pace. Job gains have been strong, and the unemployment rate has remained low. Against this backdrop, the Federal Open Market Committee (FOMC) has maintained a restrictive stance of policy at recent meetings to keep demand in line with supply and reduce inflationary pressures. Since its July 2023 meeting, the Committee has maintained the target range for the federal funds rate at 5¼ to 5½ percent, after having raised the target range a total of 525 basis points starting in early 2022 (figure 46). The FOMC’s policy tightening actions and current policy stance reflect the Committee’s strong

commitment to return inflation to its 2 percent objective. Restoring price stability is essential to achieving maximum employment and stable prices over the long run that benefit all Americans.

With labor market tightness continuing to ease gradually and inflation easing over the past year, the risks to achieving the Committee’s employment and inflation goals have moved toward better balance. The Committee remains highly attentive to inflation risks and is acutely aware that high inflation imposes significant hardship, especially on those least able to meet the higher costs of essentials, like food, housing, and transportation. In considering any adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks. The Committee does not expect it will be appropriate to reduce the target range until it has gained greater confidence that inflation is moving sustainably toward 2 percent.

46. Selected interest rates



NOTE: The 2-year and 10-year Treasury rates are the constant-maturity yields based on the most actively traded securities.
SOURCE: Department of the Treasury; Federal Reserve Board.

Monetary Policy Independence, Transparency, and Accountability

Monetary policy is carried out by the Federal Reserve in pursuit of maximum employment and price stability—the dual-mandate goals assigned to it by Congress. Congress has also given the Federal Reserve operational independence. Under this arrangement, the Federal Reserve, rather than other parts of the government, makes determinations about the monetary policy actions that are most appropriate for achieving the dual-mandate goals. This arrangement allows monetary policy decisions to be insulated from short-term political influences.

There is broad support for the principles underlying independent monetary policy. It is widely understood that the monetary policy actions that deliver maximum employment and price stability in the longer run may involve restraining measures that entail short-run economic costs, while actions that raise output and employment to unsustainable levels have no long-run real benefits and may lead to elevated inflation rates. These considerations highlight the value of monetary policy being carried out by an independent agency whose decisions are based on the congressionally assigned dual mandate.¹ Operational independence of

monetary policy has become an international norm, and economic research indicates that economic performance has tended to be better when central banks have such independence.²

Because the Federal Reserve is accountable to Congress and has been granted independence in

(continued)

1. The same basic case for independence has been sketched by successive Federal Reserve Chairs. For example, Paul Volcker noted in congressional testimony in February 1982 that “Congress deliberately set us up with an insulation from that kind of political pressure, and that that is a trust that you have given us and that we mean to discharge,” and he elaborated in July 1987: “[Not] responding to all the short-term political considerations that exist to produce easier money than the basic situation warrants and the long-term health of the currency and the economy warrants . . . [is] the basic justification for the independence of the Federal Reserve.” Alan Greenspan testified in October 1993 that there was “an awareness that independence of the central bank is an element in keeping inflation down.” Ben Bernanke remarked in May 2010: “It is important that we maintain and protect . . . the ability of central banks to make monetary policy decisions based on what is good for the economy in the longer run, independent of short-term political considerations.” Also in 2010, Janet Yellen (who was at the time Vice Chair of the Federal Reserve Board and who later served as Federal Reserve Chair) observed: “The principle of central bank independence in the conduct of monetary policy is widely accepted as vital to achieving maximum employment and price stability.” Chair Jerome Powell likewise stated in January 2023 that “the case for monetary policy independence lies in the benefits of insulating monetary policy decisions from short-term political considerations.”

See Paul A. Volcker (1982), “Panel Discussion,” in *Federal Reserve’s First Monetary Policy Report for 1982, hearings before the Committee on Banking, Housing, and Urban Affairs*, U.S. Senate, February 11 and 25, Senate Hearing 97-48, 97th Cong. (Washington: U.S. Government Printing Office), quoted text on p. 28, <https://fraser.stlouisfed.org/title/monetary-policy-oversight-671/federal-reserve-s-first-monetary-policy-report-1982-22312>; Paul A. Volcker (1987), remarks in *Federal Reserve’s Second Monetary Policy Report for 1987, hearing before the Committee on Banking, Housing, and Urban Affairs*, U.S. Senate, July 23, 100th Cong. (Washington: U.S. Government Printing Office), quoted text on p. 45, <https://fraser.stlouisfed.org/title/monetary-policy-oversight-671/federal-reserve-s-second-monetary-policy-report-1987-22373>; Alan Greenspan (1994), remarks in *The Federal Reserve Accountability Act of 1993, hearing before the Committee on Banking, Finance, and Urban Affairs*, U.S. House of Representatives, October 13, 1993, 103rd Cong. (Washington: U.S. Government Printing Office), quoted text on p. 40, <https://fraser.stlouisfed.org/title/federal-reserve-accountability-act-1993-1154>; Ben S. Bernanke (2010), “Central Bank Independence, Transparency, and Accountability,” speech delivered at the Institute for Monetary and Economic Studies International Conference, Bank of Japan, Tokyo, May 25, quoted text in paragraph 2, <https://www.federalreserve.gov/newsevents/speech/bernanke20100525a.htm>; Janet L. Yellen (2010), “Macroprudential Supervision and Monetary Policy in the Post-crisis World,” speech delivered at the Annual Meeting of the National Association for Business Economics, Denver, Colo., October 11, quoted text in paragraph 44, <https://www.federalreserve.gov/newsevents/speech/yellen20101011a.htm>; and Jerome H. Powell (2023), “Panel on ‘Central Bank Independence and the Mandate—Evolving Views,’” speech delivered at the Symposium on Central Bank Independence, Sveriges Riksbank, Stockholm, Sweden, January 10, quoted text in paragraph 2, <https://www.federalreserve.gov/newsevents/speech/powell20230110a.htm>. A detailed discussion of the issues involved is provided by Paul Tucker (2018), *Unelected Power: The Quest for Legitimacy in Central Banking and the Regulatory State* (Princeton, N.J.: Princeton University Press).

2. See, for example, Christopher Crowe and Ellen E. Meade (2008), “Central Bank Independence and Transparency: Evolution and Effectiveness,” *European Journal of Political Economy*, vol. 24 (December), pp. 763–77.

the setting of monetary policy, it is vitally important that the Federal Reserve be transparent to Congress and the American people about its monetary policy actions. Transparency requires that the Federal Open Market Committee (FOMC) explain the reasons for its monetary policy decisions, including how these decisions relate to its statutory goals. This feature of transparency underlies the FOMC's assessment that "transparency and accountability . . . are essential in a democratic society."³

Specifically, monetary policy transparency consists of the process in which the Federal Reserve provides to the American people and their elected representatives information about the objectives and strategy of monetary policy, announces its decisions regarding the setting of its policy instruments, explains the reasoning behind those decisions, and provides detailed records of monetary policy committee meetings. The Federal Reserve promotes monetary policy transparency in multiple ways, including through testimony given by Federal Reserve policymakers at congressional hearings, speeches by the Chair and other FOMC meeting participants on economic and policy developments, the FOMC's postmeeting statements, the published minutes and transcripts of each FOMC meeting, the quarterly Summary of Economic Projections (SEP), the Chair's press conferences, and dialogues between FOMC participants and community representatives across the country.

A strong emphasis on transparency has characterized the past 30 years of U.S. monetary policy. Previously, Federal Reserve officials from the 1950s to

the 1980s regularly gave congressional testimony and speeches on monetary policy. Nevertheless, important aspects of transparency were missing. The FOMC in these decades did not provide, in a systematic and timely manner, information on its monetary policy decisions.⁴ In particular, it did not follow a regular practice of issuing, after policy meetings, an announcement of Committee policy actions and the rationale for those actions. The situation changed starting in the mid-1990s. Reflecting on this change, in 2023 Chair Powell noted: "Over the past several decades we have steadily broadened our efforts to provide meaningful transparency about the basis for, and consequences of, the decisions we make."⁵

The shift to greater transparency has reflected not only the fact that transparency supports the Federal Reserve's accountability, but also widespread acceptance that transparency can contribute to the effectiveness of monetary policy. Explanations to the general public of the FOMC's decisions, strategy, and plans tend to enhance the effects of monetary policy actions on financial conditions, economic activity, and inflation. For example, a numerical inflation objective can be helpful in anchoring longer-run inflation expectations, while forward guidance (which is at times provided in FOMC statements) about the federal funds rate can influence key longer-term interest rates by shaping the private sector's assessment of the likely future course of the funds rate. Consequently, the FOMC has observed that clarity about monetary

(continued on next page)

3. See the FOMC's Statement on Longer-Run Goals and Monetary Policy Strategy (quoted text in paragraph 1), available on the Board's website at https://www.federalreserve.gov/monetarypolicy/files/fomc_longerrungoals.pdf. More specifically, paragraph 1 of this statement indicates that "the Committee seeks to explain its monetary policy decisions to the public as clearly as possible" and that "such clarity facilitates . . . transparency and accountability, which are essential in a democratic society." In the same spirit, a major contribution to the research literature on the practice of monetary policy—the 1999 book *Inflation Targeting*—earlier observed: "Transparency and communication together enhance accountability." See Ben S. Bernanke, Thomas Laubach, Frederic S. Mishkin, and Adam S. Posen (1999), *Inflation Targeting: Lessons from the International Experience* (Princeton N.J.: Princeton University Press), quoted text on p. 296.

4. See David E. Lindsey (2003), "A Modern History of FOMC Communication: 1975–2002," memorandum to the Federal Open Market Committee, Board of Governors of the Federal Reserve System, Division of Monetary Affairs, June 24, <https://www.federalreserve.gov/monetarypolicy/files/FOMC20030624memo01.pdf>; and Ben S. Bernanke (2013), "A Century of US Central Banking: Goals, Frameworks, Accountability," *Journal of Economic Perspectives*, vol. 27 (fall), pp. 3–16.

5. See Powell, "Panel on 'Central Bank Independence,'" in box note 1 (quoted text in paragraph 4). See also Alan S. Blinder (2002), "Through the Looking Glass: Central Bank Transparency," CEPS Working Paper 86 (Princeton, N.J.: Princeton University Department of Economics, December), <https://ceps.princeton.edu/wp-content/uploads/2017/01/86blinder.pdf>.

Monetary Policy Independence *(continued)*

policy decisions “increases the effectiveness of monetary policy.”⁶

Today the acceptance of the need for, and benefits of, monetary policy transparency is reflected in the large volume of material that the FOMC and the individual Committee participants provide about their decisions and thinking.⁷ A major step in the direction of greater transparency took place in 1994, when announcements of policy changes began to be issued after FOMC meetings. By the end of the decade, these releases had evolved into the now standard and key part of the Committee’s policy communications—a statement released by the Committee after each meeting that announces the decision on the federal funds rate target range and any other policy actions, puts that decision in the context of the Committee’s assessment of incoming data and the economic outlook, and gives the record of the vote on the action.⁸ Further information about Committee decisions is provided via FOMC meeting minutes, released three weeks after each FOMC meeting (a shorter lag than that prevailing until the mid-2000s). After five years, transcripts of the FOMC meetings are made public.

6. See the FOMC’s Statement on Longer-Run Goals and Monetary Policy Strategy, in box note 3 (quoted text in paragraph 1).

7. For further details, see Board of Governors of the Federal Reserve System (2019), “Review of Monetary Policy Strategy, Tools, and Communications,” webpage, <https://www.federalreserve.gov/monetarypolicy/review-of-monetary-policy-strategy-tools-and-communications-fed-listens-timelines.htm>; and Jerome H. Powell (2024), “Opening Remarks,” speech delivered at the Stanford Business, Government, and Society Forum, Stanford Graduate School of Business, Stanford, Calif., April 3, <https://www.federalreserve.gov/newsevents/speech/powell20240403a.htm>.

8. In the past 15 years, information about the Committee’s balance sheet policy has been an important part of the postmeeting statement and related FOMC statements. A detailed account of key communications on balance sheet policy that the Committee has issued in recent years is provided in Board of Governors of the Federal Reserve System (2024), “FOMC Communications Related to Policy Normalization,” webpage, <https://www.federalreserve.gov/monetarypolicy/policy-normalization.htm>. A longer-term chronology, covering developments over the past decade, is available at Board of Governors of the Federal Reserve System (2024), “History of the FOMC’s Policy Normalization Discussions and Communications,” webpage, <https://www.federalreserve.gov/monetarypolicy/policy-normalization-discussions-communications-history.htm>.

At the end of 2007, the FOMC began publishing, on a quarterly basis, the SEP, which distills information about individual meeting participants’ economic projections. Since then, numerous features have been added to the SEP, including longer-run projections in 2009 and federal funds rate projections in 2012. In 2011, Chair Bernanke started holding regular postmeeting press conferences. In 2019, Chair Powell initiated the practice of holding press conferences after every FOMC meeting.

With regard to its strategy, in January 2012 the FOMC issued a Statement on Longer-Run Goals and Monetary Policy Strategy, or “consensus statement.” The consensus statement has been reaffirmed in the years since 2012, and it has been revised several times. From its inception, the consensus statement made the price-stability component of the dual mandate numerically precise by indicating that Federal Reserve policymakers interpret it as corresponding to a 2 percent longer-run inflation rate (in the personal consumption expenditures price index). Also in the area of strategy, in 2018 the Federal Reserve launched the practice of having a review of monetary policy strategy, tools, and communication practices roughly every five years. The first such framework review took place from 2019 to 2020. An innovation of this review was the holding, around the country, of *Fed Listens* events, consisting of a dialogue between Federal Reserve policymakers and community members on monetary policy and economic issues. The Federal Reserve has continued to hold *Fed Listens* events between the periods of framework review.

The framework review process also included internal FOMC deliberations. These deliberations took place at Committee meetings and were detailed in the publicly released FOMC meeting minutes. The Federal Reserve staff memos that served as an input into these deliberations were released publicly after the completion of the 2019–20 review. The next framework review is scheduled to begin later this year.

Along with the transparency-enhancing activities, documents, and statements described earlier, further information on monetary policy decisions is provided in the frequent speeches, interviews, and testimony given by FOMC meeting participants.

... and has continued the process of significantly reducing its holdings of Treasury and agency securities

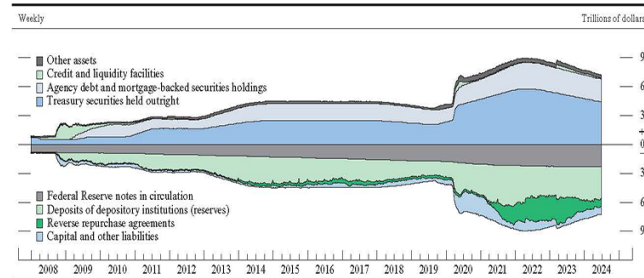
The FOMC began reducing its securities holdings in June 2022 and, since then, has continued to implement its plan for significantly reducing the size of the Federal Reserve's balance sheet in a predictable manner.⁹ For some time, principal payments from securities held in the System Open Market Account (SOMA) had been reinvested only to the extent that they exceeded monthly caps of \$60 billion per month for Treasury securities and \$35 billion per month for agency debt and agency mortgage-backed securities (MBS). On June 1, the Committee slowed the pace of decline of its securities holdings, consistent with its Plans for Reducing the Size of the Federal Reserve's Balance Sheet. Specifically, the Committee reduced the redemption cap on Treasury securities to \$25 billion per month and maintained the redemption cap on agency debt and agency MBS at \$35 billion per month. Any proceeds

in excess of the agency debt and agency MBS cap would be reinvested into Treasury securities, consistent with the Committee's intention to hold primarily Treasury securities in the longer run. The decision to slow the pace of balance sheet runoff does not have implications for the stance of monetary policy and does not mean that the balance sheet will ultimately shrink by less than it would otherwise. Rather, a slower pace of balance sheet runoff helps facilitate a smooth transition from abundant to ample reserve balances and gives the Committee more time to assess market conditions as the balance sheet continues to shrink. It will also allow banks, and short-term funding markets more generally, additional time to adjust to the lower level of reserves, thus reducing the probability that money markets experience undue stress that could require an early end to runoff.

The SOMA holdings of Treasury and agency securities have declined about \$1.7 trillion since the start of the balance sheet reduction and about \$260 billion since February 2024 to around \$6.8 trillion, a level equivalent to 24 percent of U.S. nominal gross domestic product, down from its peak of 35 percent reached at the end of 2021 (figure 47). Also, since February 2024, reserve balances—

9. See the May 4, 2022, press release regarding the Plans for Reducing the Size of the Federal Reserve's Balance Sheet, available on the Board's website at <https://www.federalreserve.gov/newsevents/pressreleases/monetary20220504b.htm>.

47. Federal Reserve assets and liabilities



NOTE: "Other assets" includes repurchase agreements, FIMA (Foreign and International Monetary Authorities) repurchase agreements, and unamortized premiums and discounts on securities held outright. "Credit and liquidity facilities" consists of primary, secondary, and seasonal credit; term auction credit; central bank liquidity swaps; support for Maiden Lane, Bear Stearns Companies, Inc., and AIG; and other credit and liquidity facilities, including the Primary Dealer Credit Facility, the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility, the Commercial Paper Funding Facility, the Term Asset-Backed Securities Loan Facility, the Primary and Secondary Market Corporate Credit Facilities, the Paycheck Protection Program Liquidity Facility, the Municipal Liquidity Facility, and the Main Street Lending Program. "Agency debt and mortgage-backed securities holdings" includes agency residential mortgage-backed securities and agency commercial mortgage-backed securities. "Capital and other liabilities" includes the U.S. Treasury General Account and the U.S. Treasury Supplementary Financing Account. The key identifies shaded areas in order from top to bottom. The data extend through June 19, 2024.

SOURCE: Federal Reserve Board, Statistical Release H.4.1, "Factors Affecting Reserve Balances."

the largest liability item on the Federal Reserve's balance sheet—have declined about \$180 billion to a level of around \$3.4 trillion. The smaller decline of reserve balances compared with the decline in SOMA holdings reflects decreases in nonreserve liabilities such as balances at the overnight reverse repurchase agreement facility. (See the box “Developments in the Federal Reserve's Balance Sheet and Money Markets.”)

The FOMC has stated that it intends to maintain securities holdings at amounts consistent with implementing monetary policy efficiently and effectively in its ample-reserves regime—that is, a regime in which an ample supply of reserves ensures that control over the level of the federal funds rate and other short-term interest rates is exercised primarily through the setting of the Federal Reserve's administered rates and in which active management of the supply of reserves is not required. To ensure a smooth transition to ample reserve balances, the FOMC slowed the pace of decline of its securities holdings in June 2024 and intends to stop reductions in its securities holdings when reserve balances are somewhat above the level that the FOMC judges to be consistent with ample reserves. Once balance sheet runoff has ceased, reserve balances will likely continue to decline at a slower pace—reflecting growth in other Federal Reserve liabilities—until the FOMC judges that reserve balances are at an ample level. Thereafter, the FOMC will manage securities holdings as needed to maintain ample reserves over time.

The FOMC will continue to monitor the implications of incoming information for the economic outlook and the balance of risks

As already indicated, the FOMC is strongly committed to returning inflation to its

2 percent objective, and, in considering any adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks. Its assessments will take into account a wide range of information, including readings on labor market conditions, inflation pressures and inflation expectations, and financial and international developments. The Committee has noted that it is also prepared to adjust its approach to reducing the size of the balance sheet in light of economic and financial developments.

In addition to considering a wide range of economic and financial data, the FOMC gathers information from business contacts and other informed parties around the country, as summarized in the Beige Book. The Federal Reserve has regular arrangements under which it hears from a broad range of participants in the U.S. economy about how monetary policy affects people's daily lives and livelihoods. In particular, the Federal Reserve has continued to gather insights into these matters through the *Fed Listens* initiative and the Federal Reserve System's community development outreach.

Policymakers also routinely consult prescriptions for the policy interest rate provided by various monetary policy rules. These rule prescriptions can provide useful benchmarks for the conduct of monetary policy. However, simple rules cannot capture all of the complex considerations that go into the formation of appropriate monetary policy, and many practical considerations make it undesirable for the FOMC to adhere strictly to the prescriptions of any specific rule. Nevertheless, some principles of good monetary policy are embedded in these simple rules. (See the box “Monetary Policy Rules in the Current Environment.”)

Developments in the Federal Reserve's Balance Sheet and Money Markets

The Federal Open Market Committee (FOMC) continued to reduce the size of the Federal Reserve's System Open Market Account (SOMA) portfolio. Since the previous report, total Federal Reserve assets have decreased \$315 billion, leaving the total size of the balance sheet at \$7.3 trillion, \$1.7 trillion smaller since the reduction in the size of the SOMA portfolio began in June 2022 (figures A and B).¹ On May 1, the FOMC

announced that beginning in June, the Committee would slow the pace of decline of its securities holdings, consistent with its Plans for Reducing the Size of the Federal Reserve's Balance Sheet.²

(continued on next page)

dated February 29, 2024. As a result, this discussion refers to changes in the Federal Reserve's balance sheet since late February.

2. See the May 4, 2022, press release regarding the Plans for Reducing the Size of the Federal Reserve's Balance Sheet, available on the Board's website at <https://www.federalreserve.gov/newsevents/pressreleases/monetary20220504b.htm>.

1. The last Federal Reserve Board statistical release H.4.1 ("Factors Affecting Reserve Balances") before the publication of the previous *Monetary Policy Report* on March 1 was

A. Balance sheet comparison

Billions of dollars

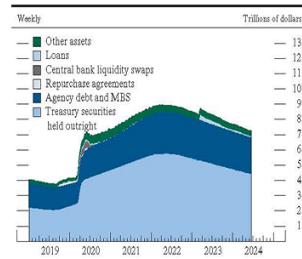
	June 19, 2024	February 28, 2024	Change (since February 2024)	Memo: Change (since Fed's balance sheet reduction began on June 1, 2022)
Assets				
Total securities				
Treasury securities	4,453	4,661	-208	-1,318
Agency debt and MBS	2,357	2,406	-49	-353
Unamortized premiums	265	274	-8	-72
Repurchase agreements	0	0	0	0
Loans and lending facilities				
PPPLF	3	3	0	-17
Discount window	7	2	5	6
BTFF	107	163	-56	107
Other loans and lending facilities	11	15	-4	-23
Central bank liquidity swaps	0	0	0	0
Other assets	49	44	6	7
Total assets	7,253	7,568	-315	-1,663
Liabilities				
Federal Reserve notes	2,301	2,282	18	70
Reserves held by depository institutions	3,366	3,541	-175	9
Reverse repurchase agreements				
Foreign official and international accounts	389	339	50	124
Others	376	570	-194	-1,589
U.S. Treasury General Account	782	768	14	2
Other deposits	158	162	-4	-90
Other liabilities and capital	-120	-94	-25	-188
Total liabilities and capital	7,253	7,568	-315	-1,663

Note: MBS is mortgage-backed securities. PPPLF is Paycheck Protection Program Liquidity Facility. BTFF is Bank Term Funding Program. Components may not sum to totals because of rounding.

Sources: Federal Reserve Board, Statistical Release H.4.1, "Factors Affecting Reserve Balances."

Federal Reserve's Balance Sheet and Money Markets *(continued)*

B. Federal Reserve assets



Note: MBS is mortgage-backed securities. The key identities shaded areas in order from top to bottom. The data extend through June 19, 2024.
Source: Federal Reserve Board, Statistical Release H.4.1, "Factors Affecting Reserve Balances."

Reserves, the largest liability item on the Federal Reserve's balance sheet, have declined \$175 billion since late February 2024 to a level of about \$3.4 trillion.³ Since the beginning of balance sheet runoff, reserves have been little changed because the

reserve-draining effect of balance sheet runoff was more than offset by a \$1.6 trillion decline in balances at the overnight reverse repurchase agreement (ON RRP) facility. Since February 2024, usage of the ON RRP facility has continued to decline, albeit at a slower pace than that seen over the second half of 2023. Usage of the facility has averaged around \$450 billion since the end of February (figure C). Reduced usage of the ON RRP facility largely reflects money market mutual funds shifting their portfolios toward higher-yielding investments, including Treasury bills and private-market repurchase agreements.

Conditions in overnight money markets remained stable. The ON RRP facility continued to serve its intended purpose of supporting the control of the effective federal funds rate (EFFR), and the Federal Reserve's administered rates—the interest rate on reserve balances and the ON RRP offering rate—remained highly effective at maintaining the EFFR within the target range.

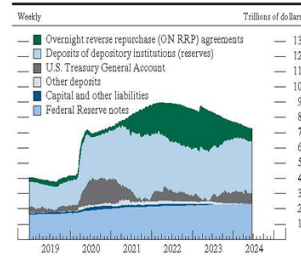
The Federal Reserve's expenses have continued to exceed its income over recent months. The Federal Reserve's deferred asset has increased \$23 billion since late February to a level of around \$175 billion.⁴ Negative net income and the associated deferred asset

(continued)

3. Reserve balances consist of deposits held at the Federal Reserve Banks by depository institutions (DIs), such as commercial banks, savings banks, credit unions, thrift institutions, and U.S. branches and agencies of foreign banks.

4. The deferred asset is equal to the cumulative shortfall of net income and represents the amount of future net income that will need to be realized before remittances to the Treasury resume. Although remittances are suspended at the time of this

C. Federal Reserve liabilities



Note: "Capital and other liabilities" includes the liability for earnings remittances due to the U.S. Treasury and contributions from the U.S. Treasury. The current sum is negative on June 19, 2024, because of the deferred asset that the Federal Reserve reports. The key identifies shaded areas in order from top to bottom. The data extend through June 19, 2024.
Source: Federal Reserve Board, Statistical Release H.4.1, "Factors Affecting Reserve Balances."

do not affect the Federal Reserve's conduct of monetary policy or its ability to meet its financial obligations.⁵

report, over the past decade and a half, the Federal Reserve has remitted over \$1 trillion to the Treasury.

5. Net income is expected to turn positive again as interest expenses fall, and remittances will resume once the temporary deferred asset falls to zero. As a result of the ongoing reduction in the size of the Federal Reserve's balance sheet, interest

While the reduction in the size of the SOMA portfolio has continued as planned, amid the banking-sector developments of spring 2023, the Federal Reserve provided liquidity to help ensure the stability of the banking system and the ongoing provision of money and credit to the economy. Loans extended under the Bank Term Funding Program (BTFP)—which made longer-term funding and liquidity available to eligible depository institutions to support American households and businesses and ceased making new loans as scheduled on March 11, 2024—have decreased \$56 billion to a level of \$107 billion since February 2024.⁶

expenses will fall over time in line with the decline in the Federal Reserve's liabilities.

6. The BTFP was established under section 13(3) of the Federal Reserve Act with the approval of the Secretary of the Treasury. The BTFP offered loans of up to one year to banks, savings associations, credit unions, and other eligible DIs against collateral such as U.S. Treasury securities, U.S. agency securities, and U.S. agency mortgage-backed securities. For more details, see Board of Governors of the Federal Reserve System (2024), "Bank Term Funding Program," webpage, June 11, <https://www.federalreserve.gov/financial-stability/bank-term-funding-program.htm>.

Monetary Policy Rules in the Current Environment

As part of their monetary policy deliberations, policymakers regularly consult the prescriptions of a variety of simple interest rate rules without mechanically following the prescriptions of any particular rule. Simple interest rate rules relate a policy interest rate, such as the federal funds rate, to a small number of other economic variables—typically including the current deviation of inflation from its target value and a measure of resource slack in the economy.

Since 2021, inflation has run above the Federal Open Market Committee's (FOMC) 2 percent longer-run objective, and labor market conditions have been tight. Although inflation remains elevated, it has eased over the past year, and labor supply and demand have come into better balance. Against this backdrop, the simple monetary policy rules considered in this discussion have called for levels of the policy interest rate over 2021, 2022, and the first half of 2023 that were elevated relative to the FOMC's target range for the federal funds rate. However, the rates prescribed by these rules for the first quarter of 2024, the most recent quarter for which data are available, are close to or below the current target range for the federal funds rate at 5¼ to 5½ percent. In support of its goals of maximum employment and inflation at the rate of 2 percent over the longer run, the FOMC has maintained the target range for the federal funds rate at 5¼ to 5½ percent since last July while continuing to

reduce its holdings of Treasury securities and agency debt and agency mortgage-backed securities.

Selected Policy Rules: Descriptions

In many economic models, desirable economic outcomes can be achieved over time if monetary policy responds to changes in economic conditions in a manner that is predictable and adheres to some key design principles. In recognition of this idea, economists have analyzed many monetary policy rules, including the well-known Taylor (1993) rule, the “balanced approach” rule, the “adjusted Taylor (1993)” rule, and the “first difference” rule.¹ Figure A shows these rules, along with a “balanced approach

(continued)

1. The Taylor (1993) rule was introduced in John B. Taylor (1993), “Discretion versus Policy Rules in Practice,” *Carnegie-Rochester Conference Series on Public Policy*, vol. 39 (December), pp. 195–214. The balanced-approach rule was analyzed in John B. Taylor (1999), “A Historical Analysis of Monetary Policy Rules,” in John B. Taylor, ed., *Monetary Policy Rules* (Chicago: University of Chicago Press), pp. 319–41. The adjusted Taylor (1993) rule was studied in David Reischneider and John C. Williams (2000), “Three Lessons for Monetary Policy in a Low-Inflation Era,” *Journal of Money, Credit and Banking*, vol. 32 (November), pp. 936–66. The first-difference rule is based on a rule suggested by Athanasios Orphanides (2003), “Historical Monetary Policy Analysis and the Taylor Rule,” *Journal of Monetary Economics*, vol. 50 (July),

A. Monetary policy rules

Taylor (1993) rule	$R_t^{T93} = r_t^{L*} + \pi_t + 0.5(\pi_t - \pi^{L*}) + (u_t^{L*} - u_t)$
Balanced-approach rule	$R_t^{BA} = r_t^{L*} + \pi_t + 0.5(\pi_t - \pi^{L*}) + 2(u_t^{L*} - u_t)$
Balanced-approach (shortfalls) rule	$R_t^{BAS} = r_t^{L*} + \pi_t + 0.5(\pi_t - \pi^{L*}) + 2\min\{(u_t^{L*} - u_t), 0\}$
Adjusted Taylor (1993) rule	$R_t^{T93adj} = \max\{R_t^{T93} - Z_t, \text{ELB}\}$
First-difference rule	$R_t^{FD} = R_{t-1} + 0.5(\pi_t - \pi^{L*}) + (u_t^{L*} - u_t) - (u_t^{L*} - u_{t-1})$

NOTE: R_t^{T93} , R_t^{BA} , R_t^{BAS} , R_t^{T93adj} , and R_t^{FD} represent the values of the nominal federal funds rate prescribed by the Taylor (1993), balanced-approach, balanced-approach (shortfalls), adjusted Taylor (1993), and first-difference rules, respectively.

R_{t-1} denotes the midpoint of the target range for the federal funds rate for quarter $t-1$. u_t is the unemployment rate in quarter t , and u_t^{L*} is the level of the neutral real federal funds rate in the longer run that is expected to be consistent with sustaining maximum employment and keeping inflation at the Federal Open Market Committee's 2 percent longer-run objective, represented by π^{L*} . π_t denotes the realized 4-quarter price inflation for quarter t . In addition, u_t^{L*} is the rate of unemployment expected in the longer run. Z_t is the cumulative sum of past deviations of the federal funds rate from the prescriptions of the Taylor (1993) rule when that rule prescribes setting the federal funds rate below an effective lower bound (ELB) of 12.5 basis points.

The Taylor (1993) rule and other policy rules generally respond to the deviation of real output from its full capacity level. In these equations, the output gap has been replaced with the gap between the rate of unemployment in the longer run and its actual level (using a relationship known as Okun's law) to represent the rules in terms of the unemployment rate. The rules are implemented as responding to core personal consumption expenditures (PCE) inflation rather than headline PCE inflation because current and near-term core inflation rates tend to outperform headline inflation rates as predictors of the medium-term behavior of headline inflation. Box note 1 provides references for the policy rules.

(shortfalls)” rule, which responds to the unemployment rate only when it is higher than its estimated longer-run level.² All of the simple rules shown embody key design principles of good monetary policy, including the requirement that the policy rate should be adjusted by enough over time to ensure a return of inflation to the central bank’s longer-run objective and to anchor longer-term inflation expectations at levels consistent with that objective.

All five rules feature the difference between inflation and the FOMC’s longer-run objective of 2 percent. The five rules use the unemployment rate gap, measured as the difference between an estimate of the rate of unemployment in the longer run (u^{LR}) and the current unemployment rate; the first-difference rule includes the change in the unemployment rate gap rather than its level.³ All but the first-difference rule include an estimate of the neutral real interest rate in the longer run (r^{LR}).⁴

pp. 983–1022. A review of policy rules is provided in John B. Taylor and John C. Williams (2011), “Simple and Robust Rules for Monetary Policy,” in Benjamin M. Friedman and Michael Woodford, eds., *Handbook of Monetary Economics*, vol. 3B (Amsterdam: North-Holland), pp. 829–59. The same volume of the *Handbook of Monetary Economics* also discusses approaches to deriving policy rate prescriptions other than through the use of simple rules.

2. The balanced-approach (shortfalls) rule responds asymmetrically to unemployment rates above or below their estimated longer-run value. When unemployment is above that value, the policy rates are identical to those prescribed by the balanced-approach rule, whereas when unemployment is below that value, policy rates do not rise because of further declines in the unemployment rate. As a result, the prescription of the balanced-approach (shortfalls) rule has been less restrictive than that of the balanced-approach rule since the first quarter of 2022.

3. Implementations of simple rules often use the output gap as a measure of resource slack in the economy. The rules described in figure A instead use the unemployment rate gap because that gap better captures the FOMC’s statutory goal to promote maximum employment. Movements in these alternative measures of resource utilization tend to be highly correlated. For more information, see the note associated with figure A.

4. The neutral real interest rate in the longer run (r^{LR}) is the level of the real federal funds rate that is expected to be consistent, in the longer run, with maximum employment and stable inflation. Like u^{LR} , r^{LR} is determined largely by nonmonetary factors. The first-difference rule shown in figure A does not require an estimate of r^{LR} , a feature that is touted by proponents of such rules as providing an element of robustness. However, this rule has its own shortcomings. For example, research suggests that this sort of rule often results in greater volatility in employment and inflation than what would be obtained under the Taylor (1993) and balanced-approach rules.

Unlike the other simple rules featured here, the adjusted Taylor (1993) rule recognizes that the federal funds rate cannot be reduced materially below the effective lower bound (ELB). By contrast, the standard Taylor (1993) rule prescribed policy rates that, during the pandemic-induced recession, were far below zero. To make up for the cumulative shortfall in policy accommodation following a recession during which the federal funds rate is constrained by its ELB, the adjusted Taylor (1993) rule prescribes delaying the return of the policy rate to the (positive) levels prescribed by the standard Taylor (1993) rule.

Policy Rules: Limitations

As benchmarks for monetary policy, simple policy rules have important limitations. One of these limitations is that the simple policy rules mechanically respond to only a small set of economic variables and thus necessarily abstract from many of the factors that the FOMC considers when it assesses the appropriate setting of the policy rate. In addition, the structure of the economy and current economic conditions differ in important respects from those prevailing when the simple policy rules were originally devised and proposed. As a result, most simple policy rules do not take into account the ELB on interest rates, which limits the extent to which the policy rate can be lowered to support the economy. This constraint was particularly evident during the pandemic-driven recession, when the lower bound on the policy rate motivated the FOMC’s other policy actions to support the economy. Relatedly, another limitation is that simple policy rules do not explicitly take into account other important tools of monetary policy, such as balance sheet policies. Finally, simple policy rules are not forward looking and do not allow for important risk-management considerations, associated with uncertainty about economic relationships and the evolution of the economy, that factor into FOMC decisions.

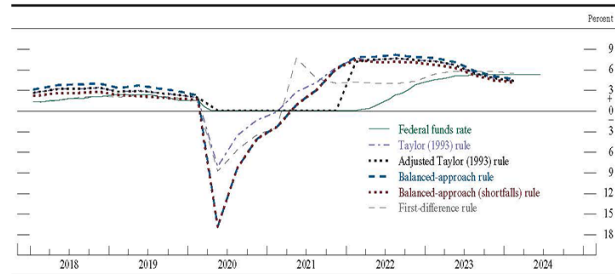
Selected Policy Rules: Prescriptions

Figure B shows historical prescriptions for the federal funds rate under the five simple rules considered. For each quarterly period, the figure reports the policy rates prescribed by the rules, taking as given the prevailing economic conditions and survey-based estimates of u^{LR} and r^{LR} at the time. All of the rules considered called for a highly accommodative stance of monetary policy in response to the pandemic-driven recession, followed by

(continued on next page)

Monetary Policy Rules *(continued)*

B. Historical federal funds rate prescriptions from simple policy rules



NOTE: The rules use historical values of core personal consumption expenditures inflation, the unemployment rate, and, where applicable, historical values of the midpoint of the target range for the federal funds rate. Quarterly projections of longer-run values for the federal funds rate, the unemployment rate, and inflation used in the computation of the rules' prescriptions are interpolations to quarterly values of projections from the Survey of Primary Dealers. The rules' prescriptions are quarterly, and the federal funds rate data are the monthly average of the daily midpoint of the target range for the federal funds rate and extend through June 2024.

SOURCE: Federal Reserve Bank of New York, Survey of Primary Dealers; Federal Reserve Bank of St. Louis, Federal Reserve Economic Data, DFEDTARL and DFEDTARU; Federal Reserve Board staff estimates.

positive values as inflation picked up and labor market conditions strengthened.⁵ In 2022 and during the first half of 2023, the prescriptions of the simple rules for

the federal funds rate were well above the prescriptions observed before the pandemic, reflecting, in large part, elevated inflation readings. Because inflation has recently run notably below levels observed at its peak in 2022, the policy rates prescribed by these rules have now declined. The current prescriptions from these rules are close to or below the current target range for the federal funds rate, though higher than survey-based estimates of the longer-run value of the federal funds rate.

5. For the adjusted Taylor (1993) rule, Z_t —the cumulative sum of past deviations of the federal funds rate from the prescriptions of the Taylor (1993) rule when that rule prescribes setting the federal funds rate below an ELB of 12.5 basis points—is positive in the third quarter of 2020, one quarter after the prescription of the Taylor (1993) rule falls below the ELB, through to the first quarter of 2022. This approach is a slight adjustment from previous editions of this

discussion in the *Monetary Policy Report*, where Z_t cumulated from the fourth quarter of 2020.

PART 3

SUMMARY OF ECONOMIC PROJECTIONS

The following material was released after the conclusion of the June 11–12, 2024, meeting of the Federal Open Market Committee.

In conjunction with the Federal Open Market Committee (FOMC) meeting held on June 11–12, 2024, meeting participants submitted their projections of the most likely outcomes for real gross domestic product (GDP) growth, the unemployment rate, and inflation for each year from 2024 to 2026 and over the longer run. Each participant's projections were based on information available at the time of the meeting, together with her or his assessment of appropriate monetary policy—including a path for the federal funds rate and its longer-run value—and assumptions about other factors likely

to affect economic outcomes. The longer-run projections represent each participant's assessment of the value to which each variable would be expected to converge, over time, under appropriate monetary policy and in the absence of further shocks to the economy. “Appropriate monetary policy” is defined as the future path of policy that each participant deems most likely to foster outcomes for economic activity and inflation that best satisfy his or her individual interpretation of the statutory mandate to promote maximum employment and price stability.

Table 1. Economic projections of Federal Reserve Board members and Federal Reserve Bank presidents, under their individual assumptions of projected appropriate monetary policy, June 2024
Percent

Variable	Median ¹				Central tendency ²				Range ³			
	2024	2025	2026	Longer run	2024	2025	2026	Longer run	2024	2025	2026	Longer run
Change in real GDP	2.1	2.0	2.0	1.8	1.9–2.3	1.8–2.2	1.8–2.1	1.7–2.0	1.4–2.7	1.5–2.5	1.7–2.5	1.6–2.5
March projection	2.1	2.0	2.0	1.8	2.0–2.4	1.9–2.3	1.8–2.1	1.7–2.0	1.3–2.7	1.7–2.5	1.7–2.5	1.6–2.5
Unemployment rate	4.0	4.2	4.1	4.2	4.0–4.1	3.9–4.2	3.9–4.3	3.9–4.3	3.8–4.4	3.8–4.3	3.8–4.3	3.5–4.5
March projection	4.0	4.1	4.0	4.1	3.9–4.1	3.9–4.2	3.9–4.3	3.8–4.3	3.8–4.5	3.7–4.3	3.7–4.3	3.5–4.3
PCE inflation	2.6	2.3	2.0	2.0	2.5–2.9	2.2–2.4	2.0–2.1	2.0	2.5–3.0	2.2–2.5	2.0–2.3	2.0
March projection	2.4	2.2	2.0	2.0	2.3–2.7	2.1–2.2	2.0–2.1	2.0	2.2–2.9	2.0–2.5	2.0–2.3	2.0
Core PCE inflation ⁴	2.8	2.3	2.0		2.8–3.0	2.3–2.4	2.0–2.1		2.7–3.2	2.2–2.6	2.0–2.3	
March projection	2.6	2.2	2.0		2.5–2.8	2.1–2.3	2.0–2.1		2.4–3.0	2.0–2.6	2.0–2.3	
Memo: Projected appropriate policy path												
Federal funds rate	5.1	4.1	3.1	2.8	4.9–5.4	3.9–4.4	2.9–3.6	2.5–3.5	4.9–5.4	2.9–5.4	2.4–4.9	2.4–3.8
March projection	4.6	3.9	3.1	2.6	4.6–5.1	3.4–4.1	2.6–3.4	2.5–3.1	4.4–5.4	2.6–5.4	2.4–4.9	2.4–3.8

Note: Projections of change in real gross domestic product (GDP) and projections for both measures of inflation are percent changes from the fourth quarter of the previous year to the fourth quarter of the year indicated. PCE inflation and core PCE inflation are the percentage rates of change in, respectively, the price index for personal consumption expenditures (PCE) and the price index for PCE excluding food and energy. Projections for the unemployment rate are for the average civilian unemployment rate in the fourth quarter of the year indicated. Each participant's projections are based on his or her assessment of appropriate monetary policy. Longer-run projections represent each participant's assessment of the rate to which each variable would be expected to converge under appropriate monetary policy and in the absence of further shocks to the economy. The projections for the federal funds rate are the value of the midpoint of the projected appropriate target range for the federal funds rate or the projected appropriate target level for the federal funds rate at the end of the specified calendar year or over the longer run. The March projections were made in conjunction with the meeting of the Federal Open Market Committee on March 19–20, 2024. One participant did not submit longer-run projections for the change in real GDP, the unemployment rate, or the federal funds rate in conjunction with the March 19–20, 2024, meeting of the two middle projections.

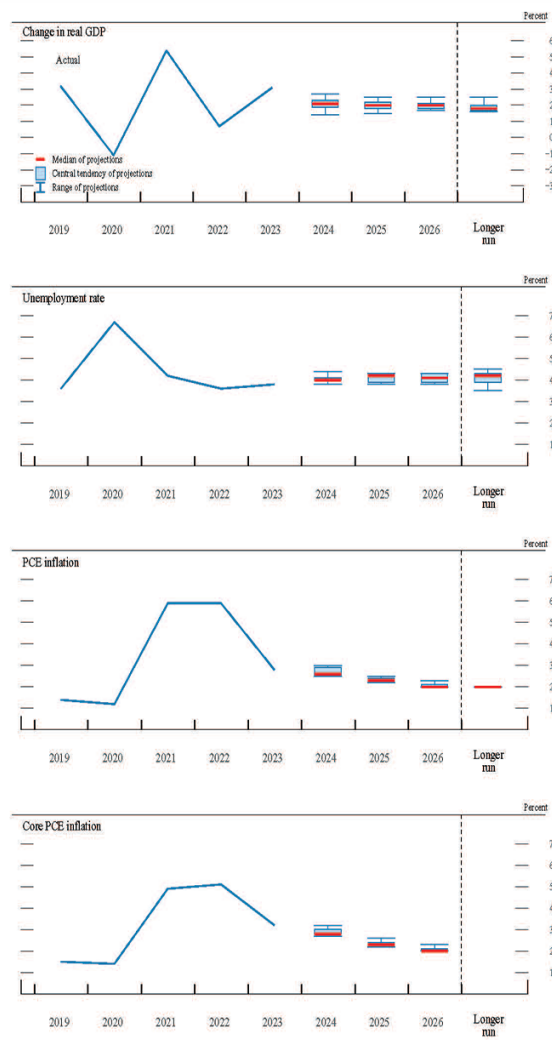
1. For each period, the median is the middle projection when the projections are arranged from lowest to highest. When the number of projections is even, the median is the average of the two middle projections.

2. The central tendency excludes the three highest and three lowest projections for each variable in each year.

3. The range for a variable in a given year includes all participants' projections, from lowest to highest, for that variable in that year.

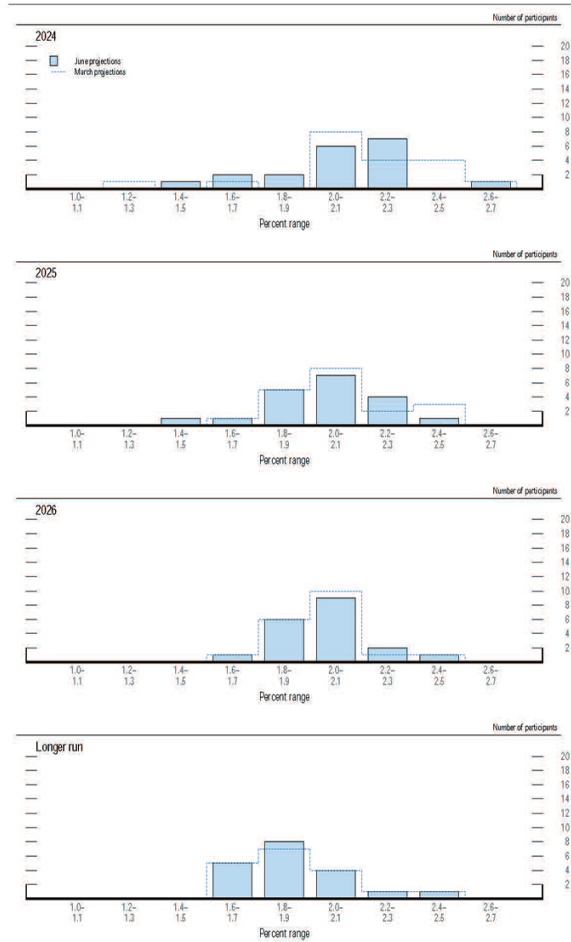
4. Longer-run projections for core PCE inflation are not collected.

Figure 1. Medians, central tendencies, and ranges of economic projections, 2024–26 and over the longer run



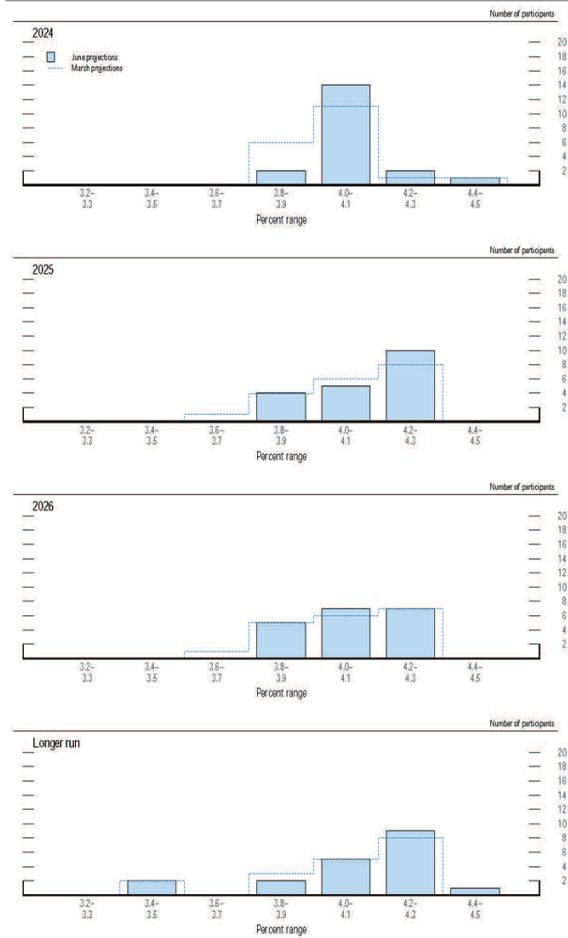
NOTE: Definitions of variables and other explanations are in the notes to table 1. The data for the actual values of the variables are annual.

Figure 3.A. Distribution of participants' projections for the change in real GDP, 2024–26 and over the longer run



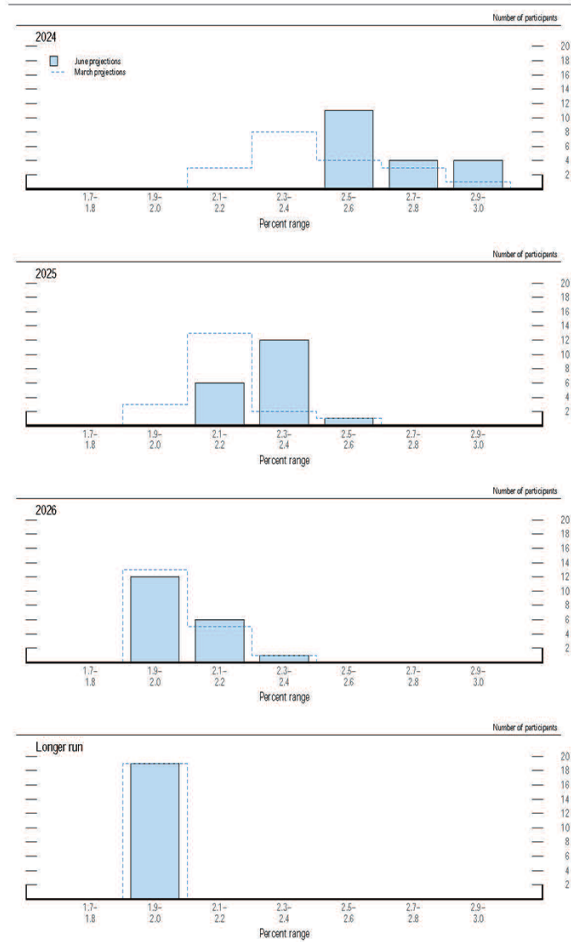
NOTE: Definitions of variables and other explanations are in the notes to table 1.

Figure 3.B. Distribution of participants' projections for the unemployment rate, 2024-26 and over the longer run



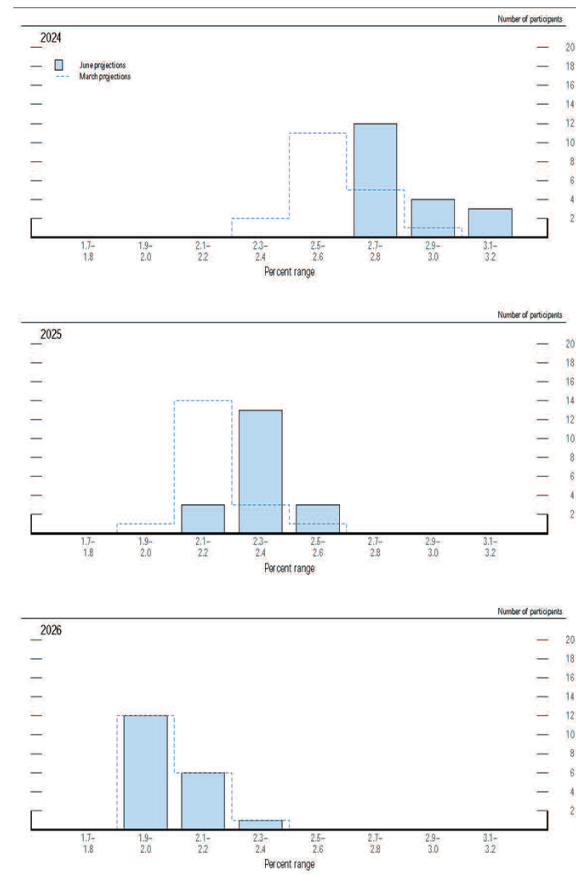
NOTE: Definitions of variables and other explanations are in the notes to table 1.

Figure 3.C. Distribution of participants' projections for PCE inflation, 2024–26 and over the longer run



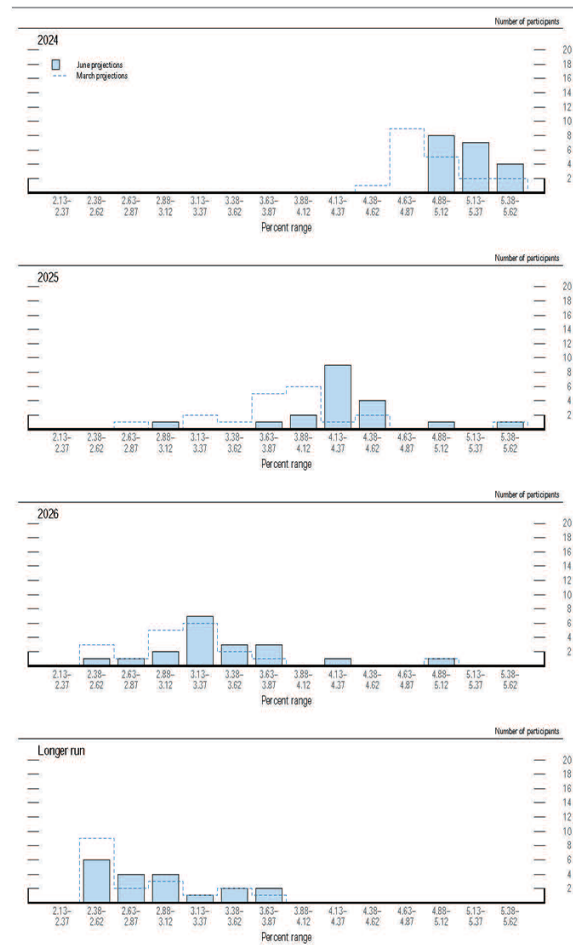
NOTE: Definitions of variables and other explanations are in the notes to table 1.

Figure 3.D. Distribution of participants' projections for core PCE inflation, 2024–26



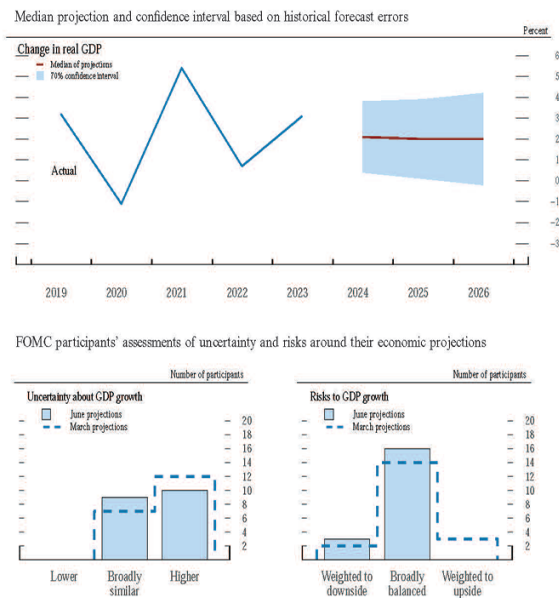
NOTE: Definitions of variables and other explanations are in the notes to table 1.

Figure 3.E. Distribution of participants' judgments of the midpoint of the appropriate target range for the federal funds rate or the appropriate target level for the federal funds rate, 2024–26 and over the longer run



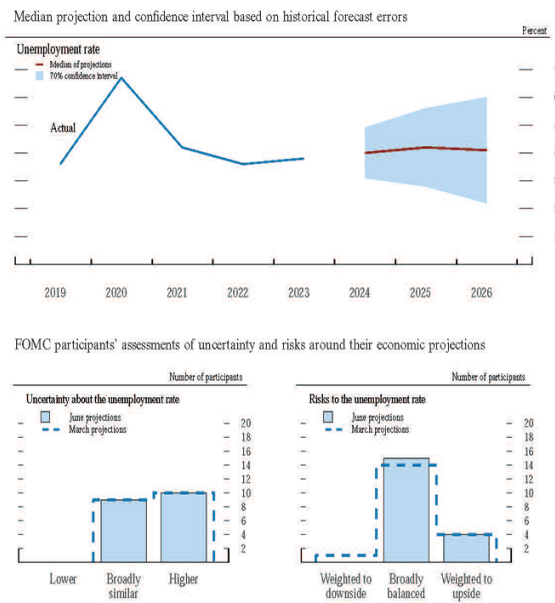
NOTE: Definitions of variables and other explanations are in the notes to table 1.

Figure 4.A. Uncertainty and risks in projections of GDP growth



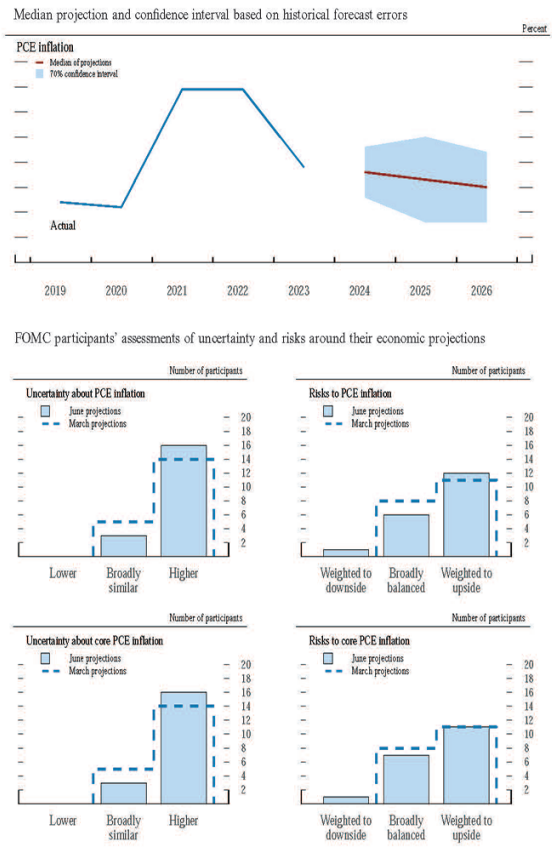
NOTE: The blue and red lines in the top panel show actual values and median projected values, respectively, of the percent change in real gross domestic product (GDP) from the fourth quarter of the previous year to the fourth quarter of the year indicated. The confidence interval around the median projected values is assumed to be symmetric and is based on root mean squared errors of various private and government forecasts made over the previous 20 years; more information about these data is available in table 2. Because current conditions may differ from those that prevailed, on average, over the previous 20 years, the width and shape of the confidence interval estimated on the basis of the historical forecast errors may not reflect FOMC participants' current assessments of the uncertainty and risks around their projections; these current assessments are summarized in the lower panels. Generally speaking, participants who judge the uncertainty about their projections as "broadly similar" to the average levels of the past 20 years would view the width of the confidence interval shown in the historical fan chart as largely consistent with their assessments of the uncertainty about their projections. Likewise, participants who judge the risks to their projections as "broadly balanced" would view the confidence interval around their projections as approximately symmetric. For definitions of uncertainty and risks in economic projections, see the box "Forecast Uncertainty."

Figure 4.B. Uncertainty and risks in projections of the unemployment rate



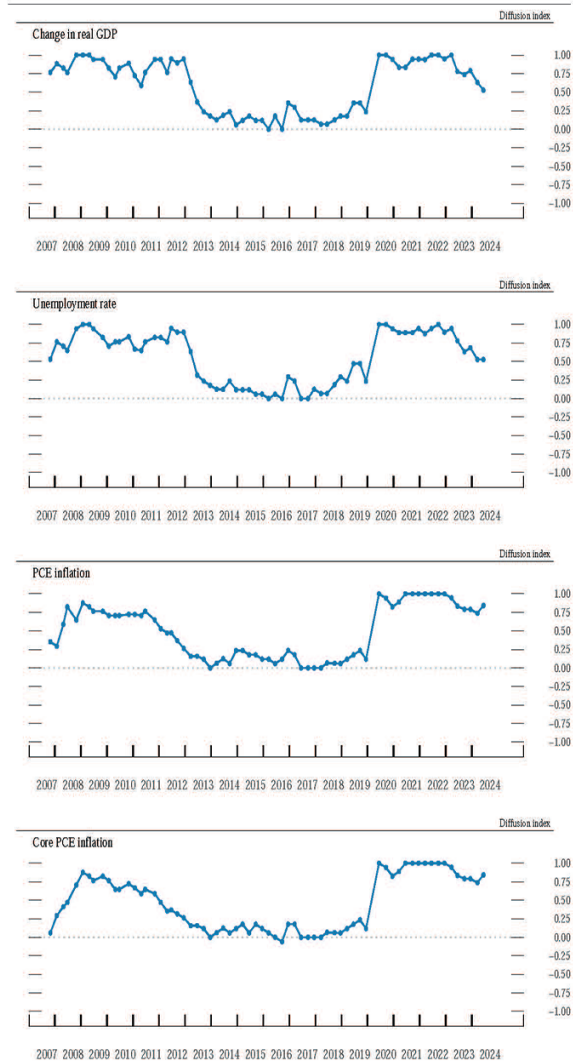
NOTE: The blue and red lines in the top panel show actual values and median projected values, respectively, of the average civilian unemployment rate in the fourth quarter of the year indicated. The confidence interval around the median projected values is assumed to be symmetric and is based on root mean squared errors of various private and government forecasts made over the previous 20 years; more information about these data is available in table 2. Because current conditions may differ from those that prevailed, on average, over the previous 20 years, the width and shape of the confidence interval estimated on the basis of the historical forecast errors may not reflect FOMC participants' current assessments of the uncertainty and risks around their projections; these current assessments are summarized in the lower panels. Generally speaking, participants who judge the uncertainty about their projections as "broadly similar" to the average levels of the past 20 years would view the width of the confidence interval shown in the historical fan chart as largely consistent with their assessments of the uncertainty about their projections. Likewise, participants who judge the risks to their projections as "broadly balanced" would view the confidence interval around their projections as approximately symmetric. For definitions of uncertainty and risks in economic projections, see the box "Forecast Uncertainty."

Figure 4.C. Uncertainty and risks in projections of PCE inflation



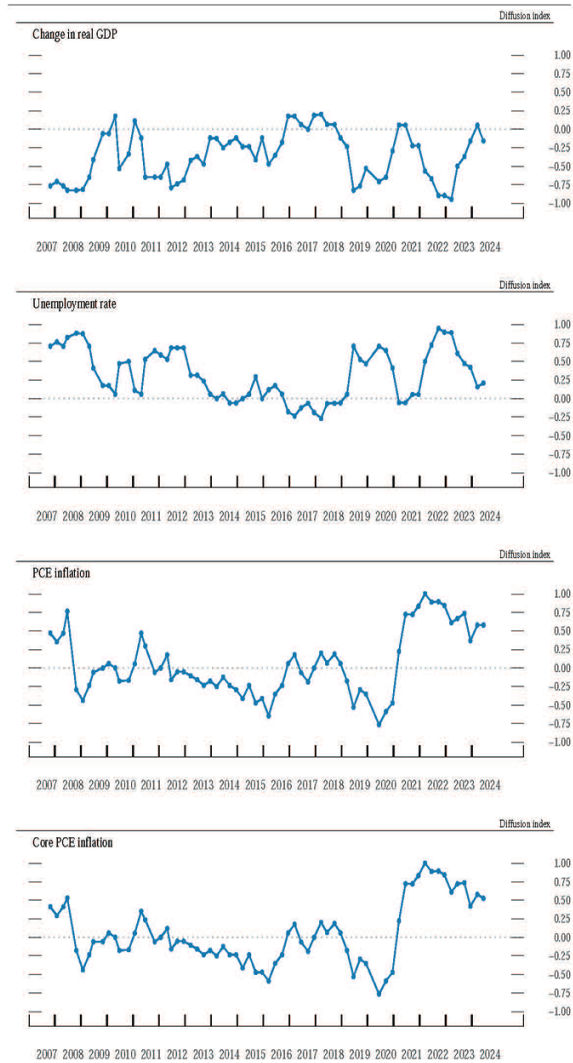
NOTE: The blue and red lines in the top panel show actual values and median projected values, respectively, of the percent change in the price index for personal consumption expenditures (PCE) from the fourth quarter of the previous year to the fourth quarter of the year indicated. The confidence interval around the median projected values is assumed to be symmetric and is based on root mean squared errors of various private and government forecasts made over the previous 20 years; more information about these data is available in table 2. Because current conditions may differ from those that prevailed, on average, over the previous 20 years, the width and shape of the confidence interval estimated on the basis of the historical forecast errors may not reflect FOMC participants' current assessments of the uncertainty and risks around their projections; these current assessments are summarized in the lower panels. Generally speaking, participants who judge the uncertainty about their projections as "broadly similar" to the average levels of the past 20 years would view the width of the confidence interval shown in the historical fan chart as largely consistent with their assessments of the uncertainty about their projections. Likewise, participants who judge the risks to their projections as "broadly balanced" would view the confidence interval around their projections as approximately symmetric. For definitions of uncertainty and risks in economic projections, see the box "Forecast Uncertainty."

Figure 4.D. Diffusion indexes of participants' uncertainty assessments



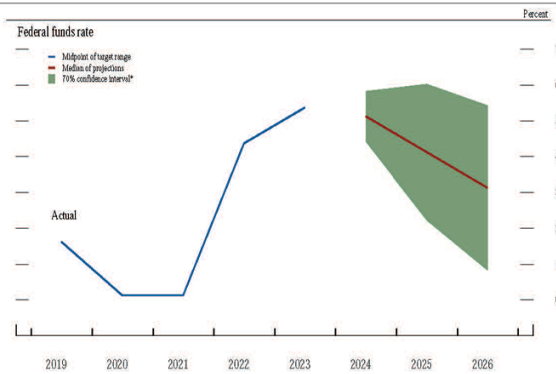
NOTE: For each SEP, participants provided responses to the question "Please indicate your judgment of the uncertainty attached to your projections relative to the levels of uncertainty over the past 20 years." Each point in the diffusion indexes represents the number of participants who responded "Higher" minus the number who responded "Lower," divided by the total number of participants. Figure excludes March 2020 when no projections were submitted.

Figure 4.E. Diffusion indexes of participants' risk weightings



NOTE: For each SEP, participants provided responses to the question "Please indicate your judgment of the risk weighting around your projections." Each point in the diffusion indexes represents the number of participants who responded "Weighted to the Upside" minus the number who responded "Weighted to the Downside," divided by the total number of participants. Figure excludes March 2020 when no projections were submitted.

Figure 5. Uncertainty and risks in projections of the federal funds rate



NOTE: The blue and red lines are based on actual values and median projected values, respectively, of the Committee's target for the federal funds rate at the end of the year indicated. The actual values are the midpoint of the target range; the median projected values are based on either the midpoint of the target range or the target level. The confidence interval around the median projected values is based on root mean squared errors of various private and government forecasts made over the previous 20 years. The confidence interval is not strictly consistent with the projections for the federal funds rate, primarily because these projections are not forecasts of the likeliest outcomes for the federal funds rate, but rather projections of participants' individual assessments of appropriate monetary policy. Still, historical forecast errors provide a broad sense of the uncertainty around the future path of the federal funds rate generated by the uncertainty about the macroeconomic variables as well as additional adjustments to monetary policy that may be appropriate to offset the effects of shocks to the economy.

The confidence interval is assumed to be symmetric except when it is truncated at zero - the bottom of the lowest target range for the federal funds rate that has been adopted in the past by the Committee. This truncation would not be intended to indicate the likelihood of the use of negative interest rates to provide additional monetary policy accommodation if doing so was judged appropriate. In such situations, the Committee could also employ other tools, including forward guidance and large-scale asset purchases, to provide additional accommodation. Because current conditions may differ from those that prevailed, on average, over the previous 20 years, the width and shape of the confidence interval estimated on the basis of the historical forecast errors may not reflect FOMC participants' current assessments of the uncertainty and risks around their projections.

* The confidence interval is derived from forecasts of the average level of short-term interest rates in the fourth quarter of the year indicated; more information about these data is available in table 2. The shaded area encompasses less than a 70 percent confidence interval if the confidence interval has been truncated at zero.

Table 2. Average historical projection error ranges
Percentage points

Variable	2024	2025	2026
Change in real GDP ¹	± 1.7	± 1.9	± 2.2
Unemployment rate ¹	± 0.9	± 1.4	± 1.9
Total consumer prices ²	± 1.0	± 1.7	± 1.4
Short-term interest rates ³	± 0.7	± 1.9	± 2.3

NOTE: Error ranges shown are measured as plus or minus the root mean squared error of projections for 2004 through 2023 that were released in the summer by various private and government forecasters. As described in the box "Forecast Uncertainty," under certain assumptions there is about a 70 percent probability that actual outcomes for real GDP, unemployment, consumer prices, and the federal funds rate will be in ranges implied by the average size of projection errors made in the past. For more information, see David Refshneider and Peter Tulp (2017), "Changing the Uncertainty of the Economic Outlook Using Historical Forecasting Errors: The Federal Reserve's Approach," Finance and Economics Discussion Series 2017-020 (Washington: Board of Governors of the Federal Reserve System, February), <https://dx.doi.org/10.17016/FEDS.2017.020>.

1. Definitions of variables are in the general note to table 1.
2. Measure is the overall consumer price index, the price measure that has been most widely used in government and private economic forecasts. Projections are percent changes on a fourth quarter to fourth quarter basis.
3. For Federal Reserve staff forecasts, measure is the federal funds rate. For other forecasts, measure is the rate on 3-month Treasury bills. Projection errors are calculated using average levels, in percent, in the fourth quarter.

Forecast Uncertainty

The economic projections provided by the members of the Board of Governors and the presidents of the Federal Reserve Banks inform discussions of monetary policy among policymakers and can aid public understanding of the basis for policy actions. Considerable uncertainty attends these projections, however. The economic and statistical models and relationships used to help produce economic forecasts are necessarily imperfect descriptions of the real world, and the future path of the economy can be affected by myriad unforeseen developments and events. Thus, in setting the stance of monetary policy, participants consider not only what appears to be the most likely economic outcome as embodied in their projections, but also the range of alternative possibilities, the likelihood of their occurring, and the potential costs to the economy should they occur.

Table 2 summarizes the average historical accuracy of a range of forecasts, including those reported in past *Monetary Policy Reports* and those prepared by the Federal Reserve Board's staff in advance of meetings of the Federal Open Market Committee (FOMC). The projection error ranges shown in the table illustrate the considerable uncertainty associated with economic forecasts. For example, suppose a participant projects that real gross domestic product (GDP) and total consumer prices will rise steadily at annual rates of, respectively, 3 percent and 2 percent. If the uncertainty attending those projections is similar to that experienced in the past and the risks around the projections are broadly balanced, the numbers

reported in table 2 would imply a probability of about 70 percent that actual GDP would expand within a range of 1.3 to 4.7 percent in the current year, 1.1 to 4.9 percent in the second year, and 0.8 to 5.2 percent in the third year. The corresponding 70 percent confidence intervals for overall inflation would be 1.0 to 3.0 percent in the current year, 0.3 to 3.7 percent in the second year, and 0.6 to 3.4 percent in the third year. Figures 4.A through 4.C illustrate these confidence bounds in "fan charts" that are symmetric and centered on the medians of FOMC participants' projections for GDP growth, the unemployment rate, and inflation. However, in some instances, the risks around the projections may not be symmetric. In particular, the unemployment rate cannot be negative; furthermore, the risks around a particular projection might be tilted to either the upside or the downside, in which case the corresponding fan chart would be asymmetrically positioned around the median projection.

Because current conditions may differ from those that prevailed, on average, over history, participants provide judgments as to whether the uncertainty attached to their projections of each economic variable is greater than, smaller than, or broadly similar to typical levels of forecast uncertainty seen in the past 20 years, as presented in table 2 and reflected in the widths of the confidence intervals shown in the top panels of figures 4.A through 4.C. Participants' current assessments of the uncertainty surrounding their projections are summarized in the bottom-left panels

(continued)

of those figures. Participants also provide judgments as to whether the risks to their projections are weighted to the upside, are weighted to the downside, or are broadly balanced. That is, while the symmetric historical fan charts shown in the top panels of figures 4.A through 4.C imply that the risks to participants' projections are balanced, participants may judge that there is a greater risk that a given variable will be above rather than below their projections. These judgments are summarized in the lower-right panels of figures 4.A through 4.C.

As with real activity and inflation, the outlook for the future path of the federal funds rate is subject to considerable uncertainty. This uncertainty arises primarily because each participant's assessment of the appropriate stance of monetary policy depends importantly on the evolution of real activity and inflation over time. If economic conditions evolve in an unexpected manner, then assessments of the appropriate setting of the federal funds rate would change from that point forward. The final line in table 2 shows the error ranges for forecasts of short-term interest rates. They suggest that the historical confidence intervals associated with projections of the federal funds rate are quite wide. It should be noted, however, that these confidence intervals are not strictly consistent with the projections for the federal funds rate, as these projections are not forecasts of the most likely quarterly outcomes but rather are projections of participants' individual

assessments of appropriate monetary policy and are on an end-of-year basis. However, the forecast errors should provide a sense of the uncertainty around the future path of the federal funds rate generated by the uncertainty about the macroeconomic variables as well as additional adjustments to monetary policy that would be appropriate to offset the effects of shocks to the economy.

If at some point in the future the confidence interval around the federal funds rate were to extend below zero, it would be truncated at zero for purposes of the fan chart shown in figure 5; zero is the bottom of the lowest target range for the federal funds rate that has been adopted by the Committee in the past. This approach to the construction of the federal funds rate fan chart would be merely a convention; it would not have any implications for possible future policy decisions regarding the use of negative interest rates to provide additional monetary policy accommodation if doing so were appropriate. In such situations, the Committee could also employ other tools, including forward guidance and asset purchases, to provide additional accommodation.

While figures 4.A through 4.C provide information on the uncertainty around the economic projections, figure 1 provides information on the range of views across FOMC participants. A comparison of figure 1 with figures 4.A through 4.C shows that the dispersion of the projections across participants is much smaller than the average forecast errors over the past 20 years.

ABBREVIATIONS

AFE	advanced foreign economy
AI	artificial intelligence
BOJ	Bank of Japan
BTFP	Bank Term Funding Program
CBO	Congressional Budget Office
CES	Current Employment Statistics
COVID-19	coronavirus disease 2019
CPI	consumer price index
CRE	commercial real estate
DI	depository institution
EFFR	effective federal funds rate
ELB	effective lower bound
EME	emerging market economy
EPOP ratio	employment-to-population ratio
FOMC	Federal Open Market Committee; also, the Committee
GDI	gross domestic income
GDP	gross domestic product
JOLTS	Job Openings and Labor Turnover Survey
LFPR	labor force participation rate
MBS	mortgage-backed securities
MMF	money market fund
NFIB	National Federation of Independent Business
OER	owners' equivalent rent
ON RRP	overnight reverse repurchase agreement
OPEC	Organization of the Petroleum Exporting Countries
PCE	personal consumption expenditures
QCEW	Quarterly Census of Employment and Wages
SEP	Summary of Economic Projections
SLOOS	Senior Loan Officer Opinion Survey on Bank Lending Practices
SOMA	System Open Market Account
S&P	Standard & Poor's
VIX	implied volatility for the S&P 500 index





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July 9, 2024

The Honorable Sherrod Brown
 Chairman
 Committee on Banking, Housing,
 and Urban Affairs
 United States Senate
 Washington, DC 20510

The Honorable Tim Scott
 Ranking Member
 Committee on Banking, Housing,
 and Urban Affairs
 United States Senate
 Washington, DC 20510

Re: Today's Hearing: "The Semiannual Monetary Policy Report to the Congress"

Dear Chairman Brown and Ranking Member Scott:

On behalf of America's Credit Unions, I am writing regarding the Committee's hearing entitled, "The Semiannual Monetary Report to the Congress." America's Credit Unions is the voice of consumers' best option for financial services: credit unions. We advocate for policies that allow the industry to effectively meet the needs of their over 140 million members nationwide.

As you prepare to hear from the Federal Reserve Chairman, America's Credit Unions wants to reiterate that we strongly oppose the Federal Reserve Board's (the Board) recently proposed rule to drastically reduce the Regulation II debit interchange fee cap. This proposal is seriously flawed. A skewed methodology for assessing base component costs fails to give appropriate weight to the cost experience of most covered issuers, especially credit unions. Additionally, the Notice of Proposed Rulemaking (NPRM) does not consider the market impact of recent amendments which went into effect in July 2023, requiring dual routing for card-not-present transactions. The July 2023 amendments and resulting changes in merchant routing behavior will have a direct bearing on the overall monetary impact of the revised interchange fee cap for both covered and exempt issuers.

The Board is not required to lower the debit interchange fee cap. The Durbin Amendment directed the Board to establish a cap that was "reasonable and proportional" to the costs of the issuer. In 2011, the Board determined that the cap met this standard when only 80 percent of covered debit card issuers would see cost recovery for their authorization, clearance, and settlement (ACS) costs—the largest banks. The latest data collection shows only 77.4 percent of debit card issuers are experiencing full recovery of ACS costs—once again leaving high-cost, low-volume issuers, including many credit unions, operating at a deficit. If anything, this data suggests the interchange fee cap should be raised, not lowered.

The small financial institution exemption does not work. Downward market pressure on interchange fees driven by the largest issuers cannot be contained by regulatory thresholds. The Federal Reserve's Regulation II data indicates the average per transaction interchange fee for

July 9, 2024
Page 2 of 2

exempt single-message debit transactions is down nearly 31 percent in inflation-adjusted dollars from 2011 to 2021.

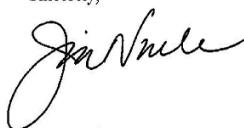
Merchants did not pass on their cost savings to consumers from the initial regulation. They will not pass it along with further cuts. Research conducted by the Federal Reserve Bank of Richmond shows that only about 1 percent of merchants passed savings on to consumers after the initial adoption of Regulation II and more than 20 percent increased their prices. The Electronic Fund Transfer Act (EFTA) requires the Federal Reserve to consider the impact of its regulations on consumers, and research shows that consumers were harmed when the debit interchange fee cap was introduced as costs were passed on by issuers.

Consumers lost with the first regulation and will continue to lose with further reductions. The Government Accountability Office ranks the Durbin Amendment "among the top five laws and regulations most cited...as having significantly affected the cost and availability of basic banking services." One study has estimated \$1-3 billion in annual transfers from low-income households to large retailers and their shareholders due to the Durbin Amendment.

We urge the Committee to support S. 4570, the Secure Payments Act, and call for the Board to withdraw this flawed proposal.

On behalf of America's Credit Unions and their over 140 million credit unions members, thank you for holding today's hearing. We look forward to continuing to work with you to create an environment where credit unions can thrive.

Sincerely,



Jim Nussle, CUDE
President & CEO

cc: Members of the Committee on Banking, Housing, and Urban Affairs



July 8, 2024

US Senator Sherrod Brown
503 Hart Senate Office Building
Washington, DC 20510

US Senator Tim Scott
104 Hart Senate Office Building
Washington, DC 20510

Honorable Senators Brown and Scott:

The City of Springfield, Ohio is facing a significant housing crisis in our community. Many factors have played in to where we are today, but without significant support at the Federal level, I believe, that the situation and the need for housing in our community will become much worse.

The City of Springfield and its partners have been proactively working towards solutions for this crisis since a Housing Consortium made up of both public and private sector leaders formed in 2018. This led to two macro-level studies focused on addressing the housing situation prepared by the Greater Ohio Policy Center on behalf of Springfield. This identified the challenges that Springfield's Housing Market faced, while also identifying key initiatives, policies, and programs that our community could implement to address the situation.

Many of the recommendations have been adopted and put into practice, and we have seen positive results. But most recently, Springfield has seen a surge in population through immigration that has significantly impacted our ability as a community to produce enough housing opportunities for all. Springfield's Haitian population has increased to 15,000 – 20,000 over the last four years in a community of just under 60,000 previous residents, putting a significant strain on our resources and ability to provide ample housing for all of our residents. Despite 2000 additional housing units set to come online over the next three to five years, this is still not enough.

Again, without further support at the Federal level, communities like Springfield are set up to fail in being able to meet the housing needs of its residents.

Sincerely,

City Manager

CC: US Senator JD Vance