TREASURY AND FEDERAL RESERVE FOREIGN EXCHANGE OPERATIONS

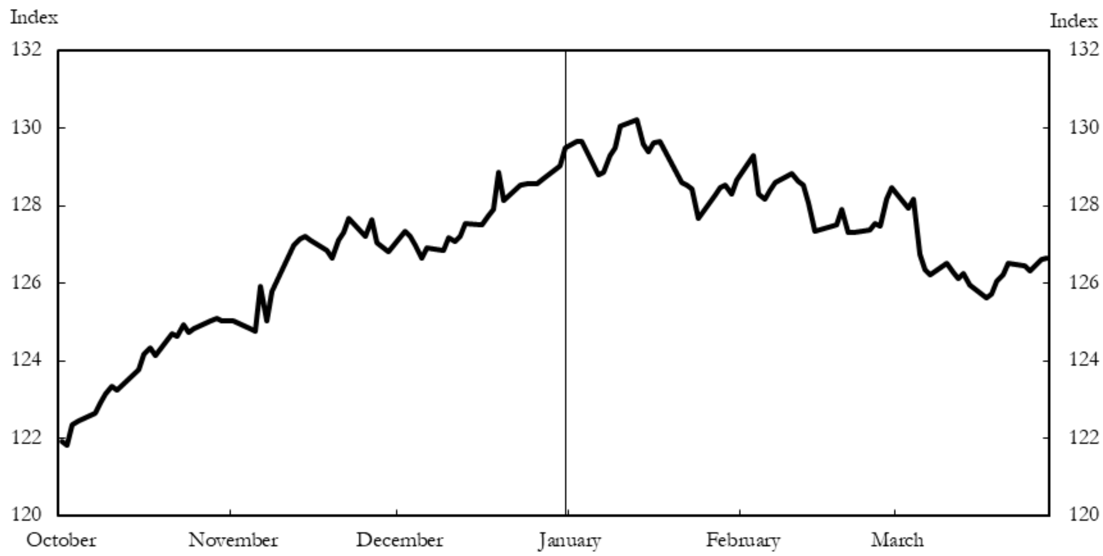
January – March 2025

During the first quarter of 2025, the U.S. dollar, as measured by the Federal Reserve Board's broad trade-weighted dollar index, depreciated 2 percent on net, partially retracing its notable appreciation leading up to and following the U.S. presidential election in the last quarter of 2024. The dollar depreciated against most advanced economy and emerging market currencies in the first quarter. Market contacts reported that the dollar's depreciation was driven by a narrowing in interest rate differentials between the U.S. and the rest of the world, a downward shift in the outlook for U.S. growth relative to the rest of the world and particularly Europe, and a rise in uncertainty related to the new U.S. administration's trade policies. On net over the period, these factors contributed to lower Treasury yields while the Federal Reserve's path of policy was mostly unchanged. On a bilateral basis, the dollar depreciated 4.3 percent against the euro, accounting for almost half of the overall broad dollar move, and 4.6 percent against the Japanese yen. The Federal Reserve and U.S. Treasury did not intervene in foreign exchange markets during the quarter.

This report, presented by Roberto Perli, Federal Reserve Bank of New York System Open Market Account Manager, describes the foreign exchange operations of the U.S. Department of the Treasury and the Federal Reserve System for the period from January through March 2025. Thomas Campbell was primarily responsible for preparation of the report.

Chart 1

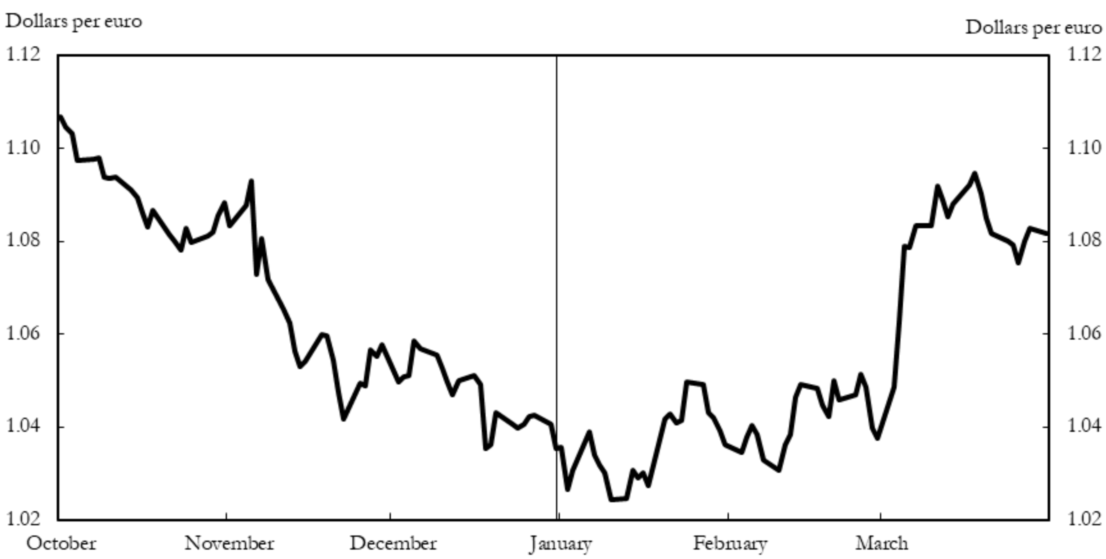
BROAD TRADE-WEIGHTED U.S. DOLLAR INDEX



Sources: Board of Governors of the Federal Reserve System; Bloomberg L.P.

Chart 2

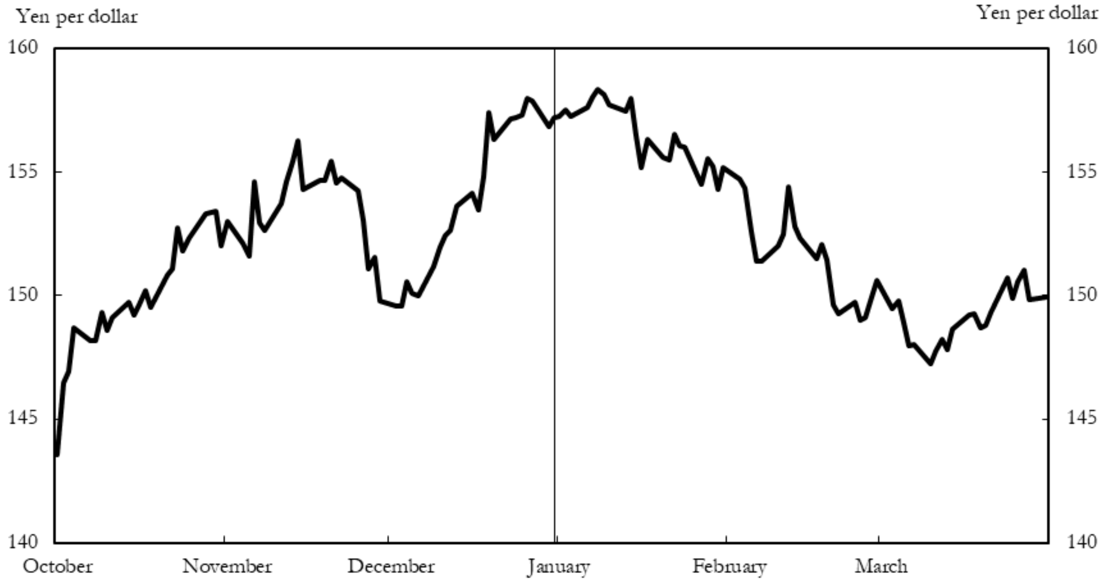
EURO–U.S. DOLLAR EXCHANGE RATE



Source: Bloomberg L.P.

Chart 3

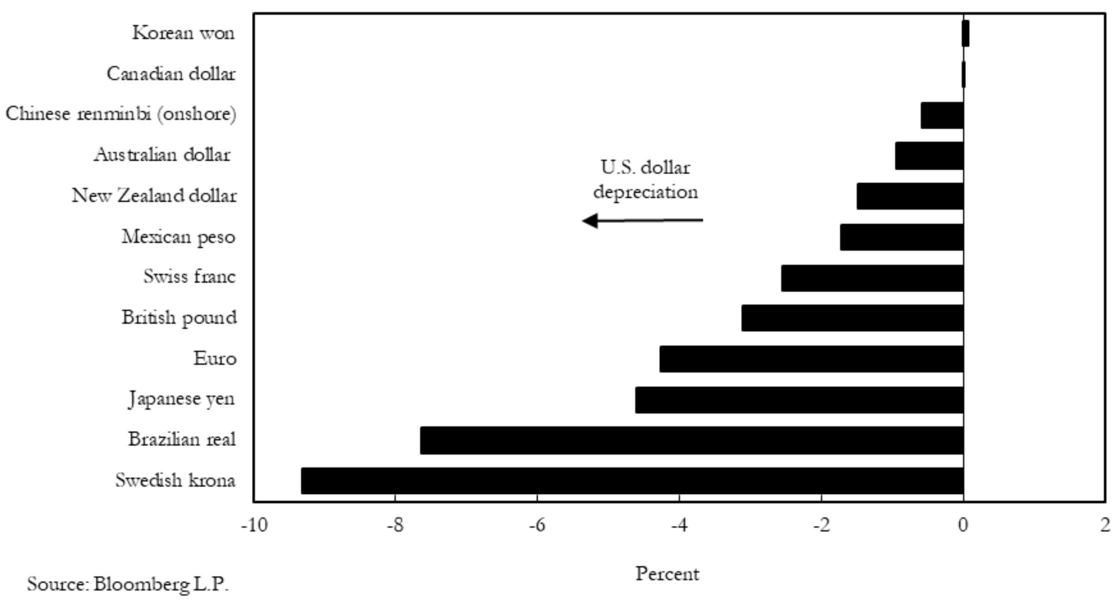
U.S. DOLLAR–YEN EXCHANGE RATE



Source: Bloomberg L.P.

Chart 4

U.S. DOLLAR PERFORMANCE AGAINST ADVANCED AND EMERGING MARKET CURRENCIES DURING THE FIRST QUARTER



Source: Bloomberg L.P.

U.S. DOLLAR DEPRECIATES ON EXPECTATIONS FOR LOWER U.S. GROWTH AND UNCERTAINTY AROUND U.S. TRADE POLICY

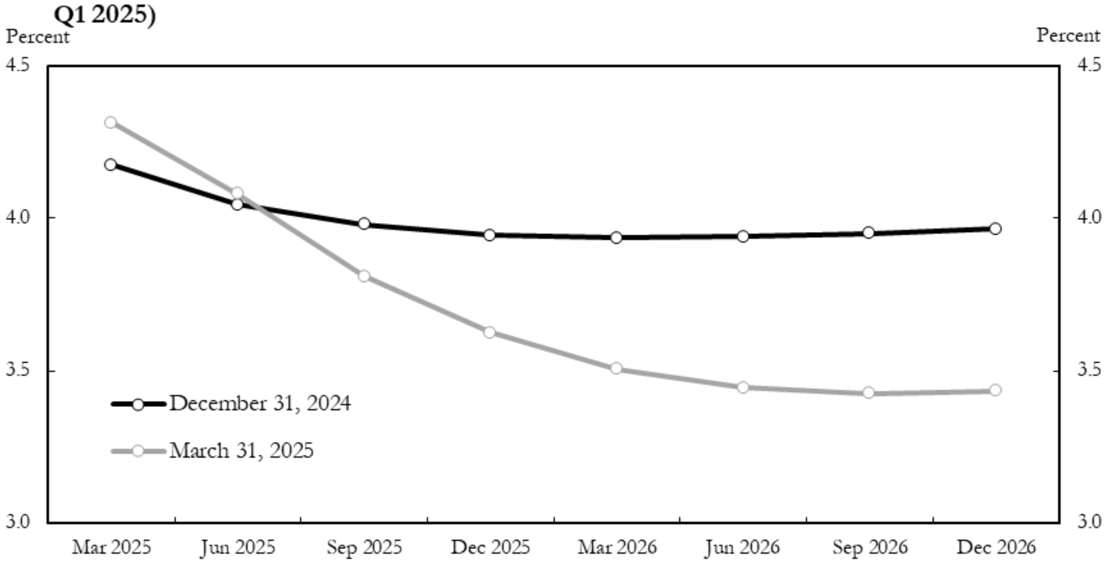
During the first quarter of 2025, the U.S. dollar, as measured by the Federal Reserve Board's broad trade-weighted dollar index, depreciated 2 percent on net, partially retracing the notable appreciation observed leading up to and following the U.S. election in late 2024. In the first quarter, the dollar depreciated against most advanced economy currencies, accounting for roughly three-quarters of the broad dollar move. The dollar also depreciated against most emerging market currencies. Market contacts reported that the dollar's depreciation was driven by a downward shift in the outlook for U.S. growth relative to the rest of the world and particularly Europe, and a rise in uncertainty related to the new U.S. administration's trade policies. On net, nominal two-year Treasury yields fell by 36 basis points over the quarter, driving a narrowing of interest rate differentials in favor of most foreign jurisdictions and supporting dollar depreciation. Furthermore, foreign exchange markets exhibited heightened volatility in the first quarter, particularly in currencies perceived as directly affected by U.S. trade policy, such as the Canadian dollar and the Mexican peso.

U.S. economic data during the quarter were broadly indicative of continued growth, labor market stability, and slowing disinflation. However, market participants were also attentive to signs of weakness in "soft," or survey, data, which showed notable increases in consumer inflation expectations and declines in consumer sentiment and business investment.

The Federal Open Market Committee (FOMC) maintained its federal funds target range at 4.25 to 4.50 percent at both the January and March meetings, in line with market expectations. Contacts interpreted Federal Reserve communications as suggesting that the FOMC views the current policy rate as well-positioned to respond to risks to both higher inflation and a decline in growth output as they wait for greater clarity on the economic outlook. While the median expected federal funds rate for year-end 2025 was unchanged in the Summary of Economic Projections released at the March FOMC meeting, GDP expectations were notably lower, contributing to the decline in Treasury yields. Implied yields from federal funds futures for year-end 2025 declined by 28 basis points, as markets increased the cumulative amount of easing priced for 2025 from 42 basis points at the end of December to 70 basis points at the end of March.

Chart 5

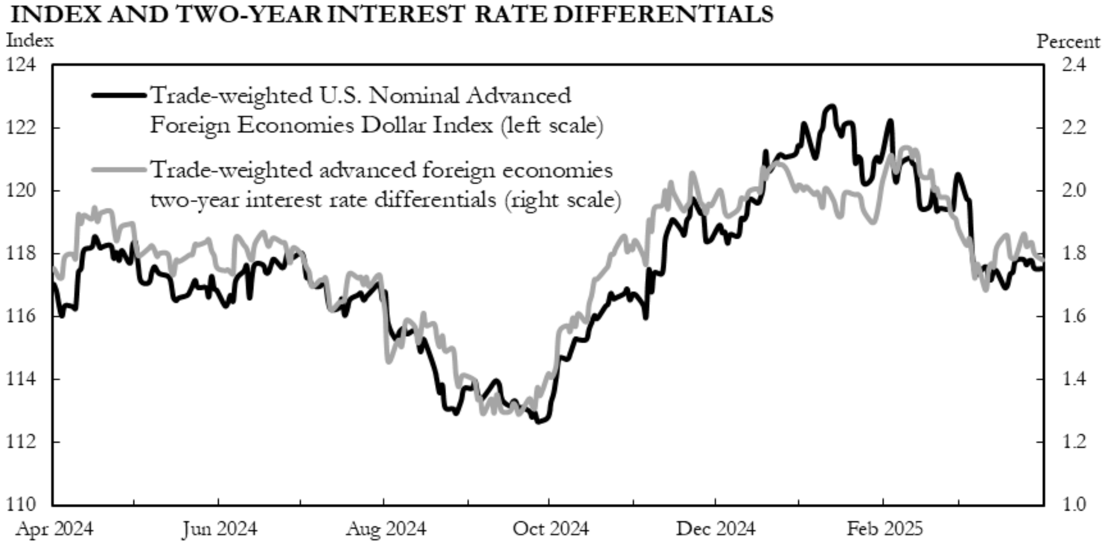
SOFR FUTURES-IMPLIED PATH OF FOMC POLICY (Q4 2024 VERSUS Q1 2025)



Source: Bloomberg L.P.

Chart 6

U.S TRADE-WEIGHTED ADVANCED FOREIGN ECONOMIES DOLLAR INDEX AND TWO-YEAR INTEREST RATE DIFFERENTIALS



Sources: Bloomberg L.P.; New York Fed staff calculations.

U.S DOLLAR DEPPRECIATES AGAINST EURO AMID NARROWING IN U.S.–EURO AREA INTEREST RATE DIFFERENTIALS AND PROPOSED INCREASES IN EUROPEAN FISCAL SPENDING

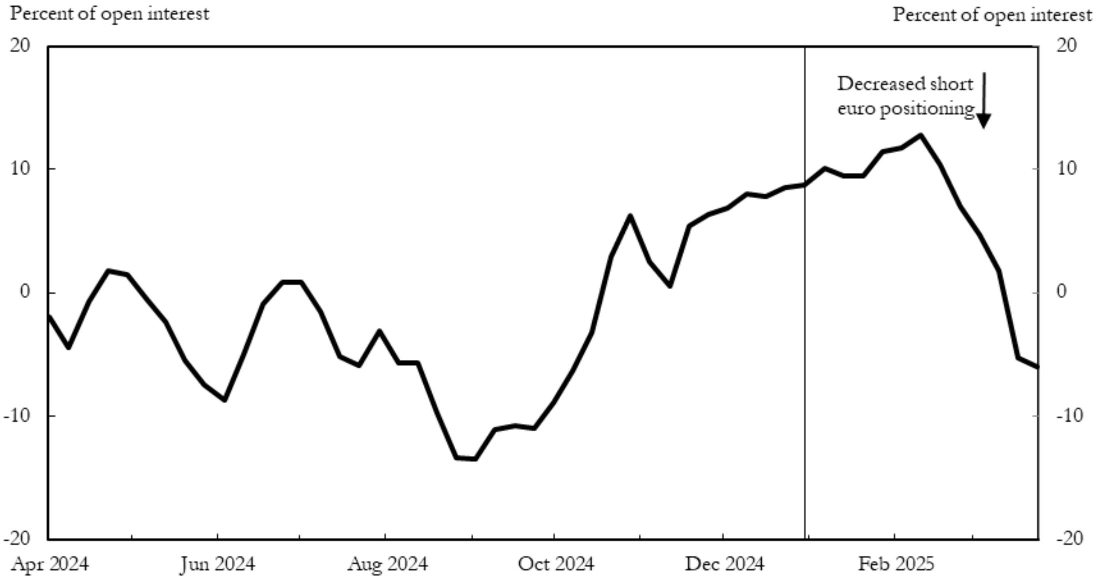
The dollar depreciated 4.3 percent against the euro over the first quarter, which market participants generally attributed to a narrowing in U.S.–euro area interest rate differentials in favor of the euro area. Euro area yields were supported by a proposal from the newly established German government to relax defense spending constraints and to establish a fund for infrastructure investment. The proposals, which were signed into law at the end of the quarter, were generally viewed by market participants as enhancing Germany's ability to respond to defense and infrastructure needs, buoying euro area growth forecasts, while the outlook for growth in the U.S. had declined. Market participants also noted euro appreciation in the context of shifting views on the economic impact of U.S. tariff policy, contributing to expectations for slower growth in the U.S. relative to expectations for stronger growth in the euro area. Concurrent with the rise in the euro relative to the dollar, the Swedish krona appreciated 10.3 percent against the dollar as Swedish defense companies are expected to benefit from the anticipated rise in military expenditures in Europe.

Euro area economic data prints in the first quarter were suggestive of continued disinflation while the market revised its euro area growth expectations higher. Against this backdrop and as was widely expected, the European Central Bank (ECB) reduced its policy rate by 25 basis points at both its January and March meetings. On net over the quarter, two-year U.S.–German interest rate differentials narrowed by about 33 basis points, driven primarily by decreases in U.S. Treasury yields, which further supported the euro.

Consistent with market expectations for continued euro strength over the quarter, Commodity Futures Trading Commission data showed a notable decrease in short euro positioning against the dollar, with speculative short euro futures market positioning reversing and ending the quarter near neutral levels against the dollar.

Chart 7

U.S. DOLLAR NET LONG POSITIONING AGAINST EURO



Sources: Commodity Futures Trading Commission; Bloomberg L.P.

U.S. DOLLAR DEPRECIATES AGAINST JAPANESE YEN AMID NARROWING INTEREST RATE DIFFERENTIALS AND RISING BOJ TERMINAL RATE EXPECTATIONS

The dollar depreciated 4.6 percent against the Japanese yen amid a narrowing of U.S.–Japan interest rate differentials. On net over the quarter, ten-year U.S.–Japan interest rate differentials narrowed by about 76 basis points, driven by the concurrent rise in Japanese government bond yields and decline in U.S. Treasury yields. The yen was also supported by Bank of Japan (BOJ) communications that were viewed by market participants as reinforcing expectations for the central bank to continue raising rates. Core measures of inflation accelerated throughout the quarter amid rising food prices, while early spring wage negotiations indicated a continuation of strong wage growth, both of which supported rising expectations for further BOJ rate increases. The BOJ raised its policy rate 25 basis points at its January meeting and held it unchanged at its March meeting. Expectations for the BOJ's terminal rate increased by around 30 basis points to around 1.1 percent during the quarter, contributing to the narrowing of interest rate differentials.

U.S. DOLLAR DEPRECIATES AGAINST BRITISH POUND AMID NARROWING IN U.S.–U.K. GROWTH DIFFERENTIALS

The dollar depreciated 3.1 percent against the British pound over the first quarter. Contacts were attentive to stronger-than-expected U.K. GDP for the fourth quarter of 2024, continued strength in wage growth coupled with a steady unemployment rate, and mixed inflation data over the quarter. U.K. growth expectations were revised slightly higher over the quarter, while U.S. growth expectations were revised slightly lower. Over the quarter, the two-year U.K.–U.S. yield differential widened by 18 basis points as the decline in Treasury yields outpaced the fall in gilt yields, further supporting the pound.

As was widely expected, the Bank of England lowered its policy rate by 25 basis points at its January meeting and subsequently voted to leave policy rates unchanged at its March meeting. Market participants were attentive to the statement's language at the March meeting reaffirming a gradual and careful approach to the further removal of policy restraint, interpreting the addition of the word "careful" as an acknowledgement of increased domestic and global uncertainty.

U.S. DOLLAR DEPRECIATES AGAINST MOST EMERGING MARKET CURRENCIES AMID FALLING U.S. TREASURY YIELDS AND U.S. TARIFF POLICY UNCERTAINTY

The dollar depreciated 1.1 percent against emerging market currencies during the first quarter, as measured by the Federal Reserve's trade-weighted Emerging Market Economies Dollar Index. Market contacts reported that the dollar depreciation was primarily driven by delays in the implementation of previously announced tariffs, market participants' perception of ongoing U.S. trade policy uncertainty, the overall decline in Treasury yields, and idiosyncratic foreign economic developments.

In Asia, the dollar depreciated 0.6 percent and 1.0 percent against the onshore and offshore Chinese renminbi, respectively, moves that market participants attributed to increased uncertainty around U.S. tariff policy, mixed Chinese economic data, and ongoing uncertainty around the impact of announced stimulus measures and expected future stimulus measures on the nation's growth outlook. Market participants were attentive to developments surrounding China's growth outlook, with some analysts uncertain over how meaningful positive initial signs in consumer sentiment and trade were given seasonal spikes associated with the Lunar New Year holiday as well as export frontloading in advance of tariff implementation. Market participants were also attentive to the People's Bank of China's (PBOC) setting of the daily dollar–renminbi fixing,[1] which was both marginally stronger over the

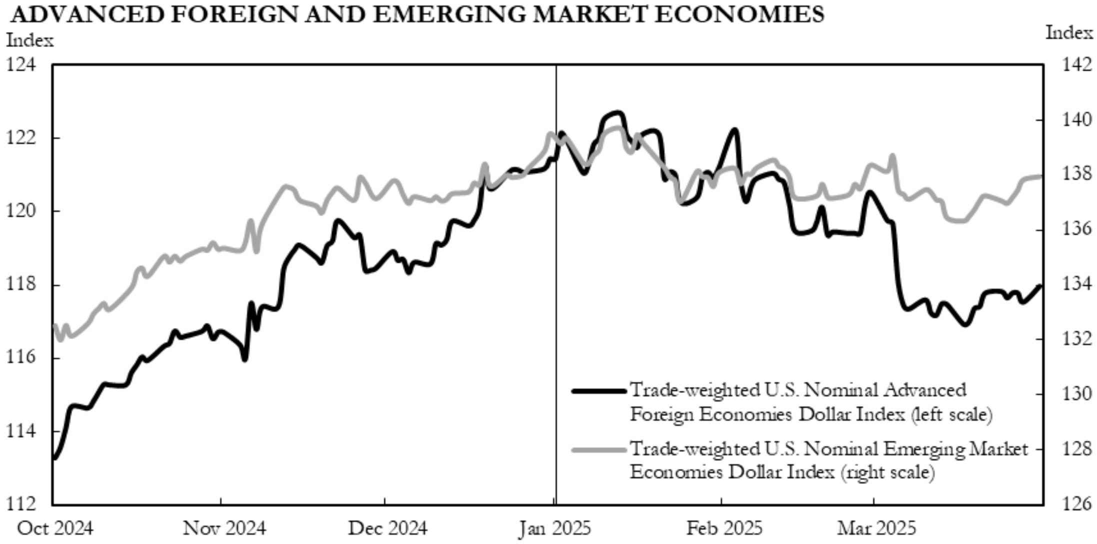
[1] The U.S. dollar–Chinese renminbi fixing is an administered rate set by the PBOC, published daily, and represents the midpoint of the +/- 2 percent daily trading band within which the USD–CNY exchange rate is managed.

quarter and stronger than market participants had anticipated given some expectations for currency depreciation to offset trade-related pressures.

The dollar depreciated against most Latin American currencies over the quarter, including by 1.7 percent against the Mexican peso, as Mexico was perceived as being a major focus of U.S. tariff policy throughout the quarter. The dollar depreciated 7.6 percent against the Brazilian real, as the currency rebounded from its late-fourth-quarter 2024 lows amid an easing of corporate outflows and government implementation of some fiscal consolidation measures.

Chart 8

U.S. TRADE-WEIGHTED DOLLAR PERFORMANCE VERSUS ADVANCED FOREIGN AND EMERGING MARKET ECONOMIES

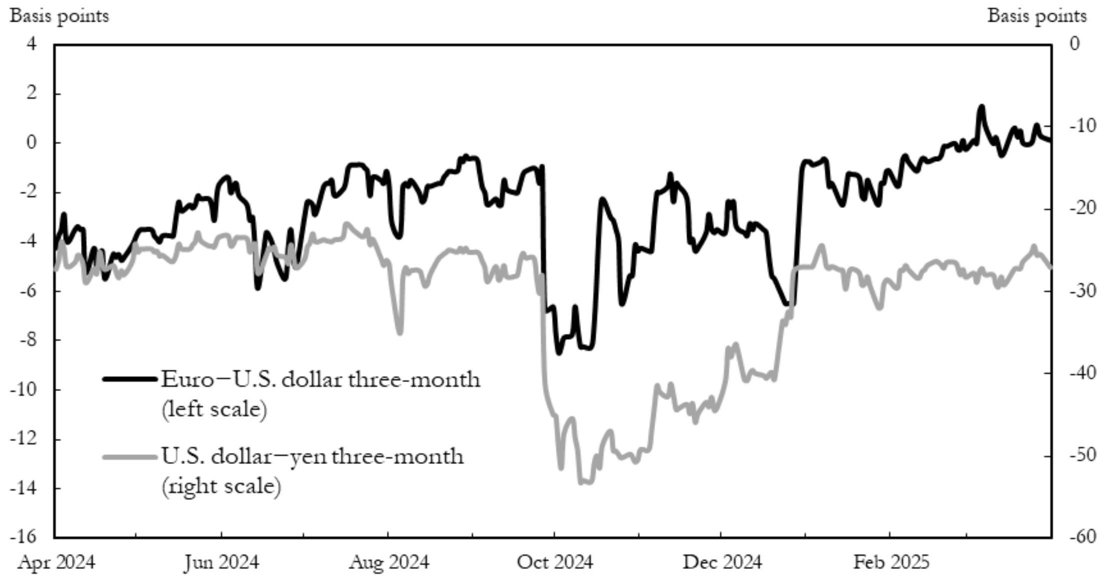


Sources: Board of Governors of the Federal Reserve System; Bloomberg L.P.

OFFSHORE U.S. DOLLAR FUNDING CONDITIONS REMAIN STABLE

Global offshore dollar funding conditions, particularly in the foreign exchange swap market, were stable during the first quarter amid abundant dollar funding liquidity. Foreign exchange swap-implied U.S. dollar borrowing premiums in major currency pairs remained generally low, with three-month foreign exchange swap basis spreads in the euro–dollar and dollar–yen pairs trading at historically tight levels of around 0 and 30 basis points, respectively. Over the quarter-end turn, short-dated foreign exchange swap basis spreads for some currency pairs, including the dollar–yen, increased modestly. These moves retraced following the turn and were generally characterized as typical of quarter-end trading conditions.

Chart 9
FOREIGN EXCHANGE THREE-MONTH SWAP-IMPLIED BASIS SPREADS



Source: Bloomberg L.P.

U.S. DOLLAR LIQUIDITY SWAP ARRANGEMENTS WITH FOREIGN CENTRAL BANKS

Aggregate swaps outstanding of the U.S. dollar liquidity swap arrangements with foreign central banks declined from $1.1 billion at the end of the fourth quarter of 2024 to $0.1 billion at the end of the first quarter of 2025, in line with comparable periods in the prior two years. The decrease reflected the maturities of swaps that had been originated in the fourth quarter of 2024. All outstanding central bank liquidity swaps at the end of March were with the ECB, while the BOJ, Bank of England, Swiss National Bank, and Bank of Canada had no U.S. dollar swaps outstanding.

TREASURY AND FEDERAL RESERVE FOREIGN EXCHANGE HOLDINGS

The Federal Reserve and U.S. Treasury did not undertake any foreign exchange intervention operations during the quarter. As of March 31, the value of the Federal Reserve System Open Market Account (SOMA) foreign-currency-denominated assets totaled $18.3 billion, comprised of euro- and yen-denominated holdings. The value of the U.S. Treasury's Exchange Stabilization Fund (ESF) foreign-currency-denominated assets also totaled $18.3 billion, comprised of euro and yen holdings.

Foreign Exchange Reserve Holdings

The Federal Reserve and U.S. Treasury invest their foreign currency reserves, which are held in the SOMA and the ESF, in a variety of instruments that yield market rates of return in their respective currencies and have a high degree of liquidity and credit quality. The Authorization for Foreign Currency Operations defines the permitted investments for the SOMA foreign currency portfolio. The Open Market Trading Desk of the Federal Reserve Bank of New York (the Desk) utilizes an investment framework for the management of the foreign currency assets. The framework involves a routine affirmation of objectives and constraints from policymakers. The Desk then utilizes an investment approach designed to meet those objectives to maximize return subject to maintaining sufficient liquidity and a high degree of safety.[2]

In terms of investment eligibility, the Federal Reserve and U.S. Treasury's foreign exchange reserves can be invested in German, French, Dutch, and Japanese government obligations; purchases of obligations of European sovereign issuers eligible to be held outright under agreements for repurchase of such securities; and in instruments at official institutions, such as the Bank for International Settlements and foreign central banks. To the greatest extent practicable, the investments are split evenly between the SOMA and the ESF.

As of March 31, 2025, the U.S. dollar value of euro-denominated deposits and government securities held by the SOMA and the ESF increased to $24.2 billion from $23.0 billion on December 31, 2024, and the U.S. dollar value of yen-denominated deposits and government securities increased to $12.5 billion from $11.9 billion on December 31, 2024. These changes were largely driven by foreign exchange translation effects.

[2] Consistent with the current Authorization for Foreign Currency Operations, the Desk conducts small-value exercises for the foreign currency reserves as a matter of prudent advance planning. No inference about policy should be drawn from these exercises.

Table 1

FOREIGN CURRENCY HOLDINGS OF U.S. MONETARY AUTHORITIES
BASED ON CURRENT EXCHANGE RATES

Millions of U.S. Dollars

		Changes in Balances by Source				
	Carrying Value, December 31, 2024[a]	Net Purchases and Sales[b]	Investment Earnings[c]	Realized Gains / Losses on Sales[d]	Unrealized Gains/Losses on Foreign Currency Revaluation[e]	Carrying Value, March 31, 2025[a]
Federal Reserve System Open Market Account (SOMA)						
Euro	11,525	0	63	0	497	12,085
Japanese yen	5,942	0	6	0	296	6,245
Total	17,467	0	69	0	793	18,330

		Changes in Balances by Source				
	Carrying Value, December 31, 2024[a]	Net Purchases and Sales[b]	Investment Earnings[c]	Realized Gains / Losses on Sales[d]	Unrealized Gains/Losses on Foreign Currency Revaluation[e]	Carrying Value, March 31, 2025[a]
U.S. Treasury Exchange Stabilization Fund (ESF)						
Euro	11,507	0	63	0	496	12,066
Japanese yen	5,942	0	6	0	296	6,245
Total	17,449	0	69	0	792	18,311

Note: Figures may not sum to totals because of rounding.

[a]Carrying value of the reserve asset position includes interest accrued on foreign currency, which is based on "day of" accrual method.

[b]Net purchases and sales include foreign currency purchases related to official activity, repayments, and warehousing.

[c]Investment earnings include accrued interest and amortization on outright holdings.

[d]Gains and losses on sales are calculated using average cost.

[e]Reserve asset balances are revalued daily at the noon buying rates.

Table 2

BREAKDOWN OF FOREIGN RESERVE ASSETS HELD

Carrying Value in Millions of U.S. Dollars, as of March 31, 2025

	U.S. Treasury Exchange Stabilization Fund (ESF)[a]	Federal Reserve System Open Market Account (SOMA)[a]
Euro-denominated assets	**12,066.2**	**12,085.3**
Cash held on deposit at official institutions	5,214.9	5,234.0
Marketable securities held under repurchase agreements[b]	0.0	0.0
Marketable securities held outright	6,851.3	6,851.3
German government securities	1,346.1	1,346.1
French government securities	4,986.4	4,986.4
Dutch government securities	518.8	518.8
Yen-denominated assets	**6,244.6**	**6,244.5**
Cash held on deposit at official institutions	4,316.2	4,316.2
Marketable securities held outright	1,928.4	1,928.4

Note: Figures may not sum to totals because of rounding.

[a]As of March 31, the SOMA and the ESF euro portfolios had Macaulay durations of 7.86 and 7.87 months, respectively; both the SOMA and ESF yen portfolios had Macaulay durations of 5.09 months.

[b]Debt obligations of the European sovereign issuers eligible to be held outright in the foreign currency reserves are eligible collateral for reverse repo transactions.

Table 3

RECIPROCAL CURRENCY ARRANGEMENTS

Millions of U.S. Dollars

Institution	Amount of Facility	Outstanding as of March 31, 2025
	Federal Reserve System Open Market Account (SOMA)	
Reciprocal currency arrangement		
Bank of Canada	2,000	0
Banco de México	3,000	0
Standing dollar liquidity swap arrangement		
European Central Bank	Unlimited	95
Swiss National Bank	Unlimited	0
Bank of Japan	Unlimited	0
Bank of Canada	Unlimited	0
Bank of England	Unlimited	0
		95
Standing foreign currency liquidity swap arrangement		
European Central Bank	Unlimited	0
Swiss National Bank	Unlimited	0
Bank of Japan	Unlimited	0
Bank of Canada	Unlimited	0
Bank of England	Unlimited	0
		0
	U.S. Treasury Exchange Stabilization Fund (ESF)	
Banco de México	9,000	0
	9,000	0