



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

No point-in-time-safe data on System Open Market Account holdings was available on or before the cutoff for this meeting, and the Committee accordingly had no current figures on the total size, composition, or period-over-period change in SOMA holdings to review. This section is limited in scope to SOMA holdings only; it does not encompass the results of repurchase or reverse repurchase operations, for which no point-in-time-safe data source currently exists. The staff noted this gap and cautioned against inferring balance-sheet developments in the absence of reliable data.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reported that economic activity continued to expand at a solid pace across most of the country. Core PCE inflation on a twelve-month basis stood at 2.14 percent, modestly above the 2.0 percent objective. The unemployment rate was 6.4 percent, roughly a full percentage point above the 5.45 percent estimate of its natural rate, indicating that some labor-market slack remained; initial claims for unemployment insurance came in at 371,000, a reading the staff characterized as elevated-to-moderate but not deteriorating. The Chicago Fed National Activity Index at 0.41 pointed to growth somewhat above trend. The current federal funds rate was 3.75 percent, and M2 stood at \$3,581.3 billion.

The most recent Beige Book, prepared in April, described solid economic growth in most parts of the country, with conditions in California still weak though showing some early positive signs. All Districts reported strong March retail sales, aided in part by improved weather, with several noting double-digit year-over-year gains; apparel sales improved and auto sales were described as very strong. Retail pricing remained competitive, with few price increases and some price cuts. Manufacturing activity was expanding overall, with production of autos, vehicle parts, steel, and building materials reported near capacity, though aerospace remained weak. Price increases were noted for some raw materials, but competitive pressures appeared to restrain prices for most manufactured goods. Home sales were brisk in most areas and improving in the Northeast and California, with several Districts attributing a temporary surge to recent interest rate hikes. Lending activity was picking up, with greater strength in consumer than in business lending.

STAFF REVIEW OF THE FINANCIAL SITUATION

Financial conditions were described as calm and orderly. The financial stress index stood at a low 0.0843, and equity-market volatility was subdued, with the VIX at 15.19. Credit markets showed no sign of strain: the Baa corporate spread over Treasuries was tight at 1.35 percentage points. The Treasury yield curve remained positively sloped, with the 10-year/2-year spread at 1.2 percentage points,



offering no recession signal from the bond market. The 3-month Treasury bill yielded 0.49 percentage point above the current funds rate, a spread the staff read as market anticipation of near-term firming already embedded in short-term rates.

STAFF ECONOMIC OUTLOOK

The staff outlook drew on the estimated neutral rate and the momentum and reference-rule inputs available for this meeting. With the real neutral rate (r^*) estimated near 0.95 percent, the corresponding neutral nominal rate would sit close to 3.1 percent; against a current funds rate of 3.75 percent, the projection implied a policy stance only modestly above neutral rather than sharply restrictive. Inflation momentum was flat at 0.0 and unemployment momentum only slightly positive at 0.05, indicating no accelerating deterioration on either side of the mandate and little forward pull toward abrupt adjustment.

The reference rules diverged in a manner the staff judged informative rather than contradictory. The Taylor rule, the Balanced Approach rule, and the ELB-adjusted rule each pointed to roughly -75 basis points, a signal driven principally by the wide unemployment gap those level-based rules mechanically weight. The First-Difference rule, which responds to momentum rather than the level of the gap, read 0 basis points. With reference rules judged reliable and momentum essentially quiescent, the deterministic loss-minimizing recommendation resolved to 0 basis points—a hold. The projection thus implied conditions likely to remain firm and near trend absent a fresh shock, with policy already close enough to neutral that neither aggressive easing toward the level rules nor further mechanical firming was indicated by the forward-looking inputs alone.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their assessment of current conditions, participants generally agreed that the economy was expanding solidly and that financial conditions were calm enough to absorb a firm policy move without disorder. All five members arrived at the same predictive judgment—a 50 basis point increase—though the reasoning behind that common conclusion varied considerably across the Committee, and the weight each member placed on the pieces of the picture differed in ways that surfaced more sharply once the discussion turned to the framework's own recommendation.

One participant, weighting above-target inflation most heavily, argued that core PCE at 2.14 percent together with near-capacity production in autos, steel, and building materials and double-digit retail gains pointed to building price pressure that warranted getting ahead of. In this view the real funds rate of roughly 1.6 percent left policy still accommodative, and the temporary surge in home sales following prior rate hikes was evidence that demand remained robust despite tightening. A participant focused



on financial stability reached the 50 basis point conclusion by a different route, emphasizing that the stress index at 0.0843, the VIX at 15.19, and the Baa spread at 1.35 all signaled markets healthy enough to absorb a firm step, and that acting while conditions were calm was preferable to being forced into sharper, more disruptive tightening later. A participant attentive to market signals stressed that the 3-month bill running 0.49 above the funds rate had essentially discounted a half-point move already, so that a 50 basis point step would validate rather than fight the priced-in path.

A participant most concerned with the labor market offered the most reluctant support. Noting that unemployment at 6.4 percent remained nearly a full point above the 5.45 percent natural rate and that claims at 371,000 pointed to a recovery still incomplete, this member observed that, left to instinct, a smaller 25 basis point step would better safeguard the healing labor market, since inflation modestly above target was not an emergency. That reluctance was tempered, however, by the breadth of growth in the Beige Book and by the absence of any recession signal, which made a firmer move defensible while counseling vigilance against overtightening. A participant taking the data at face value likewise read the combination of a modest inflation overshoot, above-trend activity, benign financial conditions, and market pricing that cleanly matched a half-point as all pointing in the same direction.

The discussion sharpened when participants turned to the framework's loss-minimizing recommendation of 0 basis points—a hold. Several members remarked on the divergence between that recommendation and the level-based reference rules calling for roughly -75 basis points, and generally found the First-Difference logic more persuasive: with inflation momentum flat and unemployment momentum barely positive, the case for a large momentum-free adjustment was weak, and the level rules were read as over-weighting the unemployment gap while assuming it must be closed immediately. Participants broadly agreed on one point—that easing into an above-target, above-trend environment with calm markets and firming demand would be a mistake, so the framework's refusal to cut was welcomed. Where members parted was on whether a flat hold went far enough.

The inflation-focused participant judged the hold too passive, arguing that standing pat left 2.14 percent inflation free to drift higher while demand accelerated, and preferred to lean further against that risk. The stability-focused member similarly read the current stance as still mildly accommodative given r^* near 0.95, and would have preferred a firmer step than a flat hold, while conceding the hold was defensible on stability grounds. The market-signal participant agreed the framework was right to reject the easing rules but felt it understated the tightening markets had already priced in. By contrast, the labor-market participant endorsed the hold as protecting the employment recovery, firmly rejecting further restraint that would, in this member's view, endanger jobs for little inflation benefit; the



data-focused member likewise endorsed the hold as the most literal reading of contained inflation, solid growth, and flat momentum, seeing no urgency to move further in either direction.

COMMITTEE POLICY ACTIONS

In the predictive vote, all five members supported a 50 basis point increase in the target for the federal funds rate, a unanimous tally of five to none. On the deterministic framework's recommendation of a 0 basis point change—a hold—the Committee did not divide over direction but did divide over magnitude: two members endorsed the recommendation as-is, three members offered partial agreement, agreeing with the direction of not easing but not with a flat hold, and none declined. The two endorsements came from the participant focused on the labor market and the participant taking the data at face value; the three partial positions came from the inflation-focused, financial-stability, and market-signal participants, each of whom would have preferred a firmer step than the framework's hold while agreeing that easing was unwarranted.