



## **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. Accordingly, the Committee is unable to report the total size of SOMA holdings, their composition across security types, or any change from the prior release. This absence pertains to SOMA holdings specifically; it should be noted separately that no point-in-time-safe data source currently exists for the results of repurchase and reverse repurchase operations, so those operations are likewise not summarized here. Members are cautioned that this section reflects a data gap rather than an inference of unchanged holdings.

## **STAFF REVIEW OF THE ECONOMIC SITUATION**

The staff review indicated that economic activity continued to expand at a solid pace through the early part of the year. Core PCE inflation on a twelve-month basis stood at 1.14 percent, well below the 2 percent objective. The unemployment rate was 4.4 percent, considerably below the estimated natural rate of 5.15 percent, and initial jobless claims of 305,000 remained low. The Chicago Fed National Activity Index registered -0.08, placing growth just below its historical trend. M2 stood at \$4,446.5 billion.

The most recent Beige Book, prepared at the Federal Reserve Bank of Richmond on information collected before March 8, reported some further gains in activity in January and February despite weakness in agriculture and a few manufacturing industries. Consumer spending remained strong, aided by post-holiday price discounting and mild weather; motor vehicle sales rose, led by light trucks, and furniture sales benefited from robust home sales. Manufacturing expanded in most districts, though foreign competition and low energy prices weighed on textile, apparel, and energy-related industries. Commercial and residential construction grew briskly. Labor markets remained tight, with several districts finding it more difficult to locate qualified workers and reports of faster wage increases described as more widespread than in recent months. Even so, prices of most goods were little changed, and several districts noted that businesses remained reluctant to press for price increases. Agriculture continued to be plagued by low commodity prices, with an increasing number of farmers under financial stress.

## **STAFF REVIEW OF THE FINANCIAL SITUATION**

Financial conditions were characterized as elevated but not acute. The financial stress index stood at 0.1812, a moderate reading, while the VIX at 27.27 pointed to meaningful market nervousness and heightened volatility. The Baa corporate spread of 2.33 percentage points indicated some persistent credit-cost caution without signaling a credit crunch, and the Beige Book's report of a pickup in



business lending with standards only stable to slightly tighter was consistent with that reading. The 10-year/2-year Treasury spread was slightly positive at 0.17, a flat but non-inverted curve that muted any near-term recession signal. The 3-month Treasury bill yield sat 0.37 percentage point below the current 4.75 percent funds rate, suggesting that market participants anticipated some easing rather than tightening ahead.

## STAFF ECONOMIC OUTLOOK

The staff outlook drew on the forward-looking quantities available. With the estimated neutral rate ( $r^*$ ) at 3.32 percent and core inflation near 1.1 percent, the prevailing 4.75 percent funds rate appeared modestly restrictive in real terms. Inflation momentum was very slight at 0.05, and unemployment momentum was mildly negative at -0.15, together implying subdued underlying dynamics: no accelerating price pressure demanding restraint, and only a small continued tightening in the labor market. On these measures the likely near-term path of conditions is one of continued solid activity with inflation remaining below target rather than breaking higher.

The reference-rule outputs, judged reliable, spanned a wide range. The Taylor rule pointed to +50 basis points, the Balanced Approach rule to +75, and the ELB-adjusted rule to +75, each driven largely by the sizable unemployment gap relative to the 5.15 percent natural rate. The First-Difference rule, which responds to momentum rather than the level of the gap, pointed to -50 basis points, reflecting the soft inflation momentum and negative unemployment momentum. The deterministic optimal policy engine's loss-minimizing recommendation of -25 basis points sat between these poles, tempering the momentum-based easing signal against the level-based rules and implying that, absent a change in the incoming data, the stance carries quiet room to ease as insurance rather than any pressure to tighten.

## PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their initial predictive assessments, all five participants independently favored no change in the funds rate. The convergence, however, rested on genuinely mixed signals rather than a single shared read. The inflation hawk framed the central tension directly: core PCE at 1.14 percent gave no immediate reason to hike, yet the very tight labor market — 4.4 percent unemployment against a 5.15 percent natural rate — together with the Beige Book's report of more widespread wage increases, represented building future inflation risk. The offsetting consideration was that businesses remained reluctant to press for price increases and goods prices were little changed, so wage pressure had not passed through. On that basis the hawk judged a pre-emptive hike unwarranted, while stating a bias toward leaning against future price pressures.



The labor market dove approached the same data from the opposite mandate and reached the same place. With unemployment well below the natural rate, jobless claims low, and no visible labor deterioration, there was no employment-based case for easing; with inflation well below target, there was no case for tightening. The financial stability voice emphasized that the VIX at 27.27 and the Baa spread at 2.33 reflected residual nervousness rather than crisis-level distress, and that the pickup in business lending argued against any credit crunch — conditions that counseled against both a hike into nervous markets and a cut that might signal alarm. The data-dependent centrist read the mixed picture as balanced and favored patience, and the market signal realist noted that the -0.37 T-bill spread implied a mild easing tilt but not a demand for a cut, so that holding best matched the market-implied path. The second round of rebuttal produced no movement: each participant reaffirmed the hold, and the predictive vote was unanimous.

When the discussion turned to the framework's loss-minimizing recommendation of -25 basis points, the reasoning shifted noticeably even as several participants continued to distinguish their own predictive judgment from the optimal-framework case. A number of participants found the First-Difference rule the most persuasive of the reference rules, on the grounds that it responds to momentum rather than anchoring on an uncertain natural rate; with inflation momentum near zero and unemployment momentum negative, that logic pointed away from the +50 to +75 hikes implied by the level-based rules. Several observed that those level rules leaned heavily on the wide unemployment gap and thereby overstated slack-driven price pressure that the inflation data — 0.86 point below target — simply did not show.

The labor market dove, the financial stability voice, and the market signal realist each came to view a modest cut as cheap insurance. The dove argued that pre-empting labor damage before it forces a scramble costs little when inflation provides ample cover; the stability voice stressed that financial stress can turn quickly and that a -25 basis point step correctly weighted downside financial risk against negligible upside inflation risk; the market realist held that a cut would validate the forward-looking market pricing embedded in the negative T-bill spread rather than fighting it with a hawkish level rule. The data-dependent centrist agreed the stance was at most mildly restrictive and did not reject the easing direction, but judged that an immediate cut overstated the urgency given still-expanding activity and a tight labor market.

The inflation hawk was alone in resisting the direction outright. While conceding that soft inflation left ample room and that neither a hold nor a small cut supported tightening, the hawk maintained that cutting into a labor market this tight, with wage increases accelerating, was premature insurance that risked feeding the very wage pressure the Beige Book flagged. Holding, in this view, preserved



optionality to ease later should the financial stress materialize into real weakening. Participants generally accepted that the gap between the unanimous predictive hold and the framework's -25 basis point recommendation reflected a stance that was mildly restrictive rather than too loose, with the disagreement centered on timing and magnitude rather than on the underlying diagnosis.

### **COMMITTEE POLICY ACTIONS**

On the predictive question of the appropriate policy action, the Committee voted unanimously, 5 to 0, to maintain the target federal funds rate at 4.75 percent. On the separate optimal-side question of whether to support the framework's -25 basis point recommendation, the Committee did not reach full agreement: three members — the labor market dove, the financial stability voice, and the market signal realist — endorsed the recommendation as-is; the data-dependent centrist partially concurred, agreeing with the easing direction but not with the timing or magnitude of an immediate cut; and the inflation hawk declined to support it, judging a cut premature while the labor market remained tight and wage pressures were reported to be broadening.