



## **DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS**

No System Open Market Account holdings data was available on or before the point-in-time-safe cutoff for this meeting. As a result, the Committee is unable to report the total size, composition, or change from the prior release of SOMA holdings at this time. This limitation applies to SOMA portfolio holdings specifically. It should be noted separately that this section covers SOMA holdings only and does not encompass the results of repurchase or reverse repurchase operations, for which no point-in-time-safe data source currently exists; accordingly, no representation is made here about the scale or direction of such operations.

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

Incoming data pointed to a broad softening in real activity. The Chicago Fed National Activity Index stood at -0.69, consistent with below-trend growth. Initial jobless claims were elevated at 393,000. The unemployment rate remained low at 4.2%, well beneath the estimated natural rate of 5.09%, but the most recent labor readings were mixed rather than reassuring. Core PCE inflation on a year-over-year basis was 1.29%, running below the 2.0% objective, and there was little in the wage data, as reflected in the Employment Cost Index reading of 84.7, to suggest emerging upward price pressure. M2 stood at \$4,998 billion.

The March 7 Beige Book, prepared on information collected before February 26, described a majority of Districts reporting sluggish-to-modest growth in February, with others reporting mixed conditions and St. Louis noting noticeably slower activity. Consumer spending rose slightly in most Districts as retailers offered deep discounts on winter merchandise, while auto sales were generally steady but below the prior year's pace. Manufacturing activity continued to decline in most of the nation, though Boston and Richmond manufacturers reported improvement. Commercial real estate activity eased in most reporting Districts even as vacancy rates held steady and rents were level or rising. Bank lending was sluggish apart from home mortgage refinancing, and banks in some regions had tightened credit standards. Although labor markets remained tight, over half of the Districts noted some signs of easing, with declining demand for manufacturing workers and, more recently, softening demand for construction and information technology workers.

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

Financial conditions showed signs of stress alongside a market-implied expectation of near-term easing. The VIX stood at 27.55, indicating elevated equity-market volatility, while the broader financial stress index at 0.2211 was moderate rather than extreme. The Baa corporate spread of 2.85 pointed to meaningful credit-cost pressure in lower-rated borrowing. The most striking feature of the term



structure was at the front end: the 3-month Treasury bill traded 0.96 percentage point below the current 5.5% federal funds rate, a configuration consistent with market participants pricing substantial near-term rate reductions. The 10-year/2-year yield curve spread was modestly positive at 0.49, so while the front-end pricing was aggressive, the curve was not deeply inverted in a manner that would signal an expectation of outright crisis.

### STAFF ECONOMIC OUTLOOK

Forward-looking indicators pointed toward continued modest deterioration rather than acceleration. Inflation momentum was slightly negative at  $-0.06$ , consistent with disinflation and reinforcing the reading that price pressures were not a binding constraint on policy. Unemployment momentum was mildly positive at  $+0.05$ , suggesting a labor market that, though still tight in level terms, was beginning to turn. With the estimated neutral rate ( $r^*$ ) at 3.91, the prevailing 5.5% funds rate appeared restrictive relative to a neutral setting, leaving room to ease without moving policy into accommodative territory.

The reference rules diverged sharply, and this divergence is itself informative about the outlook. The Taylor rule prescribed 0 bps and the First-Difference rule  $-25$  bps, while the Balanced Approach and ELB-adjusted rules each called for  $+75$  bps. The two hiking rules drew heavily on the wide gap between the 4.2% unemployment rate and the 5.09% natural rate, effectively weighting a still-tight labor level; the First-Difference rule, by contrast, responded to the change in conditions captured by the momentum terms. With the reference rules judged reliable, the framework's loss-minimizing output was  $-25$  bps, aligned with the First-Difference logic — a projection of a measured step toward neutral that acknowledges softening activity while not overriding the persistently low unemployment level.

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

In their initial predictive positions, all five participants independently arrived at a 50 basis point reduction, an unusual convergence given the differing mandate emphases they brought to the data. The common thread was that core PCE at 1.29%, well below the 2.0% objective, removed inflation as a constraint and gave ample room to act. Participants pointed to a consistent set of weakening signals: the Chicago Fed index at  $-0.69$ , elevated jobless claims at 393,000, broad-based manufacturing decline in the Beige Book, and labor-market easing reported in over half the Districts. Several also stressed the 3-month bill trading 0.96 point below the funds rate as evidence that markets had already priced in substantial easing, such that underdelivering risked a disorderly repricing of financial conditions.

The member most attentive to inflation observed that his usual caution simply did not bind here — with prices running below target and no wage-driven pressure evident in the Employment Cost Index,



resisting a cut could not be justified. He nonetheless flagged that unemployment at 4.2% remained well below the 5.09% natural rate and that the Beige Book still described labor markets as tight, which argued against over-easing; he settled at 50 basis points as measured but meaningful. The member weighting employment most heavily read the elevated claims and softening worker demand as leading signals of deterioration and considered a larger 75 basis point move, but held at 50 given still-low headline unemployment and softening that remained early-stage. The financial-stability voice emphasized the VIX at 27.55, the Baa spread at 2.85, and banks tightening credit standards, and likewise weighed but rejected a 75 basis point cut, reasoning that the not-deeply-inverted curve and only moderate stress index argued against a move that might itself signal alarm. The centrist and the market-signal member anchored on the front-end pricing and the breadth of the slowdown, each concluding that 50 basis points matched the market-implied path without overshooting.

When participants turned to the framework's loss-minimizing recommendation of -25 bps, the discussion sharpened around magnitude rather than direction. All five agreed the current 5.5% stance was restrictive relative to the 3.91 neutral rate and that easing, not holding, was appropriate. Participants generally found the First-Difference rule most persuasive among the reference rules: it responded to the negative inflation momentum (-0.06) and rising unemployment momentum (+0.05) rather than anchoring, as the Balanced Approach and ELB-adjusted rules did, on a stale low-unemployment level that the Beige Book indicated was already easing. There was broad agreement that the +75 bps rules were poorly suited to conditions of sub-target inflation and softening activity.

A genuine divergence remained on how fast to move. The inflation-focused member and the centrist endorsed the -25 bps recommendation outright, reading no data urgency that would warrant front-loading and viewing a measured step as the prudent, loss-minimizing choice that preserved the ability to respond if prices firmed. The employment-focused member, the financial-stability voice, and the market-signal member agreed with the easing direction but regarded -25 bps as a floor rather than the optimal step. The first argued that rising claims and slackening labor demand called for front-loading to insure against accelerating deterioration; the second feared a self-reinforcing tightening from widening spreads and cautious bank lending and preferred to preempt a possible credit spiral; the third maintained that the -0.96 bill spread implied markets were demanding roughly 75 to 100 basis points of cumulative easing, so a 25 basis point step would leave effective financial conditions restrictive at a fragile moment. None of these members were moved off their emphasis by the arguments for gradualism, though all acknowledged the -25 bps case as defensible.

## COMMITTEE POLICY ACTIONS



In the predictive vote, all five participants supported a 50 basis point reduction in the target federal funds rate, a unanimous 5-0 outcome. On the framework's loss-minimizing recommendation of -25 bps, the Committee did not divide on direction but did divide on magnitude: two members — the inflation-focused member and the centrist — endorsed the -25 bps recommendation as-is, while three members — the employment-focused member, the financial-stability voice, and the market-signal member — registered partial agreement, supporting the easing direction but preferring a larger move. No member declined the recommendation. The recorded optimal-side tally was thus 2 endorse, 3 partial, 0 decline.