



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, so the Committee was unable to review the total size, composition, or change in SOMA holdings relative to any prior release. The desk staff noted that this gap pertains specifically to the SOMA holdings series; it is distinct from repurchase and reverse-repurchase operation results, for which no point-in-time-safe data source currently exists either. Members were accordingly advised to treat the open market operations portion of this review as informational only, drawing their judgments about the appropriate stance of policy from the broader economic and financial data described below rather than from any balance-sheet detail.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reported that economic activity had continued to slow. The Chicago Fed National Activity Index stood at -0.43, consistent with growth running below trend, and the most recent Beige Book, prepared on information collected before April 23, characterized the pace of activity in March and early April as slow across almost all districts. Industrial activity had continued to weaken, with orders and production reported down in many districts. Retail sales had been weak in March but strengthened somewhat in April, though retailers in most districts expected only small gains at best in the months ahead; vehicle sales were mixed, with demand for new SUVs, trucks, and luxury cars generally softer. Home sales and new construction had held steady or picked up in almost all districts, and lower mortgage rates had spurred a resurgence of refinancing that helped bolster loan growth, even as many districts noted that credit standards had tightened relative to earlier.

On the labor and price side, the staff observed that labor market tightness had eased in almost every district and that upward wage pressures had generally abated. Initial jobless claims stood at 381,000, an elevated reading relative to recent experience. The unemployment rate was 4.5 percent, still below the estimated natural rate of 5.09 percent, indicating that measured slack had not yet opened up. Core PCE inflation was running at 1.52 percent on a year-over-year basis, below the 2.0 percent objective. The staff flagged that the abatement in wage pressures had, in many districts, been replaced by sharply higher energy costs, which they characterized as a relative-price development rather than broad-based demand-driven inflation. The Employment Cost Index reading of 85.5 and M2 of roughly \$5,098.9 billion were reported for completeness.

STAFF REVIEW OF THE FINANCIAL SITUATION

Financial conditions were characterized as somewhat tighter at the margin but not indicative of acute stress. The financial stress index stood at 0.1917, a moderate reading, while the VIX at 24.44 pointed to



elevated market volatility and risk aversion. The Baa corporate spread of 2.76 percentage points signaled meaningful borrowing-cost stress for riskier corporate issuers, a reading the staff noted was consistent with the Beige Book's report of tighter credit standards. The Treasury yield curve remained positively sloped, with the 10-year/2-year spread at +1.14, offering no acute recession signal from the term structure. At the front end, however, the 3-month Treasury bill traded 0.88 percentage point below the current 4.5 percent funds rate, an inversion the staff read as markets already pricing in substantial near-term easing.

STAFF ECONOMIC OUTLOOK

The staff's forward-looking assessment drew on the momentum measures and the reference-rule outputs rather than on any single level reading. Inflation momentum was estimated at -0.155, indicating prices were decelerating rather than accelerating, while unemployment momentum was positive at 0.1, suggesting that slack was beginning to build even though the level of unemployment remained below the estimated natural rate. Taken together, these dynamics implied a trajectory of gradually softening activity and easing price pressure over the projection horizon, consistent with the below-trend activity index and the elevated claims figure.

The reference rules were mixed in their prescriptions, which the staff attributed to their differing treatment of levels versus changes. The Taylor rule, the Balanced Approach rule, and the ELB-adjusted rule each pointed to roughly 75 basis points above the current setting, a result driven largely by unemployment sitting below the 5.09 percent natural rate and by an estimated neutral rate (r^*) near 3.927. The First-Difference rule, which responds to the direction of change rather than to level gaps, pointed instead to a 25 basis point reduction. The staff noted that the loss-minimizing recommendation from the optimal policy engine, at -25 basis points, aligned with the First-Difference prescription, reflecting a judgment that the level-based rules leaned on labor-market tightness that the Beige Book and claims data suggested was already unwinding. The rules were flagged as reliable within the framework, but the divergence itself was described as a caution that the appropriate magnitude of easing was more uncertain than its direction.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their initial predictive discussion, participants agreed almost uniformly that the economy was slowing and that inflation posed little constraint on policy, but they divided on how far to move. One participant, weighting inflation risk most heavily, favored a 25 basis point reduction. This participant noted that core PCE at 1.52 percent was comfortably below target and that Beige Book contacts reported wage pressures had generally abated, but also emphasized the sharp rise in energy costs and the fact that unemployment at 4.5 percent remained below the 5.09 percent natural rate. In this participant's view,



there was no evidence of a demand collapse requiring emergency-sized easing, and a measured move preserved optionality should price pressures re-emerge.

The other four participants favored a 50 basis point reduction. A participant focused on the labor market pointed to elevated initial claims at 381,000 and the district-wide easing of labor tightness, arguing that waiting for the unemployment rate to actually rise before acting risked falling behind a deteriorating trend. A participant attentive to financial stability stressed the Baa spread of 2.76 and the Beige Book's report of tighter credit standards, warning that under-easing could leave the credit channel restrictive and allow the slowdown to compound. A participant favoring a literal reading of the data described the 50 basis point move as the consensus reading given consistently soft activity and below-target inflation. A participant weighting market signals leaned most heavily on the -0.88 front-end spread, judging it consistent with roughly two 25 basis point cuts priced and cautioning that delivering less could tighten effective conditions relative to expectations. In the rebuttal round, none of the four were persuaded toward 25 basis points, and the participant favoring 25 held that position, granting that energy was a supply shock but maintaining that softening growth alone did not justify front-running with a larger move.

Turning to the framework's loss-minimizing recommendation of -25 basis points, the discussion converged more than the predictive votes had. Participants broadly found the First-Difference logic the most persuasive of the reference rules, agreeing that the Taylor, Balanced Approach, and ELB-adjusted prescriptions of roughly +75 basis points rested on a backward-looking read of labor-market tightness that the Beige Book showed already fading. Several observed that with inflation momentum negative and unemployment momentum positive, the direction of change argued for easing despite the level readings, and that the uncertainty around the r^* estimate of 3.927 made the level rules less reliable in the present environment. The participant focused on inflation was most comfortable here, judging that -25 basis points protected against over-easing while energy pass-through remained a risk, and that a smaller step validated market pricing without overcommitting.

The participants who had favored 50 basis points accepted that the direction of the framework's call was correct but continued to view its magnitude as insufficient. The labor-focused participant maintained that the current 4.5 percent stance was too restrictive against a turning labor market and preferred front-loading to get ahead of deterioration. The financial-stability participant, while acknowledging that the credit channel was not seized given steady home sales, refinancing, and loan growth, and that a larger cut risked sending a panic-flavored signal to fragile markets, still leaned toward deeper insurance in light of the front-end pricing. The market-signals participant conceded



that the positively sloped 10-year/2-year curve argued against panic-sized action but held that the -0.88 bill spread implied markets expected more than a single 25 basis point step. The participant favoring a literal reading, by contrast, endorsed the -25 basis point step outright, resisting front-loading on the grounds that the bill spread reflected expectations rather than realized data and that moderate stress readings did not warrant an emergency-sized move.

COMMITTEE POLICY ACTIONS

In the predictive vote on the likely policy action, four participants favored a 50 basis point reduction and one favored a 25 basis point reduction, yielding a recorded tally of -50 basis points (four votes for -50, one for -25). On the separate question of the framework's loss-minimizing recommendation of -25 basis points, no participant declined the recommendation. Two participants — the one weighting inflation risk and the one favoring a literal reading of the data — endorsed the -25 basis point recommendation as-is. The remaining three — the labor-market-focused participant, the financial-stability participant, and the market-signals participant — offered partial support, agreeing with the direction of easing but judging the magnitude insufficient relative to what they read as market-priced and momentum-based conditions. The final optimal-side tally was thus two endorsements, three partial, and none declining.