



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 therefore had no updated figures on the total size, composition, or period-to-period change in SOMA holdings to review. The staff noted that this gap pertains to SOMA holdings only; it does not cover the results of repurchase or reverse-repurchase operations, for which no point-in-time-safe data source currently exists. Discussion of open market operations at this meeting was accordingly confined to what could be inferred from broader market conditions rather than from direct holdings data.

STAFF REVIEW OF THE ECONOMIC SITUATION

Economic activity remained lackluster through March and the first two weeks of April. The Beige Book, prepared before April 15, characterized conditions across most Districts as mixed or soft, with only one District noting continued modest growth; several Districts reported that the pace of activity had slowed relative to earlier readings. Consumer spending was generally weak in March, though contacts attributed part of the softness to poor weather, the later timing of Easter this year, and the onset of the war with Iraq. The report cautioned that it was 'too early to ascertain the full effect of the war on both consumer and business confidence.' Manufacturing weakness was widespread, with only scattered pockets of growth, and commercial real estate remained in a slump. Homebuilding was strong across all Districts, and mortgage lending, supported by refinancing, remained robust, while a few Districts saw some improvement in commercial loan demand.

Labor markets remained soft, although some Districts noted moderating layoffs or firmer demand for temporary workers. The unemployment rate stood at 5.8 percent, above the estimated natural rate of 5.05 percent, and initial jobless claims were elevated at 444,000. The Chicago Fed National Activity Index at -0.63 indicated growth running below trend. On the price side, core PCE inflation was 1.23 percent on a year-over-year basis, well below the 2 percent objective. The federal funds rate stood at 1.25 percent.

STAFF REVIEW OF THE FINANCIAL SITUATION

Financial conditions were broadly stable, with no signs of acute strain. The financial stress index registered 0.0954, a low reading, and the VIX at 20.76 was elevated but consistent with post-war-onset uncertainty rather than panic. The Baa corporate spread of 2.77 was somewhat elevated, pointing to lingering caution in corporate credit costs without signaling acute dysfunction. The 10-year/2-year yield curve was steeply positive at 2.34, showing no inversion or near-term recession pricing. The 3-month T-bill spread relative to the current funds rate was slightly negative at -0.12, suggesting that



short-term markets were pricing a mild easing bias. Credit continued to flow through the mortgage channel, consistent with the strength in refinancing and homebuilding noted in the Beige Book.

STAFF ECONOMIC OUTLOOK

The forward-looking indicators available to the staff pointed to a stance of policy that was modestly restrictive relative to underlying conditions. With the estimated neutral rate (r^*) at 2.888 percent and the nominal funds rate at 1.25 percent, and with inflation drifting lower, the effective real rate had been edging up even as activity softened. Inflation momentum was negative at -0.18, indicating continued disinflation rather than stabilization near target, while unemployment momentum at 0.05 suggested labor-market slack was not yet receding. Taken together, these quantities implied that, absent a policy response, price pressures would likely continue to drift below the 2 percent objective and labor-market slack would persist.

The reference rules spanned a wide range: the Taylor rule prescribed 75 basis points, the Balanced Approach rule 25 basis points, the ELB-adjusted rule 25 basis points, and the First-Difference rule -25 basis points. The dispersion reflected the divergent weight each rule placed on the elevated r^* estimate versus the negative inflation and momentum readings. The staff's loss-minimizing framework, treating the reference rules as reliable, recommended -50 basis points, a move more accommodative than any single rule, reflecting the combined weight of below-target inflation, negative inflation momentum, and the scarcity of conventional room near the effective lower bound. The projection implied that front-loaded easing would reduce the risk of a self-reinforcing drift toward deflation, while a hold would leave conditions tighter than the framework judged optimal.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their predictive discussion, participants broadly agreed on the direction in which the data pointed but differed on whether any immediate action was warranted. A majority favored holding the funds rate steady at 1.25 percent. The member most attentive to inflation risk observed that this was an unusual configuration for that lens: core PCE at 1.23 percent was undershooting, not overshooting, and the pertinent risk was disinflation rather than acceleration. Even so, this participant judged that policy at 1.25 percent was already accommodative, that financial stress at 0.0954 was low, and that the yield curve was positively sloped, so a hold was defensible while post-war data were assessed. The participant most focused on financial stability reached a similar conclusion by a different route, noting that credit was still flowing through the mortgage channel and that no systemic strain was evident, and cautioning that an unnecessary cut with limited conventional ammunition risked unsettling money markets and reducing room to respond if genuine stress emerged.



A participant reading the data at face value for the most literal consensus concurred with holding, emphasizing that the Beige Book itself judged it 'too early to ascertain the full effect of the war' and that the indicators, while soft, were not deteriorating sharply. Two participants dissented from the hold in the predictive round, favoring a 25 basis point cut. The member most focused on the labor market pointed to unemployment at 5.8 percent, well above the 5.05 percent natural rate, elevated claims at 444,000, and a Chicago Fed index at -0.63, arguing that waiting risked labor deterioration that would be harder to reverse and that a modest cut was orderly, not an emergency action. The member weighting market pricing most heavily read the -0.12 T-bill spread as a mild easing bias consistent with a single 25 basis point move, reinforced by the uniformly soft Beige Book. Rebuttals did not move any participant from their initial position, and the predictive vote settled at a hold.

When the discussion turned to the framework's loss-minimizing recommendation of -50 basis points, the tenor shifted. Participants converged on the view that the direction of easing was correct. The inflation-focused member acknowledged that sustained sub-target inflation with negative momentum was itself an inflation risk to guard against, framing the case as protecting the 2 percent objective from below rather than above. The labor-focused and financial-stability members agreed that with r^* estimated near 2.888 percent and the real rate edging higher, the current stance was tighter than optimal, and that front-loading easing near the effective lower bound offered insurance against a destabilizing drift toward deflation. Several participants found the First-Difference rule at -25 basis points the most persuasive of the reference rules, since it responded to deteriorating momentum, and generally rejected the Taylor rule's 75 basis points as overweighting a high r^* against inflation that was actually running below target.

Despite endorsing the direction, no participant was prepared to support the full magnitude of the framework's -50 basis point recommendation. The recurring objections were the low financial stress reading of 0.0954, the steeply positive rather than inverted curve, the only moderate Baa spread of 2.77, and the war-related uncertainty that the Beige Book judged too early to assess. Participants across lenses argued that spending scarce conventional room near the lower bound on weakness that might prove partly transitory was imprudent, and that a measured step preserved ammunition and avoided signaling alarm. The market-focused member added that pricing implied only a mild easing tilt, not a 50 basis point plunge, and so did not justify a jumbo move. The common thread was agreement on easing as the loss-minimizing direction paired with a preference for gradualism over a large front-loaded cut.

COMMITTEE POLICY ACTIONS



In the predictive vote, the Committee's five members favored holding the federal funds rate unchanged at 1.25 percent by a tally of three to two, with two members preferring a 25 basis point reduction. On the staff framework's loss-minimizing recommendation of a 50 basis point cut, all five members took a partial stance: none endorsed the recommendation as-is and none declined it outright, with every member agreeing on the direction of easing while judging the -50 basis point magnitude larger than current conditions warranted. The recorded optimal-side tally was thus zero endorse, zero decline, and five partial.