



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The manager reported on developments in the System Open Market Account. As of the most recent release available on or before the point-in-time-safe cutoff, dated April 25, 2018, total SOMA domestic securities holdings stood at \$4,142.3 billion. Of this, Treasury notes and bonds accounted for \$2,262.4 billion and agency mortgage-backed securities for \$1,745.0 billion. Total holdings declined by \$11.3 billion relative to the prior release of April 18. It should be noted that these figures cover SOMA securities holdings only — total size, composition, and week-over-week change — and do not reflect the results of repo or reverse-repo operations, for which no point-in-time-safe historical data source currently exists.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reviewed incoming data on economic activity, which pointed to continued expansion at a moderate pace. The Chicago Fed National Activity Index registered 0.1, consistent with growth near its historical trend. Labor market indicators remained firm: the unemployment rate stood at 4.1 percent, below the estimated natural rate of 4.62 percent, and initial jobless claims were low at 232,000, showing no upward trend that would signal deterioration. The Employment Cost Index reading of 131.4 was consistent with wage gains that were generally described as modest, though some districts reported firmer pressures. On the price side, core PCE inflation on a twelve-month basis was 1.57 percent, still below the Committee's 2 percent objective. The M2 money supply measured \$13,926.4 billion.

District reports in the Beige Book characterized activity as expanding at a moderate pace across regions. Several districts described solid hiring against a backdrop of tight labor markets, with wages generally rising modestly, though one district noted that wage and price growth remained 'elevated.' Manufacturing, energy, and consumer spending were reported to be expanding, while some districts observed easing or mixed conditions in manufacturing and continued weakness in agriculture. Residential real estate reports were mixed, with sales declines in some areas alongside price increases attributed to very low inventories. A recurring theme across districts was concern about new tariffs and trade policy uncertainty, though contacts' overall outlooks were described as still positive.

STAFF REVIEW OF THE FINANCIAL SITUATION

The staff reported that financial conditions remained benign. The financial stress index stood at 0.063, a very low reading indicative of calm markets and the absence of systemic strain. The VIX, at 17.84, was moderate and showed no sign of disorderly volatility. Credit conditions appeared accommodative: the Baa corporate spread was narrow at 1.77, signaling no pricing of credit distress. The yield curve remained positively sloped, with the 10-year/2-year spread at 0.54, though it had flattened somewhat;



there was no inversion and thus no recession signal from the curve. The 3-month T-bill spread relative to the current policy rate was 0.215, consistent with market expectations of further near-term tightening rather than an immediate move.

STAFF ECONOMIC OUTLOOK

The staff outlook incorporated several forward-looking quantities. Inflation momentum was estimated at 0.125, indicating that core PCE, while still below the 2 percent objective, was firming and likely to drift upward toward target in coming months. Unemployment momentum was 0.0, implying no dynamic pressure toward either rising or falling joblessness from current conditions, consistent with a labor market that was tight but stable. Taken together, these momentum readings suggested only modest cyclical pressure in either direction over the projection horizon.

The reference policy rules presented a wide range of prescriptions. The Taylor rule, the Balanced Approach rule, and the ELB-adjusted rule each indicated -75 basis points, while the First-Difference rule indicated -25 basis points. The level-based rules were heavily influenced by an estimated neutral rate (r^*) of -0.5 percent, which pulled their implied policy levels sharply lower given inflation below target. The staff noted that the loss-minimizing recommendation from the optimal policy engine was 0 basis points, and that the reference rules were judged reliable as diagnostic inputs even where their point prescriptions diverged from that recommendation. The staff assessment was that the level-rule cut signals largely reflected the contested low r^* estimate, while the more temperate First-Difference output, keyed to the change in conditions rather than the level gap, better captured the weak momentum in the data. With activity near trend and financial conditions calm, the projected path implied a gradual glide of policy toward the previously projected 2.1 percent level rather than the deep easing the level rules mechanically implied.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their discussion of current conditions, participants generally judged that the economy was expanding at a moderate pace, that the labor market was strong, and that inflation, though still below the 2 percent objective, was firming toward it. Against that backdrop, most participants entered the meeting inclined to hold the target range unchanged this meeting while continuing to regard further gradual increases as appropriate over time. Several observed that core PCE at 1.57 percent removed any urgency to tighten immediately, even as they expected inflation to move higher, and that with no acute inflation overshoot in the data, benign conditions permitted patience rather than compelling action.



A participant focused on inflation risk emphasized that the balance of risks was tilting upward: the Beige Book's references to 'elevated' wage and price growth in some districts, combined with tariff-driven cost pressures and an unemployment rate of 4.1 percent well below the 4.62 percent natural rate, pointed to building upside risk even though realized inflation remained short of target. This participant stressed that the localized nature of the elevated readings warranted vigilance rather than accelerated action, and that the current 1.5 to 1.75 percent range, still below the projected 2.1 percent level, left the gradual normalization path intact without a move now. A participant attentive to employment concurred that no labor-market weakness was present to justify easing — jobless claims were low, hiring solid, and wages rising only modestly — while also seeing no overheating pressure demanding an immediate hike.

One participant, weighing financial stability, initially favored a 25 basis point increase, reasoning that the very low financial stress index of 0.063, a moderate VIX, a narrow Baa spread of 1.77, and a positively sloped curve all indicated that a gradual hike would not destabilize markets. Over the course of the discussion, however, this participant came to place greater weight on the observation that calm conditions cut both ways — the absence of stress meant there was no destabilization risk from hiking, but equally no financial-stability urgency forcing a move at this specific meeting. Persuaded by the point that the 3-month T-bill spread of 0.215 and broader market pricing anticipated tightening but did not strongly price a move at this meeting, this participant revised to supporting a hold, judging that deferring to the well-telegraphed gradual path best preserved orderly markets and avoided surprising investors. Participants attentive to market signals and to the incoming data reinforced this reading, noting that market pricing pointed to the next hike at a following meeting rather than an immediate one.

Turning to the framework's loss-minimizing recommendation of 0 basis points, participants engaged directly with the sharp divergence between that recommendation and the reference rules, three of which called for -75 basis points and one for -25. There was broad agreement that the deep cut signals rested on an estimated neutral rate near -0.5 percent and overweighted the current sub-target inflation gap while underweighting the risks and conditions participants actually observed. The participant focused on inflation argued that cutting into a tightening labor market and firming prices — with inflation momentum at 0.125 — would be a clear policy error, and that the framework's 0 basis point recommendation rightly overrode the mechanical cut signals. The employment-focused participant made a parallel point from the other direction: the cut signals reflected the inflation shortfall, not any employment weakness, and with unemployment momentum at 0.0 there was no deterioration to defend against; easing would risk overheating an already tight labor market. Several participants found the First-Difference rule the most persuasive of the reference outputs, since it



responded to the change in conditions rather than a contested neutral-rate estimate, but judged that even its -25 basis point signal was not compelling given the weak momentum in both inflation and unemployment.

In closing the discussion, participants noted that the calm financial backdrop, near-trend growth as reflected in the CFNAI reading of 0.1, and a positively sloped yield curve together offered no cyclical or stability rationale for aggressive rate action in either direction. Trade and tariff uncertainty flagged across districts was widely cited as a reason to preserve optionality and to favor patience over preemptive moves. The prevailing view was that holding the target range at 1.5 to 1.75 percent kept policy roughly appropriate — neither restrictive nor forcing a cut — while awaiting confirmation that inflation was stabilizing near 2 percent, with a further gradual increase seen as likely at a following meeting.

COMMITTEE POLICY ACTIONS

On the predictive question of the appropriate policy action at this meeting, all five members judged that the target range should be held at 1.5 to 1.75 percent, a unanimous 0 basis point outcome. On the framework's loss-minimizing recommendation of 0 basis points, the Committee was likewise in full agreement: all five members endorsed the recommendation as-is, with none declining and none registering partial support. The two votes were thus fully aligned, reflecting a genuine consensus that patience was warranted given below-target but firming inflation, a strong labor market showing no deterioration, and benign financial conditions.