



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The Committee reviewed the most recent System Open Market Account holdings data, as of April 24, 2019. Total SOMA domestic securities holdings stood at \$3,717.4 billion, composed of \$2,000.2 billion in Treasury notes and bonds and \$1,583.4 billion in agency mortgage-backed securities. This represented a decline of \$4.5 billion from the prior release of April 17, a modest continuation of the gradual runoff in the portfolio. Staff noted that this review covers SOMA holdings only -- total size, composition, and the week-over-week change -- and does not encompass repo or reverse-repo operation results, for which no point-in-time-safe data source currently exists; accordingly, no characterization of temporary operations was offered.

STAFF REVIEW OF THE ECONOMIC SITUATION

Economic activity expanded at a slight-to-moderate pace through March and early April, according to the most recent Beige Book. Most Districts reported growth continuing at a pace similar to the prior report, with a few noting some strengthening, and the outlook among contacts changed little, generally pointing to slight-to-modest growth ahead. Consumer spending reports were mixed and suggested sluggish sales for both general retailers and auto dealers, while tourism reports were more upbeat. Manufacturing activity was described as favorable, though contacts in many Districts flagged trade-related uncertainty. Most Districts reported stronger home sales, with some noting weak demand at higher price points, and agricultural conditions remained weak amid concerns about rainfall and flooding. The Chicago Fed National Activity Index at -0.15 was consistent with growth modestly below trend.

Labor markets remained tight. Employment continued to increase across all twelve Districts, with nine reporting modest or moderate growth and three reporting slight growth; gains were most concentrated in high-skilled positions, and a majority of Districts cited shortages of skilled labor, particularly in manufacturing and construction. Firms reported using bonuses and expanded benefits to attract and retain workers, and most Districts described moderate wage growth. The national data corroborated this picture: the unemployment rate stood at 3.8%, well below the estimated natural rate of 4.6%, and initial jobless claims were low at 192,000. On prices, the Beige Book noted that prices rose modestly on balance, with input costs in the modest-to-moderate range and tariffs, freight, and wages cited as key drivers; the ability of firms to pass those costs through to consumers was mixed. Core PCE inflation stood at 1.26% on a year-over-year basis, well below the Committee's 2% objective.

STAFF REVIEW OF THE FINANCIAL SITUATION



Financial conditions were benign across the indicators staff reviewed. The financial stress index registered 0.036, a very low reading, and the VIX at 13.14 pointed to calm equity market conditions. Credit markets showed no sign of strain, with the Baa corporate spread at 2.14, a moderate and contained level. The Treasury yield curve was positive but flat, with the 10-year/2-year spread at 0.21, indicating some embedded caution about the growth outlook without an outright inversion. At the short end, the 3-month T-bill spread against the current policy rate was just 0.025, consistent with market pricing that anticipated no imminent change in the stance of policy. Taken together, these readings described markets that were calm and functioning normally, with no evident distress requiring a policy response.

STAFF ECONOMIC OUTLOOK

The staff outlook drew on the forward-looking quantities available. The estimated neutral real rate (r^*) was -0.5, implying a low nominal neutral rate; against that benchmark, the current target range of 2.25% to 2.50% sits meaningfully above neutral, so the prevailing stance of policy is properly characterized as restrictive rather than neutral. With inflation momentum reading -0.075, price pressures appeared to be softening further rather than stabilizing at or near target, suggesting that, absent a policy adjustment, the gap between realized inflation and the 2% objective could persist or widen. Unemployment momentum was slightly positive at +0.05, a small upward drift from an otherwise strong labor market -- not a deterioration, but a change in direction worth monitoring.

The deterministic reference rules reinforced this reading and were judged reliable given the calm financial backdrop. The Taylor rule, the Balanced Approach rule, and the ELB-adjusted rule each pointed to -75 bps, driven principally by the inflation shortfall alongside a labor market operating well beyond its estimated natural rate, while the First-Difference rule, which adjusts more gradually from current settings, indicated -25 bps. The optimal policy engine's loss-minimizing recommendation of -50 bps fell between these signals. The projection these figures imply is one in which a restrictive stance held against sub-target and softening inflation would continue to exert passive tightening, gradually restraining activity and prices, whereas a move toward the negative- r^* neutral level would arrest that dynamic before the inflation undershoot became more entrenched.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their first-round assessments, participants independently converged on maintaining the target range at 2.25% to 2.50%. The participant most attentive to inflation risk observed that core PCE at 1.26% sits well below target rather than above it, leaving his usual caution against easing little to work with, though he flagged tight labor markets, skilled-labor shortages, moderate wage growth, and cost-pass-through as sources of latent upside risk worth watching. The participant focused on the



labor mandate emphasized that unemployment at 3.8% and claims at 192,000 showed no deterioration to lean against, so that even from his dovish vantage a preemptive cut was not yet justified. The participant attentive to financial stability found no stress to counteract -- the stress index at 0.036, the VIX at 13.14, and the Baa spread at 2.14 all pointing to calm. The participant taking a data-dependent, neutral stance read the balance of soft inflation against a strong labor market and calm conditions as leaving no compelling case to move in either direction, and the participant who weights market-implied signals most heavily noted that the 3-month T-bill spread of 0.025 and the current range's proximity to prior expectations implied markets anticipated no change. In the second round, no participant was moved from this position; the discussion largely reinforced the shared view that soft realized inflation blocked a hike while a firm labor market and benign financial conditions blocked a cut, with several participants noting the modestly below-trend CFNAI reading and sluggish consumer and auto sales as items to monitor rather than act upon.

The tenor of the discussion shifted when participants turned to the deterministic framework's recommendation of -50 bps and reasoned within an optimal-policy lens. Here the emphasis moved from what conditions demanded immediately to what a restrictive stance implied over time. Participants generally acknowledged that with r^* estimated at -0.5, the current range sits well above neutral, so that holding steady while inflation runs at 1.26% amounts to a passive tightening. The participant focused on inflation risk found this reframing telling: the precondition for his anti-cutting caution -- elevated inflation risk -- simply did not hold, and with inflation momentum negative and pass-through described as mixed, the risk he was obligated to weigh was an entrenched undershoot rather than an overshoot. The participant attentive to the labor mandate pointed to the slight positive drift in unemployment momentum and the fragile real-side backdrop -- slight-to-moderate growth, sluggish sales, trade uncertainty -- as grounds for preemptive easing that would protect employment before any softening spread. The financial-stability participant argued that easing while markets are calm is safer than being forced to ease reactively amid stress later, and that persistent below-target inflation with a low neutral rate could seed future credit-cycle risk.

Participants weighed the reference-rule signals with care in explaining why -50 bps, rather than the -75 bps implied by three of the level rules or the -25 bps of the gradualist First-Difference rule, represented the loss-minimizing middle. Several found the Balanced Approach logic most persuasive on direction, since it weights the large inflation shortfall alongside a labor market well beyond its natural rate; others anchored more on the First-Difference rule's respect for gradual adjustment from stable conditions. The tension between direction and magnitude organized much of the fourth-round rebuttal. Two participants endorsed the -50 bps recommendation as-is: the labor-focused participant, who framed it as preemptive protection of jobs that stopped prudently short of -75 bps, and the



financial-stability participant, who framed it as recalibrating toward a negative- r^* neutral before disinflation entrenched, while markets remained calm.

Three participants agreed with the easing direction but judged the magnitude larger than the data supported at this meeting. The inflation-focused participant accepted that excess restriction against 1.26% inflation was hard to justify, but held that CFNAI at only slightly below trend, still-expanding growth, and a tight labor market that a full -50 bps might re-ignite argued for a smaller -25 bps step preserving optionality. The neutral, data-dependent participant made a parallel case from a literal reading of the real-side data: expansion continuing, wages growing only moderately, no distress in financial conditions, and market pricing that saw the current range as roughly appropriate -- a gradual move fitting better than a large single step. The market-signals participant agreed that soft inflation and negative momentum made the easing direction defensible, but stressed that markets had not priced -50 bps, and that the near-flat 3-month T-bill spread argued specifically against front-loading that much; the First-Difference rule's -25 bps sat closest to his market-implied read. Across these views, participants distinguished between what markets and institutional patience suggested policymakers would do and what the mandate math indicated conditions warranted -- a genuine gap that the framework brought into relief.

COMMITTEE POLICY ACTIONS

On the predictive question of the policy decision expected at this meeting, all five participants supported maintaining the target range for the federal funds rate at 2.25% to 2.50%, a unanimous outcome of 5 to 0. On the separate question of the deterministic framework's -50 bps recommendation, the Committee did not reach full agreement: two participants -- those focused on the labor mandate and on financial stability -- endorsed the recommendation as-is, and the remaining three -- the participants focused on inflation risk, on data-dependent neutrality, and on market-implied signals -- expressed partial support, agreeing with the easing direction the framework identified but judging its -50 bps magnitude larger than current conditions warranted and preferring a smaller, more gradual step. No participant declined the direction of the recommendation outright.