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Data Insights: FOMC Minutes

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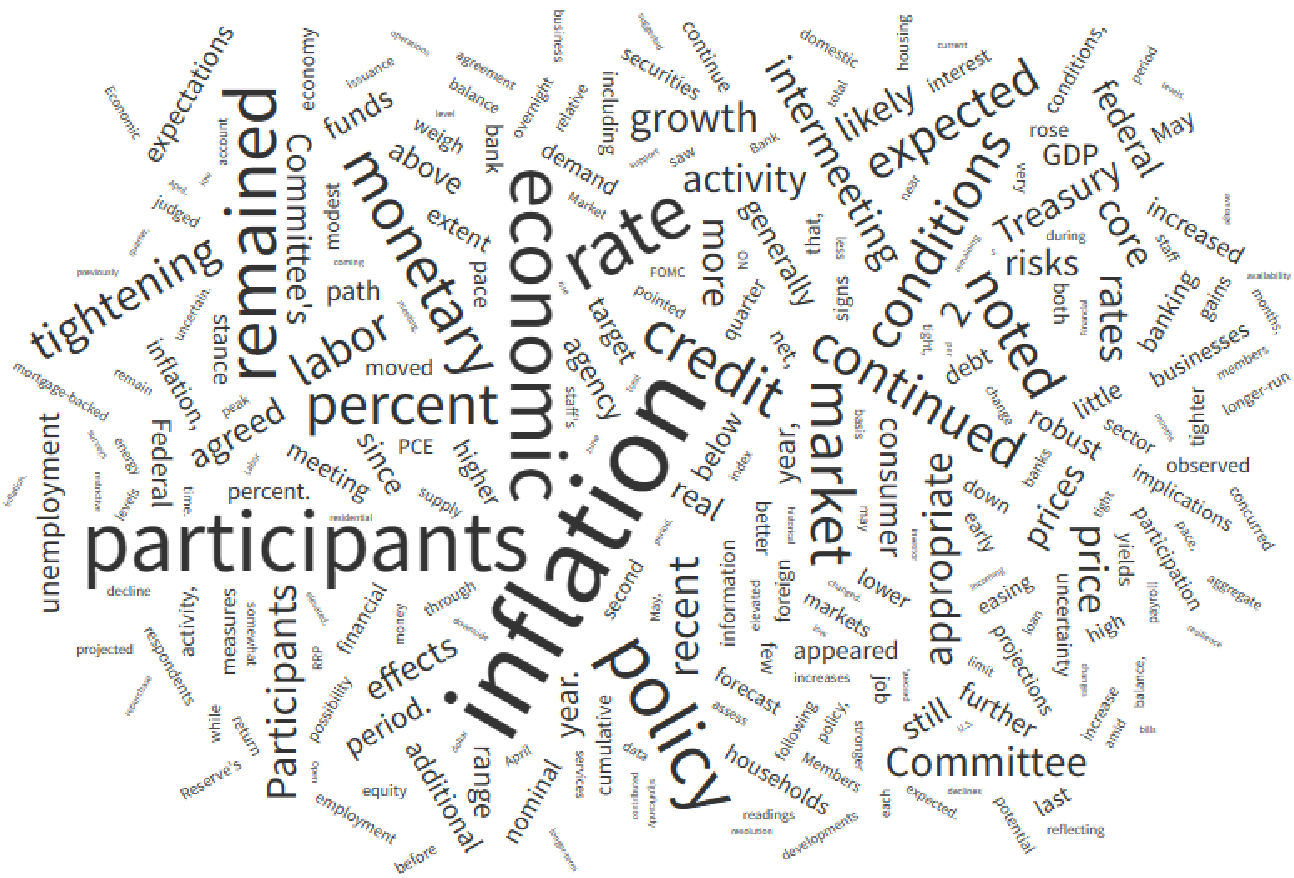
June minutes | Key signaling language: Featured | Important | Very important



In their discussion of current economic conditions, participants noted that economic activity had continued to expand at a modest pace. Nonetheless, job gains had been robust in recent months, and the unemployment rate had remained low. Inflation remained elevated. Participants agreed that the U.S. banking system was sound and resilient. They commented that tighter credit conditions for households and businesses were likely to weigh on economic activity, hiring, and inflation. However, participants agreed that the extent of these effects remained uncertain. Against this background, participants concurred that they remained highly attentive to inflation risks.

In assessing the economic outlook, most participants noted that real GDP growth had been resilient in recent quarters. Participants generally judged that growth would be subdued over the remainder of this year. They assessed that the cumulative tightening of monetary policy over the past year had contributed significantly to more restrictive financial conditions and lower demand in the most interest rate sensitive sectors of the economy, especially housing and business investment. Participants also acknowledged uncertainty about the lags with which monetary policy affects the economy and discussed the extent to which the full effects of monetary tightening on the economy had been realized. While total inflation had moderated over the past year, core inflation had not shown a sustained easing since the beginning of the year. With inflation well above the Committee's longer-run 2 percent objective, participants expected that a period of below-trend growth in real GDP and some softening in labor market conditions would be needed to bring aggregate supply and aggregate demand into better balance and reduce inflationary pressures sufficiently to return inflation to 2 percent over time.

Participants generally noted that banking stresses had receded and conditions in the banking sector were much improved since early March. Participants generally continued to judge that a tightening in credit conditions spurred by banking-sector stress earlier in the year would likely weigh further on economic activity, but the extent remained uncertain. Several participants mentioned that credit conditions had not appeared to have tightened significantly beyond what would be expected in response to the monetary policy actions taken since early last year. Some participants judged that it was still too early to assess with confidence the eventual effects of tighter bank credit conditions on economic activity and noted that it would be important to monitor closely the potential effects of banking-sector developments on credit conditions and economic activity.

In their discussion of the household sector, participants generally noted that consumer spending so far this year had been stronger than expected. Several participants noted that aggregate household wealth remained high, as equity and home prices had not declined much from their recent highs. A few participants mentioned that while, overall, the household sector still retained much of the excess savings it had accumulated during the pandemic, there were signs that consumers were facing increasingly tighter budget constraints, given high inflation and, especially for low-income households, depleted savings.

Regarding the business sector, various participants said that reports from their contacts were mixed, with some pointing to softening economic conditions and others indicating greater-than-expected strength. Many participants noted that developments in the banking sector appeared to have had only a modest effect so far on credit availability for firms. Some participants remarked that the effect of high interest rates on the housing sector appeared to be bottoming out, with home sales, builder sentiment, and new construction all having improved a little since the start of the year.

In their discussion of economic activity, several participants pointed out that recent GDP readings had been stronger than expected earlier in the year, while gross domestic income (GDI) readings had been weak. Of those who noted the discrepancy between GDP and GDI, most suggested that economic momentum may not be as strong as indicated by the GDP readings. In discussing that possibility, a couple of these participants also cited the recent subdued growth in aggregate hours worked.

Participants noted that labor market conditions remained very tight, with robust payroll gains and the unemployment rate still near historically low levels. Nevertheless, they noted some signs that supply and demand in the labor market were coming into better balance, with the prime-age labor force participation rate moving up in recent months and further reductions in rates of job openings and quits, and declines in average weekly hours. A couple of participants conveyed that they heard at a recent Fed Listens event that, in various parts of the country, the lack of affordable housing in the area was preventing some lower-income workers from relocating to accept jobs. Similarly, a few participants noted that their District contacts reported less difficulty in hiring and retaining workers, lower turnover rates, and some layoffs. Some participants pointed out that payroll gains had remained robust but noted that some other measures of employment—such as those based on the Bureau of Labor Statistics' household survey, the Quarterly Census of Employment and Wages, or the Board staff's measure of private employment using data from the payroll processing firm ADP—suggested that job growth may have been weaker than indicated by payroll employment. Participants anticipated that employment growth would likely slow further, consistent with their projections of below-trend economic growth. Participants noted that nominal wage growth had shown signs of easing but observed that it was still running at a pace that, given current estimates of trend productivity growth, was above what would be consistent over the longer run with the Committee's 2 percent inflation objective. Participants expected supply and demand conditions in the labor market to come into better balance over time, easing pressures on wages and prices.

Participants agreed that inflation was unacceptably high and noted that the data, including the CPI for May, indicated that declines in inflation had been slower than they had expected. Participants observed that although core goods inflation had moderated since the middle of last year, it had slowed less rapidly than expected in recent months, despite data and reports from business contacts indicating that supply chain constraints had continued to ease. Some participants noted the recent moderation in housing services inflation and expected this trend to continue. However, a few participants pointed to upside risks to the outlook for housing services inflation associated with near-record low inventories of homes for sale, solid housing demand, and less-than-expected deceleration recently in measures of rents for leases signed by new tenants. Additionally, some participants remarked that core nonhousing services inflation had shown few signs of slowing in the past few months. Several participants noted that longer-term measures of inflation expectations from surveys of households and businesses remained well anchored. Participants emphasized that, with appropriate firming of monetary policy, well-anchored longer-term inflation expectations would support a return of inflation to the Committee's 2 percent longer-run goal over time.

Participants generally noted a high degree of uncertainty regarding the cumulative effects on the economy from both already-enacted monetary policy tightening and the potential additional tightening in credit conditions stemming from recent banking-sector developments. Participants noted that the full effects of monetary tightening had likely yet to be observed, though several highlighted the possibility that much of the effect of past monetary policy tightening may have already been realized. Regarding downside risks to economic activity, participants noted the possibility that the cumulative and rapid tightening of monetary policy would eventually affect economic activity more than expected, and that the additional effects of the tightening of bank credit conditions could prove more substantial than anticipated. Regarding risks to inflation, with inflation remaining well above the Committee's longer-run goal, some participants mentioned the possibility that longer-term inflation expectations could become unanchored, particularly in light of stronger-than-expected consumer demand and a still-tight labor market. Several participants cited the possibility of delayed effects of tighter credit conditions potentially contributing to a slowdown in economic activity that reduces inflationary pressures.

In their consideration of appropriate monetary policy actions at this meeting, participants concurred that while inflation had moderated since the middle of 2022, it remained well above the Committee's longer-run goal of 2 percent. Economic activity had continued to expand at a modest pace. The labor market remained very tight, with robust job gains in recent months and the unemployment rate still low, but there were some signs that supply and demand in the labor market were coming into better balance. The economy was facing headwinds from tighter credit conditions, including higher interest rates, for households and businesses, which would likely weigh on economic activity, hiring, and inflation, al-though the extent of these effect remained uncertain. Against this backdrop, and in consideration of the significant cumulative tightening in the stance of monetary policy and the lags with which policy affects economic activity and inflation, almost all participants judged it appropriate or acceptable to maintain the target range for the federal funds rate at 5 to 5-1/4 percent at this meeting. Most of these participants observed that leaving the target range unchanged at this meeting would allow them more time to assess the economy's progress toward the Committee's goals of maximum employment and price stability. Some participants indicated that they favored raising the target range for the federal funds rate 25 basis points at this meeting or that they could have supported such a proposal. The participants favoring a 25 basis point increase noted that the labor market remained very tight, momentum in economic activity had been stronger than earlier anticipated, and there were few clear signs that inflation was on a path to return to the Committee's 2 percent objective over time. All participants agreed that it was appropriate to continue the process of reducing the Federal

Reserve's securities holdings, as described in its previously announced Plans for Reducing the Size of the Federal Reserve's Balance Sheet.

In discussing the policy outlook, all participants continued to anticipate that, with inflation still well above the Committee's 2 percent goal and the labor market remaining very tight, maintaining a restrictive stance for monetary policy would be appropriate to achieve the Committee's objectives. Almost all participants noted that in their economic projections that they judged that additional increases in the target federal funds rate during 2023 would be appropriate. Most participants observed that uncertainty about the outlook for the economy and inflation remained elevated and that additional information would be valuable for considering the appropriate stance of monetary policy. Many also noted that, after rapidly tightening the stance of monetary policy last year, the Committee had slowed the pace of tightening and that a further moderation in the pace of policy firming was appropriate in order to provide additional time to observe the effects of cumulative tightening and assess their implications for policy. Participants agreed that their policy decisions at every meeting would continue to be based on the totality of incoming information and its implications for the economic outlook as well as the balance of risks. They also emphasized the importance of communicating to the public their data-dependent approach. Most participants observed that postmeeting communications, including the SEP, would help clarify their assessment regarding the stance of monetary policy that is likely to be appropriate to bring inflation down to 2 percent over time.

Participants also discussed several risk-management considerations that could bear on future policy decisions. Almost all participants stated that, with inflation still well above the Committee's longer-run goal and the labor market remaining tight, upside risks to the inflation outlook or the possibility that persistently high inflation might cause inflation expectations to become unanchored remained key factors shaping the policy outlook. Even though economic activity had been resilient recently and that the labor market remained strong, some participants commented that there continued to be downside risks to economic growth and upside risks to unemployment. Despite the receding of the stresses in the banking sector, some participants commented that it would be important to monitor whether developments in the banking sector lead to further tightening of credit conditions and weigh on economic activity. Some participants noted concerns about the potential risks stemming from weakness in commercial real estate.

A number of participants observed that the resolution of the federal government debt limit had removed one source of significant uncertainty for the economic outlook. A few participants noted that there could be some upward pressure on money market rates in the near term as the Treasury issued more bills to meet expenditures and return the balance in the TGA to the Treasury's preferred level. Those participants observed that upward pressure on money market rates relative to the rate offered on the ON RRP facility could lead to a decline in usage of the facility.

Source: Federal Reserve Board