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Data Insights: FOMC Minutes

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July minutes   Key signaling language: Featured   Important   Very important

Respondents to the Open Market Desk's Survey of Primary Dealers and Survey of Market Participants in July continued to place significant probability of a recession occurring by the end of 2024. However, the timing of a recession expected by survey respondents was again pushed later, and the probability of avoiding a recession through 2024 grew noticeably. Survey respondents anticipated that both headline and

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core personal consumption expenditures (PCE) inflation will decline to 2 percent by the end of 2025…

The economic forecast prepared by the staff for the July FOMC meeting was stronger than the June projection. Since the emergence of stress in the banking sector in mid-March, indicators of spending and real activity had come in stronger than anticipated; as a result, the staff no longer judged that the economy would enter a mild recession toward the end of the year. However, the staff continued to expect that real GDP growth in 2024 and 2025 would run below their estimate of potential output growth, leading to a small increase in the unemployment rate relative to its current level…

In their discussion of current economic conditions, participants noted that economic activity had been expanding at a moderate pace. Job gains had been robust in recent months, and the unemployment rate 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, the Committee remained highly attentive to inflation risks.

In assessing the economic outlook, participants noted that real GDP growth had continued to exhibit resilience in the first half of the year and that the economy had been showing considerable momentum. A gradual slowdown in economic activity nevertheless appeared to be in progress, consistent with the restraint placed on demand by the cumulative tightening of monetary policy since early last year and the associated effects on financial conditions. Participants remarked on the uncertainty about the lags in the effects of monetary policy on the economy and discussed the extent to which the effects on the economy stemming from the tightening that the Committee had undertaken had already materialized. Participants commented that monetary policy tightening appeared to be working broadly as intended and that a continued gradual slowing in real GDP growth would help reduce demand–supply imbalances in the economy. Participants assessed that the ongoing tightening of credit conditions in the banking sector, as evidenced in the most recent surveys of banks, also would likely weigh on economic activity in coming quarters. Participants noted the recent reduction in total and core inflation rates. However, they stressed

that inflation remained unacceptably high and that further evidence would be required for them to be confident that inflation was clearly on a path toward the Committee's 2 percent objective. Participants continued to view a period of below-trend growth in real GDP and some softening in labor market conditions as needed to bring aggregate supply and aggregate demand into better balance and reduce inflation pressures sufficiently to return inflation to 2 percent over time.

Participants noted that consumer spending had recently exhibited considerable resilience, underpinned by, in aggregate, strong household balance sheets, robust job and income gains, a low unemployment rate, and rising consumer confidence. Nevertheless, tight financial conditions, primarily reflecting the cumulative effect of the Committee's shift to a restrictive policy stance, were expected to contribute to slower growth in consumption in the period ahead. Participants cited other factors that were likely leading to, or appeared consistent with, a slowdown in consumption, including the declining stock of excess savings, softening labor market conditions, and increased price sensitivity on the part of customers. Some participants observed that recent increases in home prices suggested that the housing sector's response to monetary policy restraint may have peaked.

In their discussion of the business sector, participants cited various improvements in firms' cost structures. These included better-functioning supply chains, lower input costs, and an increased ability to hire and retain workers. Participants also discussed conditions that could lead to higher economic activity—such as leaner inventories and reduced expectations of a sharp economic slowdown—and factors that could lead to lower economic activity—such as continuing economic uncertainty, the vulnerabilities of the CRE market, and the ongoing weakness of manufacturing output. Participants judged that, over coming quarters, firms would reduce the pace of their investment spending and hiring in response to tight financial conditions and the slowing of economic activity.

Participants remarked that the labor market continued to be very tight but pointed to signs that demand and supply were coming into better balance. They noted evidence that labor demand was easing—including declines in job openings, lower quits rates, more part-time work, slower growth in hours worked, higher unemployment insurance claims, and more moderate rates of nominal wage growth. In addition, they remarked

on indications of increasing labor supply, including a further rise in the prime-age participation rate to a post-pandemic high. Participants also observed, however, that although growth in payrolls had slowed recently, it continued to exceed values consistent over time with an unchanged unemployment rate, and that nominal wages were still rising at rates above levels assessed to be consistent with the sustained achievement of the Committee's 2 percent inflation objective. Participants judged that further progress toward a balancing of demand and supply in the labor market was needed, and they expected that additional softening in labor market conditions would take place over time.

Participants cited a number of tentative signs that inflation pressures could be abating. These signs included some softening in core goods prices, lower online prices, evidence that firms were raising prices by smaller amounts than previously, slower increases in shelter prices, and recent declines in survey estimates of shorter-term inflation expectations and of inflation uncertainty. Various participants discussed the continued stability of longer-term inflation expectations at levels consistent with 2 percent inflation over time and the role that the Committee's policy tightening had played in delivering this outcome. Nonetheless, several participants commented that significant disinflationary pressures had yet to become apparent in the prices of core services excluding housing.

Participants observed that, notwithstanding recent favorable developments, inflation remained well above the Committee's 2 percent longer-term objective and that elevated inflation was continuing to harm businesses and households—low-income families in particular. Participants stressed that the Committee would need to see more data on inflation and further signs that aggregate demand and aggregate supply were moving into better balance to be confident that inflation pressures were abating and that inflation was on course to return to 2 percent over time.

Participants generally noted a high degree of uncertainty regarding the cumulative effects on the economy of past monetary policy tightening. Participants cited upside risks to inflation, including those associated with scenarios in which recent supply chain improvements and favorable commodity price trends did not continue or in which aggregate demand failed to slow by an amount sufficient to restore price stability over time, possibly leading to more persistent elevated inflation or an

unanchoring of inflation expectations. In discussing downside risks to economic activity and inflation, participants considered the possibility that the cumulative tightening of monetary policy could lead to a sharper slowdown in the economy than expected, as well as the possibility that the effects of the tightening of bank credit conditions could prove more substantial than anticipated.

In their discussion of financial stability, participants observed that the banking system was sound and resilient and that banking stress had calmed in recent months. Participants also noted that the most recent stress-test results indicated that large banks appeared to be well positioned to withstand a severe recession. Various participants commented on risks that could affect some banks, including unrealized losses on assets resulting from rising interest rates, significant reliance on uninsured deposits, and increased funding costs. Participants also commented on risks associated with a potential sharp decline in CRE valuations that could adversely affect some banks and other financial institutions, such as insurance companies, that are heavily exposed to CRE. Several participants noted the susceptibility of some nonbank financial institutions, such as money market funds or digital asset entities, to runs or instability. In addition, several participants emphasized the need for banks to establish readiness to use Federal Reserve liquidity facilities and for the Federal Reserve to ensure its own readiness to provide liquidity during periods of stress.

In their consideration of appropriate monetary policy actions at this meeting, participants concurred that economic activity had been expanding at a moderate pace. The labor market remained very tight, with robust job gains in recent months and the unemployment rate still low, but there were continuing signs that supply and demand in the labor market were coming into better balance. Participants also noted that tighter credit conditions facing households and businesses were a source of headwinds for the economy and would likely weigh on economic activity, hiring, and inflation. However, the extent of these effects remained uncertain. Although inflation had moderated since the middle of last year, it remained well above the Committee's longer-run goal of 2 percent, and participants remained resolute in their commitment to bring inflation down to the Committee's 2 percent objective. Amid these economic conditions, almost all participants judged it appropriate to raise the target range for the federal funds rate to 5-1/4 to 5-1/2 percent at this meeting. Participants noted that this action would put the stance of monetary policy further into restrictive

territory, consistent with reducing demand–supply imbalances in the economy and helping to restore price stability. A couple of participants indicated that they favored leaving the target range for the federal funds rate unchanged or that they could have supported such a proposal. They judged that maintaining the current degree of restrictiveness at this time would likely result in further progress toward the Committee's goals while allowing the Committee time to further evaluate this progress. 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. A number of participants noted that balance sheet runoff need not end when the Committee eventually begins to reduce the target range for the federal funds rate.

In discussing the policy outlook, participants continued to judge that it was critical that the stance of monetary policy be sufficiently restrictive to return inflation to the Committee's 2 percent objective over time. They noted that uncertainty about the economic outlook remained elevated and agreed that policy decisions at future meetings should depend on the totality of the incoming information and its implications for the economic outlook and inflation as well as for the balance of risks. Participants expected that the data arriving in coming months would help clarify the extent to which the disinflation process was continuing and product and labor markets were reaching a better balance between demand and supply. This information would be valuable in determining the extent of additional policy firming that may be appropriate to return inflation to 2 percent over time. Participants also emphasized the importance of communicating as clearly as possible about the Committee's data-dependent approach to policy and its firm commitment to bring inflation down to its 2 percent objective.

Participants discussed several risk-management considerations that could bear on future policy decisions. With inflation still well above the Committee's longer-run goal and the labor market remaining tight, most participants continued to see significant upside risks to inflation, which could require further tightening of monetary policy. Some participants commented that even though economic activity had been resilient and the labor market had remained strong, there continued to be downside risks to economic activity and upside risks to the unemployment rate; these included the possibility that the macroeconomic effects of the tightening in financial

conditions since the beginning of last year could prove more substantial than anticipated. A number of participants judged that, with the stance of monetary policy in restrictive territory, risks to the achievement of the Committee's goals had become more two sided, and it was important that the Committee's decisions balance the risk of an inadvertent overtightening of policy against the cost of an insufficient tightening.

Source: Federal Reserve Board