USA: FOMC Minutes Note Participants Would Support Unchanged or Lower Rates if Inflation Dissipates "Soon" but Higher Rates if Inflation

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BOTTOM LINE: The minutes to the FOMC's June meeting noted that "all" participants supported keeping the fed funds rate unchanged in June, although "a few" participants thought there was "a case" for a hike. "Almost all" participants who discussed scenarios where inflation dissipated "soon" would support an unchanged or lower fed funds rate in such cases, while "almost all" who discussed scenarios where inflation remained elevated would support "some policy firming" in such cases. We expect year-over-year core PCE inflation to slow to 3.0% by December 2026 (vs. 3.4% currently), partially reflecting the effects of methodological changes announced by the BEA a few weeks after the June meeting. We forecast core CPI inflation of 2.6% by December 2026 (vs. 2.9% currently) and expect tame month-over-month readings for core CPI over the next few months. While we see some risk of hikes this year, our base case remains that the FOMC keeps the policy rate unchanged in 2026.

MAIN POINTS:

1. The minutes to the FOMC's June meeting noted that "all" participants supported the decision to maintain the target range for the fed funds rate at 3.5-3.75%. "A few" participants judged that "there was a case" for raising the fed funds rate in June.

2. The minutes noted that "various participants" discussed a range of macroeconomic scenarios with respect to the outlook for monetary policy. "Most" participants discussed scenarios in which inflationary pressures dissipated and inflation "soon" began to return to 2%, and "almost all" of these participants said that it would likely be appropriate to "maintain or eventually lower" the fed funds rate in such cases. "Most" participants also discussed scenarios in which inflation remained elevated as a result of AI-related demand, the Middle East conflict, or tariffs, and "almost all" of these participants indicated that "some policy firming would likely be warranted" in such cases.

3. Participants generally noted that inflation had "increased further and remained well above" the 2% target, reflecting tariffs, supply chain disruptions, and AI-related investment demand. "Several" participants noted that price pressures had become more broad-based—partly reflecting higher transportation, airfares, petrochemicals, and agricultural input prices—and "several" also noted that services inflation excluding housing "remained high." "Most" participants noted that above-potential growth as a result of strong AI-related investment demand "could contribute to more persistent inflationary pressures."

4. Participants judged that the labor market remained stable, and "many" participants noted that the labor market was "not currently a source of inflationary

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pressures." Participants also noted that economic activity was growing at a "solid" pace, supported by strong business investment concentrated in AI-related spending. "Most" participants noted that higher equity prices and tax refunds earlier this year had supported consumer spending, especially among higher-income households.

5. The Fed staff's inflation forecast for this year and next was "higher" than at the April meeting, reflecting incoming data, higher energy prices, and AI effects. The staff expected core inflation to "change little" over the rest of the year before stepping down next year and moving "further down to about 2 percent" in 2028. The staff expected the unemployment rate to remain close to its longer-run rate before "edging slightly below it" in 2028.

6. We expect year-over-year core PCE inflation to slow to 3.0% by December 2026 (vs. 3.4% currently), partially reflecting the effects of methodological changes announced by the BEA a few weeks after the June meeting. We forecast core CPI inflation of 2.6% by December 2026 (vs. 2.9% currently) and expect tame month-over-month readings for core CPI over the next few months. While we see some risk of hikes this year, our base case remains that the FOMC keeps the policy rate unchanged in 2026.