



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

No point-in-time-safe data on System Open Market Account holdings was available on or before the cutoff for this meeting, and accordingly the Committee is unable to report the total size, security composition, or change from the prior release of SOMA holdings on a basis consistent with the disclosure standard applied elsewhere in these minutes. This section covers SOMA holdings only; it does not describe the results of repurchase or reverse repurchase operations, for which no point-in-time-safe data source currently exists. The absence of these figures should be read as a gap in the available record rather than as an indication that no operations occurred over the intermeeting period.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reported that economic activity continued to expand at a moderate pace. The Chicago Fed National Activity Index stood at 0.06, near its trend value, and initial claims for unemployment insurance were 317,000, a level consistent with a stable labor market. The unemployment rate was 4.6 percent, below the estimated natural rate of 5.21 percent, pointing to tight conditions across the labor market. Core PCE inflation on a year-over-year basis was 1.45 percent, running below the 2 percent objective. M2 stood at \$3,975.8 billion.

The most recent Beige Book, prepared before November 24, characterized growth as continuing at a 'moderate pace' since the prior report. Non-auto retail sales improved in most Districts, aided in the eastern half of the country by the late arrival of winter weather, while automobile sales remained sluggish with inventories on the high side. Manufacturers reported high levels of activity, with some constrained by capacity limits and, in the West and South, by rail bottlenecks. Virtually all regions reported tight labor markets, with wage pressures in specific industries and occupations facing labor shortages and particular difficulty hiring and retaining seasonal workers; employers were reported to be using a variety of nonwage incentives to attract and retain staff. Despite this tightness, business respondents described price pressures as remaining 'neutral, on balance,' with steady-to-declining commodity prices, productivity gains, and increasing overseas competition offsetting the effects of wage gains. Asian financial turmoil and currency weakness were cited as having reduced demand for manufactured and agricultural exports and, in some Districts, as raising competition from imports.

STAFF REVIEW OF THE FINANCIAL SITUATION

Financial conditions were broadly stable, with pockets of elevated volatility tied to overseas developments. The financial stress index stood at 0.1563, a moderate reading, while the VIX at 23.36 indicated a degree of market nervousness. Credit markets showed no acute distress: the Baa corporate



spread was 1.5 percentage points, a contained level. The Treasury yield curve was only slightly positive, with the 10-year/2-year spread at 0.14 percentage point, a flat profile that offered no strong recession signal but little sign of expected tightening either. The 3-month Treasury bill traded 0.37 percentage point below the current federal funds rate of 5.5 percent, suggesting that markets anticipated no near-term hike and possibly an eventual easing of policy.

STAFF ECONOMIC OUTLOOK

The staff outlook, drawing on the forward-looking quantities available, pointed to a mildly restrictive current policy stance against a backdrop of soft and decelerating inflation. With the estimated neutral rate (r^*) at 3.086 percent and core inflation near 1.45 percent, the real federal funds rate at the prevailing 5.5 percent setting sits above neutral. Inflation momentum was negative at -0.145, consistent with disinflation rather than acceleration, while unemployment momentum was essentially flat at 0.05, implying no meaningful further tightening of labor-market slack in the near term.

The reference rules straddled the current stance. The Taylor rule prescribed -50 basis points, reflecting inflation running materially below target combined with the output and employment picture; the First-Difference rule prescribed -25 basis points, responding to the direction of change in inflation; and both the Balanced Approach and ELB-adjusted rules prescribed +25 basis points, driven chiefly by the sub-natural unemployment rate. The deterministic policy engine, judging the reference rules reliable, reconciled these to a recommended -25 basis points. Taken together, the neutral-rate estimate, the negative inflation momentum, and the clustering of the First-Difference and engine outputs at -25 basis points imply a likely path in which conditions warrant a modest reduction in the degree of restraint, with the more aggressive Taylor signal tempered by still-tight labor markets and the hawkish rules discounted by the absence of realized price acceleration.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their initial predictive discussion, all five participants independently arrived at holding the federal funds rate steady at 5.5 percent. Participants generally judged that core PCE inflation at 1.45 percent, below the 2 percent objective, removed any case for tightening, while tight labor markets and the absence of any realized weakness removed any case for easing. Several observed that the Beige Book's characterization of price pressures as neutral was doing considerable work in this assessment: productivity gains, steady-to-declining commodities, and overseas competition were seen as absorbing the wage gains associated with a 4.6 percent unemployment rate running below the 5.21 percent natural rate.



The genuine points of emphasis differed by participant. One participant, focused on inflation risk, framed tight labor as the one latent threat worth monitoring but stressed that wage-to-price transmission was not yet visible and that Asian financial turmoil was itself a disinflationary and growth-dampening force. A participant weighting employment most heavily noted that his usual bias toward easing to protect jobs was not triggered, since claims at 317,000 were low and the Beige Book reported tight labor everywhere; he judged that holding preserved the ability to cut quickly should Asian contagion begin to bite. A participant attentive to financial stability weighed the elevated VIX and the explicit Beige Book references to Asian turmoil against contained credit spreads and a moderate stress index, concluding that a surprise hike could destabilize already-nervous conditions while no acute stress justified a cut. A participant reading markets most closely pointed to the 3-month bill trading 37 basis points below the funds rate and the near-flat yield curve as market-implied signals of steady-to-easier policy ahead. A centrist participant read the balance of indicators at face value and found no data-supported justification for a move in either direction. On rebuttal, none of the participants was moved off a hold; the convergence, if anything, reinforced each in his own reasoning.

When the discussion turned to the deterministic framework's -25 basis point recommendation, the emphasis shifted. Participants generally accepted the framework's logic that, with r^* near 3.086 percent and inflation near 1.45 percent, the current 5.5 percent setting was mildly restrictive, and that negative inflation momentum argued for correcting a stance tighter than conditions warranted. Most found the First-Difference rule's -25 basis points more persuasive than the Taylor rule's -50, judging that the larger cut would overshoot given how tight labor markets remained; the +25 basis point rules were discounted on the grounds that wage tightness was not feeding through to prices and that markets were not pricing hikes.

Differences emerged over whether to endorse the cut in full. The participant weighting employment came to view a measured 25 basis point cut as insurance for the labor market against Asian spillover to manufacturing employment while inflation stayed benign, and endorsed the recommendation. The financial-stability participant was persuaded that the insurance value against overseas turmoil, set against a flattening curve and contained-but-not-loose credit conditions, aligned with the optimal call, and likewise endorsed. The market-focused participant found that the -25 basis point recommendation mapped cleanly onto the bill spread's implied quarter-point of easing and endorsed it, noting the financial-stability case had strengthened his conviction on magnitude.

Two participants agreed with the easing direction but not with acting now. The inflation-focused participant conceded that his usual trigger was absent and that policy was mildly restrictive, but held that cutting into a hot labor market risked unlocking latent wage-price pressure and that he would



prefer to confirm disinflation before locking in a cut. The centrist participant, favoring the most literal reading of the data, judged that at-trend activity and tight labor gave no urgent case to move ahead of confirmation, even as he agreed the easing direction was supportable. Both thus supported the direction while parting company on timing and magnitude.

COMMITTEE POLICY ACTIONS

In the predictive vote, all five participants supported holding the federal funds rate unchanged at 5.5 percent, a unanimous 5-0 outcome. On the deterministic framework's separate recommendation of a 25 basis point cut, the Committee did not divide over direction but did divide over magnitude and timing: three participants -- those weighting employment, financial stability, and market signals -- endorsed the -25 basis point recommendation as-is, while two participants -- the one focused on inflation risk and the data-dependent centrist -- registered partial support, agreeing with the easing direction but not with cutting at this meeting. No participant declined the recommendation outright.