PREDICTED FED DECISION **HOLD**

1.00%–1.25%

OPENFED OPTIMAL RATE **−25 bps**

0.75%–1.00%

KEY TAKEAWAY

The Committee expects the real Federal Reserve to hold at 1.0%-1.25%, but judges the optimal policy to be a 25 basis point cut, given a persistent inflation shortfall its predictive hold leaves unaddressed.

STATEMENT

The most striking feature of the incoming data is a labor market and an inflation reading pointing in opposite directions. Unemployment at 4.2% sits below the 4.74% estimate of its natural rate, jobless claims are low at 222,000, and the Beige Book describes tight labor markets with hiring that has picked up and, in a few districts, broadening wage pressures. Yet core PCE inflation is running at just 1.07%, nearly a full percentage point below the 2% objective, with most districts reporting wage and price pressures as 'modest' or 'subdued.' Financial conditions are calm on every measure the Committee reviews: the financial stress index near zero at 0.027, the VIX unusually low at 11.23, the Baa credit spread tight at 1.92, and a yield curve that remains positively sloped at 0.83, with no recession signal in the front end.

In forming its judgment about the likely action of the real Federal Reserve, participants weighed the tight labor market against the soft inflation print. Some participants argued that unemployment below its natural rate, together with financial conditions loose enough to absorb a modest move, favored a 25 basis point increase as a preemptive step along the gradual normalization path implied by the prior median projection of 1.4%. Others placed decisive weight on market pricing and on the inflation shortfall itself: the 3-month T-bill spread of -0.025 indicates no hike is priced for this meeting, and with core PCE well below target there is no near-term urgency forcing a move. Participants favoring patience noted that the prior meeting held unanimously with data-dependent 'gradual increases' guidance, that hurricane price effects are viewed as transitory, and that the next hike is more plausibly expected at a later meeting than at this one. On balance, the Committee's predictive judgment is that policy will be left unchanged, with the target range held at 1.0% to 1.25%.

The Committee's own deterministic framework, by contrast, points toward easing. Its recommended action is a reduction of 25 basis points. That conclusion rests on the same inflation shortfall the predictive discussion set against labor-market tightness, but read through the loss function it weighs more heavily: inflation momentum of -0.1 indicates the shortfall is drifting lower rather than self-correcting, and an estimated r* of -0.5 implies that the current range is modestly restrictive relative to neutral. Every reliable reference rule points in the same direction and more aggressively than the framework's own recommendation. The Taylor rule, the balanced-approach rule, and the ELB-adjusted rule each read -75 basis points, and the first-difference rule reads -50. The framework tempers these mechanical readings to a single -25 basis point step, a magnitude that respects the tight labor market and the possibility of hurricane-distorted prints while still taking the persistent undershoot at face value.

The gap between the predictive hold and the optimal cut is the substance of this meeting. Participants reconciled the two by locating the predictive hold in institutional caution mid-normalization and the prior 'gradual increases' guidance, while acknowledging that the framework's math correctly flags current policy as leaning against, rather than with, the inflation mandate. Even the more inflation-focused reasoning accepted that chronic undershooting erodes the 2% anchor as surely as overshooting, so the usual caution about easing does not apply when inflation is below target and softening. With unemployment momentum near flat at +0.05 and no employment deterioration to fear, and with tranquil credit and volatility conditions making a small cut low-risk, the Committee judged the optimal policy to be a gradual, insurance-oriented -25 basis points toward target.

COMMITTEE VOTE	The predictive vote favored no change to the target range, 3 to 2, with two participants preferring a 25 basis point increase. On the framework's recommendation of a 25 basis point cut, the Committee's optimal-side deliberation was unanimous, 5 to 0 in support.
NOTES	*On the predictive side, two participants would have preferred a 25 basis point hike, resting their case on unemployment below the 4.74% natural rate, low jobless claims, and broadening wage pressures in a few districts, together with loose financial conditions they judged able to absorb a preemptive move along the gradual path implied by the 1.4% prior median projection.*