



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The Committee reviewed the most recent data on the System Open Market Account. As of September 11, 2019, total SOMA domestic securities holdings stood at \$3,568.9 billion. The composition was dominated by Treasury notes and bonds at \$1,941.3 billion and agency mortgage-backed securities at \$1,489.6 billion, with a comparatively small \$3.0 billion in Treasury bills. Relative to the prior release of September 4, total holdings rose by \$5.6 billion. It was noted that this review covers SOMA securities holdings only — total size, composition, and the week-over-week change — and does not extend to the results of repo or reverse-repo operations, for which no point-in-time-safe data source currently exists.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reported that inflation remained soft. Core PCE inflation stood at 1.41 percent on a year-over-year basis, well below the Committee's 2 percent objective. The labor market continued to look tight by conventional measures: the unemployment rate was 3.7 percent, below the estimated natural rate of 4.57 percent, and initial jobless claims were low at 217,000. At the same time, the Chicago Fed National Activity Index registered -0.36, consistent with growth running somewhat below its trend pace. The Employment Cost Index reading of 137.0 and the various Beige Book descriptions of wage growth as having 'picked up a bit' or as 'moderate' did not point to an acceleration of the kind a fully overheating labor market would produce.

The Beige Book pointed to activity expanding at a modest pace on balance, with a recurring split between softening goods production and firmer services. Several Districts reported declines or slowing in manufacturing, trucking, and freight, while tourism, ports, staffing, and nonfinancial services generally saw increasing activity. Labor markets remained tight across Districts, with contacts continuing to report difficulty finding qualified workers, though some Districts described job creation as 'sluggish.' Prices were broadly characterized as rising 'modestly' or 'little changed,' with contacts in one District citing a lack of materials cost inflation, intense competition, and softening demand. Residential inventories were reported down, with bidding wars noted in some areas, while commercial real estate strengthened on balance. Several contacts expressed more caution in their six-month outlook, citing uncertainty.

STAFF REVIEW OF THE FINANCIAL SITUATION

The staff characterized financial conditions as calm and non-distressed. The financial stress index was very low at 0.087, and the VIX stood at a subdued 14.61, indicating benign volatility. The Baa corporate spread of 2.22 was moderate and did not signal credit-market distress or a widening in borrowing costs.



The yield curve, however, drew particular attention: the 10-year/2-year spread was barely positive at 0.07, near inversion, while the 3-month T-bill spread against the current policy rate was -0.215, indicating that the short end had already priced in expectations of near-term easing. Taken together, the picture was one of orderly markets absent acute stress, alongside a curve configuration that markets appeared to be reading as a forward-looking recession-risk signal.

STAFF ECONOMIC OUTLOOK

The staff outlook drew on the forward-looking quantities available. The estimated neutral real rate (r^*) was negative at -0.366, implying that the current target range of 2.00 to 2.25 percent was likely modestly restrictive relative to a low neutral setting. Both momentum measures were small: inflation momentum was 0.015 and unemployment momentum was -0.05, suggesting that underlying conditions were evolving gradually rather than shifting abruptly. This combination — a low neutral rate but only slight momentum in either direction — pointed toward a projection of continued modest support for activity without a sharp repricing of the policy stance.

The reference rules spanned a notable range. The Taylor rule, the Balanced Approach rule, and the ELB-adjusted rule each prescribed -75 bps, reflecting the large gap between core PCE at 1.41 percent and the 2 percent objective together with unemployment well below the natural rate. The First-Difference rule, by contrast, prescribed -25 bps, consistent with its reliance on the small momentum figures rather than on level gaps. With the reference rules judged reliable, the framework's loss-minimizing recommendation aligned with the First-Difference reading at -25 bps — an incremental adjustment that leaned against the aggressive level-based rules. The staff projection thus implied a path of gradual accommodation: enough to counter below-trend activity signals and curve-flattening risk, but short of the front-loaded easing the level-gap rules would imply.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their discussion of current conditions, participants converged early on the view that a further 25 basis point reduction was the appropriate step, framed as a continuation of the insurance easing begun at the prior meeting. The member most attentive to inflation risk observed that his usual caution against cutting was at its weakest in the present configuration: with core PCE at 1.41 percent, well below target, there was simply no upside inflation to defend against. He checked explicitly for hidden price pressure and found none — the Employment Cost Index and Beige Book wage descriptions did not signal a wage-price spiral, and prices were repeatedly described as modest or little changed. Tight labor at 3.7 percent versus a 4.57 percent natural rate was not translating into inflation. On that basis he found no inflation-grounded reason to prefer a hold, while noting that the recession and growth signals — the near-flat 10y-2y spread, the sub-trend Chicago Fed index, and softening manufacturing — argued



affirmatively for accommodation.

The participant weighting employment risk most heavily emphasized that levels alone understated the case for pre-emptive action. Although unemployment was low, several Districts flagged 'sluggish' job creation, and wage growth had only 'picked up a bit' — not the acceleration a genuinely tight market would generate. Recurring manufacturing declines across Districts were, in his reading, a leading warning for future employment that he preferred to get ahead of before layoffs materialized. He was not persuaded toward a larger move: with claims low at 217,000 and financial stress benign, insurance easing rather than a response to any domestic collapse was the right posture. The participant focused on financial stability agreed that the stress metrics — the 0.087 stress index, the 14.61 VIX, and the contained 2.22 Baa spread — ruled out any case for a 50 or 75 basis point move that could itself signal alarm and destabilize orderly markets. What weighed against holding, in his view, was the curve: letting policy sit while the 10y-2y spread flirted with inversion riskened tightening effective financial conditions and validating a recession signal.

The participant most attentive to market pricing anchored the discussion on the -0.215 T-bill spread, which he read as the most direct available signal of the expected path — consistent with roughly one 25 basis point cut priced at or near this meeting. Delivering that cut, he argued, would avoid a hawkish surprise, while going deeper than priced would be a destabilizing shock in its own right. The data-dependent member reached the same destination from a face-value reading: below-target inflation and a near-inverted curve supported easing, while solid labor and calm markets argued against anything aggressive. Across the rebuttal round, no participant was moved toward either a hold or a deeper cut, and all five settled on -25 bps to a range of 1.75 to 2.00 percent.

When the discussion turned to the framework's loss-minimizing recommendation, participants engaged directly with the divergence among the reference rules. Several noted that the Taylor, Balanced Approach, and ELB-adjusted rules all prescribed -75 bps, driven mechanically by the large inflation gap and unemployment far below the natural rate. Participants were broadly skeptical of that magnitude. The inflation-focused member judged that a 3.7 percent unemployment rate with tight labor did not warrant large easing and that 75 basis points risked seeding a future overshoot he would later have to fight. The First-Difference rule's -25 bps, by contrast, drew the most support: it responds to the small inflation (0.015) and unemployment (-0.05) momentum readings rather than to distant level gaps, favoring gradualism and preserving optionality. The participant weighting employment risk added that the aggressive rules implicitly assumed policy was very restrictive, but claims and unemployment momentum did not yet justify front-loading; cutting now preserved room to ease again if hiring deteriorated.



Participants also drew on the negative neutral-rate estimate of -0.366 to characterize the current stance as modestly, not dramatically, too tight — implying that the Committee need not cut hard to reach an accommodative posture. The financial-stability participant tied this together with the calm stress readings to argue that incremental adjustment threaded the needle between curve-flattening risk and orderly credit conditions. The market-focused member likewise found the First-Difference logic most persuasive precisely because it tracked the incremental easing markets had already discounted, and read the independent convergence of his own predictive vote and the framework's recommendation as confirmation that a measured step was appropriately calibrated. A recurring theme was a preference to avoid language implying an extended easing path, keeping the action framed as reversible insurance should price pressures firm.

COMMITTEE POLICY ACTIONS

In the predictive vote on the policy decision, all five participants supported a 25 basis point reduction in the target range, to 1.75 to 2.00 percent from the current 2.00 to 2.25 percent, a unanimous tally of five to zero. On the separate question of the framework's optimal-policy recommendation of -25 bps, the Committee was likewise in full agreement: all five members endorsed the recommendation as-is, with none declining and none registering only partial agreement. The two votes thus pointed in the same direction, reflecting a shared judgment that measured, incremental easing — rather than the larger moves prescribed by several level-based reference rules — best fit below-target inflation, still-solid labor conditions, calm financial markets, and a near-inverted yield curve.