



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The System Open Market Account's domestic securities holdings totaled \$7,373.4 billion as of September 13, 2023, the most recent release available on or before the point-in-time-safe cutoff. Within that total, Treasury notes and bonds accounted for \$4,237.0 billion, Treasury bills for \$252.0 billion, and agency mortgage-backed securities for \$2,490.5 billion. Holdings declined by \$6.2 billion from the prior release of September 6. The staff noted that this account covers SOMA securities holdings only — total size, composition, and week-over-week change — and does not encompass repo or reverse-repo operation results, for which no point-in-time-safe data source currently exists; accordingly, no discussion of those operations is included here.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reviewed incoming data on activity, labor markets, and prices. Core PCE inflation stood at 3.19 percent on a twelve-month basis, still well above the Committee's 2 percent objective though continuing to run below its earlier peaks. The unemployment rate was 3.8 percent, below the estimated natural rate of 4.42 percent, and initial jobless claims remained low at 216,000, indicating no meaningful softening in labor demand. The Chicago Fed National Activity Index registered 0.12, a reading slightly above its historical trend, and the Employment Cost Index stood at 159.0. M2 money supply measured \$20,902.7 billion. The current target range for the federal funds rate was 5.25 to 5.50 percent, with a midpoint of 5.375 percent.

Beige Book reports described activity as generally flat to modestly higher across districts. Several districts noted that manufacturing demand had softened while freight and transportation volumes had largely stabilized. Consumer spending was characterized as picking up modestly in some districts, with strong new auto sales aided by improved inventories, while demand for high-end goods weakened. On the labor side, employment was reported to have increased moderately with hiring remaining healthy, and wage pressures were described as easing or flat across multiple districts. On prices, contacts in several districts reported that price growth had eased slightly and that firms were increasingly struggling to pass on higher costs amid greater price sensitivity. Commercial real estate activity and lending were reported to have declined in at least one district, and financial conditions were described as having tightened moderately in another.

STAFF REVIEW OF THE FINANCIAL SITUATION

Financial conditions were broadly calm. The financial stress index stood at 0.186, a low reading indicating no acute systemic strain, and the VIX was subdued at 13.48. The Baa corporate spread of 1.79 was moderate and showed no sign of credit-market distress or widening. The 10-year/2-year Treasury



yield curve was deeply inverted at -0.71 , a configuration historically associated with expectations of slower growth ahead. The 3-month T-bill spread relative to the current rate was -0.055 , with the bill sitting just below the current target range — consistent with market participants viewing the policy rate as at or near its cyclical peak and pricing little expectation of a further increase in the near term.

STAFF ECONOMIC OUTLOOK

The staff's forward-looking assessment drew on the neutral-rate estimate, the momentum in inflation and unemployment, and the outputs of the reference policy rules. The estimate of r^* used in the framework was -0.5 , which places the current 5.25 to 5.50 percent target range meaningfully above neutral and implies that policy is exerting restraint on demand. Inflation momentum was slightly negative at -0.005 , suggesting price pressures were easing modestly rather than reaccelerating, while unemployment momentum was slightly positive at 0.05 , consistent with a labor market that is gradually loosening from very tight levels rather than deteriorating.

The reference rules diverged sharply. The Taylor rule, the Balanced Approach rule, and the ELB-adjusted rule each pointed to -75 basis points, reflecting inflation moving down toward target relative to a low neutral rate. The First-Difference rule, which prescribes changes from the current stance rather than a jump to an implied level, pointed to $+75$ basis points, reflecting inflation still well above 2 percent and unemployment below the natural rate. The loss-minimizing recommendation, with the reference rules judged reliable, netted to 0 basis points. Taken together, these quantities imply an economy in which restraint is still in place and disinflation is proceeding gradually, but in which the appropriate near-term path is best characterized as holding steady and allowing the cumulative effects of prior tightening to continue transmitting through lags, rather than moving decisively in either direction.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their discussion of current conditions, participants agreed that core PCE inflation at 3.19 percent remained well above the 2 percent objective, and this judgment anchored much of the conversation. Several participants stressed that inflation this elevated ruled out any easing at the present meeting, while also emphasizing that the incoming evidence pointed to disinflation gaining traction. One participant, whose primary lens was inflation risk, observed that firms across multiple districts reported difficulty passing on price increases and that wage pressures had eased in the Atlanta, Chicago, St. Louis, and Minneapolis reports, with price growth easing slightly in Richmond. In this view, cumulative tightening appeared to be propagating through the economy without requiring an additional increase, and the modestly negative inflation momentum reinforced the case that a further hike was not yet demanded.



Participants attentive to labor conditions noted that the market showed no signs of the deterioration that would justify a cut. Unemployment at 3.8 percent remained below the 4.42 percent natural rate, jobless claims at 216,000 were low, and the Beige Book described employment increasing moderately with healthy hiring. One participant remarked that cutting into a still-tight labor market with inflation above 3 percent would be premature and could risk reigniting demand, and cautioned that premature easing might force sharper tightening later that would be far more damaging to employment. At the same time, this participant, along with others, framed a hold rather than a hike as the way to guard against over-tightening into an economy showing broadly flat-to-modest activity, with the Chicago Fed index near trend at 0.12.

From a financial-stability perspective, participants judged that conditions were calm enough to support patience in either direction. The stress index at 0.186 and the VIX at 13.48 indicated no acute market strain, and the Baa spread at 1.79 signaled orderly if tight borrowing conditions. Two considerations drew particular attention. First, the deeply inverted 10-year/2-year curve at -0.71 was cited as a caution flag: adding a hike into an inverted curve was seen as risking amplified credit tightening without a clear inflation justification, particularly given Beige Book reports of declining commercial real estate lending and moderately tighter financial conditions in some districts. Second, the 3-month T-bill spread of -0.055 was read as evidence that markets viewed the rate at or near its peak and priced neither a further hike nor an imminent cut. A participant focused on market-implied pricing emphasized that these signals aggregated to a pause, reconciling the tension in the data toward holding.

When the discussion turned to the optimal-policy framework, participants engaged directly with the wide dispersion in the reference rules. Several observed that three rules calling for -75 basis points against one calling for +75 basis points itself argued for restraint, with the loss-minimizing output of 0 basis points representing a prudent middle path amid genuinely conflicting signals. The inflation-focused participant noted that the First-Difference rule aligned most closely with an inflation-weighted instinct but accepted that slightly negative inflation momentum meant a hike was not yet warranted, and firmly rejected the deep cuts implied by the level rules while core PCE exceeded 3 percent. The labor-focused participant likewise found the First-Difference logic persuasive for changing policy from the current stance rather than jumping to an implied level, and reasoned that the divergence between the -75 rules and the 0 outcome revealed policy as near, but not clearly beyond, appropriate restriction.

Across both the predictive and the framework discussions, participants converged on the view that the current stance was appropriately restrictive and that holding preserved optionality. They generally judged that no member had made a case for easing that the data supported, and that none saw grounds



for a further hike given the prior signal of a possible pause, the working of policy lags, and the broadly easing wage and price pressures in the Beige Book. Participants indicated they would remain vigilant: some noted they stood ready to support resuming increases if inflation stalled or reaccelerated, while others said they would advocate cuts only if labor data softened materially or if stress indicators broke higher. The prevailing sentiment was that letting prior cumulative tightening continue to work through lags was the disciplined choice.

COMMITTEE POLICY ACTIONS

In the predictive round, all five members supported holding the target range at 5.25 to 5.50 percent, an unchanged stance, yielding a unanimous 5-0 vote for 0 basis points. On the framework's loss-minimizing recommendation of 0 basis points, the Committee was likewise in full agreement: all five members — the inflation hawk, the labor market dove, the financial stability voice, the data-dependent centrist, and the market signal realist — endorsed the recommendation as-is, with none declining and none registering partial agreement. The predictive vote and the optimal-side outcome were therefore fully consistent, both reflecting the judgment that the current range was appropriately restrictive and that patience was warranted while prior tightening continued to transmit through lags.