



DEVELOPMENTS IN FINANCIAL MARKETS AND OPEN MARKET OPERATIONS

The System Open Market Account portfolio stood at \$6,641.6 billion in domestic securities as of the July 24 release, the most recent report available on or before the point-in-time-safe cutoff. Composition was concentrated in longer-dated Treasury securities, with notes and bonds accounting for \$3,762.5 billion and Treasury bills making up a comparatively small \$195.3 billion, while agency mortgage-backed securities totaled \$2,324.1 billion. The portfolio declined by \$3.7 billion relative to the prior release on July 17, a modest reduction. Members were reminded that this review covers SOMA securities holdings only — total size, composition, and the 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.

STAFF REVIEW OF THE ECONOMIC SITUATION

The staff reported that core PCE inflation stood at 2.27 percent on a twelve-month basis, above but not far from the 2 percent objective. Labor market indicators pointed to a solid but gradually cooling picture: the unemployment rate was 4.1 percent, below the estimated natural rate of 4.41 percent, while initial jobless claims registered 243,000, elevated relative to recent lows. The Chicago Fed National Activity Index at 0.05 was consistent with growth near trend, and the Employment Cost Index reading was 164.0. M2 money supply stood at \$21,024.7 billion. The current federal funds target range was 5.25 to 5.50 percent, restrictive relative to the Committee's own last median projected rate of 5.1 percent.

The Beige Book described economic activity as expanding at a slight to modest pace across a majority of Districts, though the balance had shifted: seven Districts reported some increase in activity while five noted flat or declining conditions — three more than in the prior reporting period. Household spending was little changed, and most Districts reported soft demand for both consumer and business loans. On employment, the staff noted that hiring rose only at a slight pace overall, with several Districts reporting manufacturing job declines tied to slower new orders, lower labor turnover, and contacts indicating they expected to be more selective and not backfill all open positions. Wages continued to grow at a modest to moderate pace, though several Districts reported some slowing owing to improved worker availability and less competition for labor. Prices were generally reported to have risen modestly, with a couple of Districts noting only slight increases. Contacts broadly expected slower growth over the coming six months, citing uncertainty around the election, domestic policy, geopolitical conflict, and inflation.

STAFF REVIEW OF THE FINANCIAL SITUATION



Financial conditions were broadly calm. The financial stress index at 0.1255 sat at a low level, and the VIX at 18.04 pointed to moderate, unremarkable equity volatility. The Baa corporate spread of 1.59 was tight, indicating no borrowing-cost distress or credit-market strain. Two term-structure measures carried a distinct signal: the 10-year/2-year Treasury spread remained inverted at -0.09, a lingering though nearly flat recession-risk indicator, while the 3-month T-bill traded 0.195 below the current target range. Taken together, the staff read these measures as markets anticipating some near-term easing while displaying no acute stress or funding disruption that would demand action.

STAFF ECONOMIC OUTLOOK

The staff outlook drew on several forward-looking quantities. The estimated real neutral rate was -0.389, implying that a real policy rate derived from the current 5.25 to 5.50 percent range sits well above equilibrium and that the stance is meaningfully restrictive. Inflation momentum was mildly positive at 0.07, indicating that the disinflation observed in the level of core PCE has not yet translated into clearly downward near-term pressure, while unemployment momentum was flat at 0.0, consistent with a labor market that is loosening only gradually rather than deteriorating sharply.

The reference rules were judged reliable this cycle. Three level-based rules — the Taylor rule, the Balanced Approach rule, and the ELB-adjusted rule — each pointed to -75 basis points, reflecting the wide gap between the current stance and the low estimated neutral rate. The First-Difference rule, which weights the change in conditions rather than the level gap, pointed to no change, consistent with the flat unemployment momentum and still-positive inflation momentum. The loss-minimizing recommendation blended these signals to arrive at -25 basis points. On balance, these figures imply that conditions are likely to evolve toward a gradual normalization of the policy stance: restriction appears to exceed what a near-target inflation reading and a labor market near balance would require, but the absence of downward inflation momentum argues for a measured pace rather than an abrupt adjustment.

PARTICIPANTS' VIEWS ON CURRENT CONDITIONS AND THE ECONOMIC OUTLOOK

In their predictive discussion, all five participants converged on maintaining the target range at 5.25 to 5.50 percent, though they arrived there from distinctly different starting points and with different degrees of conviction. Participants generally agreed that core PCE at 2.27 percent, while close to the objective, had not yet cleared the prior meeting's stated bar of 'greater confidence' that inflation is moving sustainably toward 2 percent, and that a single cycle of favorable data was insufficient to establish that confidence. Several observed that the economy showed no urgent recession signal — jobless claims at 243,000 were elevated but not distressed, and the activity index near 0.05 was consistent with growth near trend.



One participant, weighting inflation risk most heavily, emphasized that inflation remained above target and that easing before disinflation was convincingly established risked reigniting price pressures; with the labor market not weak in absolute terms and financial stress low, this participant judged patience the prudent course. A second participant, focused on the employment mandate, expressed an honest preference for a 25 basis point cut, pointing to slight employment growth, manufacturing job declines, contacts declining to backfill open positions, and slowing wage growth as evidence of a loosening labor market. This participant nonetheless concluded that unemployment at 4.1 percent remained below the natural rate and that a solo push to cut would appear premature relative to the committee's stated guidance, and so was persuaded to hold this meeting while signaling a low tolerance for further labor softening. A participant attentive to financial stability judged conditions benign — low stress, a contained Baa spread, and a moderate VIX — and saw no systemic justification for accommodation, cautioning that cutting without a stress rationale could itself unsettle calm markets. Two further participants, one oriented toward the literal data reading and one toward market pricing, likewise favored holding: the latter read the T-bill spread of -0.195 as pricing a cut that was near but described this meeting as more likely the 'setup' than the 'execution.'

After the predictive vote was recorded, participants took up the deterministic policy engine's loss-minimizing recommendation of -25 basis points, and the discussion sharpened around whether the current stance had drifted behind conditions. Participants noted the wide gap between the three level rules pointing to -75 basis points and the First-Difference rule at zero, and generally agreed that the -25 basis point figure represented the framework splitting that difference — a measured first step rather than the aggressive move the level rules implied. The estimated neutral rate near -0.389 featured prominently: several participants acknowledged that it placed the real policy stance well above equilibrium and that mechanical rules were 'craving relief.'

Views on whether to begin easing now diverged genuinely. The participant weighting employment risk argued that holding while labor softens risks over-tightening onto a weakening market, finding the Balanced Approach rule most persuasive given its explicit employment weight, and endorsed -25 basis points as a cautious first step. The stability-focused participant reasoned that the very absence of stress cut both ways — with markets calm, a 25 basis point move carried little risk of disruption, whereas holding too long risked a disorderly credit snapback once softening accelerated — and supported preemptive, orderly easing. The market-oriented participant judged that pricing already embedded roughly one cut, validating -25 basis points over -75 , and concluded that its predictive hold had reflected institutional caution rather than a superior read of the signal. On the other side, the inflation-focused participant, while conceding that a single quarter-point cut would barely dent a deeply restrictive stance and could insure against labor softening, declined to affirmatively endorse a



cut while inflation momentum remained positive at 0.07 and the confidence bar was unmet, trusting the First-Difference rule's zero signal most. The data-oriented participant similarly agreed the stance was somewhat restrictive and the direction toward easing reasonable, but held that positive inflation momentum and a labor market near balance made the case to begin this meeting insufficiently compelling absent more favorable inflation data.

Across both strands of the discussion, participants broadly shared a reading that the disinflation-progress-versus-confidence tension was real and that easing was drawing near, even as they differed on whether the appropriate moment had arrived. Those inclined to hold framed their caution around inflation credibility and the prior guidance; those inclined toward the framework's step framed their view around a restrictive real stance, an inverted curve, and building slack in five Districts. All acknowledged that the gap between the predictive hold and the -25 basis point recommendation illuminated how far the stance sat above neutral.

COMMITTEE POLICY ACTIONS

In the predictive vote, all five members supported maintaining the target range for the federal funds rate at 5.25 to 5.50 percent, a unanimous 5-0 outcome. On the deterministic framework's loss-minimizing recommendation of -25 basis points, the Committee did not reach full agreement: three members — the labor market dove, the financial stability voice, and the market signal realist — endorsed the recommendation as stated, while two members — the inflation hawk and the data-dependent centrist — declined to support it, preferring to await additional favorable inflation data before beginning to ease. No member took a partial position on magnitude or timing.