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Federal Reserve Monitor | North America

September FOMC Quick Reaction: Supporting the labor market at the expense of higher inflation

The Fed views downside risk to employment as having risen, justifying a 25bp cut today and 75bp in cuts by year end. The updated forecasts signal that inflation is likely to run further above 2.0% and for longer: PCE inflation was revised higher to 2.6% in 2026 from 2.4%. On net, a dovish signal.

Key Takeaways

- The Fed cut by 25bp as expected, and signaled more cuts are forthcoming.
- The statement acknowledged both slower job gains, a higher unemployment rate, and higher inflation. They further emphasized downside risks to employment.
- The dot plot has three cuts this year, though only by a 10-9 margin. With inflation running hotter next year, the Fed sees a slower glide path to neutral.
- There was one dissent in favor of a 50bp cut. Governor Miran favors 150bp in cuts this year based on our reading of the dot plot.

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Quick Reaction

The FOMC lowered the target rate for the Fed Funds rate by 25bp to 4.0 - 4.25%. The statement acknowledged that both job gains have slowed and inflation has moved up. They separately highlighted rising downside risks to employment. Their rate cut reflected the "shift in the balance of risks." And the language around future policy changes became more immediate.

The SEP showed a median of three cuts for this year, but only just: a shift of one voter to two cuts would have left the median there. Still, this is dovish relative to our expectation for the SEP but is in-line with our base case for consecutive cuts through January.

Governor Miran dissented from the statement in favoring a 50bp cut. And in a silent dissent, one dot showed no cuts this year.

Changes to statement from July:

- Added "Job gains have slowed" and the unemployment rate "has edged up"
- Added inflation "has moved up"
- Added "downside risks to employment have risen"
- Justified the rate cut "in light of the shift in the balance of risks"
- Made "additional adjustments" to rates more immediate by dropping language that considered the "extent and timing" of future cuts.

Consistent language with July:

- "Growth of economic activity moderated in the first half of the year"
- Inflation still characterized as "somewhat elevated" and unemployment rate "remains low"

Exhibit 1: September statement changes from July

Although swings in net exports continue to affect the data, recent indicators suggest that growth of economic activity moderated in the first half of the year. The job gains have slowed, and the unemployment rate has edged up but remains low, and labor market conditions remain solid. Inflation has moved up and remains somewhat elevated.

The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. Uncertainty about the economic outlook remains elevated. The Committee is attentive to the risks to both sides of its dual mandate and judges that downside risks to employment have risen.

In support of its goals and in light of the shift in the balance of risks, the Committee decided to maintain lower the target range for the federal funds rate at 4- by 1/4 percentage point to 4- to 4-1/24 percent. In considering the extent and timing of additional adjustments to the target range for the federal funds rate, the Committee will carefully assess incoming data, the evolving outlook, and the balance of risks. The Committee will continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities. The Committee is strongly committed to supporting maximum employment and returning inflation to its 2 percent objective.

In assessing the appropriate stance of monetary policy, the Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee's goals. The Committee's assessments will take into account a wide range of information, including readings on labor market conditions, inflation pressures and inflation expectations, and financial and international developments.

Voting for the monetary policy action were Jerome H. Powell, Chair; John C. Williams, Vice Chair; Michael S. Barr; Michelle W. Bowman; Susan M. Collins; Lisa D. Cook; Austan D. Goolsbee; Philip N. Jefferson; Alberto G. Musalem; and Jeffrey R. Schmid; and Christopher J. Waller. Voting against this action were Michelle W. Bowman and Christopher J. Waller was Stephen J. Miran, who preferred to lower the target range for the federal funds rate by 1/42 percentage point at this meeting. Absent and not voting was Adriana D. Kugler.

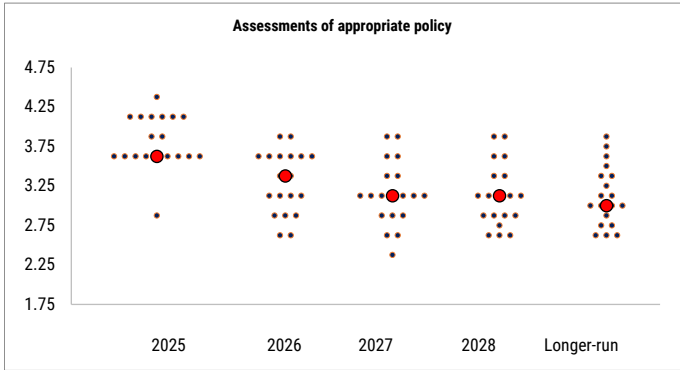
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 2: Summary of Economic Projections

Changes to the Summary of Economic Projections					
	2025	2026	2027	2028	Longer Run
Real GDP (% 4Q/4Q)					
FOMC September SEP	1.6	1.8	1.9	1.8	1.8
FOMC June SEP	1.4	1.6	1.8		1.8
Difference	0.2	0.2	0.1		0.0
Unemployment Rate (4Q Avg)					
FOMC September SEP	4.5	4.4	4.3	4.2	4.2
FOMC June SEP	4.5	4.5	4.4		4.2
Difference	0.0	-0.1	-0.1		0.0
Core PCE Inflation (% 4Q/4Q)					
FOMC September SEP	3.1	2.6	2.1	2.0	
FOMC June SEP	3.1	2.4	2.1		-
Difference	0.0	0.2	0.0		-
Headline PCE Inflation (% 4Q/4Q)					
FOMC September SEP	3.0	2.6	2.1	2.0	2.0
FOMC June SEP	3.0	2.4	2.1		2.0
Difference	0.0	0.2	0.0		0.0
Fed Funds Target					
FOMC September SEP	3.6	3.4	3.1	3.1	3.0
FOMC June SEP	3.9	3.6	3.4		3.0
Difference	-0.3	-0.2	-0.3		0.0

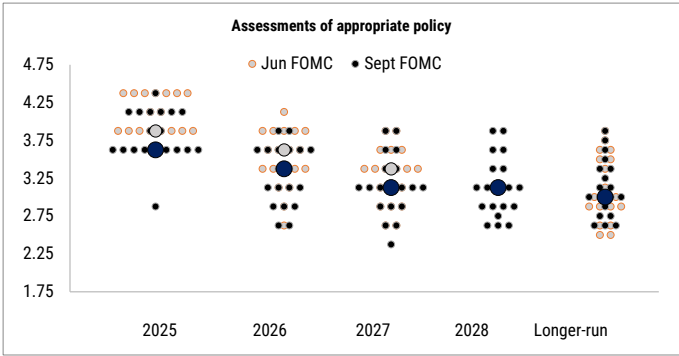
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 3: September dot plot



Source: Federal Reserve Board, Morgan Stanley Research

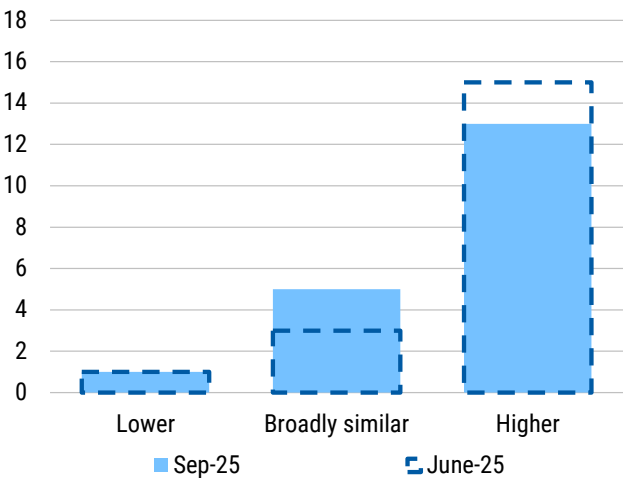
Exhibit 4: September versus June dot plot



Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 5: Uncertainty about GDP growth still elevated

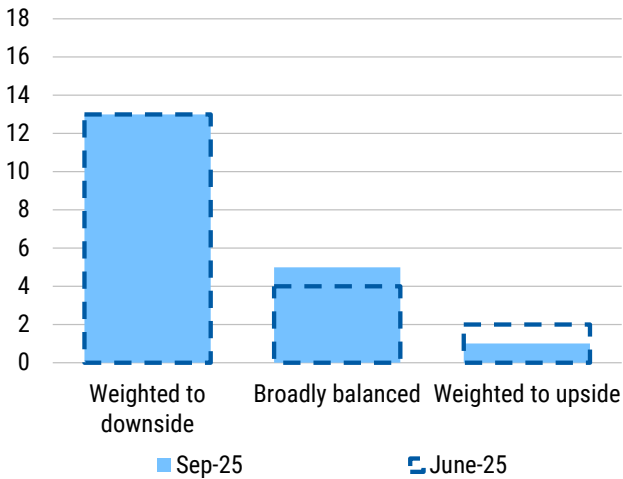
Uncertainty about GDP growth - number of participants



Source: Federal Reserve Board, Morgan Stanley Research

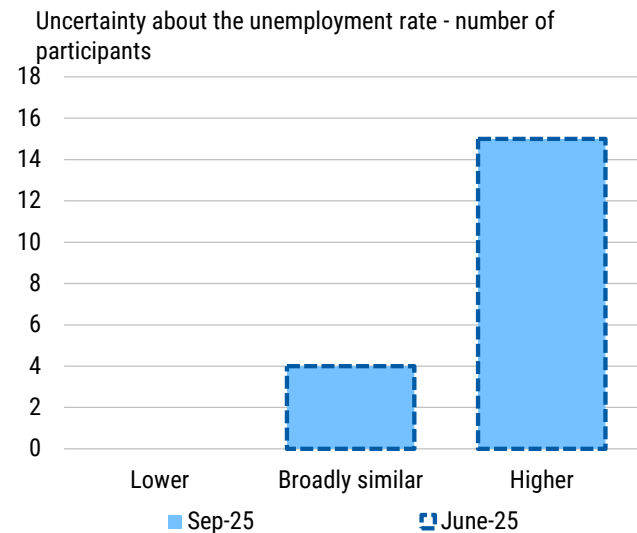
Exhibit 6: With risks to GDP growth skewed to the downside

Risks to GDP growth - number of participants



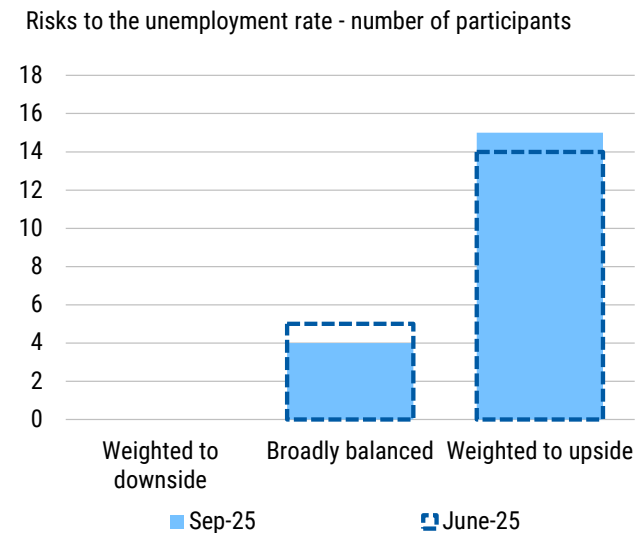
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 7: Uncertainty about the unemployment rate still elevated



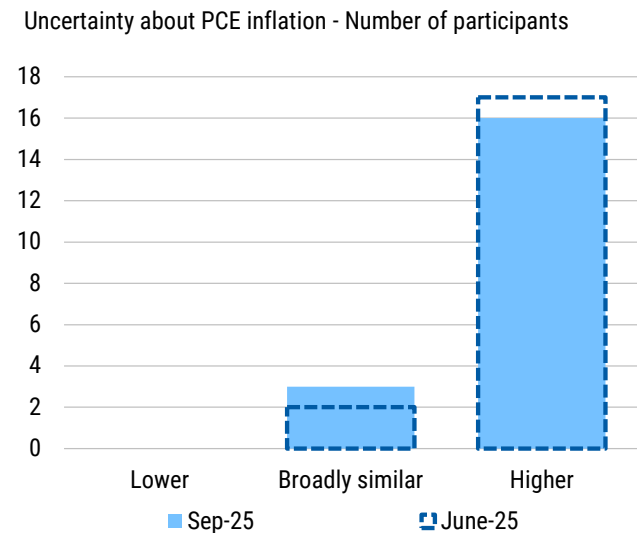
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 8: With risks to the unemployment rate skewed to the upside



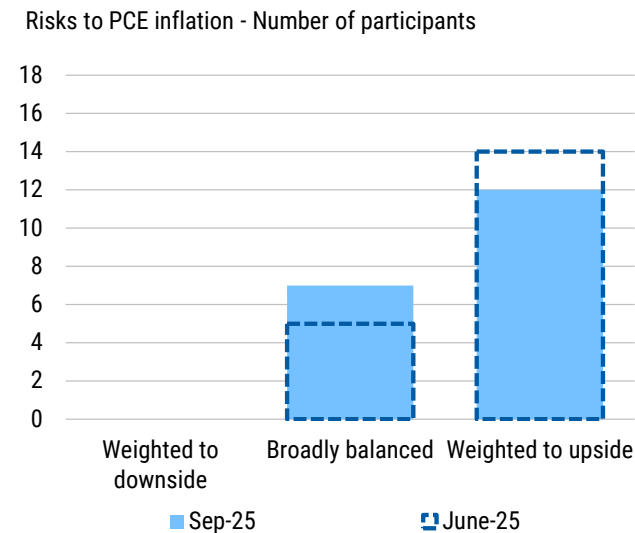
Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 9: Uncertainty about inflation still elevated



Source: Federal Reserve Board, Morgan Stanley Research

Exhibit 10: With risks to inflation skewed to the upside



Source: Federal Reserve Board, Morgan Stanley Research

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