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Alberto Musalem: The outlook for the US economy and monetary policy

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MODERATOR

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WESSEL: Good morning, I'm David Wessel, director of the Hutchins Center on Fiscal and Monetary Policy here at Brookings. Very glad to welcome Alberto Musalem to our stage today. President Musalem has been at the St. Louis Fed since April 2024, April 2024. He has a very distinguished career before that, both in the private sector and in the public sector, the IMF and the New York Fed. Alberto has to leave at 10.50, so I'm going to skip all the glowing remarks I was going to say. I'll give them to you next time when you come and you give us the 10 minutes you owe us. Alberto Musalem.

MUSALEM: I'd like to thank the Brookings Institution for this kind invitation to speak with you today. I look forward to an engaging discussion with David Wessel. First, I will offer a few remarks on the U.S. economic outlook and monetary policy. These are my personal views and do not necessarily reflect those of my FOMC colleagues. At last week's FOMCs meeting, I supported the Committee's decision to reduce its target range for the federal funds rate by 25 basis points. Although the labor market is currently at or near full employment and inflation is meaningfully above the Committee's 2 percent target, I supported this action because recent data indicate that downside risks to employment have increased relative to the risk of inflation remaining persistently above target. To be clear, I expect the labor market will remain near full employment or soften only modestly, and inflation will return to a path towards 2 percent as the effects of tariffs wane.

However, there are two-sided risks, and I believe we should remain forward-looking and take account of these when making policy decisions. I see a risk that above-target inflation could be more persistent than is desirable. I supported the rate decision because I perceived the risk of labor market weakening had increased sufficiently to warrant a policy adjustment. I'll now expand on these points. Real GDP grew at an annual rate of 1.4 percent in the first half of 2025, which is slightly below estimates of long-run potential. Tracking forecasts indicate a strong third quarter, so it's possible that real GDP growth will accelerate and exceed 1.4 percent in the second half of this year. I expect growth near long-run potential in 2026 and possibly higher. Consumers are resilient. Adjusted for inflation, consumer spending rose in July. Retail sales in August were solid. Spending has remained especially strong among high-income households, but has slowed among low and moderate-income household and certain demographic groups. For example, context reports slower consumption growth among Hispanic households. Financial conditions and positive wealth effects are supportive of economic activity. A buoyant stock market, historically low credit spreads, healthy bank lending and capital market issuance are indicative of accommodative financial conditions. Profit margins are elevated, driven more by cost control and efficiencies than by revenue growth. Publicly traded companies reported solid earnings and revenues in the first half of the year and earnings guidance for the third quarter was mostly positive.

The outlook is shaped by both structural and cyclical factors. Economic policy uncertainty is having mostly cyclical effects while immigration, tariffs, and AI are having mostly structural effects. AI continues to fuel a surge in non-residential construction spending, which is expected to continue. The AI boom is also dampening demand for entry-level technology and administrative jobs. Reduced immigration is contributing to slower growth in consumer spending and labor supply. Economic policy uncertainty remains elevated, but has declined over the past few months. My contacts are now telling me that businesses are adjusting to tariffs and fewer are in a wait-and-see mode, suggesting that greater policy certainty could have a positive impact on economic growth later this year and into 2026. Fiscal policy looks likely restricted this year, is also likely to provide more support early next year. The weak housing market continues to pose some downside risks to the economic outlook. Residential fixed investment declined the first half of 2025. New construction has slowed as inventories of unsold homes have risen, while the mortgage lock-in effect continues to weigh on the market for existing homes, keeping prices high. Mortgage origination and refinancing activity is sluggish, and mortgage rates and spreads remain elevated despite some recent declines. Price appreciation has slowed. And home prices have begun to fall in some markets. Industry contacts expect that prices of single-family homes will be flat over the next 12 months nationwide.

Turning to the labor market. The unemployment rate, job-to-job transition rate, wage growth, and low level of layoffs are all indicative of a market around full employment. Sluggish payroll growth reflects both structural and cyclical factors. Research by St. Louis Fed economists finds that negative supply shocks have contributed meaningfully to the down shift in private sector hiring and above-trend wage growth in the services sector. Lower immigration and labor force participation have reduced the growth of labor supply while economic policy uncertainty and perhaps other cyclical factors have reduced labor demand. St. Louis Fed economists estimate payroll growth in the range of thirty to eighty five thousand jobs per month is currently required to prevent the unemployment rate from rising, with confidence weighed toward the low end of that range. Looking ahead, labor market risks appear weighted to the downside. Recent data have reinforced my perceptions of those risks. The unemployment rate of cyclically sensitive demographic groups, such as younger workers and African Americans, have been rising, as has the broader U6 unemployment rate, which includes workers marginally attached to the labor force and those working part-time who would prefer to be working full-time. The percentage of unemployed workers who have been out of work for more 27 weeks has also been rising while job-finding expectations have been falling. My business contacts have not been reporting plans for layoffs, and actual layoffs have remained low. However, some measures of layoff announcements have been rising. The modest pace of economic activity and low hiring rates suggest that the unemployment rate could increase sharply if layoffs were to rise significantly.

Turning now to our price stability goal, inflation remains above the FOMC's 2% target. The PC inflation rate for August will be reported on Friday. Economists expect a core PC inflation of 2.9%, which I view as the best measure of underlying inflation. This is nearly a full percentage point above target. August data on the Consumer Price Index indicates that inflation is rising. Measures of goods, services, and shelter inflation all moved higher on a three-month annualized basis, and super core inflation exceeded 4% for the first time since February. Tariffs have been contributing to inflation, but the effects are uncertain in terms of measurement, magnitude, and persistence. St. Louis Fed economists estimate a direct pass-through of realized tariffs to core PCE of 0.2% from January to July and and of 0.3% to core CPI from January to August. Estimates of direct plus indirect effects are about 0.1 percent higher. So far, the effects on inflation have been more muted than expected, suggesting that factors other than tariffs are contributing to above-target inflation. Business contacts tell us it takes three to six months to adjust to an increase in tariffs, and only four months of data are available since tariffs rose meaningfully in April. Business contacts report that producers of intermediate goods are fully passing on tariffs to their customers in the form of price increases and surcharges, while firms closer to the final consumer are less able to do so. Some firms have also told us that rather than making frequent price adjustments, they are waiting until tariff rates and policies seem to be set before making price adjustments. This suggests that the pass-through of tariffs to consumer prices could rise later as final tariffs become more certain and inventories are restocked.

Let me conclude with a few comments on monetary policy. Given the economic outlook and the balance of risks, I supported a 25 basis point reduction in the FOMC's policy rate last week as a precautionary move intended to support the labor market at full employment and against further weakening. The stance of monetary policy now lies between modestly restrictive and neutral, which I view as appropriate. However, there is limited room for easing further without policy becoming overly accommodative, and we should tread cautiously for three reasons. As I said earlier, financial conditions, which are how monetary policy transmits to the economy, are already supportive of economic activity. Second, looking through the direct one-time effects of tariffs on inflation is appropriate, but this posture could risk price stability if taken too far or maintained for too long. While providing insurance against labor market weakness, I believe that monetary policy should continue to lean against persistence in above-target inflation, whether it materializes from the impact of tariffs, lower labor supply growth, or for other reasons. Finally, the ex-ante real policy rate is already close to neutral. The nominal policy rate is now 4.1%. Markets expect the inflation rate of 3.3% over the 12 months. So the ex ante real policy rate is 0.8%. This is below the 1% median long-run real neutral rate of IFOMC participants. I do not view 1% as the floor below which the real policy rate must not go. But to go there, I believe the outlook or balance of risk must shift further from where they are today, especially if inflation looks likely to remain persistently above target. Should further signs of labor market weakness emerge, I would support additional reductions in the policy rate, provided the risk of above-target inflation persistence has not increased, and long-term inflation expectations remain anchored. The risks of persistence above target inflation would be especially problematic if long-term inflation expectations begin to move higher. Both market measures and surveys indicate the public expects inflation to exceed 2% over the next year or so. Most measures of long- term inflation expectations have remained stable and consistent with our 2% target. But people are already sensitive to inflation, which could increase the possibility of elevated expectations becoming entrenched. If the public begins to doubt that inflation will converge to 2%, the job of restoring price stability would be more difficult and potentially costly for the economy. Looking ahead, my focus is on a policy path that equally weighs both sides of our dual mandate. Pursuing a balanced approach to policy requires care. Putting too much weight on one goal at the expense of the other can lead undesirable outcomes. Over-emphasizing the labor market objective runs the risk of excessive policy easing which could cause a further steepening of the yield curve, a rise in the term premium, or an increase in inflation expectations. Any of those effects could do more harm than good to the labor market and contribute to more persistent above-target inflation. However, if inflation expectations are well anchored, over-emphasing the inflation objective runs the risk of not providing enough support to maintain a full employment labor market, at a time when downside risks have risen. Again, balance is key. I do not have a preset course of policy. In the weeks and months ahead, I will continue to refine my economic outlook and assessment of the balance of risks to seek a forward-looking path of interest rates that best positions monetary policy for achieving and maintaining maximum employment and price stability for all Americans.

WESSEL: Thank you very much. I want to tell you that almost everybody who comes and speaks here who says they're going to speak for 10 minutes speaks for somewhere between 20 and 40. So you're right on target. So appropriate balance. As I listen to your discussion of your outlook for the economy, your reference to the 25 basis point cut as a precautionary cut, it seems to me your base case is pretty optimistic about the economy. You don't see a recession in the works. You think the tariff inflation is likely to be a one-off, maybe some labor supply inflation, but inflation expectations long term are well anchored. The markets seem to expect, when I looked at Fed funds this morning, a couple of rate cuts more this year and two or three rate cuts next year. That doesn't seem to me consistent with your base case for the economy. How am I doing?

MUSALEM: So is the question about why I supported the 25 base points or about the outlook?

WESSEL: The outlook.

MUSALEM: So in terms of the outlook, I am open to further adjusting the interest rates lower. As I said, monetary policy for me now lies somewhere between modestly restrictive and neutral, which I think is appropriate. I think there is limited room for further policy easing without getting into overly accommodative territory so I think we should tread with in a cautious way, in a gradual way, for three reasons. As I mentioned, financial conditions are accommodative of economic activity, number one. Number two, a look through posture vis-a-vis the first round effect of tariffs is appropriate but if that posture is taking too far or stays in place for too long it could risk price stability. And I think it's important to continue to lean against above-target inflation while supporting the labor market.

WESSEL: I don't think I was specific enough. Tell me about where your dots were.

MUSALEM: I don't typically share my dots, but I'm giving you the reasons, and I think the reasons are important. And the last reason is if you look at the real Fed funds right now on a 12-month forward-look basis, it's already below the 1% long-term neutral rate of the FOMC. So for those three reasons, I think, you know, we need to tread cautiously. If I observed more signs of potential deterioration in the labor market, and if I did not observe further persistence in above-target inflation, and if inflation expectations remained anchored, I would support additional --

WESSEL: And when you talk about the further signs of the labor market, what are the measures that you find most useful?

MUSALEM: So what I've, I look at all measures.

WESSEL: Everybody on the Fed looks at everything, we know that.

MUSALEM: Yeah, well, I mean, that's the job description, right? But what has been giving me signs more recently is if you look at the cyclically sensitive demographic groups, their unemployment rate's been increasing. If you look the proportion of folks unemployed that are long-term unemployed, that's been increasing. If you at expectations of job findings, that's being decreasing. So the U6, which has marginally attached workers, has been has been increasing. So even though the unemployment rate is low and consistent with full employment and even though supply and demand growth have both come down together, therefore the unemployment rate's been somewhat stable at full employment, if you look under the surface, there are some things that tell you that at the margin, the labor market is softening.

WESSEL: All the numbers you mentioned are compiled by the Bureau of Labor Statistics. And you know there's a lot of concern the president fired the Commissioner of Labor statistics and there's lot of anxiety about the reliability of the statistics going forward so I want to ask you two questions. One is how important are, is the reliability government statistics to you as a monetary policymaker, and two how worried are you about their continued reliability?

MUSALEM: The reliability and integrity of data are critical for making any economic decision, monetary policy being one of them, but they're also very critical for businesses and households in terms of making important economic decisions. There's a reason, not the only reason, why the U.S. is the largest, most dynamic economy in the world with the deepest capital markets is because it is and has been the best measured economy in the word, which that leads to good economic decisions, which leads to., you know a bigger economy and more growth and deeper capital market. So so integrity and and reliability of data is is key. In terms of the Fed, we look at three types of data. We look at government statistics. We look at a lot of privately produced data sources and we cross validate between, on a particular theme, we look a different types of date are for different sources. And in addition you know we have a twelve Reserve banks spread around the country and the these banks, including my bank, are permanently in close contact with businesses and households, elected officials and so on, talking about the economy. So we get a lot of anecdotal impressionistic information which we used to cross validate what the data saying, so I'm very confident that we continue to do our job well.

WESSEL: Are you worried about the reliability of government data going forward?

MUSALEM: I think there are opportunities for improving the timeliness and the revisions, variability of data across a whole host of releases.

WESSEL: Are you worried that they're going to be corrupted?

MUSALEM: I think there're opportunities for improvement.

WESSEL: So as you also know there's a lot of concern now about the continued independence of the Fed. We seem to be in an era in Washington where things that we took for granted are no longer taken for granted. I think we all know why we have an independent central bank and how important that is in maintaining price stability and a stable economy, but like on a scale of, compared to say one or two years ago, how worried are you about the continued ability of the Fed to operate as an independent central bank?

MUSALEM: Monetary policy independence is important as you said, because if you look across countries in time, countries with more central bank independence -- and even across the history of the U.S. you can see that lead to outcomes that are better for for the people, the country. With, which means in our case, lower, more stable inflation and higher, more stable employment, so that's that's very important. It's very important that monetary policy independence come hand-in-hand with accountability and transparency, that's really important. At the Fed we are accountable to Congress and through the accountability of Congress, we're accountable to the people we serve, the people that elected folks in Congress. That's really important. We try to be as transparent as possible through events like these, through testimonies to Congress, through data releases, through speeches, etc. So all that's very important. Over the history of the Fed, Congress has realized and recognized the value of central bank independence. And over different periods of time, Congress has protected the Fed against political dominance. So at its creation in the 1913 Federal Reserve Act, that was the case. In the 1935 Banking Act, that was case and in 1977 Federal Reserve Reform Act that was also the case. And Congress was also very supportive of the Treasury-Fed Accord of 1951 which clearly demarcated the responsibilities of debt management at the Treasury and monetary policy at the Fed. So, those are my views.

WESSEL: And do you think it's at risk?

MUSALEM: I think there is more awareness of the issue and there's more debate about the issue.

WESSEL: So you mentioned the demarcation between debt management and the Fed's portfolio and you've been watching the Fed for a long time. So what do you think we've learned about the tool quantitative easing? What is it? How well has it worked? What are the questions we've answered? What of the questions that we still don't know?

MUSALEM: So quantitative easing, I think, was very useful when we hit the zero lower bound of interest rates twice after the global financial crisis and after COVID. It provided the Fed with an additional degree of freedom and additional tool it needed to make sure monetary conditions were consistent with achieving the dual mandate of maximum employment and price stability. So it proved to be a very useful tool. There has been a whole host of academic studies which investigate the issue and have concluded that it is a very useful tool. I, I think it's very important for quantitative easing when it's used to be very clearly communicated to the public as to why is being used. As to whether it's because rates, nominal rates are at zero, that is. So more guidance about future monetary policy and and more impact across the interest rate curve is required through an additional tool. Or whether QE is being used for market function reasons. I think it's very important to communicate that to the public. I think it's important to only use QE to support the dual mandate and to not be perceived as direct or indirectly be helping with debt management responsibilities, which in my mind are the domain of the U.S. Treasury.

WESSEL: And do you think that, so one of the complaints that's made about QE is that somehow it exacerbated inequality by driving up asset prices and rich people own more assets than poor people. Is that A, is that true? And B, if it is, is just a cost of monetary policy?

MUSALEM: In my view inequality's being driven by, has been driven by many factors other than monetary policy, including homeownership rates across different demographics, contractual savings plans across different types of employment which allow asset accumulation, so there are many many factors driving inequality other than monetary policy.

WESSEL: So, the Federal Reserve system as a whole, largely the board, but it delegates some to the Reserve banks, has responsibility for supervision and regulation of the banking system. We did a lot after the global financial crisis to raise capital requirements, tighten regulations. We're now in the process of somehow undoing some of them, and I'm curious how you the balance. Is this the right time to be easy? We are in a boom time in many respects. Is this is the right time to be adjusting these requirements? Is this a necessary correction? Is there a risk that we'll go too far?

MUSALEM: So, I'll refer you to Vice Chair Bowman's recent remarks, and to the Board of Governors. What the board is focused on is a few areas, so tailoring of regulations to risk profiles, which tend to be correlated with size of financial institutions and complexity of financial institution, so that's one area in which work is being done. There's a fresh look at the capital regime, whether it's Basel III or, or the ESLR. In addition, there's an emphasis on training supervisors, et cetera, which is really important. I think it's always important to review the regulatory framework, make sure that it's working for the financial system of the time and the risk profiles of the different players in the financial systems. In passing, let me say that the stress tests were just concluded a few months ago. And they show that with the current regime, the banking system is capable of withstanding a very material negative shock to growth and to asset prices and remaining very well capitalized.

WESSEL: So when you talk to the banks in your district, you have a number of regional banks in your district, what do you hear from them about the quality and the severity of regulation and supervision?

MUSALEM: So the bankers in my district tell me that bank conditions are really good right now. Credit quality is good, capital's good, funding costs are good, long growth is good. In terms of your direct question, I have in my district the benefit of having different types of banks. I have very small community banks and larger regional banking organizations. And all of them say that, particularly the smaller ones that have less potential overhead operations and have less risky, less complex operations, the message is, a tailored approach to regulation would be beneficial and would be helpful to banking conditions and activity.

WESSEL: If you look ahead, I don't know, five to seven years, do you think that stablecoins and other forms of digital assets will be a significant part of our daily life and our financial system?

MUSALEM: I think, I think the payment system is going through, you know, quite an evolution now. We live in the age of AI and technology, so I, I do see an evolution in payments. The Genius Act just passed a few months ago and I think has the potential to unlock, you know, innovation in terms of the exchange of value in the economy. I think it's very important that, you know, as you may know, the Genius Act says that stablecoins can't pay interest. I think it's very important that in the implementation and in the emergence of stablecoins that that part of the act be respected and enforced.

WESSEL: And why is that?

MUSALEM: Because if stablecoins were to pay interest there could be some financial stability implications for competition with bank deposits and the like. So, so, it's very important that they remain, from my standpoint, a payments instrument and not a savings instrument.

WESSEL: But do you think they'll play some bigger role in the payment system, I presume? Seems hard to imagine they'll pay less of a role.

MUSALEM: I think there's a potential for them to increase. Right now, the volume and transaction of stablecoins is mostly in the crypto space and in the international payments space. But with the new bill and the enabling regulation of that bill, I could imagine the use of stablecoins might increase. And you've seen some retailers exploring, issuing their own stablecoins for their own purposes because they pay, you know, very high fees to credit card companies and it's in their interest to internalize those, those costs.

WESSEL: Exactly. So I want to take you back to something you said in your speech, and then I have one more question and I'm going to turn to the audience. You made a really interesting point that it's easy to have a simplistic view of inflation, that tariffs went up and therefore we have more prices went up. But you made a point in your speech of talking about the labor supply aspects, which I presume you mean largely the decline in the number, the net immigration. Can you talk a little bit about how you view immigration, both in terms of the short-term cyclical thing as you described, or maybe it's not cyclical, short-term structural thing there, but also the sort of the long-term potential for the U.S. economy?

MUSALEM: Yeah, we're trying to and I'm trying to disentangle cyclical and structural factors that are all at play right now so we can understand, so I can understand where the slack in the economy is or isn't, so understand where potential is and where the cycle is relative to that potential. So we've had a labor market, as you know, is cyclically the uncertainty about tariffs and other policies was very high initially in the year. That led employers to cyclically pull back on hiring, and they are right-sizing their labor forces through attrition by not hiring and by letting folks that are departing just depart and not backfilling. So that's kind of the cyclical story behind the labor market. The more structural stories behind the market are on the supply side, the number of immigrants participating in the labor force likely declined. And there are estimates out there of a change this year -- I think those are overestimates -- a change in immigrants this year in labor force of close to two million people. That's a meaningful number. Our economists think that's an overestimate, but you know, that's the number that's out there. And that's a meaningful change in the supply of labor. I don't hear that too much in my district, but if you go further west in the country, in the agricultural sector, you begin to that it is impacting labor supply there.

WESSEL: And that affects wages and that affects inflation.

MUSALEM: So as I said, we observe negative supply shocks in the services side of the economy right now, in the labor market service side of economy, which means that those supply shocks, or the footprint of those negative supply shocks are a lower pace of hiring in the service sector, possibly through the supply side effects, and a higher rate of wage growth above the long-term potential. So we're starting to see the footprints of that. Is that immigration one-to-one? Hard to say, but the fact that this is beyond to happen when the flow of immigration has declined suggested the two things are related.

WESSEL: And what about the long-term productivity growth in the U.S.? What effect does this have on that?

MUSALEM: So right now, we are, if you think of the U.S.'s history as being either in a high productivity regime or in a lower productivity regime or more kind of average productivity regime, and for example, in the late 90s, we were in a higher productivity regime. Right now, my understanding is we are close to an average productivity regime. So there's a tremendous promise of AI. That promise still isn't visible in the macro data. It is visible in the micro data, in certain sectors, very much so. And beyond AI, there's just business process automation. You know I visit plants, manufacturing plants all over the country, particularly my district, and and what you see is, the plant manager tells you, you see all those machines here on the left-hand side of the plant? These are enormous plants. Well a few years ago those machines were people. And you see all these people on this right hand side of plant? Well, a few years from now, there'll be much more machines. So there's, even in manufacturing, there's a, beyond just AI, there is this capital deepening and drive towards efficiencies.

WESSEL: I was asking you about what effect on long-term productivity growth will limiting the number of immigrants the United States have?

MUSALEM: It's hard to say that that's going to increase productivity. Whether it will decrease productivity is an open question. What for sure I can say is that there will be less labor force growth. That doesn't mean a less productive labor force, but it probably does not mean a more productive labor force.

WESSEL: And finally, as you well know, Federal Reserve Bank presidents are appointed for five-year terms and in their infinite wisdom, the Congress of the United States, I think it was the

Congress, maybe it was Fed Board, said all the terms expire at the end of February of next year. Are you worried about being reappointed?

MUSALEM: So, reserve banks are a cornerstone of central bank independence, and that's the case because it's through the 12 reserve banks that different views about the economy get brought to the FOMC table, different information about the economy gets brought to FOMC table, and different policy views, given the views about economy, get brought the FOMC table. So to the extent that this is a large country, a large economy, the 12 Reserve Banks are a very important part of central bank independence. And I spend, and my team spends, our entire working hours focused on being in touch with the districts we represent precisely to bring that anti-group-think wherewithal to the policy discussions. So I'm 100% focused on that. Beyond monetary policy, reserve banks do a lot of other things. We, of course, come to the FOMC and participate in monetary policy deliberations. We help run the payment system. We supervise financial institutions for delegated authority from the Board of Governors. We provide fiscal agency services to the U.S. Treasury. And we participate in community development. And all of those things occupy 100% of my time, and that's all I'm focused on.

WESSEL: I see, I see. I can't believe you gave that long list and you didn't call out Fred. All right, we have time for some questions. I think I'm gonna take a couple and then we'll see in the back. Wait for a mic.

AUDIENCE QUESTION: Thanks. Nick Timmeros of the Wall Street Journal. Alberto, you said the outlook must shift further to justify going below or much more below a 1 percent real rate, and I'm wondering how much confidence you will have that you'll see any such shift in the outlook by the end of October, given how top-line employment data have been more revision-prone recently. So the question here is, if you were comfortable with one precautionary cut based on incomplete data. Would the same logic apply to a second cut, especially when you may not have reliable employment readings for several more months?

WESSEL: Over here, Jonathan.

AUDIENCE QUESTION: Thanks, Alberto. So I was just curious, as you weigh which risk to address and consider the outlook for the funds rate, does the usefulness of the tool matter at all, right? I mean, it seems unlikely restrictive monetary policy is going to prevent the cost push inflation of tariffs, yet it may play a larger role in restraining the labor market. So I was curious if that had entered the decision-making at all in terms of also the balance of risks.

MUSALEM: Okay, yeah, thank you. So let me start with Nick's question. So I am open to further adjustments in the policy rate. As I said, I think the space for doing so before policy becomes accommodative is limited. There'll be judgments about risk, risk value judgments as we go along. And I'll be weighing where the economy is today, where the baseline path is that I outlined, and how the risks look relative to that baseline path. And we're gonna get some more data between now and the October meeting. I'm really focused on a path rather than the next meeting. I am taking a meeting by meeting approach because I believe every piece of incremental information is important. And when I say information, I don't just mean data releases, I mean talking to businesses, talking to households, just seeing the whole mosaic of information along the way. So data releases is just one of the things I look at. In terms of the question of --

WESSEL: The question was basically that, if you, interest rates can't do much to deal with the cost of --

MUSALEM: I got it. So what central banking practice says is, if you have a supply shock that is one off, by the time monetary policy reacts to it, because of the lags of monetary policy, that one-off shock is come and gone. So that is the reason why central banks tend to look through the one-off effects of shocks. Now, there are many things driving inflation. Tariffs are one of those things. And as I said, it's appropriate to look through the direct effects of tariffs on imported goods and be very vigilant about the indirect effects on non-imported goods and services and lean against any second-round effects that could occur. So that's how I'm thinking about monetary policy. I expect tariffs to to fade, the effect of tariffs on inflation to fade after two to three quarters, but I'm monitoring that very carefully to make sure that that expectation is validated by data.

WESSEL: Why don't we go to this side, there's two people on the aisle here. Sir, there's a mic on your left.

AUDIENCE QUESTION: Alberto, Rob Dugger, retired. Alberto, you spent much of your career in the international economics and assessing the relationships that economic conditions affect, how they affect economies. In your presentation, you talked about the U.S. as just simply the U.S., almost as if it's a closed economy. But you know it isn't. So what international factors figure into your thinking about U.S. economic conditions? Thanks. Do you want to pass it back?

AUDIENCE QUESTION: Hello, I'm Chesapeake. I'm an undergraduate student. You talked a little bit about QEQT already, but I was just wondering what indicators or other information you're looking at to determine whether reserves are reaching a level somewhat above ample?

WESSEL: That's a good question, not one usually one hears from an undergraduate, I'm impressed.

MUSALEM: So to Rob's question, it's great to see you, Rob. You know, I look at everything within and outside our borders. I think two or three things are important now. When the tariffs were first announced, there was a angst about large retaliation of tariffs. And so far, the retaliation has been more modest or almost nonexistent compared to what was expected. So that's, that's an important, you know, call it international factor. The other two things that are important are, you know, we're still have large current account deficits in the country and large fiscal deficits. So, you, know, monitoring the flow of capital into the U.S. is something that I do a lot. And the other thing is as retaliation, just going back to the first point, has been more moderate than was expected earlier in the year, growth in foreign economies looks better today than it did a few months ago. So the international environment in terms of growth looks somewhat better. So those are things I factor into my outlook. Thank you. On the balance sheet question, wow, what a question. So the New York Fed operates monetary policy and the New York desk monitors very carefully whether we are still in an abundant reserves situation.And they've published many indicators that suggests that we're still in abundant reserves situation. Our balance sheet has been declining gradually, we we reduced the rate of roll-off earlier this year so it's declining gradually. I would expect at some point in the future the committee to make a decision before we or as we feel that we are reaching that transition point between abundant reserves and ample reserves to at that point potentially pause the balance sheet roll off. I've seen some market surveys that suggest and these are not, the committee still needs to decide, but I've seen market surveys suggest that could happen somewhere in Q1, Q2 of next year and could happen at around $2.9 trillion in reserves, plus overnight RPs but those are market surveys.

WESSEL: There's one here. And then we'll take one other one and then we're done.

AUDIENCE QUESTION: Hello, my name is [inaudible] from AFP, Agence France-Presse. My question is, Governor Miran earlier said that he hopes he will convince his colleagues that we need to go further to lower further the rates and that they might have some really comprehensive arguments to share with them. Do you think there is some data that you might have missed? For instance, on the effects on tariffs, on inflation that you can be convinced by your new colleague?

WESSEL: And then over here, Pedro, just coming to your right, Pedro.

AUDIENCE QUESTION: Thank you so much. Pedro da Costa with Market News. My question is, given your view of where neutral rates stand, is it fair to say that you don't see this as the start of an extensive rate-cutting cycle? In other words, is there a possibility that the Fed could actually be on hold either now or after, say, another quarter point rate cut?

MUSALEM: I can't prejudge -- I'm going to come back to your question --- what the committee will do at each future meeting, so I won't be able to answer that question, but I did say in terms of my own opinion, or my own view, that I would be prepared to go below that 1% long-term real neutral rate, provided I did see labor market weakness risks rising, and if inflation expectations remain anchored and if there's no further persistence of the inflation path. So, you know, I never think of the long-run mutual rate as some sort of artificial boundary below which you can never go but you have to go there under the right baseline outlook and shift in balance of risks.

Uh, sorry, can you repeat your question, I didn't --

WESSEL: She wanted to know, is there anything you might have missed that would have justified the Miran-style rate cut?

MUSALEM: So let me just say I have a tremendous respect for all of my FOMC colleagues. All 19 bring very valuable insights about the economy and overlay their own policy views on those insights. I take vigorous notes during the meetings, and I learn a tremendous amount from all of my colleagues. And everyone does the same. So this is a tremendous learning situation. Right now, I'm not going to opine directly on one governor or one reserve bank president's views, but as I said earlier, right now the real rate is already at or slightly below our neutral real rate. And at this juncture, taking it much further below that would mean a zero or negative real interest rate at a time when the economy is at full employment, when inflation is above target, and financial conditions are accommodated. So that's what I think about policy

WESSEL: You mentioned communications a couple times. I understand the Federal Reserve is thinking about changes to its communication posture. If you could make some changes to the summary of economic projections or other communications, what would you recommend?

MUSALEM: So I think communications or changes to communications always have to be anchored with the objective of making sure the public can better understand our reaction function. More information for the sake of more information isn't what we should be seeking. We should be taking the right information so folks can understand our reaction function better in real time. So with that in mind, I think that the world is an uncertain place. You have to bring a healthy dose of humility when you're making policy decisions or policy recommendations and therefore i would favor in communications talking both about the modal path, in other words, the most likely path for the economy, and about alternative paths for the economies so that the public can understand better how we would behave in the modal paths and an alternative path. So I favor that in communications and I think I did that, some of that today.

In terms of the SEP itself, I think there are a few areas of improvement in the direction of better understanding our reaction function. Number one, it's very important that people understand the SEP is not an output of the FOMC meetings, it is an input into the FOMCs meetings. That's a very important thing. Two more things on the SEP. I would favor connecting the dots. By that, I mean connecting the inflation, growth, unemployment, and interest rate paths anonymously for each FOMC participant, so with a number you could connect, okay, number 22 that -- no, sorry, 22 is not possible -- number 12, number 12 has, you know, this growth path, this inflation path, this industry path, and it's all internally consistent. Why is that important? That would allow the public to understand the individual reaction functions of these anonymized folks and the collective reaction function. More importantly, different participants have different scenarios in mind and going back to my earlier comment about baseline and alternative scenarios, that would provide the public with information without outing any one participant. The other thing I would recommend in terms of the SEP is, right now the SEPs is calendar-based, so yearly-based. I would favor an SEP that had a fixed horizon. So. Instead of looking at the end of '25, it always looked forward one year, or two years, or three years. I think that would make it a more effective communication tool, because when you get to the end the year, those SEPs become very informative and the public is very focused on what that means for that one December meeting, as opposed to thinking more long-term about a path.

WESSEL: In regard to your first part, do you think the FOMC itself should give alternative scenarios? Is that what you're suggesting? Or just people in speeches like you did?

MUSALEM: I think both. I think it would be helpful, not all the time, but when necessary, it would be productive for the FOMC to maybe consider an alternative scenario in the SEP. I would be supportive of that. And of course, there are other opportunities like this one, where folks can talk about alternative scenarios that they're considering.

WESSEL: Please join me in thanking President Musalem. And if you could, two things, if you can stay in your seats because he has to run to catch a plane and also if there are coffee cups at your seat, if you put them in the receptacle at the back, our maintenance staff will appreciate it.