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Data Insights: Federal Reserve

Wednesday, January 29, 2014

Today's FOMC statement: how the language changed from prior meeting

Release Date: ~~December 18, 2013~~January 29, 2014

For immediate release

Information received since the Federal Open Market Committee met in ~~October~~December indicates that growth in economic activity ~~is expanding at a moderate pace.~~picked up in recent quarters. Labor market ~~conditions have shown~~indicators were mixed but on balance showed further improvement~~; the~~. The unemployment rate ~~has~~ declined but remains elevated. Household spending and business fixed investment advanced more quickly in recent months, while the recovery in the housing sector slowed somewhat~~ in recent months.~~. Fiscal policy is restraining economic growth, although the extent of restraint ~~may be~~is diminishing. Inflation has been running below the Committee's longer-run objective, but longer-term inflation expectations have remained stable.

Consistent with its statutory mandate, the Committee seeks to foster maximum employment and price stability. The Committee expects that, with appropriate policy accommodation, economic ~~growth~~activity will ~~pick up from its recent~~expand at a moderate pace and the unemployment rate will gradually decline toward levels the Committee judges consistent with its dual mandate. The Committee sees the risks to the outlook for the economy and the labor market as having become more nearly balanced. The Committee recognizes that inflation persistently below its 2 percent objective could pose risks to economic performance, and it is monitoring inflation developments carefully for evidence that inflation will move back toward its objective over the medium term.

Taking into account the extent of federal fiscal retrenchment since the inception of its current asset purchase program, the Committee ~~sees~~continues to see the improvement in economic activity and labor market conditions over that period as consistent with growing underlying strength in the broader economy. In light of the cumulative progress toward maximum employment and the improvement in the outlook for labor market conditions, the Committee decided to ~~modestly reduce~~ make a further measured reduction in the pace of its asset purchases. Beginning in ~~January~~February, the Committee will add to its holdings of agency mortgage-backed securities at a pace of $30 billion per month rather than $35 billion per month~~ rather than $40 billion per month~~, and will add to its holdings of longer-term Treasury securities at a pace of $35 billion per month rather than $40 billion per month~~ rather than $45 billion per month~~. The Committee is maintaining its existing policy of reinvesting principal payments from its holdings of agency debt and agency mortgage-backed securities in agency mortgage-backed securities and of rolling over maturing Treasury securities at auction. The Committee's sizable and still-increasing holdings of longer-term securities should maintain downward pressure on longer-term interest rates, support mortgage markets, and help to make broader financial conditions more accommodative, which in turn should promote a stronger economic recovery and help to ensure that inflation, over time, is at the rate most consistent with the Committee's dual mandate.

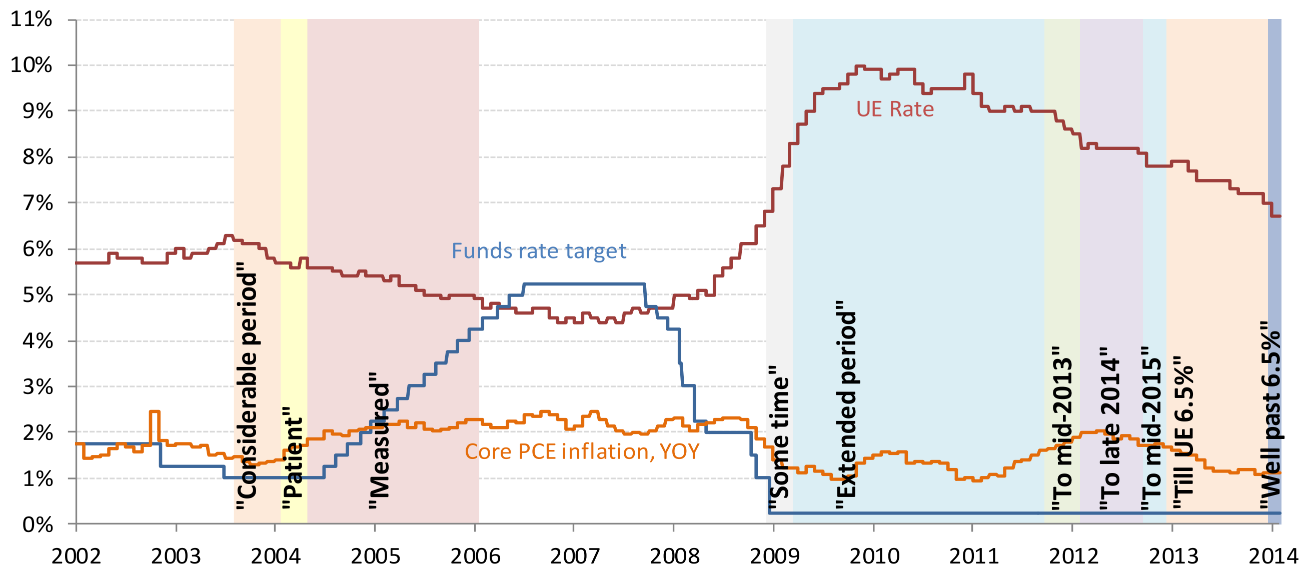
The Committee will closely monitor incoming information on economic and financial developments in coming months and will continue its purchases of Treasury and agency mortgage-backed securities, and employ its other policy tools as appropriate, until the outlook for the labor market has improved substantially in a context of price stability. If incoming information broadly supports the Committee's expectation of ongoing improvement in labor market conditions and inflation moving back toward its longer-run objective, the Committee will likely reduce the pace of asset purchases in further measured steps at future meetings. However, asset purchases are not on a preset course, and the Committee's decisions about their pace will remain contingent on the Committee's outlook for the labor market and inflation as well as its assessment of the likely efficacy and costs of such purchases.

To support continued progress toward maximum employment and price stability, the Committee today reaffirmed its view that a highly accommodative stance of monetary policy will remain appropriate for a considerable time after the asset purchase program ends and the economic recovery strengthens. The Committee also reaffirmed its expectation that the current exceptionally low target range for the federal funds rate of 0 to 1/4 percent will be appropriate at least as long as the unemployment rate remains above 6-1/2 percent, inflation between one and two years ahead is projected to be no more than a half percentage point above the Committee's 2 percent longer-run goal, and longer-term inflation expectations continue to be well anchored. In determining how long to maintain a highly accommodative stance of monetary policy, the Committee will also consider other information, including additional measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial developments. The Committee ~~now anticipates~~continues to anticipate, based on its assessment of these factors, that it likely will be appropriate to maintain the current target range for the federal funds rate well past the time that the unemployment rate declines below 6-1/2 percent, especially if projected inflation continues to run below the Committee's 2 percent longer-run goal. When the Committee decides to begin to remove policy accommodation, it will take a balanced approach consistent with its longer-run goals of maximum employment and inflation of 2 percent.

Voting for the FOMC monetary policy action were: Ben S. Bernanke, Chairman; William C. Dudley, Vice Chairman; ~~James Bullard~~Richard W. Fisher; Narayana Kocherlakota; Sandra Pianalto; Charles ~~L. Evans; Esther L. George~~I. Plosser; Jerome H. Powell; Jeremy C. Stein; Daniel K. Tarullo; and Janet L. Yellen~~. Voting against the action was Eric S. Rosengren, who believes that, with the unemployment rate still elevated and the inflation rate well below the target, changes in the purchase program are premature until incoming data more clearly indicate that economic growth is likely to be sustained above its potential rate~~.

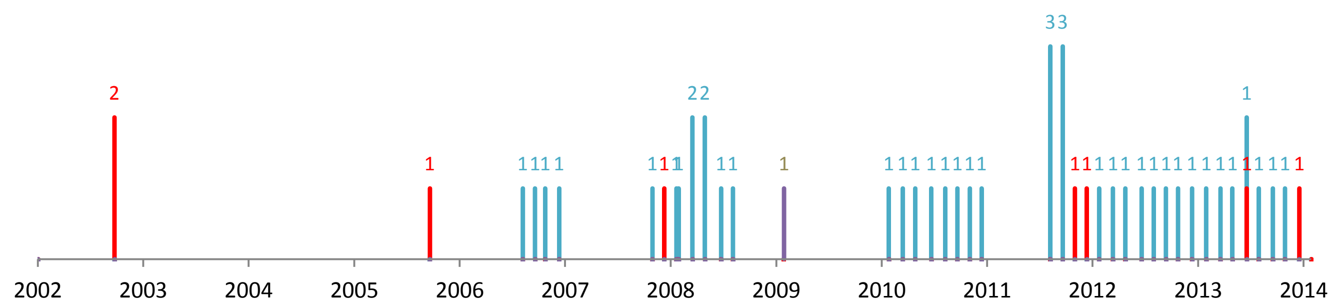
Source: FOMC, TrendMacro analysis

Fedspeak regime change



Source: FOMC, Federal Reserve H.15, BLS, BEA, TrendMacro calculations

Other voices: number of FOMC decision dissents

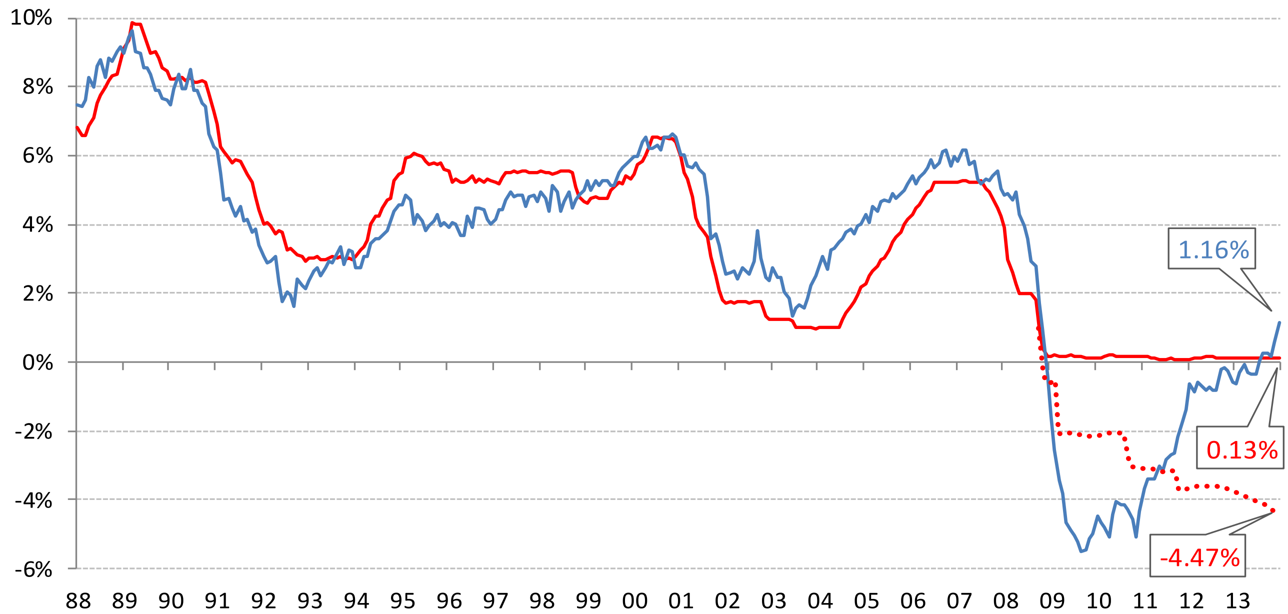


Source: FOMC, TrendMacro calculations

Yellen's Taylor Rule (per Rudebusch 2009): Is the Fed tight or loose?

Rule: 2.07 + 1.28 x 12-mo core PCE inflation - 1.95 x (UE - CBO natural rate)

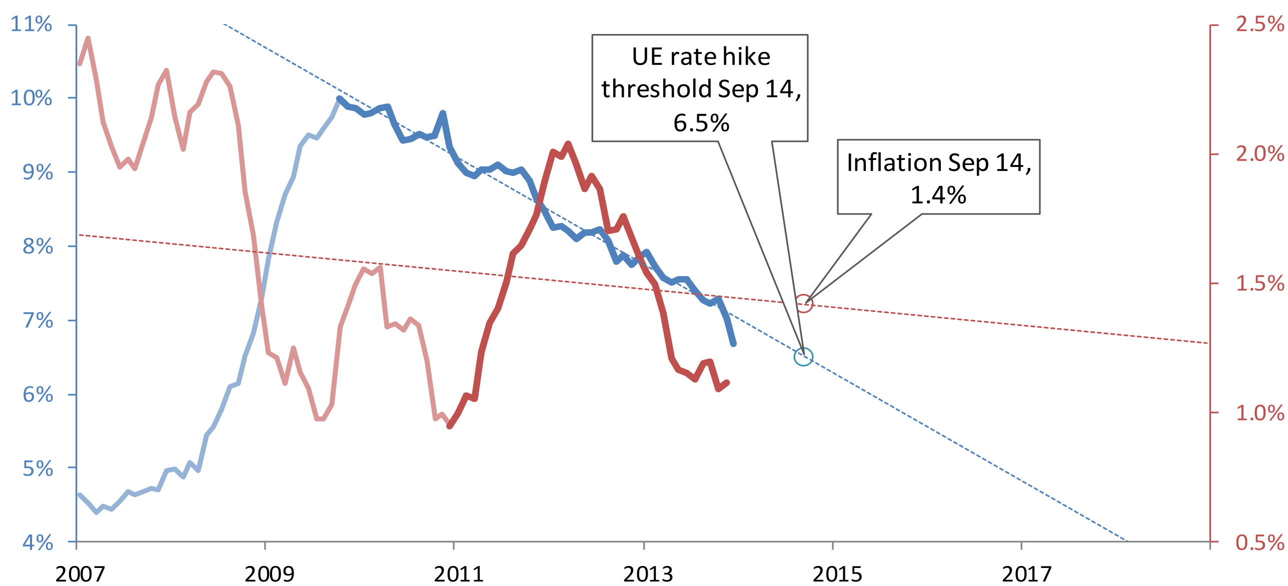
Actual funds rate ⋯ Balance sheet-augmented funds rate



Source: BLS Current Population Survey, TrendMacro calculations

Yellen's Evans Rule: When will the Fed start hiking rates?

Unemployment rate ⋯ Trend from peak   Core PCE inflation YOY ⋯ Trend from trough

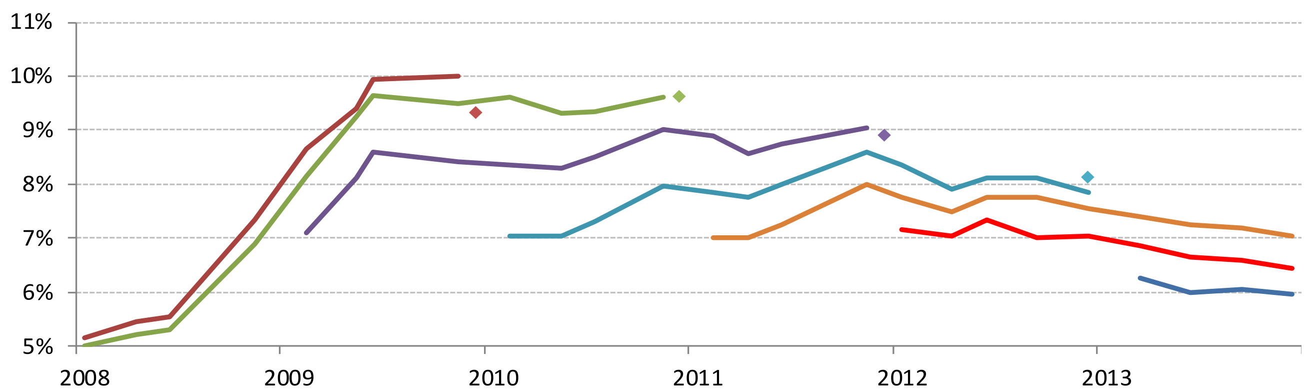


Source: BLS, BEA, TrendMacro calculations

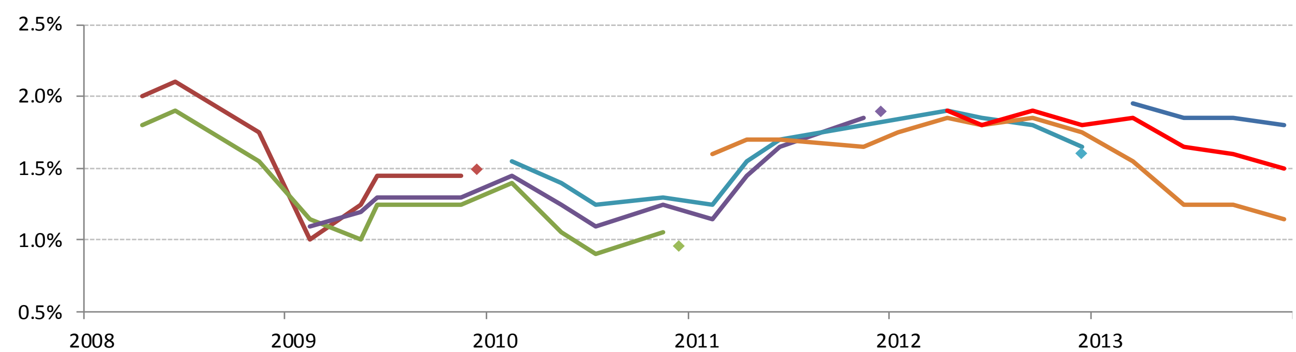
Forecast versus actual: economic projections of the FRB and the presidents

— Forecast ◆ Actual ■ for 2009 ■ for 2010 ■ for 2011 ■ for 2012 ■ for 2013 ■ for 2014 ■ for 2015

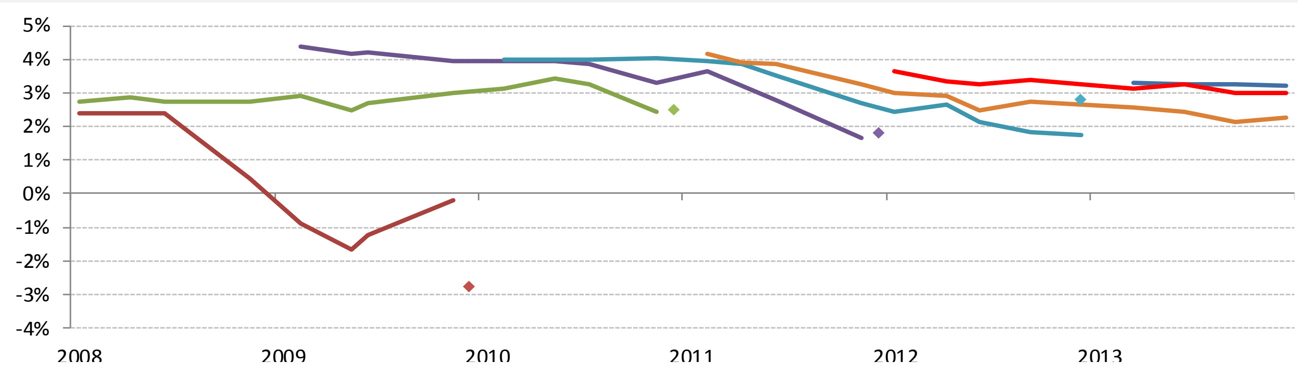
Unemployment



Core PCE inflation



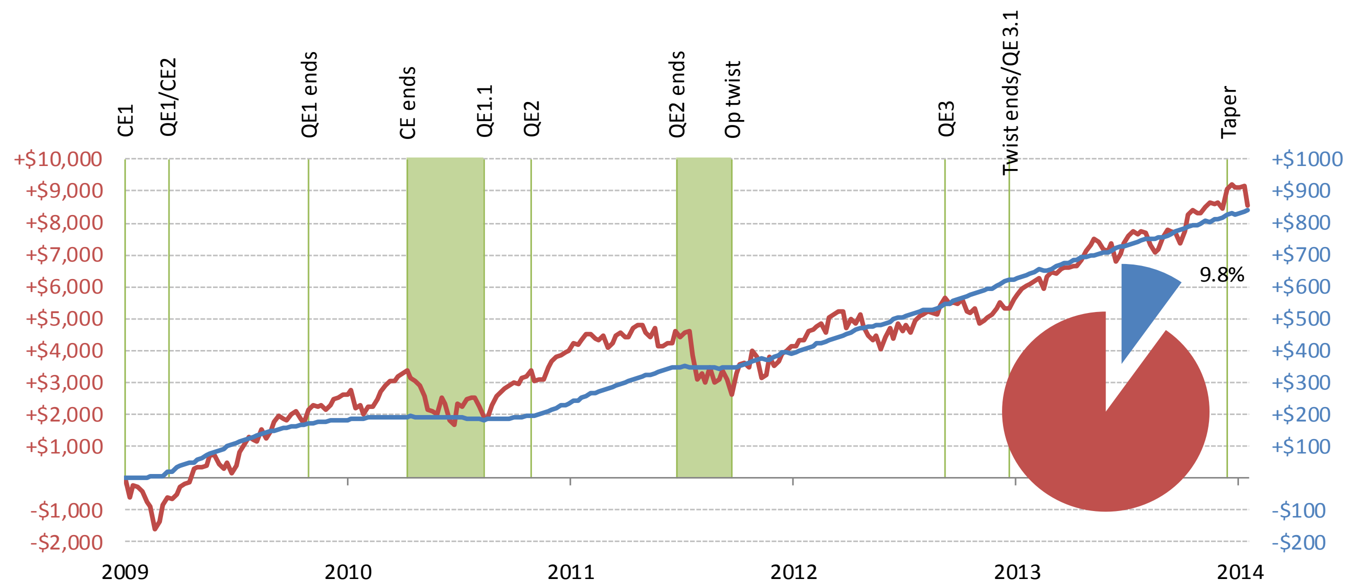
Real GDP



Source: Federal Reserve, BEA, BLS, TrendMacro calculations

How much of the US stock market is effectively owned by the Fed?

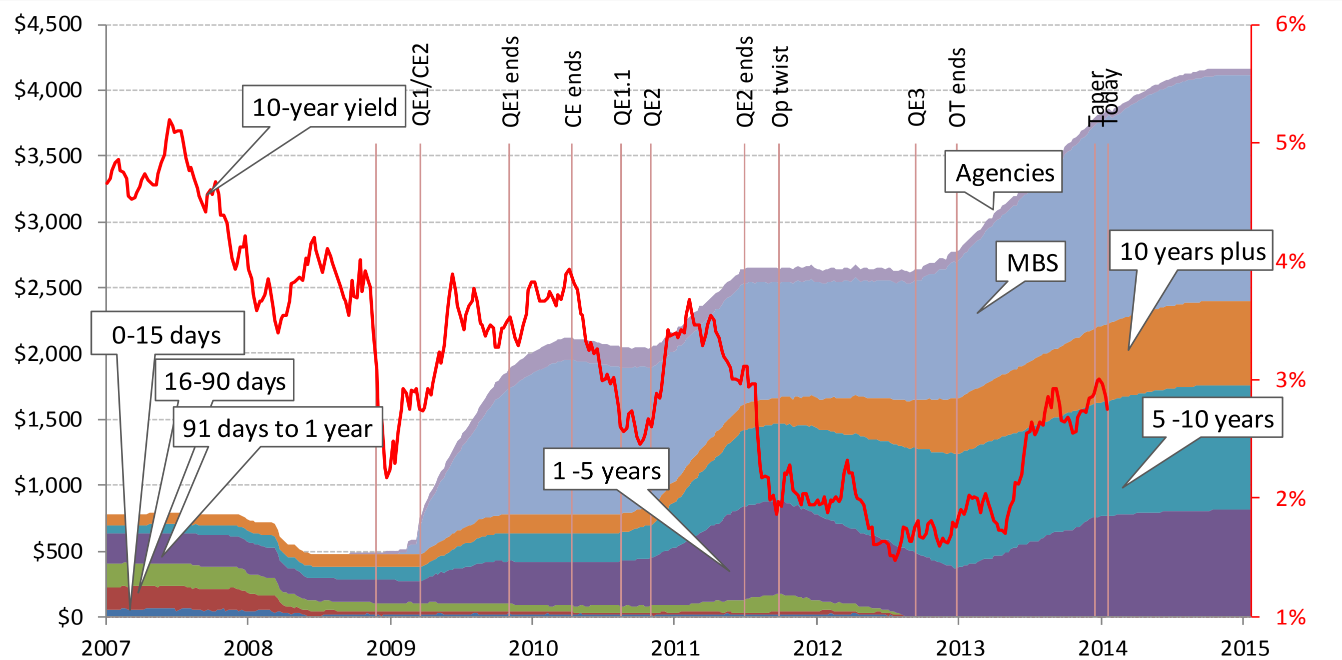
S&P 500 change from January 2009, USD billions — Market cap — Fed balance sheet risk equivalent



Source: Bloomberg, TrendMacro calculations

Actual and projected Fed LSAPs (Large-Scale Asset Purchases) vs. Treasury yield

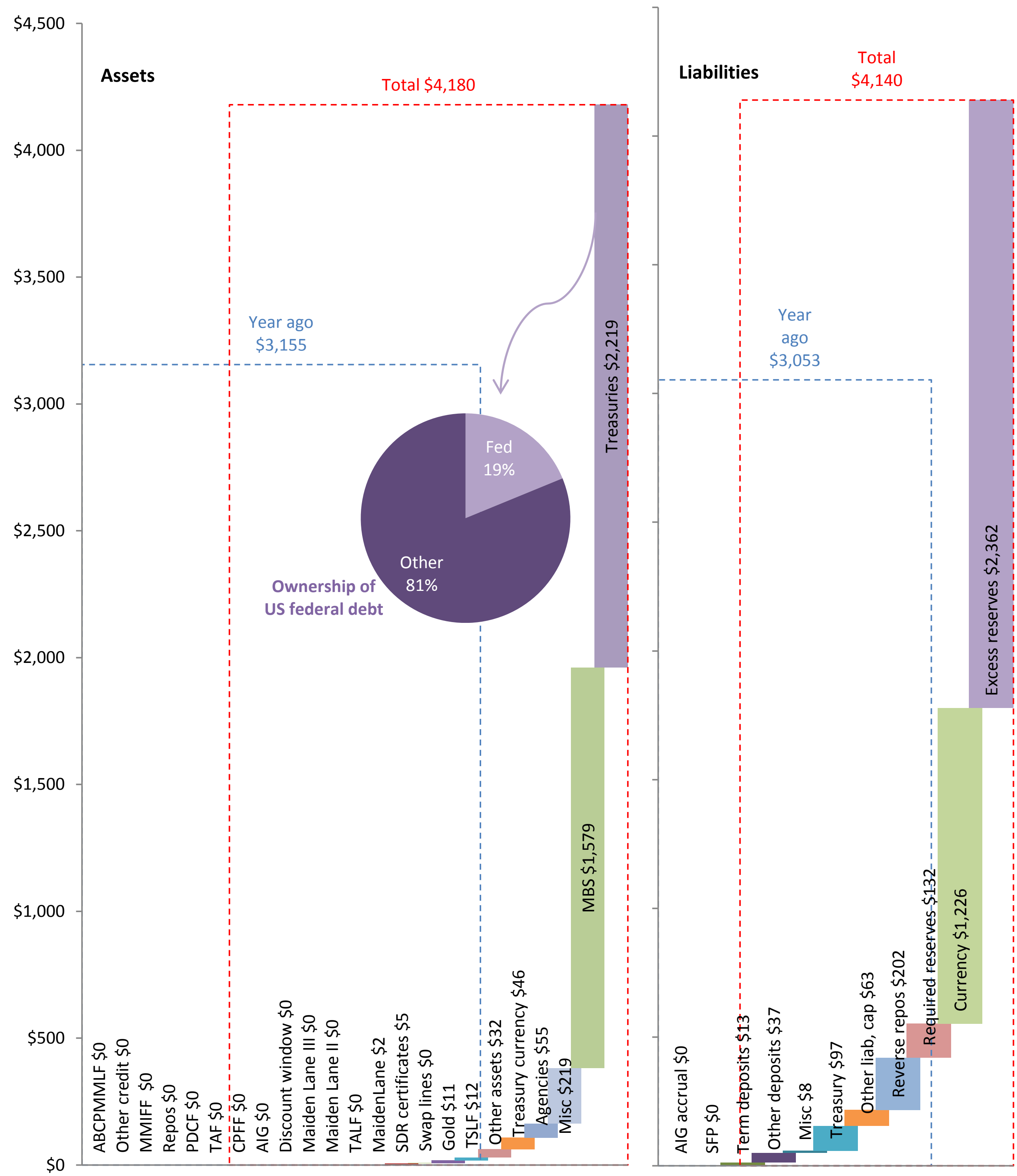
Projected at current run-rates



Source: Federal Reserve H.4, H.15, TrendMacro calculations

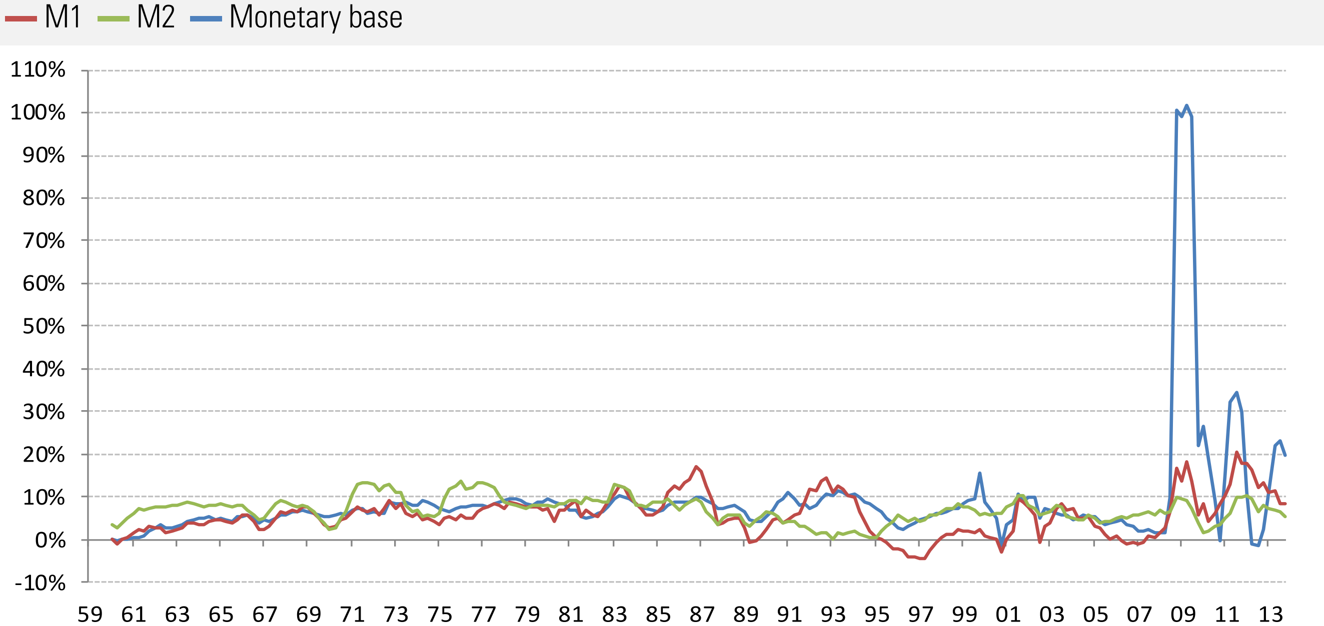
The Fed's assets, and how they are funded (USD billions)

Assets do not perfectly match liabilities because we include unsettled MBS purchases and sales



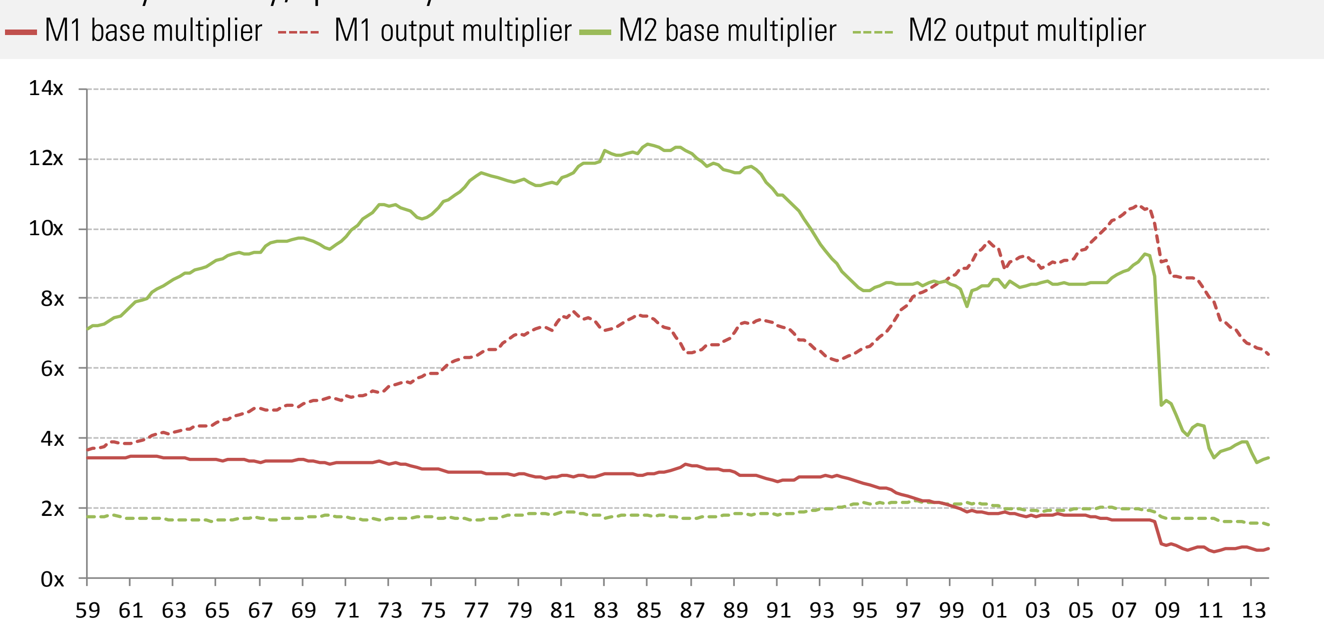
Source: Federal Reserve H.4, US Treasury, TrendMacro calculations

Money supply growth, YOY quarterly



Source: Federal Reserve H.6, TrendMacro calculations

Monetary velocity, quarterly



Source: BEA, Federal Reserve H.6, TrendMacro calculations