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Data Insights: Federal Reserve

Wednesday, December 16, 2015

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

Release Date: ~~October 28~~December 16, 2015

For immediate release

Information received since the Federal Open Market Committee met in ~~September~~October suggests that economic activity has been expanding at a moderate pace. Household spending and business fixed investment have been increasing at solid rates in recent months, and the housing sector has improved further; however, net exports have been soft. ~~The pace~~A range of recent labor market indicators, including ongoing job gains ~~slowed~~ and ~~the~~declining unemployment ~~rate held steady. Nonetheless, labor market indicators, on balance, show~~, shows further improvement and confirms that underutilization of labor resources has diminished appreciably since early this year. Inflation has continued to run below the Committee's 2 percent longer-run objective, partly reflecting declines in energy prices and in prices of non-energy imports. Market-based measures of inflation compensation ~~moved slightly lower;~~remain low; some survey-based measures of longer-term inflation expectations have ~~remained stable~~edged down.

Consistent with its statutory mandate, the Committee seeks to foster maximum employment and price stability. The Committee currently expects that, with ~~appropriate~~gradual adjustments in the stance of monetary policy ~~accommodation~~, economic activity will continue to expand at a moderate pace~~, with~~ and labor market indicators ~~continuing to move toward levels~~will continue to strengthen. Overall, taking into account domestic and international developments, the Committee ~~judges consistent with its dual mandate. The Committee continues to see~~sees the risks to the outlook for both economic activity and the labor market as ~~nearly~~ balanced ~~but is monitoring global economic and financial developments.~~. Inflation is ~~anticipated to remain near its recent low level in the near term but the Committee expects inflation~~expected to rise ~~gradually toward~~to 2 percent over the medium term as the ~~labor market improves further and the~~ transitory effects of declines in energy and import prices dissipate~~.~~ and the labor market strengthens further. The Committee continues to monitor inflation developments closely.

~~To support continued progress toward maximum employment and price stability, the~~ The Committee ~~today reaffirmed its view that the current 0~~judges that there has been considerable improvement in labor market conditions this year, and it is reasonably confident that inflation will rise, over the medium term, to ~~1/4~~its 2 percent ~~target range~~objective. Given the economic outlook, and recognizing the time it takes for policy actions to affect future economic outcomes, the Committee decided to raise the target range for the federal funds rate to 1/4 to 1/2 percent. The stance of monetary policy remains

~~appropriate.~~ accommodative after this increase, thereby supporting further improvement in labor market conditions and a return to 2 percent inflation.

In determining ~~whether it will be appropriate~~the timing and size of future adjustments to ~~raise~~ the target range ~~at its next meeting~~for the federal funds rate, the Committee will assess ~~progress--both~~ realized and expected~~--toward~~ economic conditions relative to its objectives of maximum employment and 2 percent inflation. This assessment will take into account a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial and international developments. ~~The Committee anticipates that it will be appropriate to raise the target range for the federal funds rate when it has seen some further improvement in the labor market and is reasonably confident that inflation will move back to its 2 percent objective over the medium term.~~ In light of the current shortfall of inflation from 2 percent, the Committee will carefully monitor actual and expected progress toward its inflation goal. The Committee expects that economic conditions will evolve in a manner that will warrant only gradual increases in the federal funds rate; the federal funds rate is likely to remain, for some time, below levels that are expected to prevail in the longer run. However, the actual path of the federal funds rate will depend on the economic outlook as informed by incoming data.

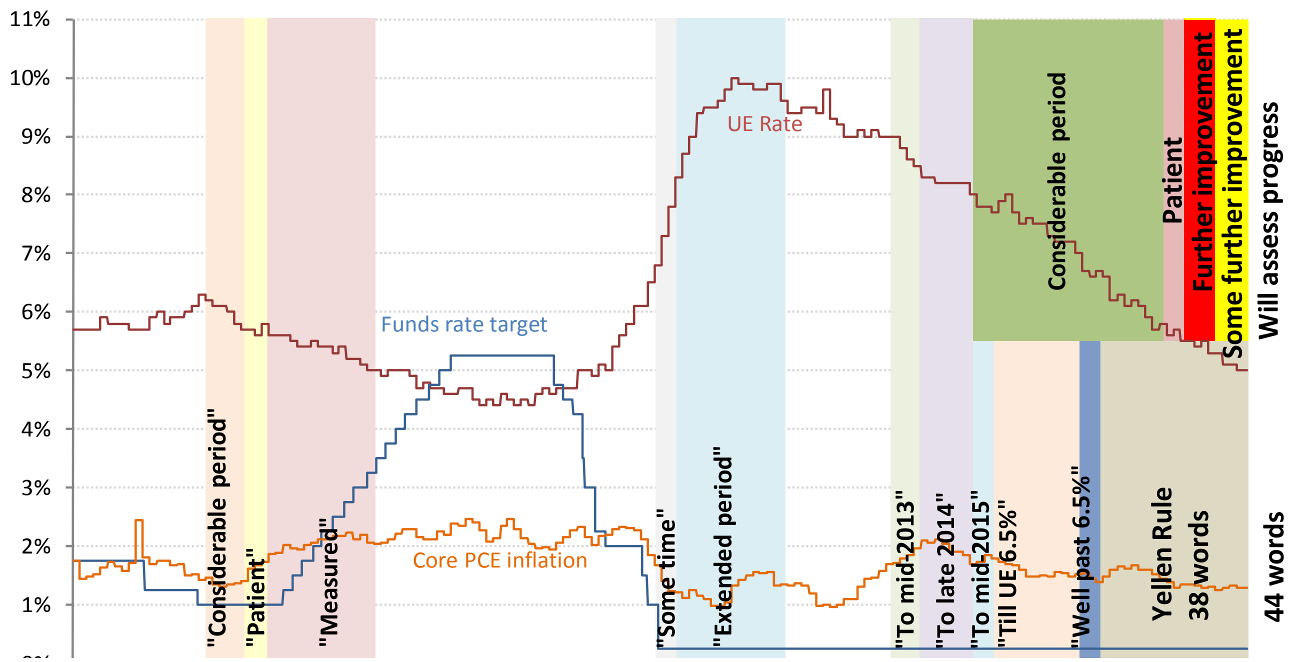
The Committee is maintaining its existing policy of reinvesting principal payments from its holdings of agency debt and agency mortgage-backed securities in agency mortgage-backed securities and of rolling over maturing Treasury securities at auction~~.~~, and it anticipates doing so until normalization of the level of the federal funds rate is well under way. This policy, by keeping the Committee's holdings of longer-term securities at sizable levels, should help maintain accommodative financial conditions.

~~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. The Committee currently anticipates that, even after employment and inflation are near mandate-consistent levels, economic conditions may, for some time, warrant keeping the target federal funds rate below levels the Committee views as normal in the longer run.~~

Voting for the FOMC monetary policy action were: Janet L. Yellen, Chair; William C. Dudley, Vice Chairman; Lael Brainard; Charles L. Evans; Stanley Fischer; Jeffrey M. Lacker; Dennis P. Lockhart; Jerome H. Powell; Daniel K. Tarullo; and John C. Williams. ~~Voting against the action was Jeffrey M. Lacker, who preferred to raise the target range for the federal funds rate by 25 basis points at this meeting.~~

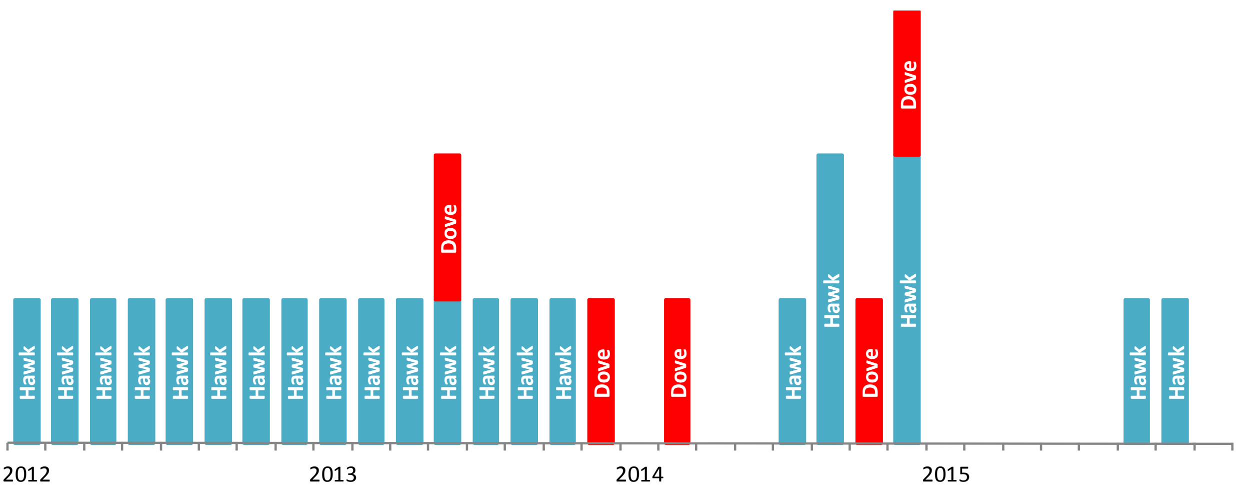
Source: FOMC, TrendMacro analysis

Fedspeak regime change: the evolution of forward guidance



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

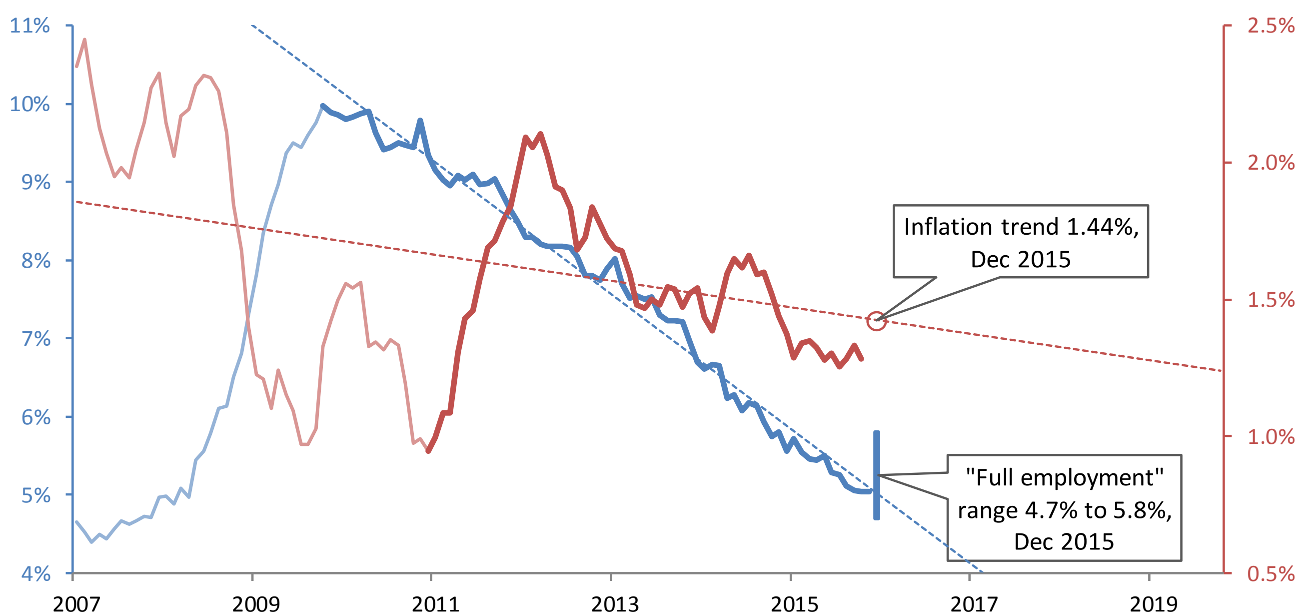
Other voices: number and direction of FOMC decision dissents



Source: FOMC, TrendMacro calculations

Yellen beyond the Evans Rule at "later this year"

Unemployment rate ··· Trend from peak — Core PCE inflation YOY ··· Trend from trough

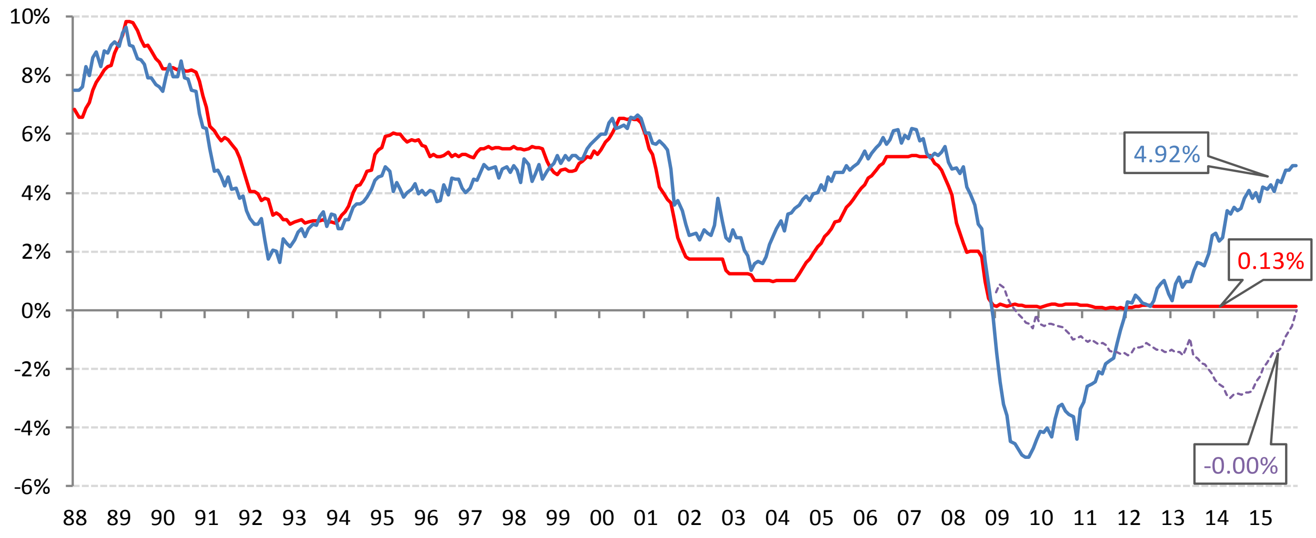


Source: BLS Current Population Survey, TrendMacro calculations

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 "Shadow interest rate" per Wu-Xia (2015) after Black (1995)

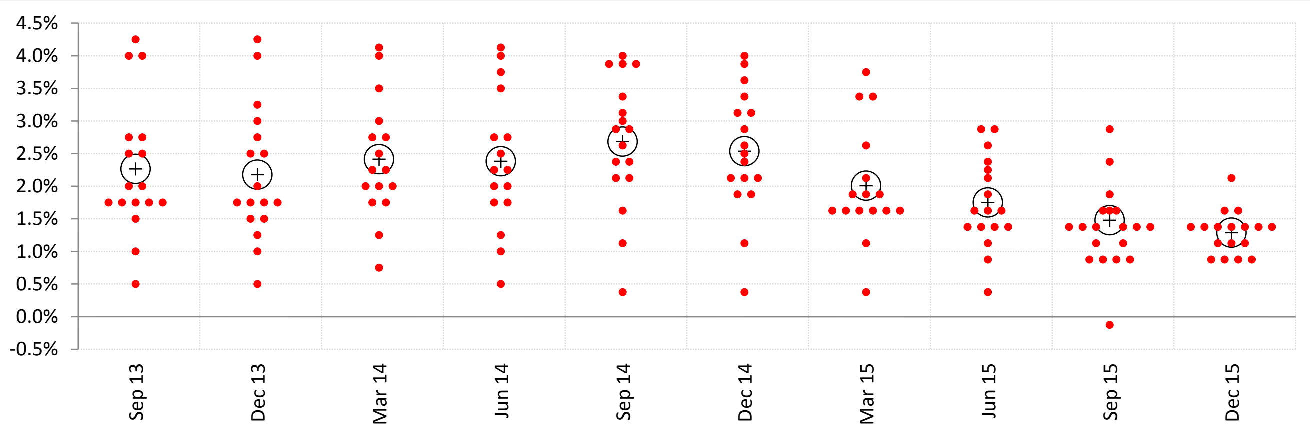


Source: BLS, BEA, TrendMacro calculations

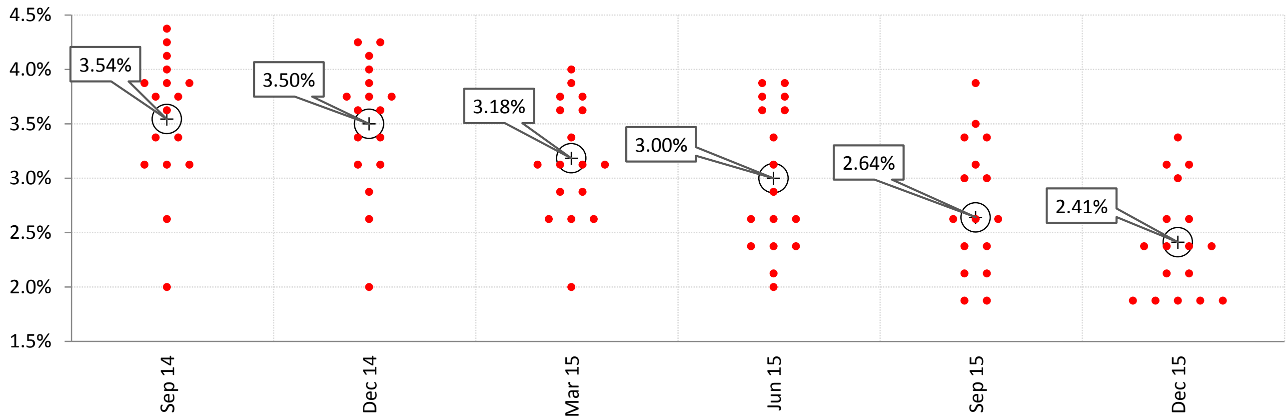
Tracking the "dotplots"

FOMC participants' estimate of "appropriate" target fed funds rate ● Vote by participant ○ Average

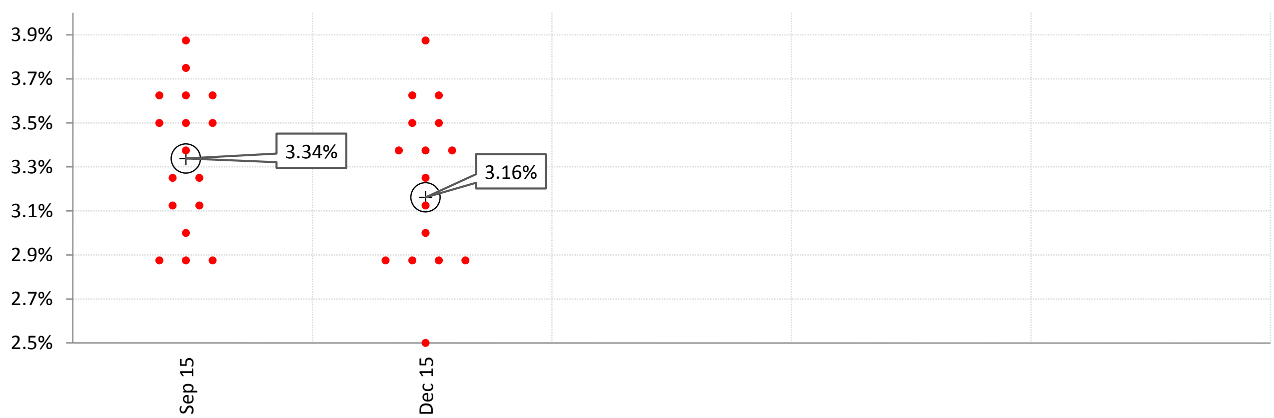
For year-end 2016



For year-end 2017



For year-end 2018

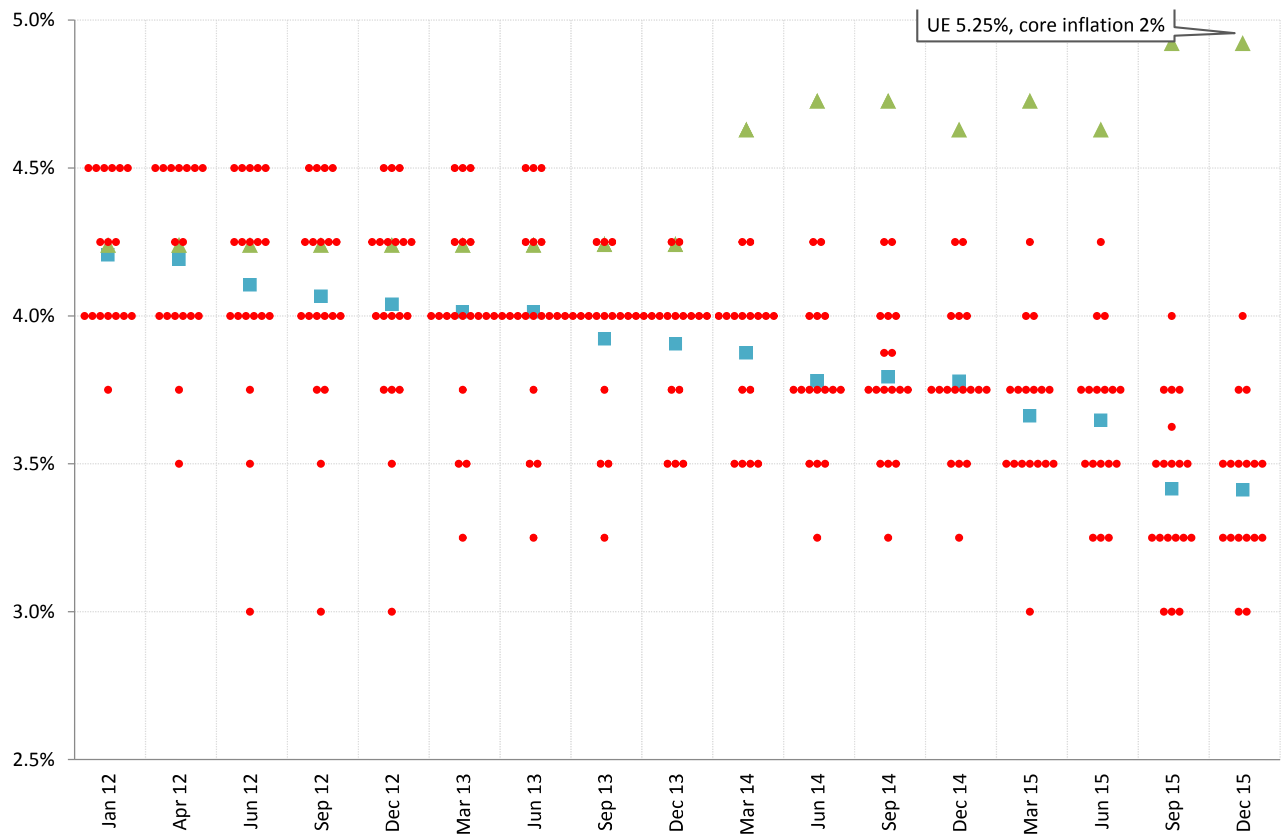


Source: Federal Reserve, TrendMacro calculations

The ultimate dots

FOMC participants' estimate of "appropriate" target fed funds rate ● Vote by individual participant
■ Weighted average ▲ Taylor Rule rate based on participants' core PCE and UE estimates

For "longer run"

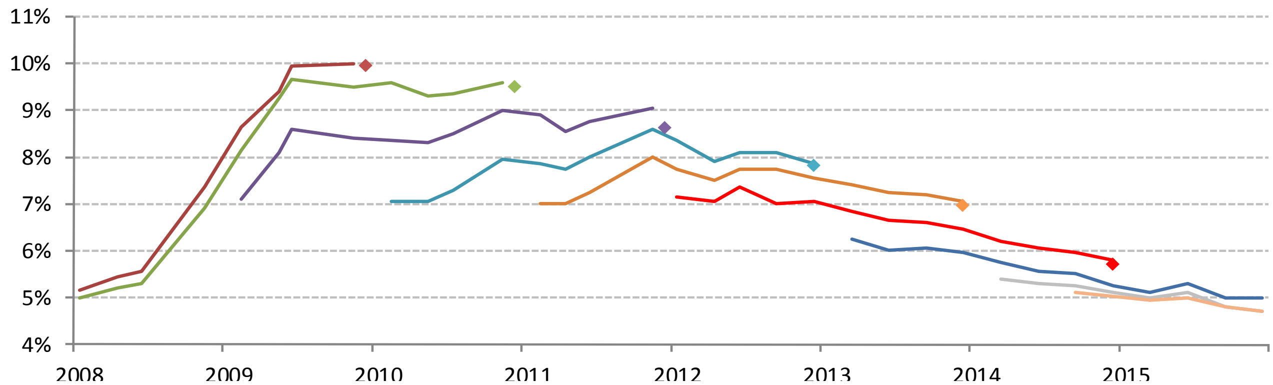


Source: Federal Reserve, TrendMacro calculations

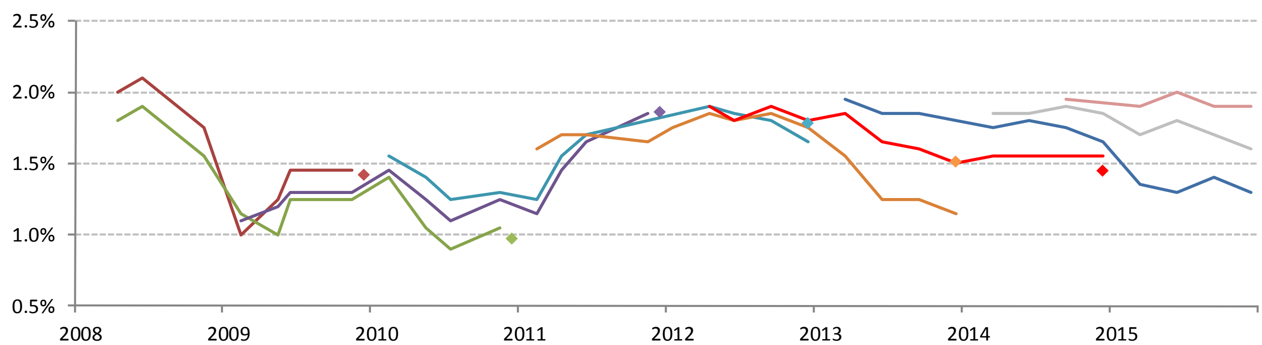
Forecast versus actual: economic projections of the FRB and the presidents

— Forecast ◆ Actual ■ for 2009 ■ 2010 ■ 2011 ■ 2012 ■ 2013 ■ 2014 ■ 2015 ■ 2016 ■ 2017

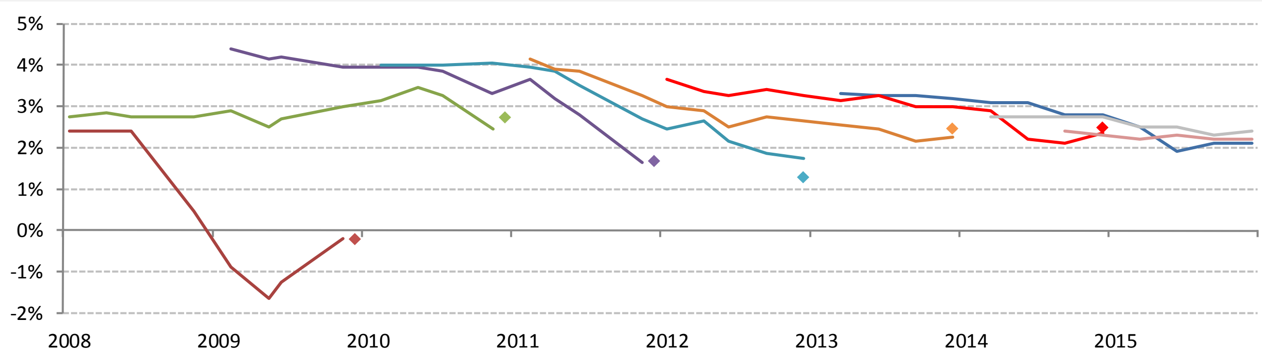
Unemployment



Core PCE inflation



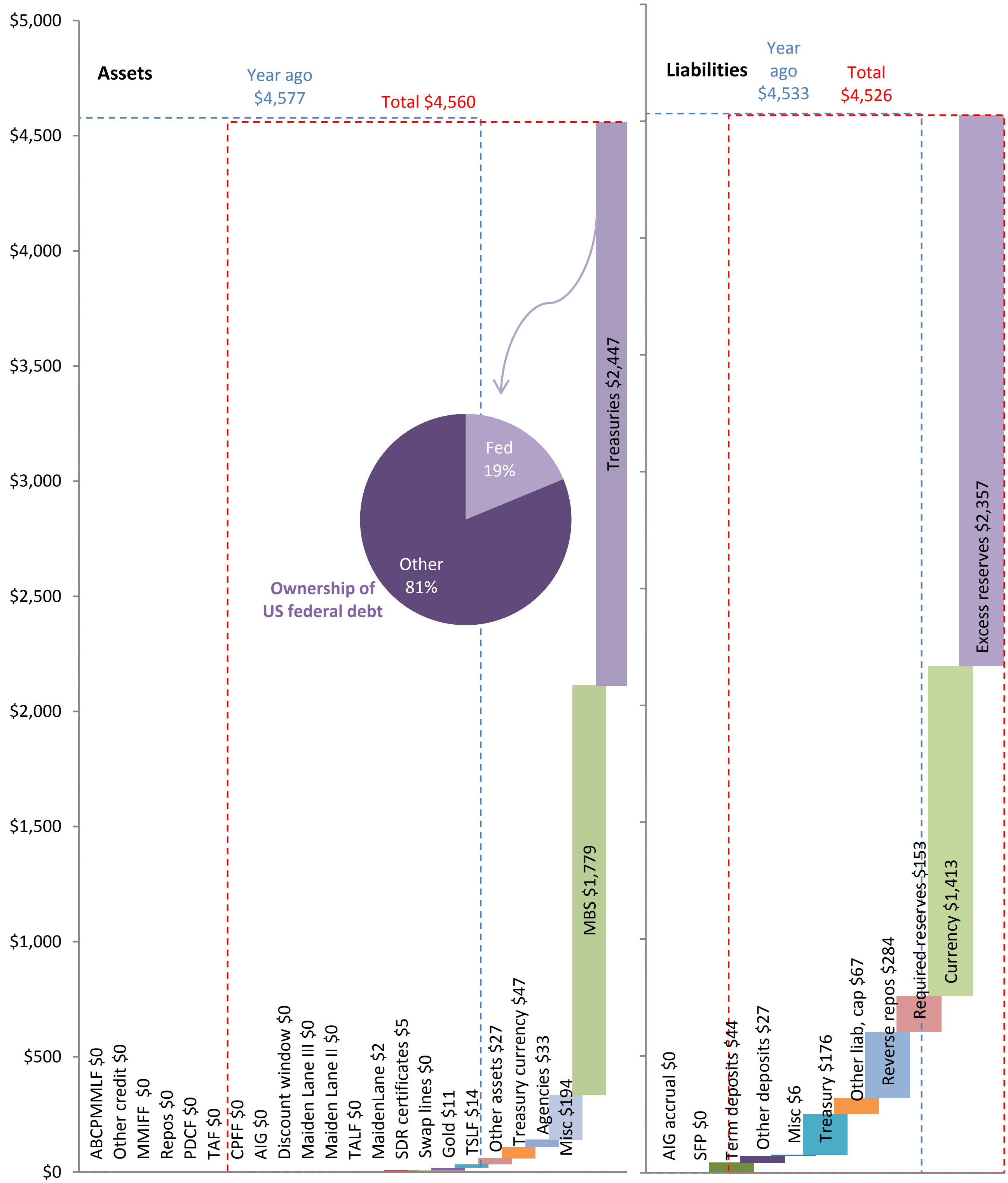
Real GDP



Source: Federal Reserve, BEA, BLS, TrendMacro calculations

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

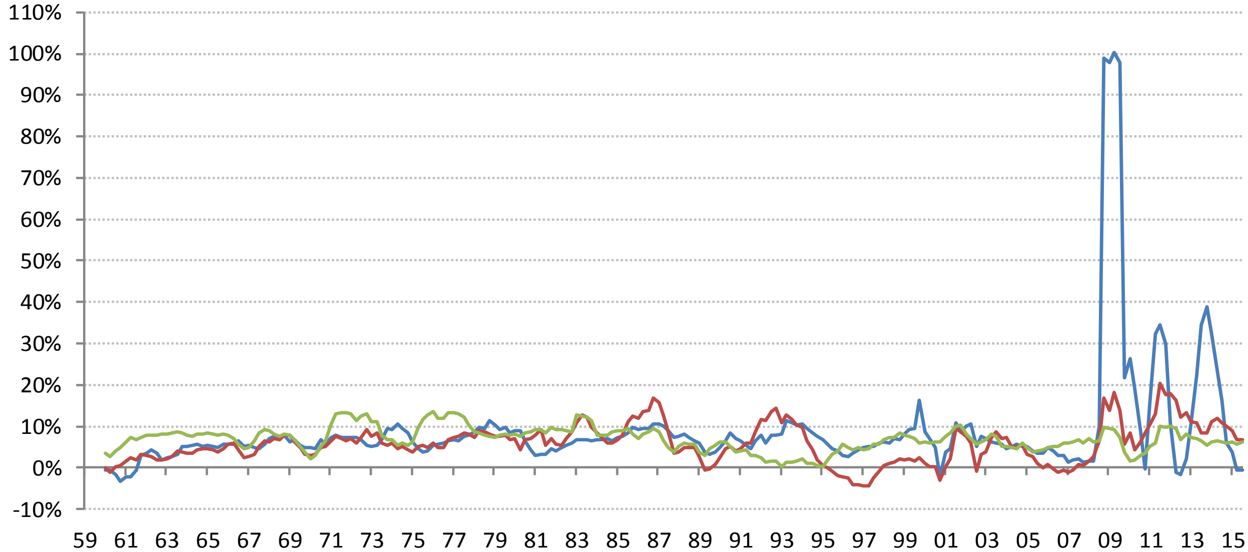
Assets do not perfectly match liabilities because we include unsettled MBS purchases and sales



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

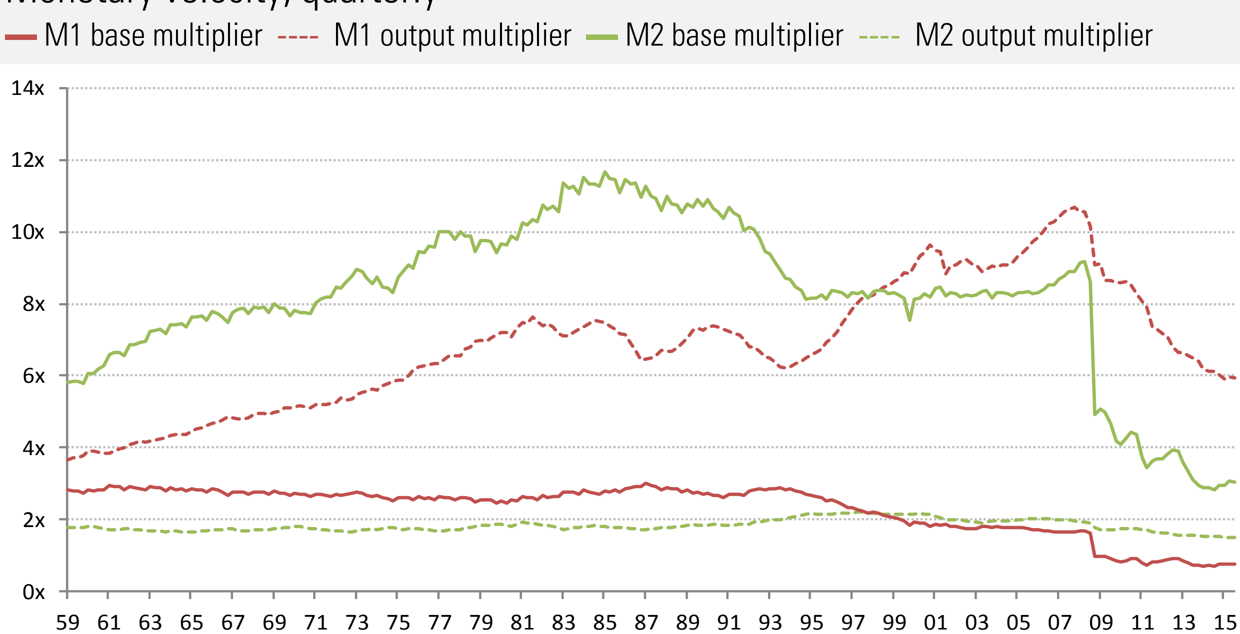
Money supply growth, YOY quarterly

M1 M2 Monetary base



Source: Federal Reserve H.6, TrendMacro calculations

Monetary velocity, quarterly



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