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Data Insights: Federal Reserve

Wednesday, July 26, 2017

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

~~June 14~~July 26, 2017

For release at 2:00 p.m. EDT

Information received since the Federal Open Market Committee met in ~~May~~June indicates that the labor market has continued to strengthen and that economic activity has been rising moderately so far this year. Job gains have ~~moderated but have~~ been solid, on average, since the beginning of the year, and the unemployment rate has declined. Household spending ~~has picked up in recent months,~~ and business fixed investment ~~has~~have continued to expand. On a 12-month basis, overall inflation ~~has declined recently~~ and~~, like~~ the measure excluding food and energy prices~~, is~~ have declined and are running ~~somewhat~~ below 2 percent. Market-based measures of inflation compensation remain low; survey-based measures of longer-term inflation expectations are little changed, on balance.

Consistent with its statutory mandate, the Committee seeks to foster maximum employment and price stability. The Committee continues to expect that, with gradual adjustments in the stance of monetary policy, economic activity will expand at a moderate pace, and labor market conditions will strengthen somewhat further. Inflation on a 12-month basis is expected to remain somewhat below 2 percent in the near term but to stabilize around the Committee's 2 percent objective over the medium term. Near-term risks to the economic outlook appear roughly balanced, but the Committee is monitoring inflation developments closely.

In view of realized and expected labor market conditions and inflation, the Committee decided to ~~raise~~maintain the target range for the federal funds rate ~~to~~at 1 to 1-1/4 percent. The stance of monetary policy remains accommodative, thereby supporting some further strengthening in labor market conditions and a sustained return to 2 percent inflation.

In determining the timing and size of future adjustments to the target range for the federal funds rate, the Committee will assess realized and expected 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 will carefully monitor actual and expected inflation developments relative to its symmetric inflation goal. The Committee expects that economic conditions will evolve in a manner that will warrant gradual increases in the federal funds rate; the federal funds rate is likely to remain, for some time, below

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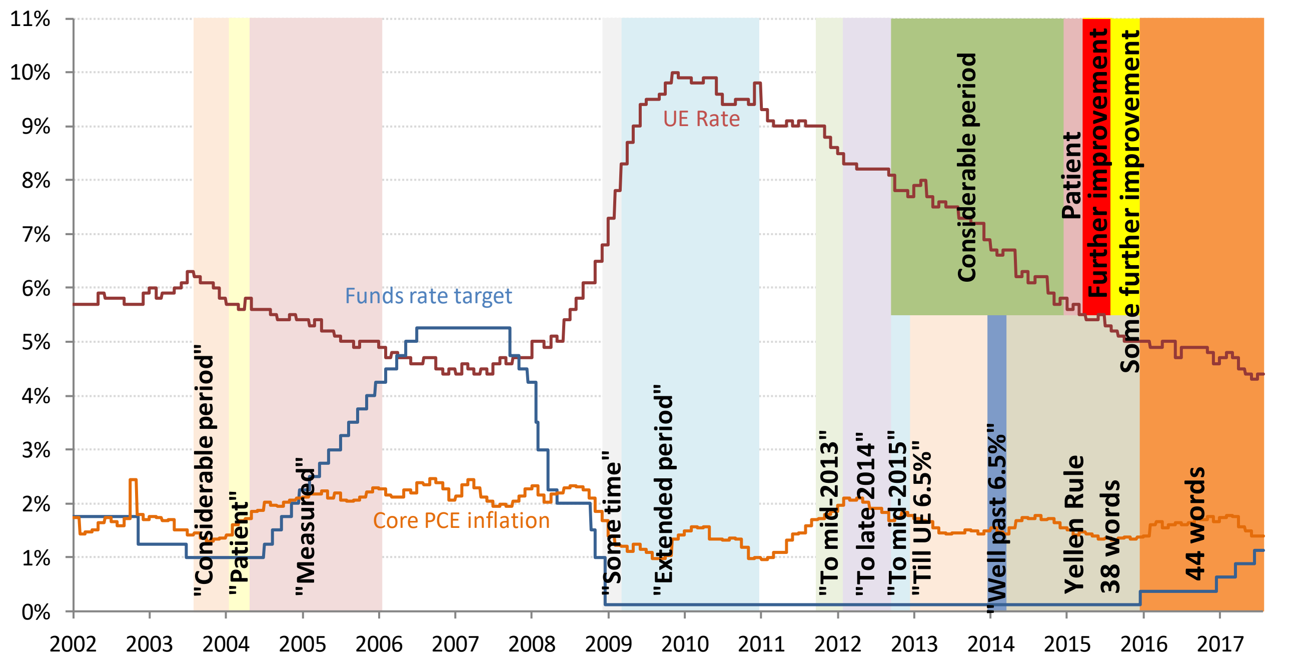
levels that are expected to prevail in the longer run. However, the actual path of the federal funds rate will depend on the economic outlook as informed by incoming data.

~~The~~For the time being, 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 ~~currently~~ expects to begin implementing ~~a~~its balance sheet normalization program ~~this year~~relatively soon, provided that the economy evolves broadly as anticipated~~. This~~; this program~~, which would gradually reduce the Federal Reserve's securities holdings by decreasing reinvestment of principal payments from those securities,~~ is described in the ~~accompanying addendum~~June 2017 Addendum to the Committee's Policy Normalization Principles and Plans.

Voting for the FOMC monetary policy action were: Janet L. Yellen, Chair; William C. Dudley, Vice Chairman; Lael Brainard; Charles L. Evans; Stanley Fischer; Patrick Harker; Robert S. Kaplan; Neel Kashkari; and Jerome H. Powell~~. Voting against the action was Neel Kashkari, who preferred at this meeting to maintain the existing target range for the federal funds rate~~.

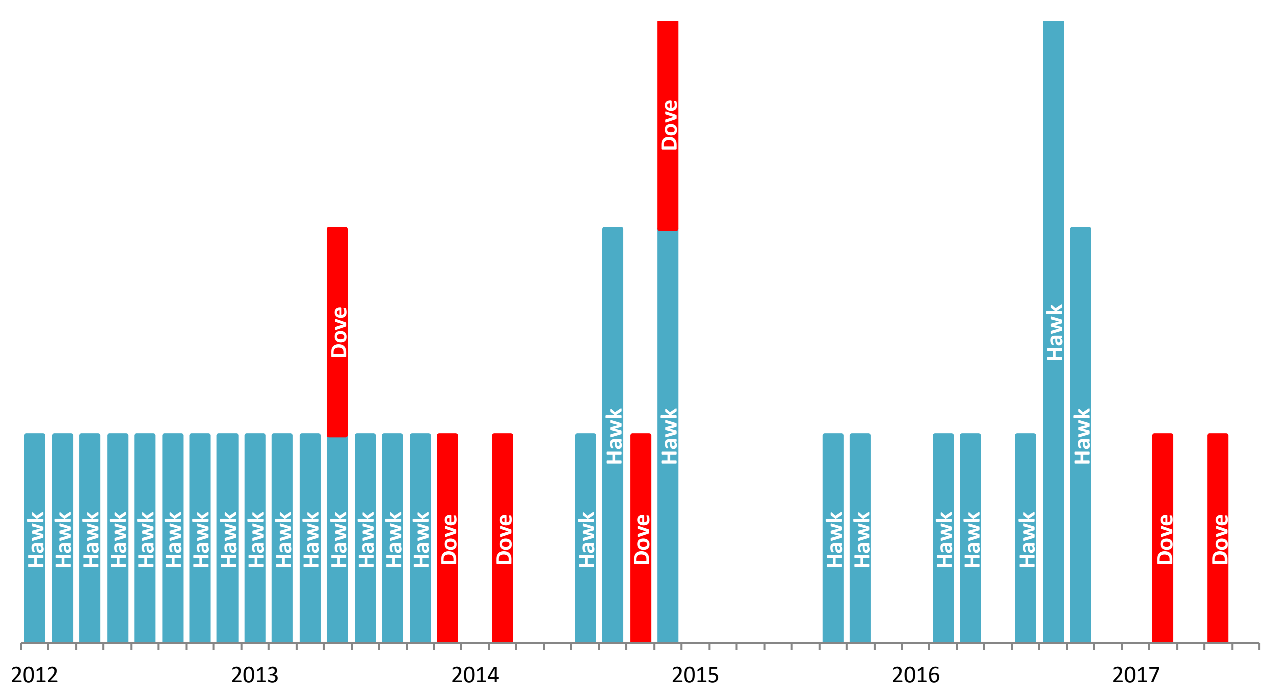
Source: FOMC, TrendMacro analysis

Fedspeak regime change: the evolution of forward guidance



Source: FOMC, Federal Reserve, BLS, BEA, TrendMacro calculations

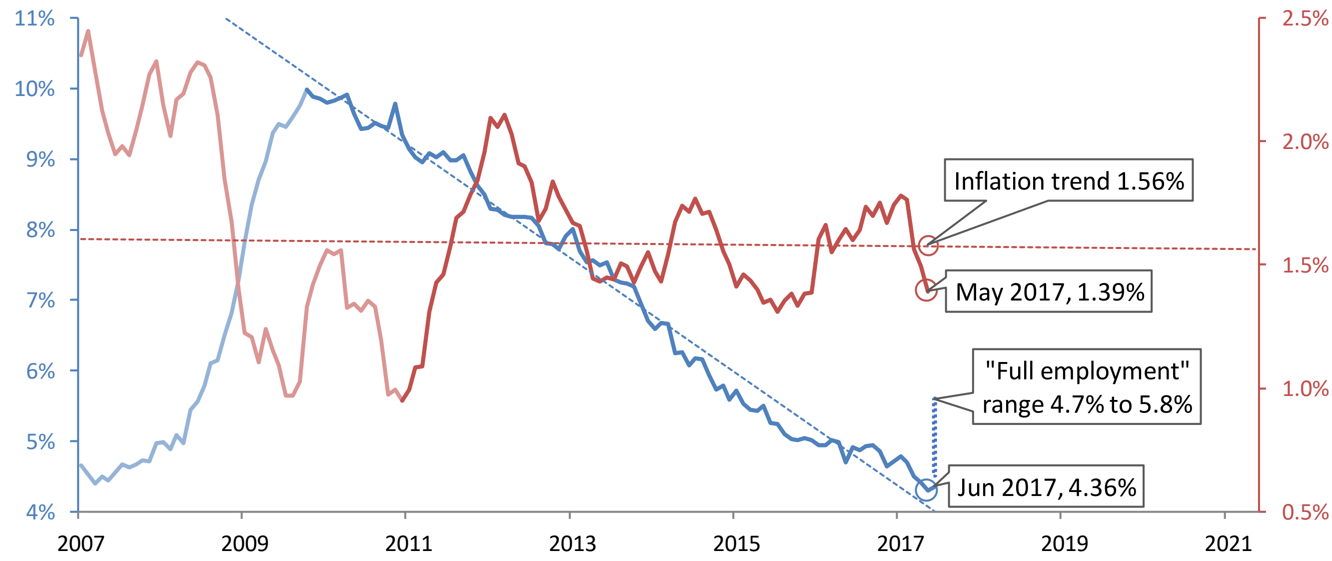
Other voices: number and direction of FOMC decision dissents



Source: FOMC, TrendMacro calculations

The dual mandate: garbage in, garbage out

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

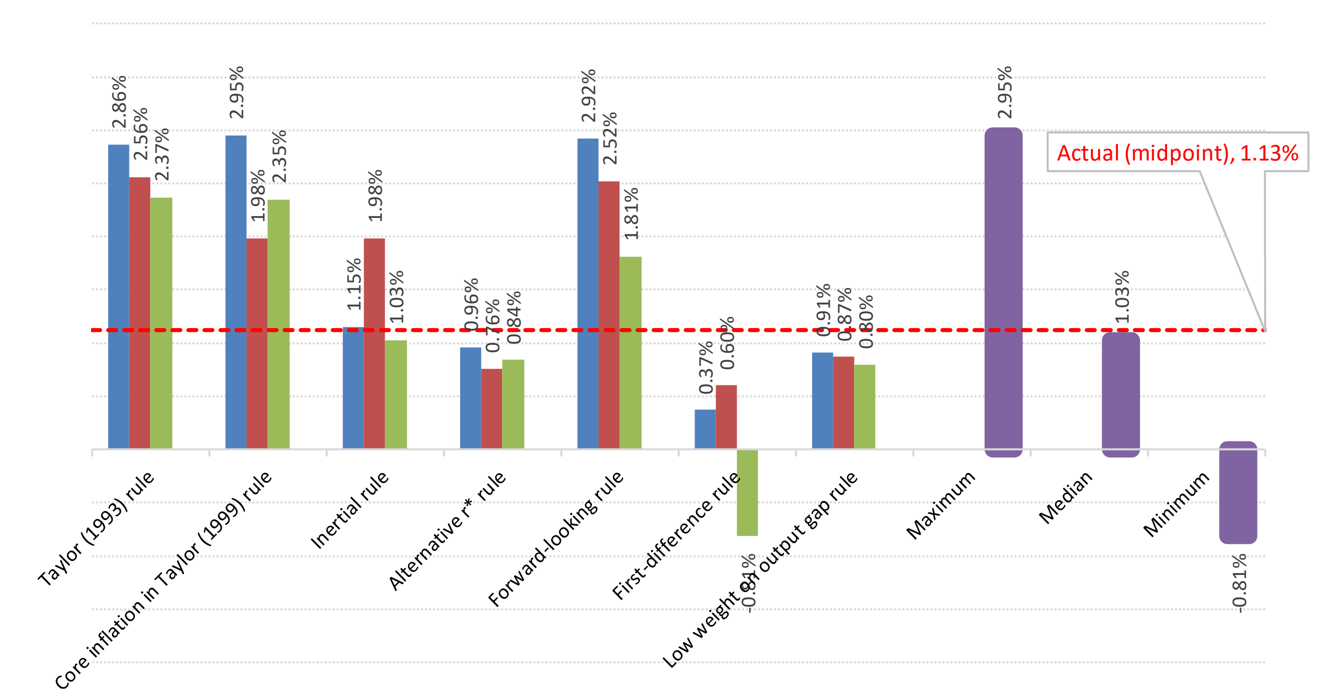


Source: BLS Current Population Survey, TrendMacro calculations

So many policy rules, so little time…

As of May 18, 2017 Based on inputs from:

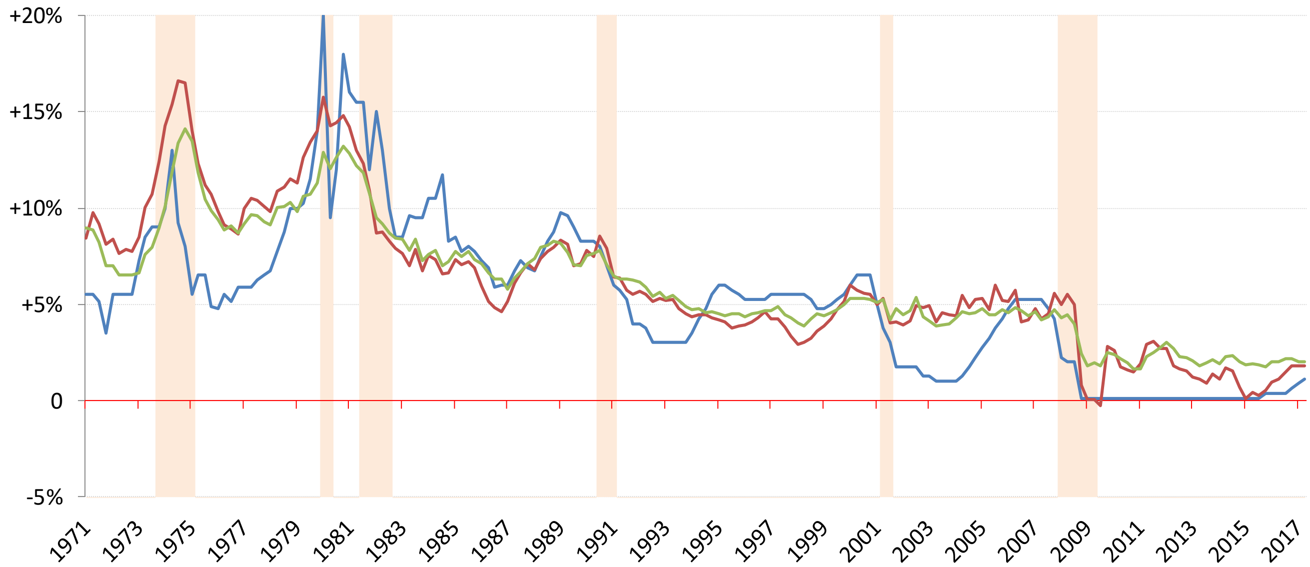
FOMC Summary of Economic Projections Congressional Budget Office Cleveland Fed



Source: Cleveland Fed, TrendMacro calculations

Estimating the “natural rate of interest”

Actual funds rate   Neutral real funds rate (headline PCE)   Neutral (core)   Recession

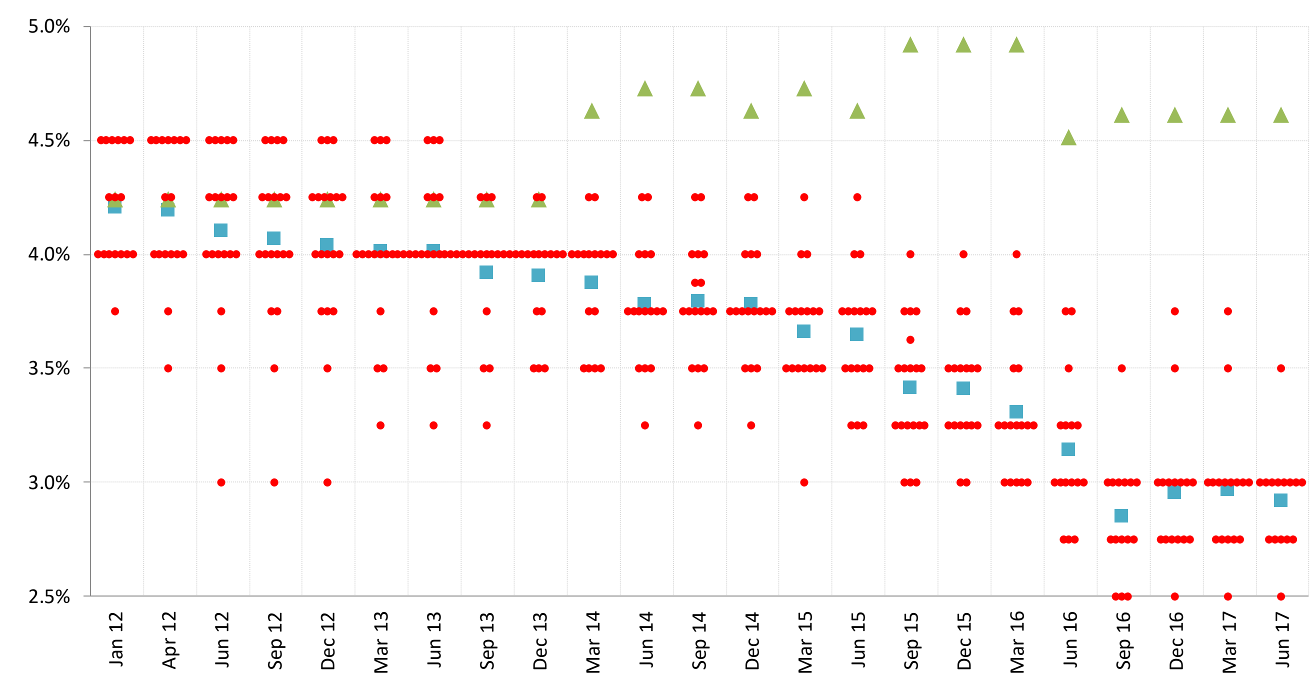


Source: [San Francisco Fed](), Federal Reserve, BEA, TrendMacro calculations

“R-star” – the ultimate ["dotplot"]()

FOMC participants' estimate of “longer run” target fed funds rate   ● Vote by individual participant

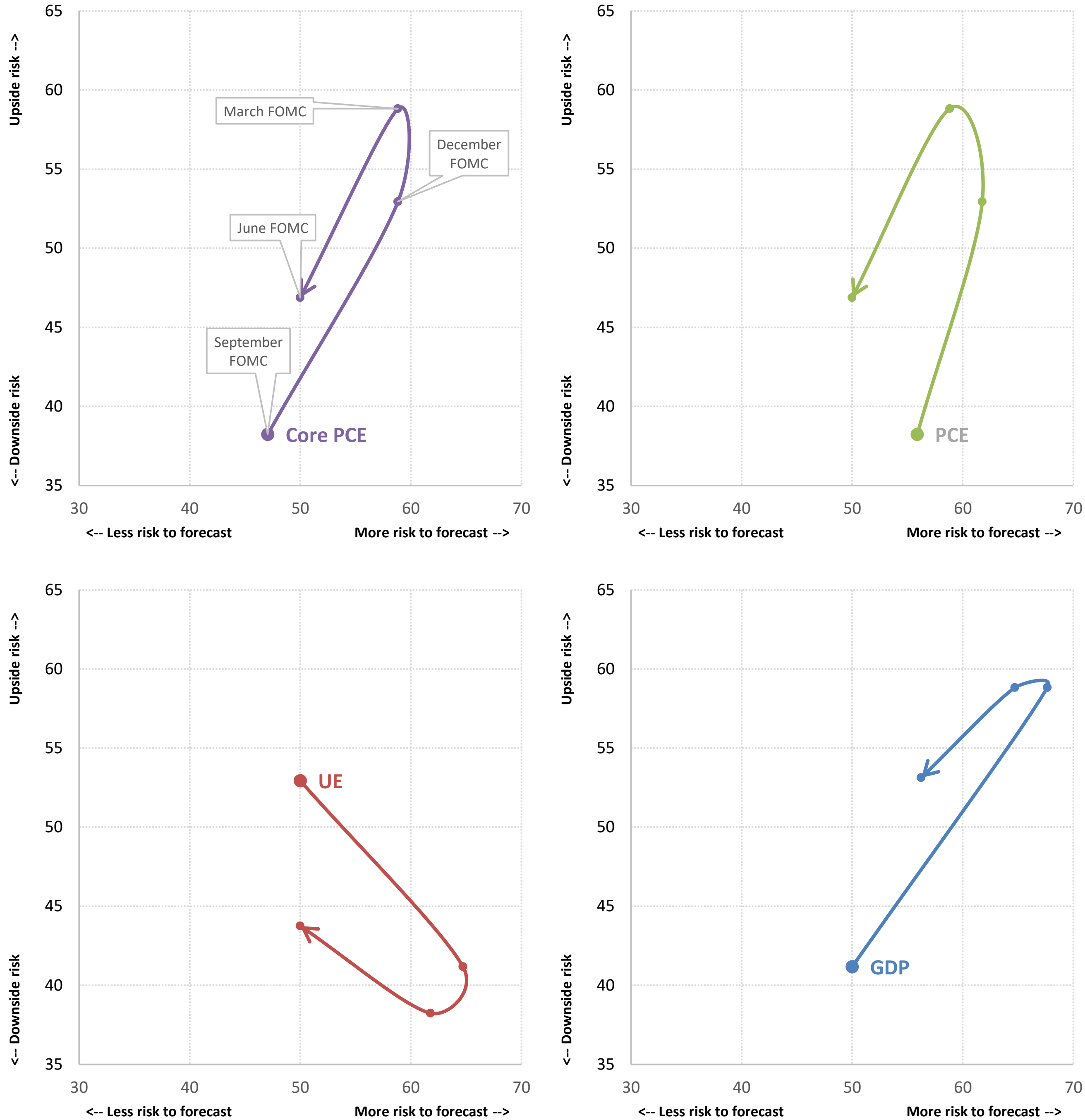
■ Weighted average   ▲ Taylor Rule rate based on participants' core PCE and UE estimates



Source: Federal Reserve, TrendMacro calculations

The evolution of uncertainty

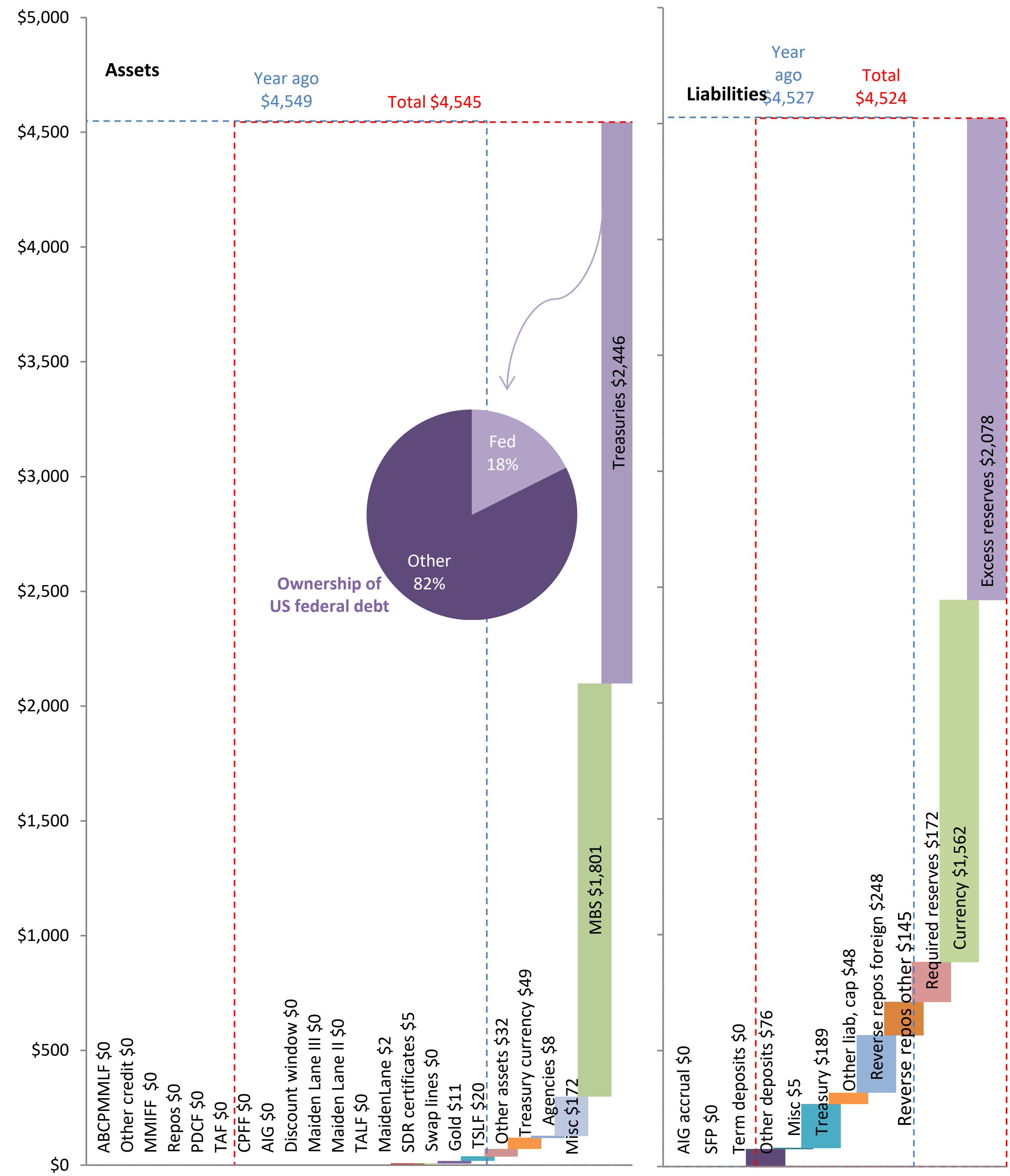
Diffusion indices from FOMC participants' risk self-assessments in Summary of Economic Projections



Source: Federal Reserve Board, TrendMacro calculations

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

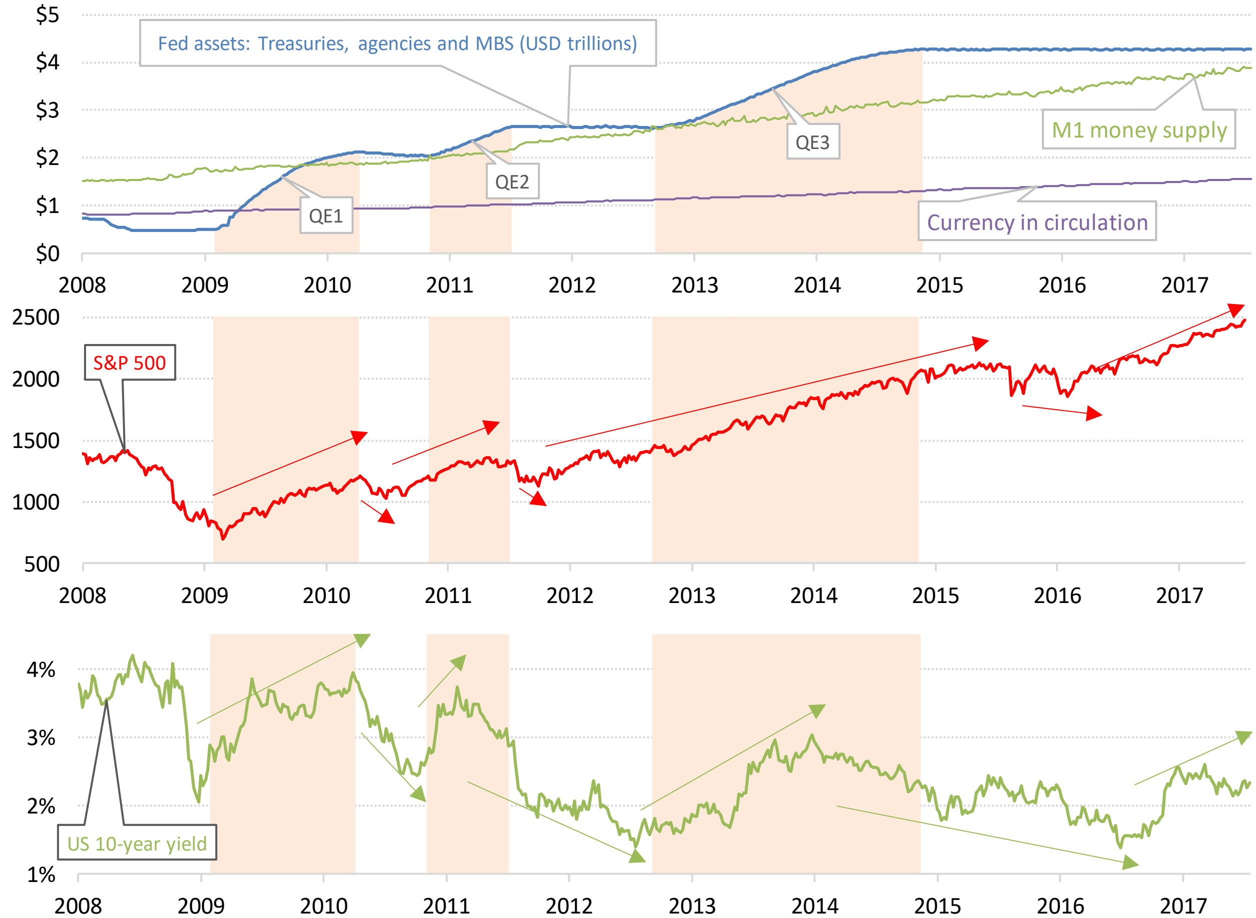
Assets do not perfectly match liabilities because we include unsettled MBS purchases and sales



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

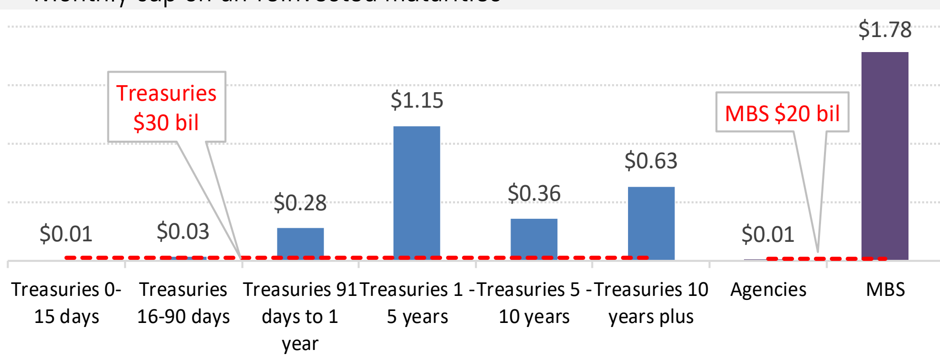
The Fed's asset purchases, and their effects on markets

Stocks and bond yields react to changes in Fed Treasury, agency and MBS holdings

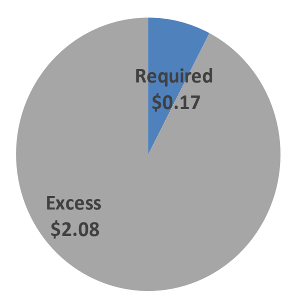


Sector and maturity breakdown of Fed assets, USD trillions

--- Monthly cap on un-reinvested maturities

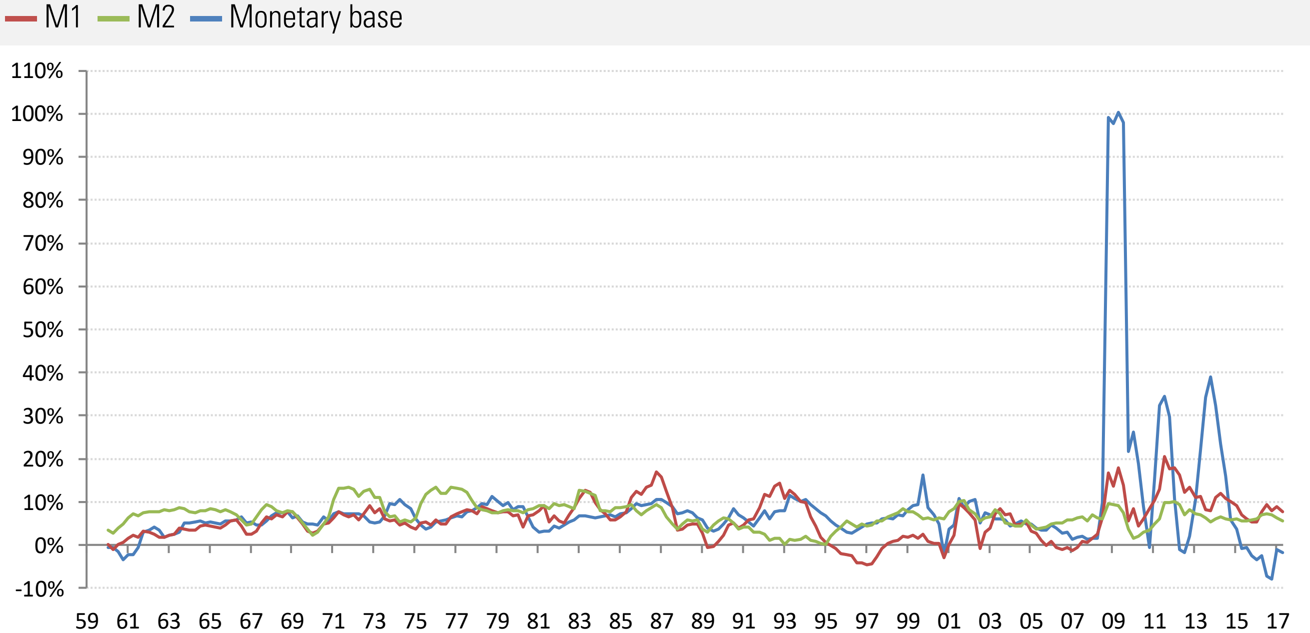


Banking reserves, USD trillions



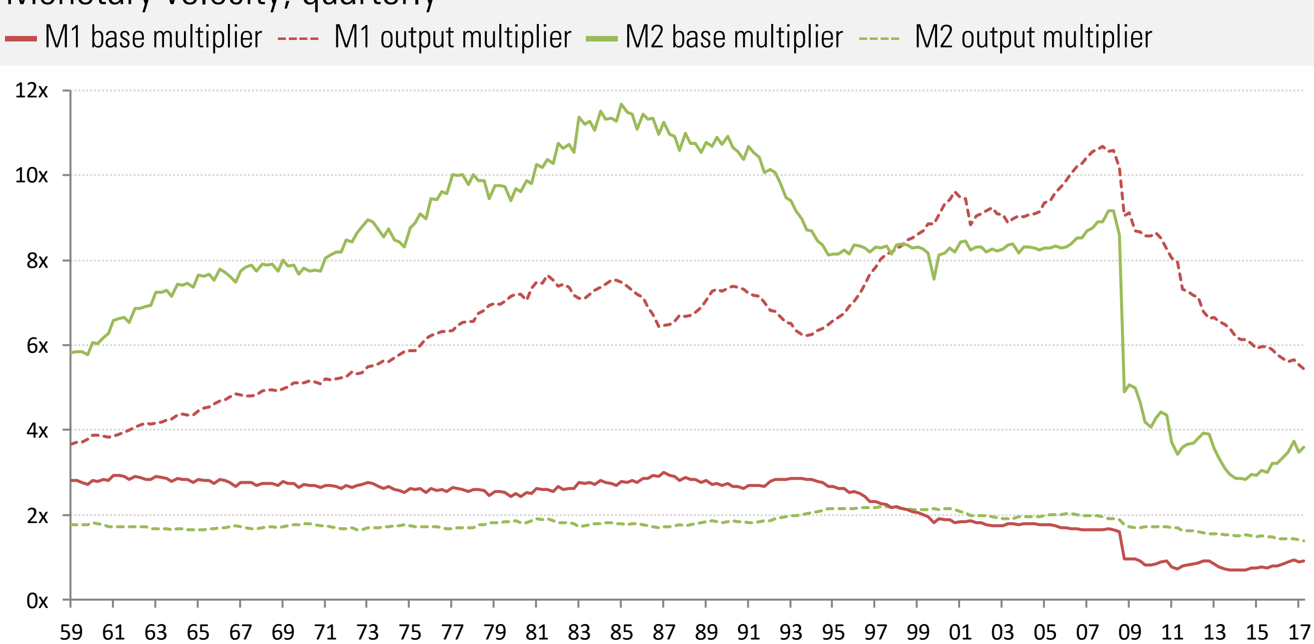
Source: Federal Reserve, Bloomberg, TrendMacro calculations

Money supply growth, YOY quarterly



Source: Federal Reserve H.6, TrendMacro calculations

Monetary velocity, quarterly



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