Take Five (with Bill Emmons)

Parsing the FOMC Statement

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Parsing the FOMC Statement

- The Fed’s Federal Open Market Committee (FOMC)
- How to read the FOMC statement

How the Fed makes monetary policy

- The Federal Open Market Committee (FOMC)
  – Creates the Fed's monetary-policy strategy and actions
  – FOMC = 7 Federal Reserve Board Governors + 5 voting Federal Reserve Bank Presidents (+ 7 non-voting Presidents)
    - St. Louis Fed president is on a 3-year rotation
  – 8 scheduled meetings per year plus occasional conference calls
    - Next meeting is June 18-19

Federal Open Market Committee
= 12 Voting Members + 7 Non-Voters

How to read the FOMC statement

- Inside the FOMC statement
  - Goal: Concise, clear update on monetary policy communicated to all interested parties at once
  - Elements:
    1) The policy statement—what the FOMC decided to do
    2) Explanation for the policy—why they are acting (or not)
    3) Summary of economic conditions—background info
    4) Balance of risks—what they are worried about
    5) How members voted and reasons for any dissents
  - The trade-off: Being concise vs. being clear

The FOMC statement of May 1, 2013

1) The policy statement—what the FOMC decided to do

"To support a stronger economic recovery and to help ensure that inflation, over time, is at the rate most consistent with its dual mandate, the Committee decided to continue purchasing additional agency mortgage-backed securities at a pace of $40 billion per month and longer-term Treasury securities at a pace of $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. Taken together, these actions should maintain downward pressure on longer-term interest rates, support mortgage markets, and help to make broader financial conditions more accommodative."

The FOMC statement of May 1, 2013

2) Explanation for the policy—why they are acting (or not)

"Information received since the Federal Open Market Committee met in March suggests that economic activity has been expanding at a moderate pace. Labor market conditions have shown some improvement in recent months, on balance, <u>but the unemployment rate remains elevated</u>. Household spending and business fixed investment advanced, and the housing sector has strengthened further, <u>but fiscal policy is restraining economic growth</u>. Inflation has been running somewhat below the Committee's longer-run objective, apart from temporary variations that largely reflect fluctuations in energy prices. <u>Longer-term inflation expectations have remained stable</u>."

The FOMC statement of May 1, 2013

3) Summary of economic conditions—background info

"Information received since the Federal Open Market Committee met in March suggests that economic activity has been expanding at a moderate pace. Labor market conditions have shown some improvement in recent months, on balance, but the unemployment rate remains elevated. Household spending and business fixed investment advanced, and the housing sector has strengthened further, but fiscal policy is restraining economic growth. Inflation has been running somewhat below the Committee's longer-run objective, apart from temporary variations that largely reflect fluctuations in energy prices. Longer-term inflation expectations have remained stable."

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4) Balance of risks—what they are worried about

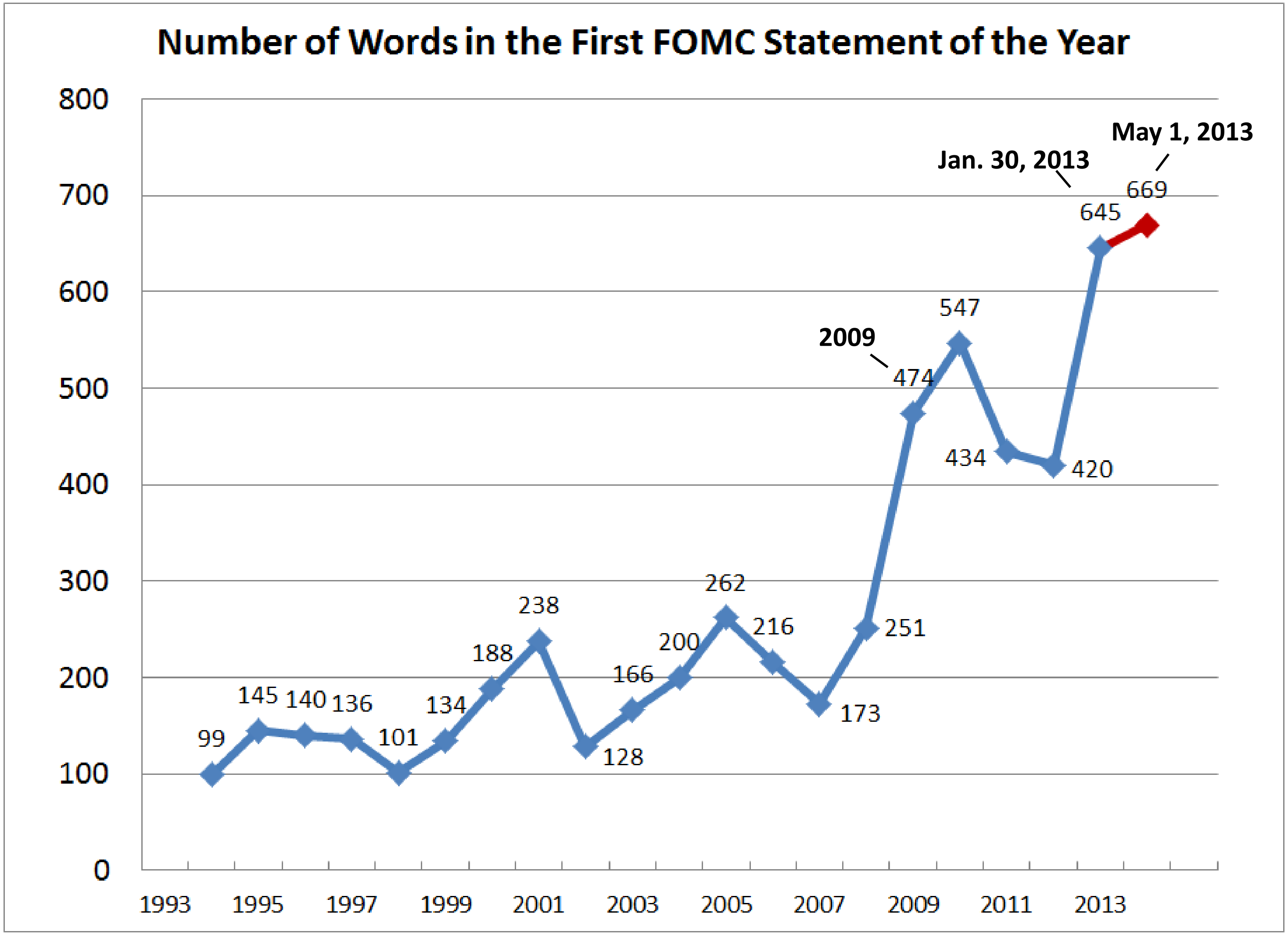
"Consistent with its statutory mandate, the Committee seeks to foster maximum employment and price stability. The Committee expects that, with appropriate policy accommodation, economic growth will proceed at a moderate pace and the unemployment rate will gradually decline toward levels the Committee judges consistent with its dual mandate. <u>The Committee continues to see downside risks to the economic outlook</u>. <u>The Committee also anticipates that inflation over the medium term likely will run at or below its 2 percent objective</u>."

The FOMC statement of May 1, 2013

5) How members voted and reasons for any dissents

"Voting for the FOMC monetary policy action were: Ben S. Bernanke, Chairman; William C. Dudley, Vice Chairman; James Bullard; Elizabeth A. Duke; Charles L. Evans; Jerome H. Powell; Sarah Bloom Raskin; Eric S. Rosengren; Jeremy C. Stein; Daniel K. Tarullo; and Janet L. Yellen. Voting against the action was Esther L. George, who was concerned that the continued high level of monetary accommodation increased the risks of future economic and financial imbalances and, over time, could cause an increase in long-term inflation expectations."

May 1 statement was very long



What to look for in the June 19 statement

- Any changes in FOMC policy actions?
- Any changes in the FOMC's description of the economy or risks to the outlook?
- Can the FOMC shift the balance back toward being concise without losing clarity?

Future Take Five Topics

- How long will interest rates remain at their current low levels?
- Quarterly economic update