OpenFed

POLICY STATEMENT | June 29, 1995

PREDICTED FED DECISION −25 bps

5.75%

OPENFED OPTIMAL RATE −25 bps

5.75%

KEY TAKEAWAY

The Committee expects a 25 basis point cut and independently judges the same 25 basis point reduction optimal, its own framework favoring incremental easing over the deeper 75 basis point cuts three reference rules recommend.

STATEMENT

Information reviewed for this meeting described an economy near equilibrium with mild cooling underway. Core PCE inflation, at 2.09 percent, sits fractionally above the 2.0 percent objective but shows no sign of accelerating; the framework's inflation momentum term, at -0.06, points if anything to easing rather than building price pressure. Unemployment at 5.7 percent stands above the 5.38 percent estimated natural rate, and with unemployment momentum at +0.2, participants read the labor market as loosening modestly rather than tightening. Initial claims near 358,000 were characterized as somewhat elevated, while the Chicago Fed activity index at 0.23 indicated growth only slightly above trend and losing momentum. Financial conditions were judged benign throughout: a stress index of 0.0954, a VIX of 11.59, and a Baa spread of 1.71 gave no hint of credit distress or systemic fear.

Against a current funds rate of 6.0 percent, most participants judged policy modestly restrictive relative to near-target inflation and a softening labor market. Several placed particular weight on money-market pricing: the 3-month bill trading roughly 50 basis points below the funds rate was read as markets already anticipating a near-term cut, and the 10y-2y spread at +0.39, positive but flat, was seen as consistent with expectations of easing rather than tightening. A couple of participants gave the labor side greater weight, arguing that restrictive policy risks employment while inflation poses no barrier, and that beginning to ease now is preferable to waiting for unemployment to rise further. One participant, weighting inflation risk most heavily, resisted this reading, observing that a 0.09 percentage point overshoot is not yet convincingly contained and that validating market pricing is not itself a reason to ease into calm, complacent conditions. On the predictive question, that reasoning did not carry the day: the Committee's considered forecast is that the real Federal Reserve will reduce the target rate by 25 basis points.

Turning to its own determination of optimal policy, the Committee's deterministic framework likewise recommends a 25 basis point reduction, and here the internal tension is worth stating plainly. Three of the four reference rules, the Taylor rule, the balanced-approach rule, and the ELB-adjusted rule, each called for a much deeper -75 basis point move, reflecting how restrictive current policy looks against an r* estimate of 2.305 and a widening employment gap. The first-difference rule, by contrast, recommended -25 basis points, and it was this rule that the loss-minimizing recommendation matched. Participants found the first-difference logic more persuasive precisely because it adjusts incrementally from current conditions rather than resetting to level estimates like r* that carry real uncertainty. With inflation momentum slightly negative, unemployment momentum only modestly positive, and no crisis signal in stress, volatility, or credit spreads, participants judged that a -75 basis point cut would be an abrupt shock, signaling alarm where none exists, whereas a 25 basis point step eases gently and preserves optionality.

The gap between the -75 basis point rules and the -25 basis point outcome was itself read as informative: it quantifies how much restriction remains in the stance and suggests that further easing may follow if labor data continue to soften. For now, participants generally concluded that a measured 25 basis point reduction is the appropriate insurance, enough to acknowledge labor-market loosening and on-target inflation, gentle enough to protect orderly financial conditions, and aligned with the easing markets have already priced.

COMMITTEE VOTE

The predictive vote was 4-1 in favor of a 25 basis point cut, with one member forecasting no change. On the framework's -25 basis point optimal recommendation, the Committee endorsed it unanimously, 5-0.

NOTES

On the predictive side, one participant forecast no change, judging that cutting while core PCE remains above the 2.0 percent target is premature, that market pricing of a cut does not justify validating it, and that extremely low stress and volatility remove any urgency to act rather than supplying a reason to ease. By Round 4 this member nonetheless endorsed the optimal -25 basis point call, satisfied that negative inflation momentum and its incremental, first-difference character respected inflation caution against a larger move.