OpenFed

POLICY STATEMENT | November 10, 1998

PREDICTED FED DECISION −25 bps

4.75%

OPENFED OPTIMAL RATE −25 bps

4.75%

KEY TAKEAWAY

The Committee expects the real Federal Reserve to cut by 25 bps, and its own deterministic framework independently arrives at the same optimal -25 bps, with all five members endorsing that recommendation.

STATEMENT

What is striking about this meeting is the completeness of the agreement it produced. Beginning from five distinct analytical vantage points, participants converged on the same reading of an economy where inflation poses no near-term threat while financial and momentum signals lean toward accommodation. Core PCE stands at 1.24%, well below the 2.0% objective, and the qualitative evidence points the same way: subdued wage pressure, producer prices flat to down, and retail prices little changed. Against that backdrop, participants generally judged that there was no inflation constraint blocking a modest easing. Labor markets remain firm, with unemployment at 4.6% still beneath the 5.16% natural rate, but participants noted early signs of softening in manufacturing labor demand, alongside elevated market volatility, with the VIX at 28.17, and credit-cost stress reflected in a Baa spread of 2.54 and widespread tightening of lending standards. The 3-month Treasury bill trading 0.57 below the current 5.0% funds rate was read as markets having already priced roughly one 25 bps cut.

On that basis the Committee's predictive judgment is that the real Federal Reserve will lower the target rate by 25 bps. Participants characterized this as insurance easing: enough to lean against accumulating downside risks from tightening credit and softening momentum, but restrained enough to respect a still-tight labor market and near-trend activity, with the CFNAI at 0.05 and initial claims at 316,000 giving no signal of collapse. Several members emphasized that a larger move risked appearing panicked or destabilizing, without a labor deterioration severe enough to justify it, and that going beyond what markets had priced could itself unsettle financial conditions.

The Committee's independent policy framework arrived at the same destination, and the reasoning behind it merits equal weight. The reference rules divided sharply: the Taylor rule, the balanced-approach rule, and the ELB-adjusted rule each prescribed +75 bps, driven almost entirely by the tight labor market read against an r* of 3.305, while the first-difference rule, which responds to changing conditions rather than static gaps, prescribed -50 bps. The loss-minimizing recommendation of -25 bps splits that difference. Participants found the level rules unpersuasive here precisely because they lean on a low jobless rate rather than realized inflation, and inflation momentum of -0.09 signals ongoing disinflation, not building pressure. At the same time, participants resisted the full -50 bps of the first-difference rule, reasoning that activity indicators remain near trend and the softening is a risk rather than a realized deterioration. The gap between the +75 bps of the level rules and the -25 bps recommendation reflects how heavily financial stress and negative momentum discount the strong static readings.

Taken together, the Committee judged that the current 5.0% stance is modestly restrictive relative to where conditions are heading, with the real rate near 5% against an r* of roughly 3.3% leaving room to ease. A 25 bps cut was seen as the disciplined, market-consistent, and loss-minimizing response: it relieves credit-driven fragility and validates the market's easing expectation while inflation, well below target, supplies the room to do so without recklessness.

COMMITTEE VOTE

The predictive vote was unanimous at 5-0 for a 25 bps cut, and on the optimal side all five members endorsed the framework's -25 bps recommendation as-is, with none declining and none dissenting on magnitude.