OpenFed

POLICY STATEMENT | January 24, 2001

PREDICTED FED DECISION −50 bps

5.50%

OPENFED OPTIMAL RATE −25 bps

5.75%

KEY TAKEAWAY

The Committee unanimously expects the real Federal Reserve to cut 50 basis points, but its own framework judges the optimal move to be a more measured 25 basis point cut off a restrictive 6.0% stance.

STATEMENT

Information reviewed for this meeting pointed to a broad, fairly rapid deceleration in activity alongside inflation running well under target. Core PCE stood at 1.38%, comfortably below the 2.0% objective, and the Beige Book corroborated limited price pressures: manufactured goods flat to down, holiday discounting constraining consumer prices, and wage pressures described as similar to or slightly less intense than in the prior survey. Against that, the growth signals were uniformly softer. The Chicago Fed National Activity Index at -0.66 indicated below-trend growth, all districts reported weaker manufacturing, retail was disappointing, and Philadelphia was in outright decline. Labor conditions were the one genuinely two-sided element: unemployment at 4.0% remained low and the labor market still read as tight, but initial claims at 343,000 and layoff announcements across most districts pointed to easing momentum. Financial stress was moderate rather than acute, with the VIX near 22, the Baa spread at 2.61, and a stress index of 0.2427, while the 3-month T-bill sitting 0.86 below the funds rate signaled that markets already expected substantial easing.

On the predictive question, participants converged quickly and without dissent on a 50 basis point cut as the most likely action by the real Federal Reserve. Members weighting market signals most heavily read the -0.86 T-bill gap as consistent with an expectation of roughly 50 basis points or more, and judged that a quarter-point move would underdeliver relative to that pricing and risk a disorderly repricing. Members focused on employment emphasized that the direction of travel in claims and layoffs mattered more than the still-low level of unemployment, and favored front-loading support. Even the participant most attentive to inflation risk found that his usual caution simply did not bind, given inflation notably below target and no wage-driven threat, and moved from an earlier 25-to-50 lean to the full 50. Some consideration was given to whether a still larger move was warranted, but the positive 10-2 spread of +0.52 and only moderate credit stress argued against a jumbo cut. The predictive vote was unanimous.

The Committee's own deterministic framework arrived at a more restrained answer: an optimal cut of 25 basis points. The reference rules were notably dispersed. The Taylor rule read 0 basis points, with inflation below target offsetting a labor market still tight relative to a 5.09% natural rate; the balanced-approach and ELB-adjusted rules both pointed the other way at +75 basis points, driven by the wide unemployment gap. Participants generally judged those level-based rules to be leaning on stale slack, ignoring the visible turn in activity, and gave most weight to the first-difference rule at -25 basis points, which responds to the change in conditions rather than the level. That rule aligned with the modest momentum terms the framework used—inflation momentum of just 0.12 and unemployment momentum of -0.05—and with an r* of 3.886 that leaves 6.0% meaningfully restrictive. The loss-minimizer landed at -25 basis points as well, and participants read this as the disciplined first step: easing decisively in direction while not overreacting to a slowdown that, though broad, had not become a financial rupture.

The gap between the predicted 50 basis points and the optimal 25 basis points is the real story of this meeting, and members were candid about its source. Those who endorsed the framework's call argued that with inflation contained and no crisis in the data, a measured quarter-point normalizes an overly restrictive stance without signaling panic. Those who agreed with the direction but not the magnitude located the difference in their heavier weight on preemption—protecting employment or credit conditions before deterioration deepens, and honoring a market curve they viewed as demanding faster action than backward-looking momentum coefficients capture. In the Committee's view, the -50 prediction reflects a real Federal Reserve likely to front-run recession fear, while its own optimal judgment holds that the deteriorating momentum warrants easing off 6.0%, but at a pace the current data supports.

COMMITTEE VOTE

The predictive vote was unanimous at 5-0 for a 50 basis point cut. On the framework's optimal recommendation of a 25 basis point cut, the Committee split 3-2: three members endorsed it as-is, and two agreed with the direction but not the magnitude, with none declining.

NOTES

Though the predictive vote was unanimous, the optimal-side deliberation drew two partial dissents. The labor-focused member agreed a cut was warranted but judged 25 basis points too cautious given rising claims and weak manufacturing, preferring to front-load easing to protect jobs before a turning labor market outpaced policy; the market-focused member similarly held that the -0.86 T-bill spread implied more than one small step, viewing the framework's -25 as directionally right but too timid relative to what the curve was pricing.