OpenFed

POLICY STATEMENT | October 30, 2001

PREDICTED FED DECISION −50 bps
2.00%

OPENFED OPTIMAL RATE −25 bps
2.25%

KEY TAKEAWAY

The Committee unanimously expects the real Fed to cut 50 bps in response to the post-September-11 shock, while its own framework judges a more measured 25 bps optimal — a divergence of magnitude, not direction.

STATEMENT

The data reviewed at this meeting pointed in a single direction. Core PCE inflation stood at 1.23%, well beneath the 2.0% objective, and the Beige Book reported little upward pressure on wages or prices across Districts, with some prices falling outright. Against that backdrop the September 11 shock had left activity visibly weakened: initial jobless claims of 483,000, the Chicago Fed National Activity Index at -0.18, and Beige Book accounts of layoffs and plant closings across many industries. Financial conditions remained fragile, with the VIX at 33.46 and the Baa credit spread at 3.35, and the 3-month T-bill trading roughly 49 basis points below the current 2.5% funds rate. Members approaching the question from every vantage point — inflation risk, the employment mandate, credit-market stability, data-dependence, and market pricing — arrived independently at the same read. With inflation running soft and disinflation, not inflation, the operative concern, no member found a principled reason to resist easing. The Committee's judgment as to what the Federal Reserve will do is a cut of 50 basis points.

Its own assessment of what policy should be, produced through the deterministic framework, was more restrained. The reference rules diverged sharply: the Taylor rule pointed to +75 basis points, resting on an estimated r* of 3.834 that several members judged implausible for a shocked economy; the balanced-approach and ELB-adjusted rules each called for +25; and the first-difference rule, keyed to momentum rather than levels, pointed to -50. With inflation momentum negative at -0.125 and unemployment momentum positive at 0.25, the framework's loss-minimizing balance landed at -25 basis points — a middle path that eases against clear disinflation and softening activity while respecting that unemployment at 4.9% remains below the 5.07% natural rate and that policy room from an already-low 2.5% is finite. The Committee's independent conclusion is that a 25-basis-point reduction is the optimal move.

The gap between the two figures is the substance of this meeting. Several members, weighting the labor and credit signals as urgent, read the 483,000 claims figure and the market-implied path as calling for insurance now rather than after unemployment rises, and noted that delivering less than the roughly full cut markets have priced could itself tighten conditions at a fragile moment. Others emphasized that the level rules and the still-below-natural-rate unemployment counsel a disciplined pace, and that conserving accommodation guards against a costlier stress spiral later. Both readings agree entirely on direction; they part only on magnitude. The framework's -25 reflects the more measured, rule-anchored balance, while the predictive -50 reflects the Committee's expectation that the Federal Reserve will front-load its response to the demand shock.

COMMITTEE VOTE	The predictive vote was unanimous, 5-0, for a 50-basis-point cut. On the framework's optimal recommendation of -25 basis points, the Committee split 2-3: two members endorsed it as-is, while three agreed with the direction but preferred a larger move (recorded as partial), with none declining.
NOTES	*The three partial members — reasoning from the employment, financial-stability, and market-pricing perspectives — held that -25 basis points, while correct in direction, was insufficient: with claims at 483,000 and the T-bill spread pricing a near-full 50-basis-point cut, they judged that under-delivering risked a hawkish surprise and inadequate support for a cracking labor market and stressed credit, preferring the deeper -50 consistent with the first-difference rule.*