OpenFed

POLICY STATEMENT | June 18, 2003

PREDICTED FED DECISION −25 bps

1.00%

OPENFED OPTIMAL RATE −50 bps

0.75%

KEY TAKEAWAY

The Committee unanimously expects a 25 bps cut, while its own policy framework judges the loss-minimizing move to be a deeper 50 bps cut driven by disinflation and labor-market slack.

STATEMENT

Information reviewed at this meeting pointed consistently in one direction: conditions are soft, but not in crisis. Core PCE inflation stood at 1.07%, nearly a full percentage point below the 2.0% objective and, by the framework's momentum reading, still decelerating (inflation momentum of -0.105). Unemployment at 6.1% sat well above the 5.05% estimate of its natural rate, initial claims remained elevated at 421,000, and the Beige Book reported sluggish, subdued growth with soft consumer spending and downward wage pressure across most Districts. Against this, financial conditions looked calm rather than distressed: the stress index registered a low 0.0876, the VIX was moderate at 19.76, the Baa spread was contained at 2.83, and the 2-to-10 curve remained steeply positive at 2.1. Participants also gave weight to the 3-month bill trading 0.38 below the current 1.25% funds rate, a market signal that some easing was already anticipated.

From these facts participants built a common case for easing. The inflation-focused view acknowledged that heavy attention to price risk cuts both ways here, and that the salient danger today is entrenched disinflation rather than overheating; the employment-focused view stressed that slack of more than a full point, with claims still elevated, argued for support now while inflation gave ample room; and the stability-focused view framed falling prices themselves as the real risk, since they raise real debt burdens even at a fixed nominal rate. The tension in the room was one of magnitude, not direction. The market-attentive reading observed that a -0.38 bill spread sits technically closer to a 50 bps move than a clean 25, which gave several participants pause. But with no acute stress, a normal yield curve, and policy room already scarce at 1.25%, participants generally judged that an outsized move risked exhausting ammunition and could itself signal alarm. On that reasoning, all five members converged on a predicted policy action of a 25 bps cut.

The Committee's own deterministic framework reached a different, more forceful conclusion, recommending a 50 bps cut as the loss-minimizing move. The reference rules disagreed sharply among themselves: with an r* of 2.787 and inflation near 1%, the Taylor rule prescribed +75 bps, while both the balanced-approach and ELB-adjusted rules returned 0, reflecting proximity to the effective lower bound. The first-difference rule, responding to the direction of change rather than a level estimate, returned -50 bps. In the framework's deliberation, participants across stances found the first-difference logic the most persuasive of the four, precisely because both momentum terms were negative (inflation at -0.105, unemployment at -0.1). On that reading the current stance is too tight: the Taylor rule's high neutral-rate abstraction understates the disinflation trajectory and the persistent labor gap, and holding while prices drift lower lets real conditions tighten.

Where the two conclusions part is on whether calm markets justify hoarding scarce policy room or front-loading against a worsening drift. Participants who prefer the measured step read the -0.38 bill spread as pricing partial, not full, easing, and read low stress as reason not to overshoot near the lower bound. The employment-focused view came the other way, judging that the cost of easing is lowest exactly when inflation is quiescent and that momentum shows the labor gap still widening without decisive action. Both the 25 bps predicted action and the 50 bps optimal recommendation emerge from the same body of evidence; the gap between them is the Committee's honest measure of how much weight to place on contained financial conditions against momentum-driven urgency.

The Committee's predicted policy action is a 25 bps cut; its framework's loss-minimizing recommendation is a 50 bps cut.

COMMITTEE VOTE

The predictive vote was unanimous at 5-0 for a 25 bps cut. On the framework's 50 bps recommendation, the Committee split 4-1 in the partial-versus-endorse sense: one member endorsed the deeper cut outright, and the other four agreed with the direction of easing but not its full magnitude.

NOTES

The single voice for the framework's full 50 bps, arguing from labor-market slack, held that unemployment more than a point above its natural rate with still-negative momentum means the current 1.25% stance is decisively too restrictive, and that front-loading support when inflation is quiescent carries the lowest cost; the four partial-agreement members countered that a -0.38 bill spread prices only partial easing and that scarce room near the lower bound argues against overshooting absent acute stress.