OpenFed

POLICY STATEMENT | September 11, 2013

PREDICTED FED DECISION HOLD
0.00%-0.25%

OPENFED OPTIMAL RATE HOLD
0.00%-0.25%

KEY TAKEAWAY

The Committee expects the real Federal Reserve to hold at 0.0% to 0.25%, and its own framework independently arrives at the same 0 bps conclusion, overriding the level rules' 75 bps signal on account of a deeply negative neutral rate.

STATEMENT

The unusual feature of this meeting is not disagreement but the width of the gap between what several mechanical rules prescribe and what the data actually support. Core PCE inflation is running at 1.07%, nearly a full point below the 2.0% target, and by every account the pressure is softening rather than building. The Beige Book reported steady input and output prices, with contacts neither complaining of higher costs nor raising their own prices significantly, and no evidence of wage-price acceleration. Unemployment, at 7.3%, remains well above the 5.5% natural rate and above the 6.5% threshold cited in prior guidance, so no hike is triggered on the labor side. With the federal funds target range already at the effective lower bound of 0.0% to 0.25%, a conventional cut is not feasible in any case. Participants therefore concluded, without dissent, that the real Federal Reserve is most likely to leave the target range unchanged, and the Committee's own predictive judgment is a hold of 0 bps.

On the question of what policy would be optimal, the Committee's framework returned a recommendation of 0 bps as well, but the reasoning is worth setting out because the reference rules pulled sharply in the other direction. The Taylor rule, the balanced-approach rule, and the ELB-adjusted rule each prescribed 75 bps, driven largely by the size of the unemployment gap. Participants judged these prescriptions misleading in the present setting. The estimated neutral real rate, r*, is -0.5, meaning the level rules were mechanically closing a gap toward a neutral rate that does not exist; at that r*, a 75 bps move would be genuinely restrictive rather than a modest normalization. The first-difference rule, which responds to changes in conditions rather than absolute level gaps, instead read 0 bps, and members found its logic the most persuasive: inflation momentum is negative at -0.075, indicating the undershoot is worsening, while unemployment momentum is flat at 0.0, offering no fresh acceleration in labor improvement to justify pulling tightening forward. The framework's loss-minimizing output of 0 bps reflects that combination, and the Committee adopted it as its optimal determination.

In supporting reasoning across lenses, participants reinforced why the divergence between the 75 bps rules and the 0 bps conclusion should be read as a real but not-yet-actionable accommodation gap rather than a policy error. Those weighing employment risk emphasized that hiring 'remains subdued' outside fast-growing technology firms, that the Chicago Fed activity index at -0.15 points to below-trend growth, and that anticipated sequestration effects represent a downside employment risk still to be realized. Those focused on financial conditions noted that the setting is calm rather than strained: the financial stress index at 0.075, the VIX at 13.82, and the Baa spread at 2.61 all indicate functioning credit markets with no systemic strain, and the 10-year to 2-year spread of 2.46 shows no recession signal from the term structure. That same group cautioned, however, that the Beige Book's observation of higher rates already 'nudging' housing buyers and pressuring commercial capitalization rates signals real rate-sensitivity, so an abrupt 75 bps move would risk destabilizing conditions that are currently orderly. Members attentive to market pricing added that the 3-month T-bill spread of -0.105 sits just below the current range, consistent with markets pricing continuity rather than any near-term move.

The prior dissent's concern about accommodation-driven imbalances was flagged and taken seriously, particularly by those most attentive to inflation risk, but participants judged that the low stress readings and contained spreads show such imbalances have not yet materialized in a way that would force a deviation. On balance, both of the Committee's conclusions rest on the same reading of the data: with inflation below target and falling, substantial labor slack, and a deeply negative neutral rate, holding the target range at 0.0% to 0.25% is both the most probable action of the real Federal Reserve and the Committee's own assessment of optimal policy this meeting.

COMMITTEE VOTE

The predictive vote was unanimous, 5-0, for a hold at 0.0% to 0.25%. On the framework's 0 bps recommendation, the Committee's optimal-side deliberation also landed in full agreement, with all five members endorsing the recommendation as-is.