OpenFed

POLICY STATEMENT | October 23, 2013

PREDICTED FED DECISION HOLD

0.00%-0.25%

OPENFED OPTIMAL RATE HOLD

0.00%-0.25%

KEY TAKEAWAY

The Committee unanimously expects the real Federal Reserve to hold the target range at 0.0% to 0.25%, and its own framework independently arrives at the same 0 bps as loss-minimizing, despite three reference rules prescribing 75 bps.

STATEMENT

The decisive fact this meeting is that inflation is running well below the Committee's objective. Core PCE stands at 0.97%, roughly half the 2% target, and members across every analytical lens treated that reading as removing any case for tightening. Even the participant most attentive to inflation risk observed that the danger here is undershooting rather than overshooting the objective; with price pressures this subdued, a hike would only push inflation further from target. On the other side of the mandate, unemployment at 7.2% remains far above the 5.5% natural rate, a gap of roughly 1.7 points, and elevated initial claims at 358,000 suggested to several members that the labor market is not yet healing decisively. Both legs of the mandate therefore pointed in the same direction: too little inflation to justify restraint, too much slack to justify withdrawing accommodation. Prior guidance ties continued accommodation to unemployment above 6.5%, a condition that still holds firmly.

With the target range already pinned at 0.0% to 0.25%, participants generally judged that a conventional cut is not realistically available, and nothing in the data argued for extraordinary action to push below the floor. Financial conditions were described as calm and accommodative throughout: the financial stress index at 0.051 is very low, the VIX at 13.42 is subdued, the Baa credit spread at 2.67 is moderate with no sign of distress, and the 10-year to 2-year spread at +2.2 is steeply positive with no inversion or recession warning. Market-based signals reinforced the same read, with the 3-month T-bill spread at -0.085 indicating that markets price no near-term move. The one flag members carried forward from the prior meeting was rising mortgage rates as a potential source of restraint; that was treated as a reason for caution against a premature jolt to housing and credit, not as grounds for action now. On this basis the Committee's predictive judgment is that the real Federal Reserve will hold the target range unchanged at 0.0% to 0.25%.

The Committee's own deterministic framework arrived independently at the same conclusion, and the more interesting part of that exercise is how it did so against a set of reference rules that mostly pointed the other way. The Taylor rule, the balanced-approach rule, and the ELB-adjusted rule all read 75 bps, each driven largely by the size of the unemployment gap rather than by any inflation pressure. What reconciles those prescriptions with a hold is the estimate of the neutral rate: r* is put at -0.5, deeply negative, meaning the level-based rules overstate how tight policy ought to be. With a negative neutral rate, holding at the current range is closer to neutral than those 75 bps prescriptions imply. Members found the first-difference rule, which reads 0 bps, the more persuasive guide under these conditions, because it responds to momentum rather than to an absolute gap against a possibly mismeasured neutral rate. Inflation momentum of 0.15 and unemployment momentum of -0.15 describe an economy improving slowly, with no impetus to move in either direction. Taking the reference rules as reliable but recognizing that the level-based ones describe an unconstrained world, the framework's loss-minimizing recommendation is +0 bps.

The Committee therefore reached both of its conclusions through the same argument rather than two separate ones: the low inflation reading, the wide labor slack, the negative neutral rate, and the effective floor together explain why the real Federal Reserve is expected to hold and why holding is also the optimal policy. Members took care to note what the agreement does and does not say. It does not endorse indefinite accommodation regardless of the data; the concern raised previously about imbalances from prolonged accommodation was acknowledged, but treated as a tail risk about the future rather than a claim supported by present readings of 0.97% core PCE, benign credit spreads, and calm markets. The Committee's conclusion is to maintain the target range at 0.0% to 0.25% and to watch for inflation firming toward target and further labor improvement before contemplating any change.

COMMITTEE VOTE

The predictive vote was unanimous, 5-0, in favor of 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 voting to endorse.