Wind the Clock

The Federal Reserve resets its criteria for altering monetary policy

By Jim Reber

The last two years may go down amongst Fed watchers as the period in which the calendar was introduced into policy making. As 2013 gets going, it still appears that the Federal Open Market Committee is finessing the words of its interest rate policy statements to accurately convey its thoughts. Could it be that the voting members of the most important committee of the most important central bank in the world has changed its standards for taking action?

With the Great Recession setting into the horizon, it’s interesting to note how the Fed has continued to pour on the coals to ensure that we don’t slip back into negative growth. It has employed a multi-pronged approach, utilizing both clear words (via its comments at the conclusions of the regular meetings) and strong actions (to wit: $2 trillion of quantitative easing, and counting).

But back to the wording: The Fed meets eight times per year, and each time it releases a statement regarding its just-reached conclusions about the economy’s direction and its target fed funds interest rate. The parts that interest Fed watchers most greatly are ones that contain clues as to a shift in policy, including any timing considerations. These can in fact be market-moving announcements. What’s unique about the past two years’ announcements is that they contain an on-the-fly series of adjustments regarding actual dates that the Fed had in mind. Then the Dec. 12, 2012, meeting changed all that—again.

As done before
Up until 2011, any timing suggestions fell into the obtuse category. For example, the last time the Fed actually dropped its fed funds target was Dec. 16, 2008. The statement that accompanied the action included the suggestion that “conditions are likely to warrant exceptionally low levels … for some time.” Still, the market was appreciative, and the two-year Treasury note fell in yield 9 basis points that day, which is a substantial move.

Ninety days and two meetings later, the Fed added the seemingly innocuous suffix “for an extended period” to the end of its statement, and again rates plummeted, with the two-year Treasury shaving off 22 basis points. One can see that notation and implication has a big impact on even the most liquid of markets.

In August 2011 came the first-ever, date-pegged rate change forecast. The Fed’s statement that day defined “at least through mid-2013” before it anticipated any change to fed funds. Rates once again dropped, as the FOMC appeared to be telling short- and intermediate-term investors they would be free of rate risk for a couple of years.

How, many wondered, will they talk their way out of this if something goes amiss? It’s clear the Fed doesn’t scare easily. Either that or it has continued to miss its own growth targets. Since the “mid-2013” disclosure, it has been extended twice, to “late 2014” and “mid-2015.”

This time around
In December 2012 the FOMC had yet another revision. This one removed...
Alan approved a loan that created a business — a business that created 18 new jobs in his community and became the newest supporter of the local youth baseball program. CNA tailors insurance coverages focused on the needs of financial institutions, so bankers like Alan can focus on what makes their businesses and their communities stronger. Way to swing for the fences, Alan.

At CNA, we salute the memorable instants that lead to memorable milestones.

www.cna.com/communitybanks