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Data Insights: FOMC Minutes

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September minutes: key signaling language Featured Important Very important

… The release of the revised Statement on Longer-Run Goals and Monetary Policy Strategy (consensus statement) elicited relatively modest immediate reaction across markets. However, market participants generally viewed the completion of the review as an important milestone; many indicated that growing expectations for the Committee to adopt a flexible average-inflation-targeting regime had influenced asset prices over recent months. In particular, these expectations were viewed as contributing to the recent rise in far-forward measures of inflation compensation, though market participants noted that these measures were still somewhat low by historical standards.

Market participants continued to anticipate that the Committee would update its forward guidance for the federal funds rate. Most respondents to the Desk's surveys continued to indicate that they expected the FOMC to adopt outcome-based forward guidance linked to inflation; some noted that employment measures could be part of the forward guidance as well…

Participants observed that the incoming data indicated that economic activity was recovering faster than expected from its depressed second-quarter level, when much of the economy was shut down to stem the spread of the virus. In particular, with the reopening of many businesses and fewer people withdrawing from social interactions, consumer spending was rebounding sharply and appeared to have recovered about three-fourths of its earlier decline. Prior fiscal policy actions were seen as having supported the ability and willingness of households to spend, although most participants expressed concern about the expiration of the enhanced unemployment insurance benefits from the CARES Act (Coronavirus Aid, Relief, and Economic Security Act) and judged that additional fiscal relief would help sustain the recovery in household spending. Indeed, many participants noted that their economic outlook assumed additional fiscal support and that if future fiscal support was significantly smaller or arrived significantly later than they expected, the pace of the recovery could be slower than anticipated. Participants also viewed accommodative monetary policy as contributing to gains in residential investment as well as consumer purchases of motor vehicles and other durable goods. While participants pointed to strength in consumers' purchases of goods, especially those sold online, they noted that outlays for services had been slower to recover, particularly for items such as air travel, hotel accommodations, and restaurant meals, which had been significantly disrupted by social-distancing measures. Participants generally expected spending on these services to remain subdued for some time and thus to be a restraining factor on the pace of the recovery. A few participants raised the possibility that the unwinding of the large pool of household savings accumulated during the pandemic could provide greater-than-anticipated momentum to consumption going forward. However, a couple of other participants judged that if this savings reflected reduced spending on in-person services by high-income consumers, it was unlikely to provide much momentum to future consumption.

…Although business contacts indicated that overall business activity had been stronger than they expected, it remained well below pre-pandemic levels. Business contacts pointed to several factors that could restrain further recovery, including high levels of uncertainty that were reportedly still holding back hiring and capital spending. Some contacts reported difficulties in managing disruptions in supply chains as well as elevated levels of employee absenteeism because of the pandemic. Additionally, District contacts indicated that fiscal policy had helped support small businesses, while federal aid payments had helped support farm incomes.

Participants observed that labor market conditions continued to improve in recent months and that the economy through August had regained roughly half of the 22 million jobs that were lost in March and April. The gains in employment over July and August were generally seen as larger than anticipated. Participants judged, however, that the labor market was a long way from being fully recovered. They generally agreed that prospects for a further substantial improvement in the labor market would depend on a broad and sustained reopening of businesses, which in turn would depend importantly on how safe individuals felt to reengage in a wide range of activities. Some participants noted that the majority of gains in employment so far reflected workers on temporary layoffs returning to work. These participants judged it as less likely for future job gains to continue at their recent pace, because a greater share of the remaining layoffs might become permanent. Workers facing permanent layoffs were seen as more likely to need to find new jobs in different industries, and this process could take time, especially to the extent that these workers needed to be retrained.

Participants observed that lower-paid workers had been disproportionally affected by the economic effects of the pandemic. Many of these workers were employed in the service sector or other industries most adversely affected by social-distancing measures. With a disproportionate share of service-sector jobs held by African Americans, Hispanics, and women, these groups were seen as being especially hard hit by the economic hardships caused by the pandemic. Participants viewed fiscal support from the CARES Act as having been very important in bolstering the financial situations of millions of families, and a number of participants judged that the absence of further fiscal support would exacerbate economic hardships in minority and lower-income communities. In addition, several participants observed that the effects of the pandemic were disrupting the supply of labor because of the need to care for children, many of whom were attending school virtually from home.

In their comments about inflation, participants noted that consumer prices had increased more quickly than expected in recent months and that market-based measures of inflation compensation had increased moderately over the intermeeting period, although they remained low. The upturn in consumer prices was primarily attributed to price increases in sectors such as consumer durables in which demand had risen after experiencing a large decline earlier this spring. Nevertheless, inflation remained subdued, and participants still generally judged that the overall effect of the pandemic on prices was disinflationary. While the outlook for inflation was viewed as highly uncertain, a number of participants projected that inflation would run below the Committee's 2 percent longer-run objective for a significant period before moving moderately above 2 percent for some time—consistent with the Committee's revised consensus statement.

Participants noted that financial conditions were generally accommodative and that actions by the Federal Reserve, including the establishment of emergency lending facilities in conjunction with the Treasury, were supporting the flow of credit to households, businesses, and communities. While these actions as well as prompt and forceful monetary policy measures in response to the pandemic were viewed as contributing to accommodative financial conditions, participants noted important differences in credit quality and credit availability across borrowers. While the pace of corporate downgrades was seen as having decreased significantly in recent months, the delinquency rates on business loans had risen noticeably. Bank contacts reported ample capacity to lend to creditworthy borrowers; however, surveys of credit availability indicated that bank lending was tight. Furthermore, several participants noted the stress that small- and medium-sized banks could face from defaults on loans to small businesses and CRE properties if people continued to withdraw from travel and shopping activities. Additionally, a couple of participants indicated that highly accommodative financial market conditions could lead to excessive risk-taking and to a buildup of financial imbalances.

Participants continued to see the uncertainty surrounding the economic outlook as very elevated, with the path of the economy highly dependent on the course of the virus; on how individuals, businesses, and public officials responded to it; and on the effectiveness of public health measures to address it. Participants cited several downside risks that could threaten the recovery. While the risk of another broad economic shutdown was seen as having receded, participants remained concerned about the possibility of additional virus outbreaks that could undermine the recovery. Such scenarios could result in increases in bankruptcies and defaults, put stress on the financial system, and lead to disruptions in the flow of credit to households and businesses. Most participants raised the concern that fiscal support so far for households, businesses, and state and local governments might not provide sufficient relief to these sectors. A couple of participants saw an upside risk that further fiscal stimulus could be larger than anticipated, though it might come later than had been expected. Several participants raised concerns regarding the longer-run effects of the pandemic, including how it could lead to a restructuring in some sectors of the economy that could slow employment growth or could accelerate technological disruption that was likely limiting the pricing power of firms…

All participants agreed that the completion of the framework review and the publication of the revised consensus statement provided a strong foundation for monetary policy decisions and communications going forward. Accordingly, participants agreed that it would be appropriate to incorporate some key elements of the revised consensus statement into the FOMC statement to be released following this meeting. In particular, participants reiterated their commitment to achieve maximum employment and an inflation rate of 2 percent over the longer run. With inflation running persistently below its longer-run goal, participants judged that it would be appropriate to aim to achieve inflation moderately above 2 percent for some time so that inflation would average 2 percent over time and longer-term inflation expectations would remain well anchored at 2 percent.

Against this backdrop, participants discussed a range of issues associated with providing greater clarity about the likely path of the federal funds rate in the years ahead. Most participants supported providing more explicit outcome-based forward guidance for the federal funds rate that included establishing criteria for lifting the federal funds rate above the ELB in terms of the paths for employment or inflation or both. Among the participants who favored providing more explicit forward guidance at this meeting, all but a couple supported a formulation in which the forward guidance included language indicating that it would likely be appropriate to maintain the current target range until labor market conditions were judged to be consistent with the Committee's assessments of maximum employment and inflation had risen to 2 percent and was on track to moderately exceed 2 percent for some time. These participants noted that communicating that the target range for the federal funds rate would remain at the ELB until these criteria were achieved would provide appropriately clear and strong policy guidance. Doing so at this meeting was viewed as an especially important way of affirming the Committee's commitment to achieving the economic outcomes articulated in the consensus statement.

Participants generally noted that outcome-based forward guidance for the federal funds rate of this type was not an unconditional commitment to a particular path. Indeed, outcome-based guidance of this type would allow the public to infer changes in the Committee's assessment of how long the target range for the federal funds rate would remain at its current setting. Information pointing to a weaker outlook for the economy and inflation would tend to lead to public expectations for a longer period at the current setting of the target range while information suggesting a stronger outlook for the economy and inflation would tend to lead to expectations for a shorter period at the current setting. In addition, circumstances could arise in which the Committee judged that it would be appropriate to change its guidance, particularly if risks emerged that could impede the attainment of its economic objectives.

A couple of participants preferred even stronger, and less qualified, outcome-based forward guidance that they judged would more clearly convey the Committee's commitment to its objectives and to the strategic approach that was articulated in the revised consensus statement. In particular, these participants preferred forward guidance in which the target range for the federal funds rate remained at the ELB until inflation had moved above 2 percent for some time. Especially in light of the lengthy period in which inflation has run below the Committee's longer-run 2 percent objective, these participants judged that it was critical to demonstrate the Committee's commitment to achieve outcomes in which inflation averages 2 percent over time.

Several participants noted that while they agreed it was appropriate to incorporate key elements of the consensus statement into the postmeeting statement, they preferred to retain forward guidance similar to that provided in recent FOMC statements. These participants judged that it would likely be appropriate to maintain an accommodative stance of policy for some time in order to foster outcomes consistent with the Committee's revised consensus statement. However, with longer-term interest rates already very low, there did not appear to be a need for enhanced forward guidance at this juncture or much scope for forward guidance to put additional downward pressure on yields. Moreover, these participants were concerned that forward guidance that involved the target range for the federal funds rate remaining at the ELB until employment and inflation criteria were achieved could limit the Committee's flexibility for years. Furthermore, by influencing expectations for the path of short-term interest rates, such guidance could contribute to a buildup of financial imbalances that would make it more difficult for the Committee to achieve its objectives in the future.

Regarding asset purchases, participants judged that it would be appropriate over coming months for the Federal Reserve to increase its holdings of Treasury securities and agency MBS at least at the current pace. These actions would continue to help sustain smooth market functioning and would continue to help foster accommodative financial conditions, thereby supporting the flow of credit to households and businesses. Some participants also noted that in future meetings it would be appropriate to further assess and communicate how the Committee's asset purchase program could best support the achievement of the Committee's maximum-employment and price-stability goals…

Source: Federal Reserve Board