The US Federal Reserve Qualifies Its Message Somewhat

The US Federal Reserve seems to have muted its words somewhat in today’s message. Actually, remember that in the last press release on October 28, US monetary authorities stated the risk that the inflation rate might reach too low a level was still the Federal Reserve’s chief concern. That said, the F.O.M.C. today indicated that the risk of an “unwelcome” drop in inflation is now practically equal to the probability of a rise in prices. So, this is unquestionably a change in stance, however slight, on the part of US monetary policy officials.

Therefore, even though the FED reaffirms that US monetary policy will remain expansionist for “a considerable period,” it is possible that the fed funds rates will be upped slightly over the next few quarters in order to gradually return to a more neutral position. Moreover, many signs are showing evidence of strong economic growth in the United States. In this context, the US Federal Reserve might well begin to tighten monetary conditions starting in the spring of 2004, either at their meeting in May or in June 2004. Bear in mind that, later on, the presidential elections will make it more difficult to bring changes to US monetary policy. So, investors will have to adjust to this softening in the Fed’s stance, which might temper the ardour of stock market investors as well as accentuate the yield curve.

Conclusion: The US Federal Reserve Qualifies Its Message Somewhat

- The target for the overnight rate remains at 1.00%
- The risk of disinflation over the next few months is almost equal to the probability of a rise in the rate of inflation
- Votes: For = 12; Against = 0.

1) Various signs show that output is expanding vigorously and that the labour market is improving modestly.
2) The upside and downside risks to the attainment of sustainable economic growth are equal. However, the risk of an unwelcome fall in inflation rate is practically equal to the probability of a rise in prices.
3) On the other hand, given the low inflation rate and the overcapacity in production, the current expansionist monetary policy “can be maintained for a considerable period.”