

# U.S. Fed Flash

## FOMC 2014: Fed Stays the Taper-Course

- **Crucial task of adjusting exit strategy ahead of new Fed Chair Yellen**
- **A more centrist FOMC will conclude QE3 by the end of 2014**

At the next two-day policy meeting on January 28-29, FOMC will maintain the course of gradual tapering. The Fed is likely to lower asset purchases by another \$10bn per month, split equally between Treasuries and Mortgage-Backed Securities. The upcoming meeting will be the last one chaired by Bernanke as Yellen replaces him as the new Fed Chair. Yellen, who backed Bernanke in all three rounds of bond buying and was influential in the Fed's steps to increase transparency in communication, will assure continuity of the current monetary policy course. She is certainly one of the Fed's most focused officials on labor market improvement and has a reputation of being an "inflation dove." However we believe Yellen will not hesitate to take a stance against inflation if needed.

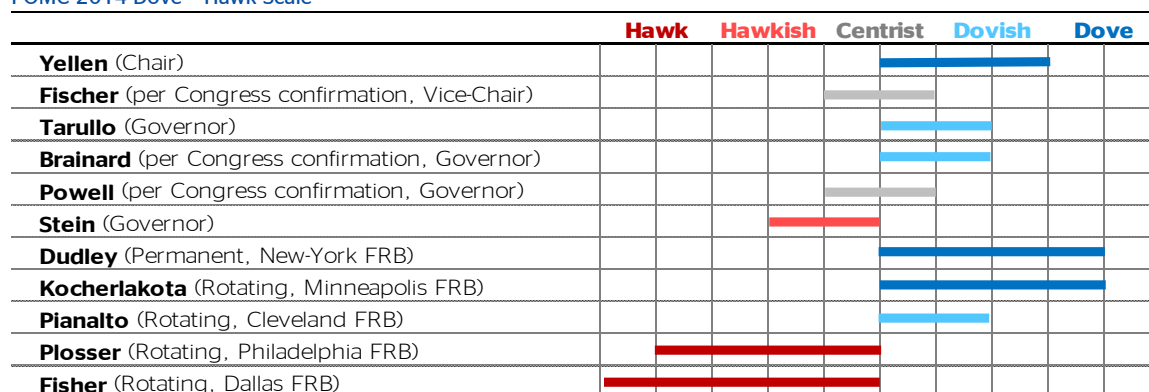
Fischer, formerly Governor of the Bank of Israel and First Deputy Managing Director of the IMF, has been nominated by President Obama to fill the vice-chair seat and is awaiting Congressional confirmation. He is perceived as being more centrist due to his skepticism on the effectiveness of employing policy thresholds and forward guidance, and is expected to have a well balanced approach to policy making adding a centrist touch. His experience and expertise in world policy coordination and financial crisis management bring powerful support to Yellen.

Three governor seats will also have to be filled in 2014. President Obama has nominated Brainard for one of the vacant Governor seats and has re-nominated Powell. Brainard, the former U.S. Under Secretary of the Treasury for International Affairs in the Obama administration, has played a major role in managing the U.S. response to Europe's sovereign debt crises and China's economic rebalancing, and will have a dovish incline. Powell, perceived as a conservative, was appointed by President Obama in 2012 for an unexpired term which will end on January 31.

While modifications within the Board of Governors are dependent on Congressional confirmation, the change in leadership will not manifest until the FOMC March 18-19 meeting, after which the FOMC will release new economic projections and Yellen will do a press conference. The incoming rotating regional FOMC members are in place for the January meeting. The new voting cast will include hawks Fisher (Dallas) and Plosser (Philadelphia), as well as Kocherlakota (Minneapolis), whose speeches advocate a lower unemployment policy threshold of 6%. Pianalto (Cleveland), who previously sided with more centrist doves, will still participate. She plans to step down in early 2014 as soon as there is a successor.

The recent decline in the unemployment rate to 6.7% -only 0.2% higher than their policy rate threshold of 6.5%-, will likely drive the FOMC to search for better ways to assess labor market conditions and alternatives to strengthen forward guidance. The FOMC will also focus on how to address the increasing gap between the date on which the 6.5% unemployment threshold will be reached and the still far away 2015 date to begin policy rate tightening. Effective communication on forward guidance is crucial for the new FOMC as it tries to avoid premature policy tightening and elevated financial volatility in 2014.

Chart 1  
FOMC 2014 Dove - Hawk Scale



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