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AG is a Yogi fan! FOMC leaves rates unchanged and muddies the water on the bias

The FOMC left the Fed Funds rate unchanged, but altered its assessment of risk to the downside. On the surface, moving the bias to weakness would seem to contradict the sense of Greenspan's testimony to the Congress last week that low inflation, accommodative monetary policy and sustained growth in productivity would ultimately put the U.S. economy on its trend growth path, and the second half of 2003 would show significantly better growth. The FOMC's downward move on the risk assessment statement today will set off any number of queries about what the Fed is going to do going forward, and it questions the Greenspan assessment of last week! Here's the operative paragraph in the statement today:

Although the timing and extent of that improvement remain uncertain, the Committee perceives that over the next few quarters the upside and downside risks to the attainment of sustainable growth are roughly equal. In contrast, over the same period, the probability of an unwelcome substantial fall in inflation, though minor, exceeds that of a pickup in inflation from its already low level. The Committee believes that, taken together, the balance of risks to achieving its goals is weighted toward weakness over the foreseeable future.

What the Committee has done is to weigh up the "timing and extent of …improvement…" and concluded that the risk of attaining sustainable growth is essentially balanced. However, the Committee now admits there is some non-zero probability that there could occur an "unwelcome substantial fall in inflation," that would upset attaining sustainable economic growth. Does that mean that there's more rate-cutting still to go in this business cycle? Is this a Greenspan defeat?

So—who's on first? Greenspan or his other committeemen? It would appear that the FOMC has chosen to make the meaning of the risk assessment even more nebulous in order to attain unanimity in the decision at the expense of clarity for the market as to the Fed's forward course. Greenspan's Congressional testimony appears to have been waylaid by District Bank Presidents who fear that the deflation risk cannot be ignored.

The missing actor at the revival party has been the business sector. While corporate profits are coming in significantly higher than the market anticipated, there seems to be an abundance of business pessimism. Clearly there has been less than robust return of capital spending, increased hiring or inventory growth. With the war over and oil prices falling from their peaks, a bounce in the economy should have occurred, but it hasn't. The FOMC is admitting it will be watching the data again, with no real firm commitment that we have reached an end to the interest rate reduction cycle.

Rates could have bottomed or there could be another round. In the meantime, as Yogi said, "You can observe a lot just by watching." The Fed will be watching the data, and the market will be watching the Fed. We just have to be careful we don't fall into another Yogi-ism**, "You've got to be very careful if you don't know where you're going, because you might not get there!"**

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