Monetary Policy

March 18, 2015

Never so much money was bet on single word “patient”. By junking the word, the FOMC has freed itself from the shackle and has taken a step toward normalization.

An April hike was ruled out. While the lift-off during the June meeting is possible, nothing is certain at the moment. At present, domestic economic numbers are mixed.

The statement said, “Economic conditions may, for some time, warrant keeping the target federal funds rate below levels the Committee views as normal in the long run.”

On the inflation front, the FOMC lowered its inflation projection for 2015. As the economy and the labor market strengthen, the central bank sees wages and the inflation rate edging close to the 2 percent target. FOMC will move when it is reasonably confident that inflation will hit the goal in the foreseeable future.

Today’s action says that the interest rate won’t remain at zero indefinitely. However, the ensuing rise in the interest rate will be slow and gradual. The Fed's "dot plots" show further cut in the inflation projection and lower interest-rate path in the future. No spike in the interest rate is in sight. Aside from the U.S. economy, here are some external reasons for cautiousness.

The muscular dollar, the plunge in the price of oil, the unstable finances of emerging market nations and China’s economic slowdown are some of the concerns at the Fed. They could cause volatility in the financial markets. The increased uncertainties will keep the FOMC cautious about hiking the interest rate.

In short, the FOMC is moving in the direction of higher interest rates, but not sure when it is appropriate to pull the trigger. The central bank has said repeatedly in the past that the interest rate outlook will be based on the performance of the economy. Decisions will be made on a meeting-to-meeting basis.