In a recent speech, Federal Reserve Bank President John Williams reassured that central bankers are on the job. “As nature abhors a vacuum,” he opened, “so monetary policy abhors stasis.”1 Huh? Stasis is conventionally defined as a condition in which things do not change. As plotted below, Fed officials have changed their policy rate complex exactly once in the past 2,800 days. That is, they acted at one meeting in the past sixty-one regularly scheduled ones, consistent with an embrace, rather than abhorrence, of stasis.

Given this eight-year track record, President Williams might want to refresh his recollection of the famous skit from the first season of Monty Python before he next characterizes the Fed’s interest-rate setting. Fed action? “This parrot is dead.”2 Deceased. Gone. Moribund. Bereft of life.

For a few days before the release of the July FOMC meeting, market participants detected some signs of life. After all, Bank Presidents Dudley and Lockhart asserted that the group might collectively dip its toe into the tightening pool, with the not-quite ringing endorsement from the former that they are “…edging closer to the point in time where it will be appropriate, I think, to raise interest rates further.”3 The Norwegian Blue was pinning for the fjords of firming.


2 Monty Python - Dead Parrot (https://www.youtube.com/watch?v=4vuW6tQ0218) John Cleese plays a disgruntled customer seeking a refund on his recently purchased and evidently deceased Norwegian Blue parrot. Despite his many descriptions of the parrot’s status, the shop clerk, Michael Palin, refuses to accept that the Blue has shuffled off this mortal coil. After all, it might be stunned after a prolonged squawk or pinning for the fjords.

Such urges were less evident in print, on balance, but it is a tricky balance to weigh.

The minutes showed FOMC participants as a little more confident about economic momentum (with the dismal May employment report further in the rearview mirror) and less concerned about global risks (with the dust from the "Brexit" blow-up settling).

The shared view was that the U.S. economy had maneuvered over some first-half potholes and would perform going forward about as expected at the prior FOMC meeting. That earlier outlook, remember, was predicated on the expectation of FOMC participants of a rate hike or two in 2016. This, which presumably explains why most post-meeting speakers wondered aloud about the low probability of action priced into futures markets, represents the hawkish core to the message.

This message was not just hawkish relative to market prices, it was also entirely conventional and repetitive. That is, the mainstream macroeconomics in the minutes followed the Fed script of midyear. With policy accommodative and financial conditions supportive, aggregate demand is likely bumping along in a two-percent channel. This performance is uninspiring compared with that of prior decades but is likely above that of potential output. Our aging population is growing slowly and not expanding the output associated with added effort much. If so, now and for a time to come, there is less headroom for demand expansion, putting inflation on a gradual uptrend toward the Fed's goal of 2 percent. The removal of some unusual accommodation is needed, but such action can be gradual for now. Moreover, in a slowly growing economy, less cumulative tightening will ultimately be required.

Uneven data and a risk event from the nation of Monty Python of similar surrealism intruded on this story line in June but it returned in the July minutes with some talk that “...economic conditions would soon warrant taking another step in removing policy accommodation.” But there was a new twist to the plotline as well. The Norwegian Blue did not squawk because the doves cried. After most participants agreed labor slack was close to, or already, gone, others “...continued to judge that labor utilization remained below that consistent with the Committee's maximum-employment objective.” What followed was a list of those items on Chair Yellen's labor-market-monitoring dashboard that had needles pointing the furthest from empty. This sentiment was reinforced in the inflation discussion, where another collection of “others” (and probably the same people) wondered if the Phillips' curve had shifted so as to lower the natural rate of unemployment and make the economy less inflation prone. A couple of them may have been the ones preferring “...to wait for more evidence that inflation would rise to 2 percent on a sustained basis.”

These are issues that they worried about before and may have been voiced more loudly because the mainstream story seems shopworn. To be sure, the inflation around the corner has been slow to turn the corner. But this time round, the insistence of these concerns in the minutes seemed to imply these were, for couple of participants, sufficiently compelling not to tighten in 2016. That is news from a committee that reported in the Summary of Economic Projections in June that everyone envisaged at least one rate hike this year.

The problem in weighing the balance is that the FOMC apparently did not finish the conversation in July about action in 2016. “Some” wanted to move soon. “One” would have done so that day (President Esther George, who dissented). And a “couple” wanted to see the whites of inflation's eyes. But that does not add up to the

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entire group. Evidently, some views on the money matter of the moment were either unexpressed or unreported. As there was no Survey of Economic Projections at that no-press-conference meeting, they did not have to come to closure on action at future meetings. Not to close the loop once opened in the meeting discussion, however, was a decision, not an omission, firmly in the ambit of the Fed chairperson.

As a result, we now have many FOMC participants favoring tightening this year, a couple do not, and Chair Yellen likely did not put her thumb on the scale to tip the balance. As to the more immediate and practical consequences:

Chair Yellen’s speech at the Jackson Hole economic Symposium is likely to be unenlightening about policy action, other than it was frankly discussed at the July meeting and in the future will be the result of data-dependent decisions made meeting by meeting. There is no decisive economic reports between now and then and it is not her style to preserve optionality in July (the lacuna in the minutes) to spend it in August.

Two dots in the Summary of Economic Projection in September will shift down to no action in 2016. The “couple” of participants worrying about downside inflation forces came across as insistent.

The risk of a modest inflation overshoot next year and thereafter is higher than we previously thought.

We think the mainstream macro story has merit and that the FOMC will appropriately raise the funds rate one-quarter point in December, taking one small step along a gradual path of removing policy accommodation. The pattern of Fed leadership, however, has been to talk that game but then grasp any reason for delay. If Chair Yellen is flanked to her left by a couple of more assertive doves, she may be more willing to put off for tomorrow what the majority of her committee wants today.

One last point. The front part of the minutes probably provides some guidance on the substantive portion of Chair Yellen’s Jackson Hole remarks, which are advertised with the title “Designing Resilient Monetary Policy Frameworks for the Future.” Staff briefed the Committee on potential long-run frameworks for monetary policy implementation, and it mostly sounded like reasons to love a big balance sheet and an expanded toolkit of policy instruments. A large balance sheet implies a sizable stock of assets, opening the possibility that shifts in the mix of holdings may influence spreads (or twist to the left and twist to the right). Given that balance sheets balance, a large stock of liabilities (reserves) gives the Fed the ability to run a large book of reverse RPs to drain reserves and control the federal funds rate. Those reverse RPs provide a safe, un-runnable instrument in a world where regulatory changes have “…raise(d) the long-run demand for safe assets.”

No one seemed in a hurry to make any decisions, in that “…policymakers agreed that decisions regarding an appropriate long-run implementation framework would not be necessary for some time.” But the destination seems inevitable: The Fed will keep its portfolio holdings larger relative to the overall economy and operate in more varied ways than prior to the financial crisis. There was, however, no mention in the minutes about whether the Holy Hand Grenade of Antioch was among the tools considered for future monetary policy implementation (if, that is, Monty Python would let them have it).
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