

Policy Normalization Principles and Plans

As adopted effective September 16, 2014

During its recent meetings, the Federal Open Market Committee (FOMC) discussed ways to normalize the stance of monetary policy and the Federal Reserve's securities holdings. The discussions were part of prudent planning and do not imply that normalization will necessarily begin soon. The Committee continues to judge that many of the normalization principles that it adopted in June 2011 remain applicable. However, in light of the changes in the System Open Market Account (SOMA) portfolio since 2011 and enhancements in the tools the Committee will have available to implement policy during normalization, the Committee has concluded that some aspects of the eventual normalization process will likely differ from those specified earlier. The Committee also has agreed that it is appropriate at this time to provide additional information regarding its normalization plans. All FOMC participants but one agreed on the following key elements of the approach they intend to implement when it becomes appropriate to begin normalizing the stance of monetary policy:

- The Committee will determine the timing and pace of policy normalization—meaning steps to raise the federal funds rate and other short-term interest rates to more normal levels and to reduce the Federal Reserve's securities holdings—so as to promote its statutory mandate of maximum employment and price stability.
 - When economic conditions and the economic outlook warrant a less accommodative monetary policy, the Committee will raise its target range for the federal funds rate.
 - During normalization, the Federal Reserve intends to move the federal funds rate into the target range set by the Committee primarily by adjusting the interest

rate it pays on excess reserve balances.

- During normalization, the Federal Reserve intends to use an overnight reverse repurchase agreement facility and other supplementary tools as needed to help control the federal funds rate. The Committee will use an overnight reverse repurchase agreement facility only to the extent necessary and will phase it out when it is no longer needed to help control the federal funds rate.
- The Committee intends to reduce the Federal Reserve's securities holdings in a gradual and predictable manner primarily by ceasing to reinvest repayments of principal on securities held in the SOMA.
 - The Committee expects to cease or commence phasing out reinvestments after it begins increasing the target range for the federal funds rate; the timing will depend on how economic and financial conditions and the economic outlook evolve.
 - The Committee currently does not anticipate selling agency mortgage-backed securities as part of the normalization process, although limited sales might be warranted in the longer run to reduce or eliminate residual holdings. The timing and pace of any sales would be communicated to the public in advance.
- The Committee intends that the Federal Reserve will, in the longer run, hold no more securities than necessary to implement monetary policy efficiently and effectively, and that it will hold primarily Treasury securities, thereby minimizing the effect of Federal Reserve holdings on the allocation of credit across sectors of the economy.
- The Committee is prepared to adjust the details of its approach to policy normalization in light of economic and financial developments.

Addendum to the Policy Normalization Principles and Plans

As adopted effective March 18, 2015

All participants agreed to augment the Committee's Policy Normalization Principles and Plans by providing the following additional details regarding the operational approach the FOMC intends to use when it becomes appropriate to begin normalizing the stance of monetary policy.¹

When economic conditions warrant the commencement of policy firming, the Federal Reserve intends to:

- Continue to target a range for the federal funds rate that is 25 basis points wide.
- Set the IOER rate equal to the top of the target range for the federal funds rate and set the offering rate associated with an ON RRP

facility equal to the bottom of the target range for the federal funds rate.

- Allow aggregate capacity of the ON RRP facility to be temporarily elevated to support policy implementation; adjust the IOER rate and the parameters of the ON RRP facility, and use other tools such as term operations, as necessary for appropriate monetary control, based on policymakers' assessments of the efficacy and costs of their tools. The Committee expects that it will be appropriate to reduce the capacity of the facility fairly soon after it commences policy firming.

¹ The Committee's Policy Normalization Principles and Plans were adopted on September 16, 2014,

and are available at www.federalreserve.gov/monetarypolicy/files/FOMC_PolicyNormalization.pdf.

Addendum to the Policy Normalization Principles and Plans

As adopted effective June 13, 2017

All participants agreed to augment the Committee's Policy Normalization Principles and Plans by providing the following additional details regarding the approach the FOMC intends to use to reduce the Federal Reserve's holdings of Treasury and agency securities once normalization of the level of the federal funds rate is well under way.¹

- The Committee intends to gradually reduce the Federal Reserve's securities holdings by decreasing its reinvestment of the principal payments it receives from securities held in the System Open Market Account. Specifically, such payments will be reinvested only to the extent that they exceed gradually rising caps.
 - For payments of principal that the Federal Reserve receives from maturing Treasury securities, the Committee anticipates that the cap will be \$6 billion per month initially and will increase in steps of \$6 billion at three-month intervals over 12 months until it reaches \$30 billion per month.
 - For payments of principal that the Federal Reserve receives from its holdings of agency debt and mortgage-backed securities, the Committee anticipates that the cap will be \$4 billion per month initially and will increase in steps of \$4 billion at three-month intervals over 12 months until it reaches \$20 billion per month.
 - The Committee also anticipates that the caps will remain in place once they reach their respective maximums so that the Federal Reserve's securities holdings will continue to decline in a gradual and

predictable manner until the Committee judges that the Federal Reserve is holding no more securities than necessary to implement monetary policy efficiently and effectively.

- Gradually reducing the Federal Reserve's securities holdings will result in a declining supply of reserve balances. The Committee currently anticipates reducing the quantity of reserve balances, over time, to a level appreciably below that seen in recent years but larger than before the financial crisis; the level will reflect the banking system's demand for reserve balances and the Committee's decisions about how to implement monetary policy most efficiently and effectively in the future. The Committee expects to learn more about the underlying demand for reserves during the process of balance sheet normalization.
- The Committee affirms that changing the target range for the federal funds rate is its primary means of adjusting the stance of monetary policy. However, the Committee would be prepared to resume reinvestment of principal payments received on securities held by the Federal Reserve if a material deterioration in the economic outlook were to warrant a sizable reduction in the Committee's target for the federal funds rate. Moreover, the Committee would be prepared to use its full range of tools, including altering the size and composition of its balance sheet, if future economic conditions were to warrant a more accommodative monetary policy than can be achieved solely by reducing the federal funds rate.

¹ The Committee's Policy Normalization Principles and Plans were adopted on September 16, 2014, and are available at www.federalreserve.gov/monetarypolicy/files/FOMC_PolicyNormalization.pdf. On

March 18, 2015, the Committee adopted an addendum to the Policy Normalization Principles and Plans, which is available at www.federalreserve.gov/monetarypolicy/files/FOMC_PolicyNormalization.20150318.pdf.