

**Appendix 1: Materials entitled, “Background Documents and Questions for Discussion on Forward Guidance,” used by participants**

Class I FOMC – Restricted Controlled (FR)

**BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM**  
**DIVISION OF MONETARY AFFAIRS**  
**FOMC SECRETARIAT**

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**Date:** February 28, 2014  
**To:** Federal Open Market Committee  
**From:** William B. English  
**Subject:** Background Documents and Questions for Discussion on  
Forward Guidance

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Attached as background for the March 4 FOMC videoconference are two documents:

- (1) The options for interest rate forward guidance that were distributed in the memo sent to the Committee on February 21, along with an additional option that aims to make smaller changes to the language used in the January statement.
- (2) A set of questions that you may want to address in your remarks during the videoconference.

The meeting is scheduled to begin (at 3:00 p.m. Washington time) with introductory remarks by the Chair. A go-round will follow.

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**The five options**

Shown below is paragraph 5 from the January statement followed by the four options discussed in the staff memo, along with an additional option that aims to make smaller changes to the language used in the January statement.. As in the staff memo, we have highlighted in blue the aspects that *differ* materially across the options. Thus, the parts in plain black text are identical, or nearly so, in all of the options.<sup>1</sup>

**Paragraph 5 from the January Statement**

5. To support continued progress toward maximum employment and price stability, the Committee today reaffirmed its view that a highly accommodative stance of monetary policy will remain appropriate for a considerable time after the asset purchase program ends and the economic recovery strengthens. The Committee also reaffirmed its expectation that the current exceptionally low target range for the federal funds rate of 0 to 1/4 percent will be appropriate at least as long as the unemployment rate remains above 6-1/2 percent, inflation between one and two years ahead is projected to be no more than a half percentage point above the Committee's 2 percent longer-run goal, and longer-term inflation expectations continue to be well anchored. In determining how long to maintain a highly accommodative stance of monetary policy, the Committee will also consider other information, including additional measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial developments. The Committee continues to anticipate, based on its assessment of these factors, that it likely will be appropriate to maintain the current target range for the federal funds rate well past the time that the unemployment rate declines below 6-1/2 percent, especially if projected inflation continues to run below the Committee's 2 percent longer-run goal. When the Committee decides to begin to remove policy accommodation, it will take a balanced approach consistent with its longer-run goals of maximum employment and inflation of 2 percent.

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<sup>1</sup> Some very minor differences arise due to the different structure of the statements.

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**Option 1. No thresholds but rule-like language**

5. To support continued progress toward maximum employment and price stability, the Committee today reaffirmed its view that a highly accommodative stance of monetary policy remains appropriate. In determining how long to maintain the current target range for the federal funds rate of 0 to 1/4 percent, the Committee will consider **the projected shortfalls of employment from its maximum sustainable level and of inflation from the Committee's longer-run goal of 2 percent. The larger these shortfalls, and the longer they are expected to persist, the longer the Committee is likely to maintain the current target range for the federal funds rate, provided that** longer-term inflation expectations continue to be well anchored. **In assessing the employment shortfall, the Committee will consider a broad range of indicators of labor market conditions.** In determining the appropriate stance of policy, the Committee will also take account of financial market developments and their implications for attaining the Committee's objectives. Based on these factors, the Committee currently anticipates that the current target range for the federal funds rate will be maintained for a considerable period of time after the asset purchase program ends, especially if projected inflation continues to run below the Committee's 2 percent longer-run goal.
  
6. When the Committee decides it is appropriate to begin to raise the level of short-term interest rates, the pace of increase will depend on the magnitude of the deviations of employment and inflation from their mandate-consistent levels and on projected progress toward those levels. The Committee currently anticipates that, even after employment and inflation are at mandate-consistent levels, economic conditions will likely warrant keeping short-term interest rates below their average level prior to the financial crisis, at least for a time.

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**Option 2. Similar to Option 1, but with thresholds for employment and inflation**

5. To support continued progress toward maximum employment and price stability, the Committee today reaffirmed its view that a highly accommodative stance of monetary policy remains appropriate. In determining how long to maintain the current target range for the federal funds rate of 0 to 1/4 percent, the Committee will consider **the projected shortfall of employment from its maximum sustainable level and the projected gap between inflation and the Committee's longer-run goal of 2 percent. In assessing the employment shortfall, the Committee will consider a broad range of indicators of labor market conditions.** In determining the appropriate stance of policy, the Committee will also take account of financial market developments and their implications for attaining the Committee's objectives. Based on these factors, the Committee currently anticipates that the current target range for the federal funds rate will be maintained **at least as long as the level of employment projected one year ahead remains below the Committee's estimate of its maximum sustainable level, inflation projected between one and two years ahead does not exceed 2 percent, and** longer-term inflation expectations continue to be well anchored. The Committee expects these conditions to hold for a considerable period of time after the asset purchase program ends.
6. When the Committee decides it is appropriate to begin to raise the level of short-term interest rates, the pace of increase will depend on the magnitude of the deviations of employment and inflation from their mandate-consistent levels and on projected progress toward those levels. The Committee currently anticipates that, even after employment and inflation are at mandate-consistent levels, economic conditions will likely warrant keeping short-term interest rates below their average level prior to the financial crisis, at least for a time.

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**Option 3. An inflation floor and few references to general principles**

5. To support continued progress toward maximum employment and price stability, the Committee today reaffirmed its view that a highly accommodative stance of monetary policy remains appropriate **and decided to maintain its 0 to 1/4 percent target range for the federal funds rate**. The Committee expects that the current target range will be appropriate **at least as long as inflation between one and two years ahead is projected to be below 2 percent and** longer-term inflation expectations continue to be well anchored. The Committee expects these conditions to hold for a considerable period of time after the asset purchase program ends. In determining the appropriate stance of policy, the Committee will also take account of financial market developments and their implications for attaining the Committee's objectives.
6. When the Committee decides it is appropriate to begin to raise the level of short-term interest rates, the pace of increase will depend on the magnitude of the deviations of employment and inflation from their mandate-consistent levels and on projected progress toward those levels. The Committee currently anticipates that, even after employment and inflation are at mandate-consistent levels, economic conditions will likely warrant keeping short-term interest rates below their average level prior to the financial crisis, at least for a time.

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**Option 4. A more significant restructuring; intent similar to Option 2**

5. To support continued progress toward maximum employment and price stability, the Committee today reaffirmed that a highly accommodative stance of monetary policy remains appropriate. **As conditions evolve, the appropriate degree of accommodation will depend on the deviation of inflation from the Committee's 2 percent longer-run goal, the divergence of employment from its maximum sustainable level, and the projected progress toward each of the Committee's objectives. Assessments of the maximum sustainable level of employment are necessarily uncertain and, in making them, the Committee considers a wide range of indicators.** [In determining the appropriate stance of policy, the Committee will also take account of financial market developments and their implications for attaining the Committee's objectives. | **Because financial stability is a precondition for meeting the FOMC's objectives, stability assessments are also a factor in determining the appropriate stance of policy.**]
6. Based on these factors, the Committee currently anticipates that the current target range for the federal funds rate will be maintained **at least as long as the level of employment projected one year ahead remains below the Committee's estimate of its maximum sustainable level, inflation projected between one and two years ahead does not exceed 2 percent, and** longer-term inflation expectations continue to be well anchored. The Committee expects these conditions to hold for a considerable period of time after the asset purchase program ends.
7. When the Committee decides it is appropriate to begin to raise the level of short-term interest rates, the pace of increase will depend on the magnitude of the deviations of employment and inflation from their mandate-consistent levels and on projected progress toward those levels. The Committee currently anticipates that, even after employment and inflation are at mandate-consistent levels, economic conditions will likely warrant keeping short-term interest rates below their average level prior to the financial crisis, at least for a time.

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**Option 5. Smaller changes to the January forward guidance**

To support continued progress toward maximum employment and price stability, the Committee today reaffirmed its view that a highly accommodative stance of monetary policy remains appropriate. **In determining how long to maintain a highly accommodative stance of monetary policy, the Committee will consider a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial developments.** The Committee anticipates, based on its assessment of these factors, that it likely will be appropriate to maintain the current 0 to 1/4 percent target range for the federal funds rate **at least as long as complete recovery in the labor market appears to be more than a year away, especially if projected inflation continues to run below the Committee's 2 percent longer-run goal.** In particular, the Committee expects to maintain the 0 to 1/4 percent target range for a considerable time after the asset purchase program ends. **When the Committee decides to begin to remove policy accommodation, it will take a balanced approach consistent with its longer-run goals of maximum employment and inflation of 2 percent.**

**Questions for Discussion of Potential Changes to the Committee’s Forward Guidance**

1. What sort of forward guidance regarding the timing of liftoff do you favor? In particular:
  - a. Should the forward guidance include a general statement regarding the Committee’s approach to its policy decisions?
  - b. Should the forward guidance link the likely timing of the first increase in the federal funds rate target to the end of the asset purchase program?
  - c. Should the forward guidance employ economic thresholds, triggers, or floors to communicate the Committee’s intentions? If so, what formulation of that portion of the guidance do you think would be most helpful?
  - d. Are there other approaches to forward guidance regarding the timing of liftoff that you would prefer?
2. Should the forward guidance include a more prominent role for financial developments than in the current statement? If so, would you prefer a general indication that the Committee will take account of financial developments and their implications for achieving the Committee’s objectives, or more explicit references to financial stability risks, unwarranted changes in financial conditions, or both?
3. Do you think that the Committee should provide additional guidance regarding the path of the policy rate after liftoff, beyond the “balanced approach” language that has been included in recent statements? If so, would you prefer a statement of broad principles, as in the first sentence of paragraph 6 in Options 1-3, or a more specific statement regarding the likely level or path of interest rates during normalization, as in the second sentence of that paragraph, or both?
4. Are there other changes to the Committee’s forward guidance that you think would be helpful?