A Day in the Life of the FOMC

An Inside Look at the Federal Reserve's Monetary Policymaking Body

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As long as the U.S. economy is growing steadily and inflation is low, few people give much thought to the Federal Open Market Committee, or FOMC, the group within the Federal Reserve System charged with setting monetary policy. Yet, when economic volatility makes the evening news, this Committee and its activities become much more prominent. Investors and workers, shoppers and savers all pay more attention to the FOMC's decisions and the wording of its announcements at the end of each meeting.

Why? Because the decisions made by the FOMC have a ripple effect throughout the economy. The FOMC is a key part of the Federal Reserve System, which serves as the central bank of the United States. Among the Fed's duties are managing the growth of the money supply, providing liquidity in times of crisis, and ensuring the integrity of the financial system. The FOMC's decisions to change the growth of the nation's money supply affect the availability of credit and the level of interest rates that businesses and consumers pay. Those changes in money supply and interest rates, in turn, influence the nation's economic growth and employment in the short run and the general level of prices in the long run.

As a result, many people have good reason to wonder about who makes these decisions about monetary policy and how they make them. In these pages, we will eliminate some of the mystery surrounding what goes on at the FOMC meetings in Washington, D.C.

The Mechanics of a Meeting

Let's take a closer look at how our nation's monetary policymakers go about their task in a typical FOMC meeting. Or, put simply, let's spend a day in the life of the FOMC.

The FOMC meets regularly — typically every six to eight weeks — in Washington, D.C., although the Committee can and does meet more often by phone or videoconference if needed. The meetings are generally one-day or two-day events, with the two-day meetings providing more time to discuss a special topic. A typical one-day meeting begins on Tuesday at 8:30 a.m. and ends between 1:00 and 2:00 p.m. Two-day meetings usually begin on the afternoon of the first day, typically a Tuesday afternoon, and end between noon and 2:00 p.m. on the second day.

Around the table in the Federal Reserve Board's headquarters sit all 19 FOMC participants (seven Governors and 12 Reserve Bank presidents) as well as select staff and economists from the Board and the Reserve Banks. Because of the nature of the discussions, attendance is restricted. A Reserve Bank president, for instance, typically brings along only one staff member, usually his or her director of research.

The objective at each meeting is to set the Committee's target for the federal funds rate — the interest rate at which banks lend to each other overnight — at a level that will support the two key objectives of U.S. monetary policy: price stability and maximum sustainable economic growth. The meeting's agenda follows a structured and logical process that results in well-informed and thoroughly deliberated decisions on the future course of monetary policy.

The meeting begins with a report from the manager of the System Open Market Account (SOMA) at the Federal Reserve Bank of New York, who is

Some Facts About the Fed

The Federal Reserve System — commonly called "the Fed" — serves as the central bank of the United States. Congress passed the Federal Reserve Act in 1913, which President Woodrow Wilson supported and signed into law on December 23, 1913. Congress structured the Fed as a distinctly American version of a central bank: a "decentralized" central bank, with Reserve Banks and Branches in 12 Districts spread across the country and coordinated by a Board of Governors in Washington, D.C. Congress also gave the Fed System a mixture of public and private characteristics. The 12 Reserve Banks share many features with private-sector corporations, including boards of directors and stockholders (the member banks within their Districts). The Board of Governors, though, is an independent government agency, with oversight responsibilities for the Reserve Banks.

The Fed conducts monetary policy, supervises and regulates banking, serves as lender of last resort, maintains an effective and efficient payments system, and serves as banker for banks and the U.S. government. Conducting the nation's monetary policy is one of the most important — and often the most visible — functions of the Fed.

President Wilson signing the Federal Reserve Act, 1913

Above: Modern-day meeting of the Federal Open Market Committee at the Eccles Building, Washington, D.C.

responsible for keeping the federal funds rate close to the target level set by the FOMC. The manager explains how well the Open Market Trading Desk has done in hitting the target level since the last FOMC meeting and discusses recent developments in the financial and foreign exchange markets.

Up next is the Federal Reserve Board's director of the Division of Research and Statistics, along with the director of the Division of International Finance. They review the Board staff's outlook for the U.S. economy and foreign economies. This detailed forecast is circulated the week before the meeting to FOMC members in what is called the "Greenbook" — named for its green cover in the days when it was a printed document.

Then the meeting progresses to the first of two "go-rounds," which are the core of FOMC meetings. During the first go-round, all of the Fed Governors and Reserve Bank presidents discuss how they see economic and financial conditions. The Reserve Bank presidents speak about conditions in their Districts, as well as offering their views on national economic conditions.

The data and information discussed vary by region and therefore spotlight a wide range of industries.

For example, one would expect the review of regional conditions in the San Francisco District to lend insight into the tech sector of Silicon Valley. The Chicago District covers a region heavily dependent on manufacturing and automobiles. Philadelphia's District has become much more diverse and representative of the national economy, so it tends to reflect what is happening across a variety of sectors.

The policymakers have prepared for this go-round through weeks of information gathering. Before the FOMC meeting, each Reserve Bank prepares a "Summary of Commentary on Current Economic Conditions," which is published two weeks before each meeting in what most people call the "Beige Book," for the color of its cover when originally printed. One Federal Reserve Bank, designated on a rotating basis, publishes the overall summary of the 12 District reports. The Reserve Bank presidents have also gathered information by talking with executives in a variety of business sectors and through meetings with the Banks' boards of directors and advisory councils. In addition, all Committee participants receive briefings on economic conditions by their Research Department staffs in the days leading up to the FOMC meeting. The briefings cover regional, national, and international business and financial conditions.

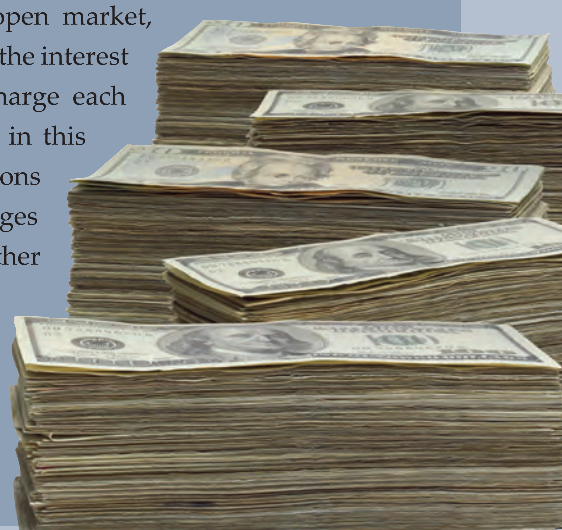
This first go-round covers valuable information about economic activity throughout the country, measured in hard data and recent anecdotal information, as well as the analysis and interpretation conveyed by the policymakers sitting around the table. This is a key way in which each region of the U.S. has input into the making of national monetary policy. This portion of the meeting concludes with the FOMC Chairman summarizing the discussion and providing the Chairman's own view of the economy.

At this point, the policy discussion begins with the Federal Reserve Board's director of the Division of Monetary Affairs, who outlines the Committee's various policy options. The policymakers receive these options usually by the Friday before the meeting in the "Bluebook," again named for its cover's color when originally printed.

A Bit of Background: Monetary Policy

So, what is monetary policy? Simply put, it refers to the actions taken by the Fed to influence the supply of money and credit in order to foster price stability and maintain maximum sustainable economic growth, which are the key objectives established by Congress for monetary policymakers in the U.S. The Federal Reserve issues the nation's currency (Federal Reserve notes) and manages the amount of funds the banking system holds as reserves. Currency and reserves make up what is called the monetary base.

The Fed's instrument for implementing monetary policy is the FOMC's target for the federal funds rate — the interest rate at which banks lend to each other overnight. By buying and selling U.S. government securities in the open market, the Fed influences the interest rate that banks charge each other. Movements in this rate and expectations about those changes influence all other interest rates and asset prices in the economy.



So Who Votes?

In the early days of the FOMC, controversy swirled around how to structure the vote. Should monetary policy be set by the 12 Reserve Banks or the Board of Governors? Or both? In 1935 Congress decided that the seven Governors would vote along with only five of the 12 presidents. The president of the New York Fed always votes — since the Open Market Trading Desk operates in that District — along with four presidents who rotate from among the groups shown below. In that way, voting members always come from different parts of the country.

Always Votes		Rotating Vote (1 president from each group)			
		Group 1	Group 2	Group 3	Group 4
Chairman of the Board (Chair of FOMC) + Six Governors	President of the NY Fed (Vice Chair of FOMC)	Boston	Chicago	Atlanta	Kansas City
		Philadelphia	Cleveland	Dallas	Minneapolis
		Richmond		St. Louis	San Francisco

One-year voting terms begin with the first scheduled meeting in January, at which time the Committee formally elects its officers. Traditionally, the Chairman of the Board of Governors chairs the FOMC, and the New York Fed president serves as vice chairman. Despite the voting design, all 19 policymakers participate equally in the analysis and deliberations. Giving each president a seat at the FOMC table ensures that a "decentralized" central bank sets monetary policy that reflects regional as well as national economic conditions.

The outlook options could include no change, an increase, or a decrease in the federal funds rate target. Each option is described, along with a clear rationale, the pros and cons, and some alternatives for how the Committee could explain its decision in a public statement to be released that afternoon.

Then, there is a second go-round. The Reserve Bank presidents and Governors each make the best case for the policy alternative they prefer, given current economic conditions and their personal outlook for the economy. They also comment on how they think the statement explaining the decision should be worded.

One of the most important aspects of an FOMC meeting is that all voices matter. The analysis and viewpoints of each committee participant — whether a voting member or not — play an instrumental role in the FOMC's policy decisions.

At the end of this policy go-round, the Chairman summarizes a proposal for action based on the Committee's discussion, as well as a proposed statement to explain the policy decision. The Fed Governors and presidents then get a chance to question or comment on the Chairman's proposed approach. Once a motion for a decision is on the table, the Committee tries to come to a consensus through its deliberations. Although the final decision is most often one that all can support, there are times when some differences of opinion may remain, and voting members may dissent.

The process brings a valuable diversity of views to monetary policy decisions. The Committee's ability to make thoughtful and sound policy choices is strengthened by the interaction of policymakers with different perspectives and varied experiences. As American writer and journalist Walter Lippmann once said, "Where all men think alike, no one thinks very much." The give and take at FOMC meetings reflects the remarkably deliberative and thoughtful nature of policymaking and makes the process more constructive.

At the end of the policy discussion, all seven of the Fed Governors and the five voting Reserve Bank presidents cast a formal vote on the proposed decision and the wording of the statement.

FOMC Statements: Communicating Policy Actions

After the vote has been taken, the FOMC publicly announces its policy decision at 2:15 p.m. The announcement includes the federal funds rate target, the statement explaining its actions, and the vote tally, including the names of the voters and the preferred action of those who dissented.

In addition, the FOMC releases its official minutes three weeks after each meeting. The minutes include a more complete explanation of the views expressed, which allows the public to get a better sense of the range of views within the FOMC and promotes awareness and understanding of how monetary policy is made.

In recent years, the FOMC has improved communications with the public. Today, more than ever before, the Fed reports more frequently and more thoroughly on the economy.

Timeline to Transparency

Much has been said about the benefits of predictable policy and its role in shaping the public's expectations. However, just two decades ago, the central bank's decisions were at times hard to discern. The Fed said relatively little about its monetary policy and allowed actions to speak for themselves.

However, markets — even those that are efficient — do not like to be kept guessing. Fed-watchers complained that FOMC decisions were made in an atmosphere of mystery,

76 77 78 80 81 82 84 85 86

1975 The Federal Reserve presents testimony twice each year to Congress on the conduct of monetary policy.

1979 The FOMC releases the first semiannual economic projections.

1983 The Federal Reserve publishes the first "Beige Book," which summarizes economic conditions in each Federal Reserve District.

with meeting minutes reflecting an ever-changing mix of possible factors influencing the Committee's decisions about its fed funds rate target, ranging from indicators of economic growth to commodity prices to exchange rates.

Despite the lack of transparency, the financial press reported extensively before each regularly scheduled FOMC meeting on the likely decision of policymakers and the supposed reasoning behind the decision. However, without clear communications, policy decisions became a source of speculation.

In recent years, the FOMC has sought to improve transparency about its policymaking. Today, the central bank is quite explicit in setting out the objectives of policy and its views on the outlook for the economy. Here are some significant milestones:

87 88 89 90 91 92 93 95 96 97 98 99 01 03 05 06 08

1994
The FOMC begins to release a statement disclosing changes in the federal funds rate target.

2000
The FOMC begins releasing a statement after every meeting and starts to include an assessment of the balance of risks to achieving its objectives.

2002
The results of the FOMC roll-call vote are added to the post-meeting statement.

2004
The FOMC speeds up the release of its minutes: Now there is only a three-week lag, instead of waiting until after the next regularly scheduled meeting, which meant a lag of about six weeks.

2007
The FOMC decides to release its economic projections four times a year.

What's more, the FOMC now releases Committee participants' projections for the economy and inflation four times a year, which provides added insight into the policymakers' perspectives. Clearer guidance about the FOMC's aims helps the economy run more smoothly. Individuals and businesses are able to make their own economic decisions armed with a better understanding of what the central bank expects to happen in the economy.

This greater transparency also helps anchor the public's expectations about the economy and the general level of inflation by explaining the actions the central bank is pursuing.

Transparency also increases the central bank's accountability to the public. In a democratic society, it is important that institutions with the delegated authority to act in the public interest be as clear and as transparent as possible about their actions. Failing to do so risks losing confidence and credibility — two essential ingredients for sound central bank policymaking. When market participants understand how the Fed will react to incoming economic information, policy is more effective.

Putting Policy in Action

Once the FOMC establishes a target for the federal funds rate, the Open Market Trading Desk at the Federal Reserve Bank of New York conducts daily open market operations — buying or selling U.S. government securities on the open market — as necessary to achieve the federal funds rate target.

Simply put, the Fed's open market purchases of government securities increase the amount of reserve funds that banks have available to lend, which puts downward pressure on the federal funds rate. Sales of government securities do just the opposite: They shrink the reserve funds available to lend and tend to raise the funds rate.

Open market operations affect the amount of money and credit available in the banking system, thereby affecting interest rates, which in turn affect the spending decisions of households and businesses and ultimately the overall performance of the U.S. economy.

In Closing

So that's it — a day in the life of the FOMC. We hope you have gained some insights into monetary policymaking in our nation's central bank. Now that you know more about how monetary policy decisions are made, you should be able to better understand news reports about FOMC meetings and the Committee's decisions.

Since the FOMC's beginnings, the U.S. economy and financial system have grown increasingly complex. In response, the FOMC has had to adapt its policymaking so that it can continue to achieve its policy objectives of price stability and maximum sustainable economic growth. In the future, since we can expect our economy and financial system to continue to change, it's likely that the FOMC will continue to have to make adjustments as it seeks to achieve its monetary policy objectives.

A Brief History of the FOMC

Although Congress created the Federal Reserve in 1913, the history of Federal Reserve open market operations begins in the 1920s when Reserve Banks started looking for a new revenue source to cover their operating costs. The Fed is fiscally independent in that it receives no government appropriations. At first, the Reserve Banks relied primarily on interest they earned on loans to banks — called discount window loans. But over time, they also began to purchase government securities in the open market with the intention of earning interest income to cover their expenses.

President Roosevelt signs the Banking Act of 1933

Soon Fed officials recognized that these open market trades had a powerful and immediate impact on short-term interest rates and the supply of money and credit. By the mid-1920s, the Federal Reserve Banks of New York, Boston, Philadelphia, Cleveland, and Chicago had set up a committee to coordinate their purchases and sales of securities. This group was called the Open Market Investment Committee.

The group was reorganized several times over the next few years, but this group involved only the Reserve Banks, not the Federal Reserve Board. Over time, open market operations were becoming the main tool for carrying out monetary policy, overtaking another of the Fed's monetary policy tools: changes in the discount rate.

Federal Reserve Board members, 1914

In the Banking Act of 1933, Congress established the name and legal structure of the FOMC as a formal committee of all 12 Reserve Banks. Then in 1935, Congress determined that the FOMC should include the seven-member Board of Governors as well as the 12 Reserve Bank presidents — bringing together both centralized and decentralized elements of the central bank. In the 1935 act, Congress also decided that only five of the 12 Reserve Bank presidents would vote at any one time, along with the seven Governors.

Fed Governors are appointed by the President of the United States and confirmed by the Senate, while Reserve Bank boards of directors appoint their presidents, subject to the Board of Governors' approval. The FOMC therefore reflects a blend of national and regional representation as well as both public and private interests.

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