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FOMC: Dovish Victory Dance

The FOMC focuses its full policy arsenal on the unemployment problem, extending the rate-guidance phrase by six months, committing not only to buy $40 billion in agency mortgage-backed securities per month starting immediately, but also, "If the outlook for the labor market does not improve substantially," to add "additional asset purchases and employ its other policy tools as appropriate until such improvement is achieved in a context of price stability."

The latter commitment is the big bazooka, promising open-ended, potentially large, asset purchases until the labor market outlook is deemed satisfactory. And, it is hinted that a decision to step up, or step up from, the $40 billion MBS program may not be too far away, with the Committee intending to "closely monitor incoming information on economic and financial developments in coming months."

Also, the rate guidance is strengthened with the new addition of a pronouncement that "the Committee expects that a highly accommodative stance of monetary policy will remain appropriate for a considerable time after the economic recovery strengthens." That addresses dovish concerns that saber-rattling by Fed hawks could stifle risk taking because of fears that any green shoots in the economy will be crushed by a too-quick shift to the exit plan.

The policy change seems to mainly reflect gnawing dovish impatience with the current rate of progress--there is no indication that the economic expansion is seen as being at any significant immediate new risk, with the economy described as having "continued to expand at a moderate pace," and the only new negative indication being that "business fixed investment appears to have slowed."

This seems to be a full-scale capitulation to the demands of the most ardent doves. Results on the economy will now be awaited--and the expectation that they will materialize is presumably quite strong among Fed theorists.

Meanwhile all of the concerns expressed by internal Fed hawks--and most forcefully in public, by outsiders like John Taylor--can only be intensified. By the time the economy has improved enough for the easing program to be halted, there may be less leeway to take preemptive steps against inflation--and the necessary balance-sheet unwinding process will be that much more overwhelming. The lack of any immediate signs of approval from the fixed-income market may reflect some contemplation of that problem.

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