

THE FOMC JULY RATE DECISION

HUGHES ECONOMICS (HE) – July 2023

The forthcoming FOMC rate decision on July 26th is another opportunity to demonstrate the probability assessment method advocated by HE. Most analyses reduce the options to a zero move or a 25 basis points (bps) rise. Below we expand the options as the “never say never” mantra is one we respect. Just assign low probabilities to low chance events as in the table below. And there could be developments in the near future that necessitate higher rate moves. All available options in increasing order of likelihood are as follows:

- 75 basis points or a 0.75% rise in the Federal Funds rate
- 50 basis points rise
- 0 rise or no change
- 25 basis points rise

All calculations outlined here are shown in the spreadsheet *FOMCJuly23.xlsx* that can be downloaded from this website.

PROBABILITIES ON THE FOMC JULY RATE DECISION

Scenarios		Pairwise Values		Probabilities				More Likely Values	
Events	Ratios	Low	High	Low End	High End	Average	%	Average	%
75 bps	Base = 1	1.00	1.00	0.012	0.005	0.009	1	Base	Base
50 bps	50/75 bps	2.00	3.00	0.024	0.016	0.020	2	2.22	2.00
0 change	0/50 bps	18.00	22.00	0.429	0.356	0.392	39	19.60	19.50
25 bps	25/0 bps	1.25	1.75	0.535	0.623	0.579	58	1.48	1.49
				1.000	1.000	1.000	100		

The second table in the spreadsheet shows the decision-maker (DM) assigning zero probabilities to the high rate changes with the 40%/60% resulting probabilities for zero change and a 25 bps rise, respectively. This reflects the further rate rises foreshadowed by the Fed as being necessary to curtail inflation. The achievement of a soft landing would be a first as the tendency for Central Banks is to keep rates higher for longer than necessary.

The third table in the spreadsheet uses HE numbers to illustrate the framework proposed by Nouriel Roubini in his **Project Syndicate** article of June 27, 2023, entitled *A Mild Global Contraction Is Coming*. It is reaffirmed that while the framework of scenarios is Roubini’s, the probabilities are those of HE.

PROBABILITIES OF ROUBINI’S FRAMEWORK FOR THE WORLD ECONOMIC OUTLOOK FOLLOWING THE FOMC JULY DECISION

Scenarios		Pairwise Values		Probabilities				More Likely Values	
Events	Ratios	Low	High	Low End	High End	Average	%	Average	%
Wage/Price Spiral	Base = 1	1.00	1.00	0.077	0.027	0.052	5	Base	Base
Soft Landing	Soft L/WPS	3.00	4.00	0.231	0.108	0.170	17	3.27	3.40
Hard Landing	Hard/Soft	1.00	2.00	0.231	0.216	0.223	22	1.31	1.29
Mild Recession	Mild/Hard	2.00	3.00	0.461	0.649	0.555	56	2.49	2.55
				1.000	1.000	1.000	100		

The Mild Recession is the most likely outcome in accordance with Roubini’s title as above, but Roubini’s probabilities may differ from those shown here. Note too that the Low and High End probabilities for some events show wide spreads, and this could lead to revisions by the DM.

HE’s view is that if different scenarios are proposed by commentators, as well as signalling the most likely scenario, probabilities on the other scenarios would be useful for economic agents. The procedures proposed for this as demonstrated here are not demanding and can easily accommodate revisions in the DM’s views.