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Big Changes in the Fed's FOMC in January 2014

Key Insights

- While most attention has focused on the new Fed Chair, between 7 and 9 voting FOMC members will differ in early 2014 compared to today.
- Departing Fed Governors include Chair Ben Bernanke, Sarah Bloom Raskin, Elizabeth Duke, and Jerome Powell. Up for consideration for the Fed Chair, Janet Yellen could resign her Governor post if not selected, opening another spot.
- Four new Fed Presidents will rotate on as voting FOMC members in 2014, possibly shifting the FOMC in a hawkish direction.
- With key monetary policy decisions coming up at the Fed, shifts in the FOMC will have significant implications on QE3 and the zero interest rate policy. If the FOMC moves in a hawkish direction, a faster tapering of QE3 and a faster to end to the zero interest rate policy are expected.

Including a new Fed Chair, between 7 and 9 voting members of the FOMC could shift between now and 2014.

The 12 voting FOMC members include 7 governors, the New York Fed president, and 4 other Fed presidents.

While all attention has been on the theatrics surrounding President Obama's selection of a new Chairman for the Fed—Larry Summers? Janet Yellen? someone else?—there also will be unusually heavy turnover on the Fed's regular Board of Governors in the coming months. And with the split between the "hawk" and "dove" camps on QE3 and monetary policy becoming ever more notable, there will be an interesting rotation of four different regional Federal Reserve Bank presidents into "voting status" in January 2014. All told, it is likely that at least 7 of the 12 voting members of the FOMC in early 2014 could be different than today, and technically it is possible that as many as 9 of the 12 could be different. With such major shifts in personnel possible, the leanings of the FOMC could easily shift, and this could have significant implications for monetary policy in 2014.

First, Some FOMC Basics

The FOMC has twelve voting members: the seven governors on the Board of Governors (including Chairman Bernanke and Vice Chairman Yellen), the president of the Federal Reserve Bank of New York (William Dudley), and four of the remaining 11 regional bank presidents. The seven governors and the president of the New York Fed are permanent voting members of the FOMC, while four regional presidents vote on an annual rotating schedule. Governor terms are for 14 years each, with terms starting on January 31, 2000, January 31,

Fed Governors serve 14-year terms and represent one of the 12 Federal Reserve regions.

Between 3 and 5 Fed governors could leave before 2014, opening up spots for Obama to fill.

If Obama does not pick Yellen as Fed Chair, he will likely choose at least two women for other governor openings.

2002, January 31, 2004, etc. Usually new Fed governors complete oddly timed remaining terms because governors rarely serve entire 14-year terms. Even the Fed Chairman and Vice Chairman need to have underlying terms as a governor. And no one can be named twice to a new 14-year term. (Alan Greenspan was able to serve as Fed Chairman for 18-1/2 years because he finished out someone else's term for a few years and then he received his own 14-year term.) Nominally, a new incoming Fed governor is supposed to represent one of the 12 Federal Reserve regions, and once another governor is considered to be from that region, that region is no longer available for a second governor. In reality, however, the rules are interpreted loosely. Having lived a region as a child, having gone to university or graduate school in a region, or even having a vacation home in a region are probably sufficient to allow a governor candidate to be considered to represent a certain Fed region. The normal quorum for an FOMC meeting is seven participants.

Openings for Fed Governors

For months, it has been widely assumed that Chairman Bernanke will not seek to be appointed for another term when his Chairman's term is up next January, so that will be one departure. Additionally, two governors have recently resigned—the White House nominated Sarah Bloom Raskin to be Deputy Secretary of the Treasury, and Elizabeth Duke will leave her governor position on August 31st. Also Fed Governor Jerome Powell's term ends in January 2014. Finally, if, say, Yellen is not selected to the Chairman's position, she might resign from the Board to remove any potential friction with a new incoming Chairman. This means that at least three and possibly five of the seven Fed governors could depart by early 2014. It is difficult at this point to know who the new governors might be, or what their views might be. On balance, Obama and his top economic advisers who will be vetting candidates, especially my former boss Gene Sperling, probably lean more in the dove direction than the hawk direction, but new Fed governors often come from technical or academic positions where their views on U.S. macroeconomics may not be well known ahead of time.

One thing to watch, however, is the gender issue. If Yellen is not selected to be Chairman, Obama will almost certainly make sure that at least two governor slots go to women. Women like Christina Romer (former Chair of his Council of Economic Advisers), Lael Brainard (Undersecretary of Treasury for International Affairs), and Sheila Bair (former head of the Federal Deposit Insurance Corporation) would all be logical people for him to consider. Romer would likely be dovish. Brainard would likely be a pragmatist. Bair would almost certainly be hawkish. If Obama does select Yellen, he will probably feel less bound to offer a certain number of governor slots to women.

Four New Voting Members – At Least One Step in the Hawkish Direction

While it is hard *a priori* to know the views of potential incoming governors, the views of the four regional bank presidents who will become voting members of the FOMC are better known. Currently, the presidents of the Boston, Chicago, Kansas City, and St. Louis Federal Reserve Banks have voting status, but they will rotate off at the end of the year. Eric Rosengren (Boston) and Charles Evans

2 doves, 1 hawk, and 1 centrist make up the 4 outgoing Fed presidents.

The 4 incoming Fed presidents are more hawkish compared to the outgoing Fed presidents.

Scheduled to become a voting FOMC member in 2014, the Cleveland Fed president is retiring and her successor has not yet been named.

A move in the hawkish direction will speed up QE3 tapering and result in a quicker end to the Fed's zero interest rate policy.

(Chicago) are seen as two of the more “dovish” officials on the FOMC, meaning that they are more concerned with boosting employment and are more likely to support easy-money policies. On the other hand, Esther George (Kansas City) is considered a strict hawk on the FOMC and has consistently voted against easy-money policies and QE3. James Bullard (St. Louis) is seen as a centrist within the FOMC. He initially disagreed with the Fed's latest round of bond purchases but recently has encouraged the Fed to take its time scaling back its purchases. So call the current configuration 2 doves, 1 hawk, and 1 centrist.

The presidents of the Dallas, Minneapolis, Philadelphia, and Cleveland Federal Reserve Banks will rotate into voting positions on the FOMC in 2014. Richard Fisher (Dallas) is a hawk and has been extremely vocal in his desire to begin tapering the Fed's bond-buying program in September. Additionally, given the recent market volatility in response to Bernanke's statements, Fisher argues that there is a risk of financial instability and bubbles in some financial markets. Charles Plosser (Philadelphia) is also a strict hawk. He also favors the tapering of asset-purchases in September and has urged more commitment to the Fed's “forward guidance” thresholds. On the other hand, Narayana Kocherlakota (Minneapolis) is considered more of a dove and believes that quantitative easing has been effective overall. However, Kocherlakota has also sided with the hawks in the past and has acknowledged that potential financial imbalances could result from the Fed's accommodative monetary policy.

Lastly, Sandra Pianalto, the president of the Cleveland Fed, is scheduled to become a voting member on the FOMC in 2014. However, Pianalto has announced her intention to retire in 2014 and the Cleveland Fed is in the process of forming a search committee to recruit her replacement. Typically the policy views of a departing president (Pianalto) and the bank's Research Director (Mark Schweitzer at the Cleveland Fed), will initially guide a successor. Pianalto is considered a centrist who favors a September start to tapering of the Fed's asset purchases, as long as the labor market continues to improve. She believes that accommodative monetary policy has contributed to economic recovery and wants to keep short-term interest rates low after the Fed's bond-buying program ends.

If Pianalto's successor follows in her footsteps and is a centrist, the FOMC will gain 2 hawks, 1 dove, and 1 centrist. That is, the net shift resulting from the rotation of regional presidents is likely to be one vote in the hawkish direction.

The Bottom Line

The rotation of regional Fed presidents in 2014 is likely to bring one additional net vote in the hawkish direction—toward faster tapering of QE3, and potentially, toward a faster end of the zero interest rate policy. However, given the extraordinary possibility that five of the seven Fed Governors might need to be replaced this autumn and winter, President Obama's selections of Fed Chairman, and other governors will likely dominate the new personality of the FOMC come January.