The Fed’s Rate Moves and Inflation – Video Transcript

Over the past year, the federal funds rate set by the Federal Open Market Committee has gone from near zero in March 2022 to a range of five to five and a quarter percent in May 2023 — a 16-year high.

The Fed has initiated this rapid series of rate increases – the fastest set of increases since the 1980s – in an attempt to slow the economy and bring down red-hot inflation.

The federal funds rate is a benchmark rate that influences other interest rates throughout the economy, such as for mortgages, credit cards, and business loans. A higher federal funds rate typically drives up the cost of borrowing.

When setting monetary policy, the Fed uses a measure of inflation called the Personal Consumption Expenditures Price Index, or PCE.

The Fed’s policy is to allow PCE inflation to rise moderately above 2% for periods of time in order to offset the periods when it is below 2%, with the aim of having inflation average 2% over the long term.

The PCE reading over the past year has been much higher than 2%, though it has been on a downward trend in recent months.

Another common measure of inflation that may be more familiar to people is the Consumer Price Index, or CPI. The CPI measures the average change in prices for a broad variety of consumer goods and services.

The CPI had been relatively low from about 2010 to 2020, but it rose rapidly during the pandemic, hitting a high of 8.0% in 2022 before moderating somewhat in 2023.

After its rapid series of rate increases, the Fed will continue to monitor economic data – including inflation and employment growth, but also likely broadening to bank sector stress and credit conditions – as it determines future moves.

Estimates are based on current conditions, are subject to change, and may not come to pass.