THE FOMC JUNE RATE DECISION

HUGHES ECONOMICS (HE) – June 2023

The forthcoming FOMC rate decision on June 14th is an 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. 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

Latest odds by at least one consultancy for the last two options are 70.5:29.5 or 2.39: 1 in favour of a 25 bps rise over a zero change. Following **HE** methodology, this implies a 2 – 3 or similar range for the "more likely" values for the pairwise value as advocated by T. L. Saaty in his 2008 article *The Analytic Hierarchy and Analytic Network Measurement Processes: Applications to Decisions Under Risk*, **European Journal of Pure and Applied Mathematics**, 1 (1), 122 – 196. Note that estimating pairwise more likely values may be more intuitive for decision-makers than forming odds between two events at a time. The latter is more exact but alternating between the two approaches is, however, straightforward.

Calculation of probabilities is shown in the following table and replicated in **FOMCjune23.xlsx.**

PROBABILITIES ON THE FOMC JUNE 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	0.024	0.012	0.018	2	Base	Base
50 bps	50/75 bps	4.00	5.00	0.098	0.058	0.078	8	4.33	4.00
0 change	0/50 bps	3.00	4.00	0.293	0.232	0.263	26	3.37	3.25
25 bps	25/0 bps	2.00	3.00	0.585	0.698	0.641	64	2.44	2.46
				1.000	**1.000**	**1.000**	**100**		

A 50 bps rise is seen as far more likely than a 75 bps rise with a 4 – 5 times more likely pairwise range. Subsequent pairwise ranges show decreasing more likely values for the higher ranked event over the lower ranked event. The last range of 2 – 3 covers the 2.39 "more likely" value above but could be narrowed to say 2.2 – 2.5. Only 1% changes in probabilities (if any) would result, and the Low and High End distributions give the decision-maker sensitivities to smaller or larger more likely values.

Increasing events to four over just two lowers all probabilities but a 25 bps rise is still a 64% chance here with the High End pairwise distribution probability of 70% for this event. The spread between the Low and High End probability options could help when finalizing event chances. Assigning zero likelihoods to the first two events above increases the probability of a 25 bps rise to 71% using the 2 – 3 pairwise range over no change.