

shopping season.

Market liquidity: slight Con.

6. Leadership transition: Bernanke's term ends January 31. Would he want to be the one to deliver the important forward-looking message that would accompany the initial taper about the future course of policy at the press conference in January and then leave two days later? Bernanke could step down or step aside and let Yellen run the meeting and do the press conference. That could be a bit awkward, but it would also make Yellen's first move one that leads the Committee in a less dovish direction.

Leadership transition: neutral.

7. Bernanke legacy: Does Bernanke want to be remembered as the Chairman that blew up the Fed's balance sheet and then left? Alternatively, would he want to risk being remembered for scuttling the recovery by tapering prematurely? Probably not important in Bernanke's case--has striven to diminish the cult of the chairmanship.

Legacy: neutral.

As I add up the pros and cons for a December taper, this is a very close one; it is quite possible they have not made any decisions yet, and that the CPI inflation data on Tuesday could still tip the scale. At this point, I am now leaning slightly in favor of a December taper. This is not a consensus view, though I note that our US Economics team has been more consistently projecting a December taper.

If they do taper, I expect it to be a taper light, on the order of \$5 to \$15 bn (skewed more toward Treasuries than MBS). This would be accompanied by a statement that is relatively dovish--i.e., that reinforces the message that they expect rates to be held at very low levels for quite some time to come. There are a number of ways they could do this. Here is my top ten list of the things they could do in this regard, starting with the least likely and ending with the most likely:

10) Lower unemployment threshold from 6.5%. The October minutes and some FedSpeak have suggested this is not likely--the 7.0 and even 6.5 numbers have created communication problems as it is. (likelihood: 15%)

9) Reduce interest on excess reserves. This got more support at the October meeting, but my sense it is not a high probability. (25%)

8) Provide weak calendar forward guidance: for example, "we expect the first rate hike is at least one year away." Possible, but I do not expect the FOMC to revert to calendar-based guidance. (25%)

7) Add a specific inflation floor. There may be more support here, but still problematic. A floor of 1.5% does not say much, a floor of 2.0 would be too high for many members, and a floor of 1.75 would be shaving things pretty finely. (35%)

6) Lower their projections for the fed funds rate for the coming years. Marking down the endpoint for the fed funds path several years out (per #5 below) would allow them to revise down their interest rate forecasts for earlier periods as well. This could be a significant message, especially if they reduce their forecast for unemployment. (60%)

5) Lower their projections for the neutral level of the fed funds rate in the longer term based on downward revisions to potential growth estimates. (60%)

4) Point out (again) that their actions could be reversed if financial markets react negatively enough to put the economic expansion at serious risk. (75%)

3) Note that they are comfortable with the apparent success of their verbal