

Minutes of the MONETARY POLICY ADVISORY PANEL

Meeting of March 28, 2014

Present - Panelists: Markus Brunnermeier, Peter Diamond, Mark Gertler, Simon Gilchrist, Nobuhiro Kiyotaki, Frederic Mishkin, Ricardo Reis, Christopher Sims, Michael Woodford. Internal Staff: Tobias Adrian, Stefania Albanesi, Christine Cumming, William Dudley, Marc Giannoni, Tom Klitgaard, Jamie McAndrews, Jonathan McCarthy, Richard Peach, Paolo Pesenti, Matthew Raskin, Julie Remache, Robert Rich, Argia Sbordone, Andrea Tambalotti.

The roundtable discussion largely focused on two issues: an assessment of the change from quantitative guidance to qualitative guidance in the March FOMC statement, and the appropriate monetary policy framework for setting and communicating the path of interest rates as employment and inflation move closer to the FOMC objectives. The panelists also discussed and offered their views on other current economic issues.

Evaluation of the change in forward guidance

Panelists noted that the 6.5% unemployment threshold for assessing raising the federal funds rate target had become less effective and thus were not surprised by the change in the statement. However, they indicated that they had not anticipated that the new statement would change expectations of the policy rate path. Their impression was that the qualitative guidance in the March statement, combined with the federal funds rate forecasts in the Summary of Economic Projections (SEP), contributed to the perception of a possible change in policy toward an earlier tightening.

Panelists noted that the SEP should be de-emphasized for communicating the FOMC's view, as it reflects individual opinions and not a consensus view, and the Committee should reiterate the importance of the statement as a principal tool for communication. They also stated that it would be better to produce a monetary policy report, following the practice at some other central banks, which would allow for a more detailed explanation of the Committee's rationale for policy decisions and their view about the outlook. However, several panelists noted the practical issues associated with producing a monetary policy report under the Federal Reserve's institutional structure and thus suggested that alternative methods to address communication issues may have to be pursued instead.

Some panelists drew attention to governance issues, noting that individual Committee members' communications to the media to highlight their individual views may raise uncertainty about the FOMC's policy stance and thus could impair the effectiveness of Committee communication.

Panelists suggested that it would be preferable at this point to switch the focus of guidance away from the unemployment rate to inflation. In light of the considerable uncertainty about the natural rate of unemployment and the likelihood that the continuing experience of low inflation and elevated unemployment are caused by common economic forces, panelists saw communication in terms of inflation as potentially less difficult and more effective.

Guidance as the economy approaches FOMC objectives

One question raised during the discussion was about how long short-term rates should stay low as employment and inflation approach the FOMC objectives. The presence of persistent headwinds and stronger demand for precautionary savings were among the reasons cited for maintaining rates lower than their historical level for quite some time.

Panelists pointed out that most private sector and SEP forecasts appear optimistic and do not seem consistent with the presence of headwinds. One panelist added that it may be difficult to distinguish headwinds from the slow recoveries typical after financial crises. Moreover, firms may have adopted a wait and see approach and this may be behind the low investment spending, although it is possible to have a fast resurgence under the right conditions. Panelists pointed to actual and expected inflation as important gauges to assess the presence and magnitude of slack or headwinds for the medium run outlook.

Panelists noted that fiscal concerns could become more prominent for monetary policy once rates begin to rise, as federal government expenditures for debt service would increase quite sharply. This potential development might generate pressure on the conduct of monetary policy.

Panelists pointed to a perception that low inflation is not a significant concern for the Committee. They argued that raising the status of the low inflation problem would allow monetary policy to be accommodative for longer, given the uncertainty on real side indicators. Low job creation and very limited inflation pressures are consistent with the low inflation outcome.

Other issues

The discussion also touched on a few other topics. One was a view that the effects of monetary policy impulses diminish over time because they largely consist in an inter-temporal shift of expenditures. Other panelists cited risks to the economic outlook that were largely external to the U.S., such as the crisis in Ukraine and ongoing concerns about the fragility of the recovery in Europe.