

MONETARY POLICY PANEL
Luncheon Meeting, October 11, 2013

AGENDA

A year since LSAP3: a perspective on outcome-based policy and FOMC communication

Background

In the latter part of 2012, the FOMC made two notable monetary policy decisions. First, it launched a third round of asset purchases in September 2012: unlike previous rounds, this one was open-ended and *outcome-based*. Second, in December it replaced the calendar-based forward guidance of the policy rate with outcome-based guidance through the announcement of economic thresholds to guide the timing of lift-off.

No explicit numerical thresholds were set for the asset purchase program in the FOMC statements, as the duration of the program was tied to the outlook for the labor market improving substantially. At his June press conference, Chairman Bernanke provided further information about the purchase program by presenting a contingent plan for purchases based on incoming economic data being broadly consistent with the Committee's expectations at that time.

Since the last meeting of this Panel in April, amid mixed signals on economic and labor market conditions (see figures 1 and 2), FOMC communications -- in particular Chairman Bernanke's May 22 JEC testimony and his remarks at the June FOMC press conference -- generated significant market reaction (see figures 3 and 4). The September "not to taper" decision also led to market movements, this time in the opposite direction, as well as considerable commentary in the media.¹

At this meeting we would like to discuss various interpretations of these market reactions, the role of Fed communication in these reactions, and the implications for policy going forward.

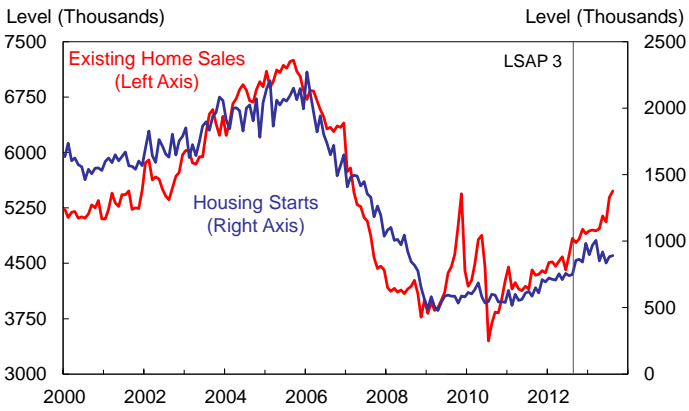
¹ See among others, Jim Hamilton ([Econbrowser, Sept 29](#)), Ed Lazear ([WSJ, Sep. 30th](#)), James Stewart ([NYT, Sep. 27](#))

Questions for Discussion

- Do you interpret the September 2013 policy decision as consistent with the illustrative scenario laid out at the June press conference and the economic and financial market developments since then?
- The September [Summary of Economic Projections \(SEP\)](#) presented for the first time the FOMC participants' economic and federal funds rate projections for 2016. For most participants, the 2016 inflation and unemployment rate forecasts appear to be close to their longer-run projections for those variables, but the federal funds rate forecasts are below the longer-run projections. How could this pattern be interpreted?
- Communication Issues
 - The FOMC statement has gradually increased in length; and this feature alone might cause market participants to settle on different interpretations of its meanings. What suggestions do you have for improving the statement?
 - With a large and diverse FOMC, what suggestions would you propose to deliver a more unified message from the Committee, while preserving the multiplicity of views?
 - The SEP: what are its strengths and weaknesses? What changes would you recommend?
- What other recommendations would you make regarding the policy framework?

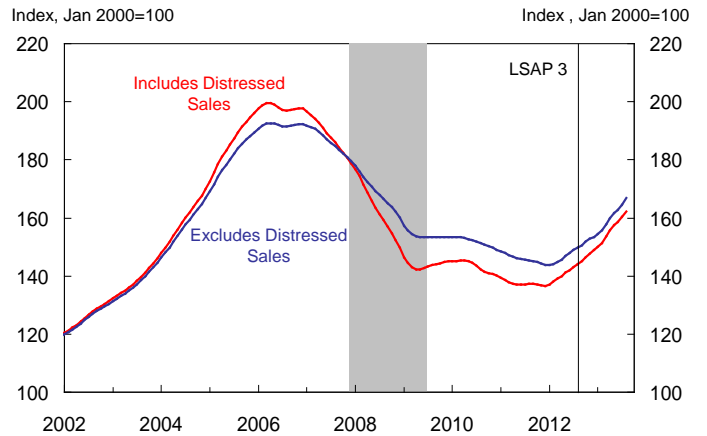
Figure 1: Recent Economic Indicators

Housing Starts and Existing Home Sales



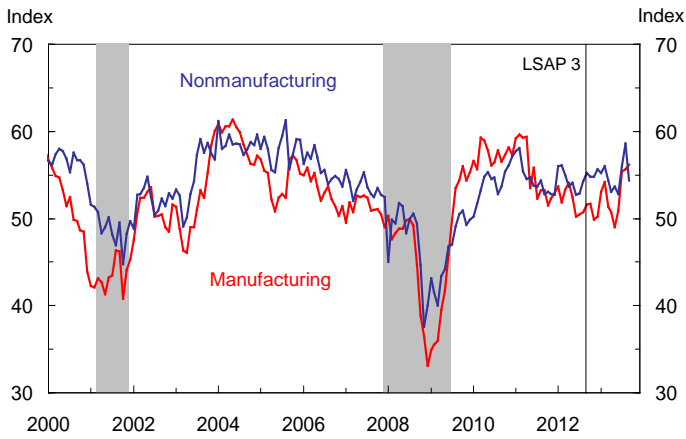
Source: National Association of Realtors, Census Bureau

CoreLogic National Home Price Index



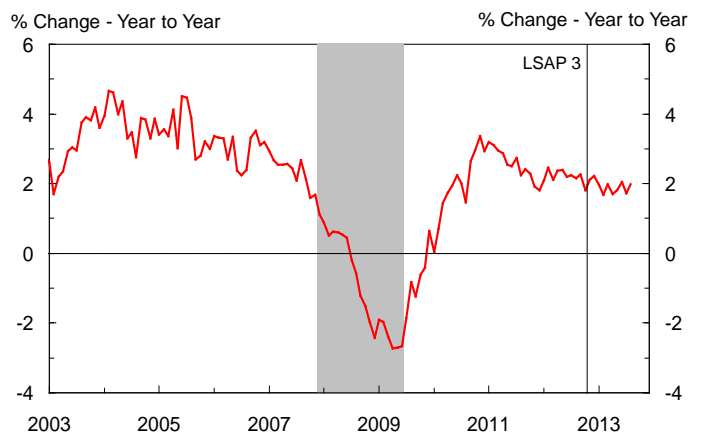
Source: CoreLogic/Haver Analytics

ISM Main Indices



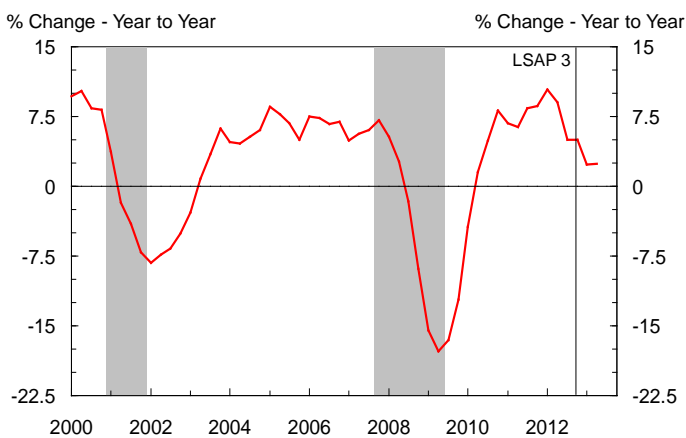
Source: Institute for Supply Management

Real Personal Consumption Expenditures



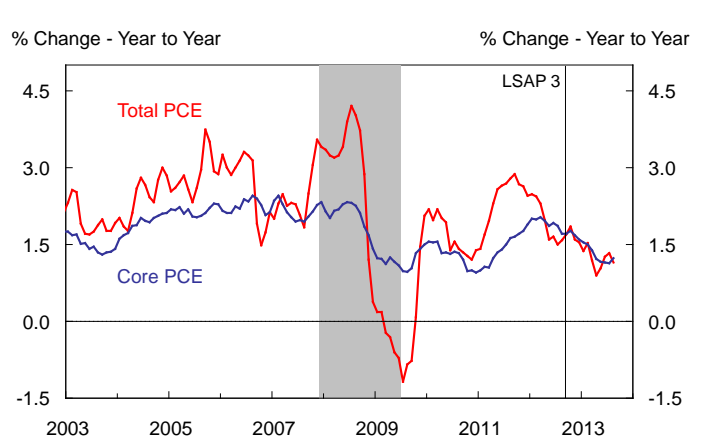
Source: Bureau of Economic Analysis

Business Fixed Investment



Source: Bureau of Economic Analysis

Total and Core PCE Deflator



Source: Bureau of Economic Analysis

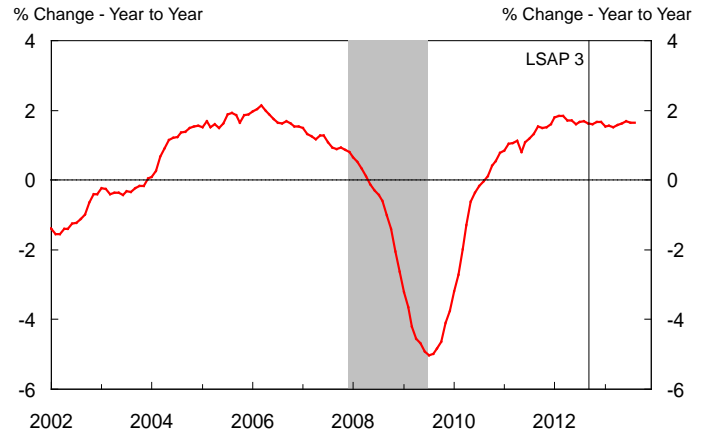
Note: Shading represents NBER recessions, unless otherwise noted.

Figure 2: Labor Market Situation

Indicators of Labor Market Demand

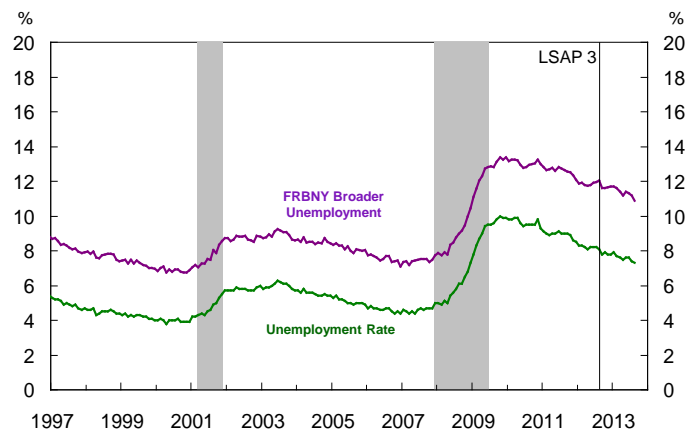
Key Indicators	Pre-LSAP 3 01/2012-09/2012	Post-LSAP 3 10/2012-Current	Current	Pre-recession 01/2004-12/2007
Payroll Employment Change (thousands)	174	188	169	160
Job-to-Job Transition Rate	1.57	1.57	1.57	2.17
Quits Rate (JOLTS)	1.58	1.62	1.7	2.1
Vacancy Rate (JOLTS)	2.6	2.7	2.6	3.0
Hires Rate (JOLTS)	3.3	3.2	3.2	3.9
Job-Finding Rate (CPS)	18.2	18.8	19.5	26.9
Vacancy to Unemployment Ratio	0.32	0.35	0.36	0.60

Total Nonfarm Payroll Growth



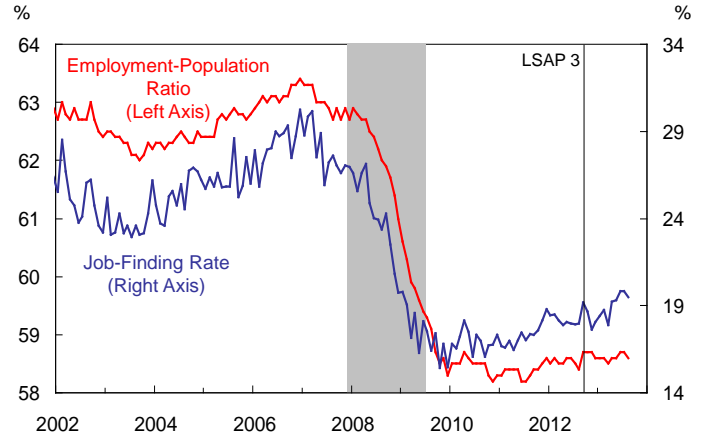
Source: Bureau of Labor Statistics

Unemployment Rate



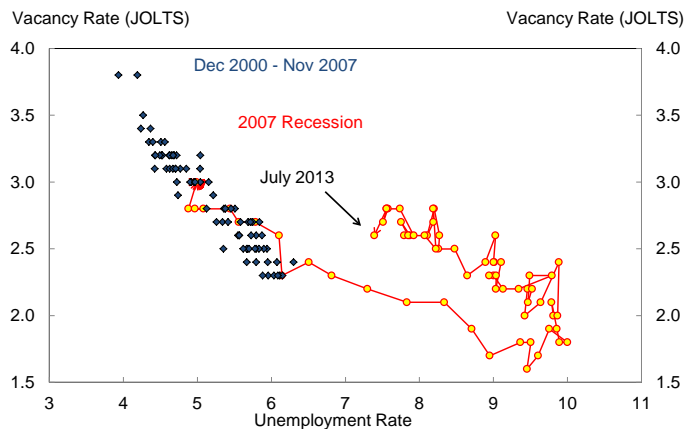
Source: Bureau of Labor Statistics, FRBNY Calculations

Employment-Population Ratio & Job-Finding Rate



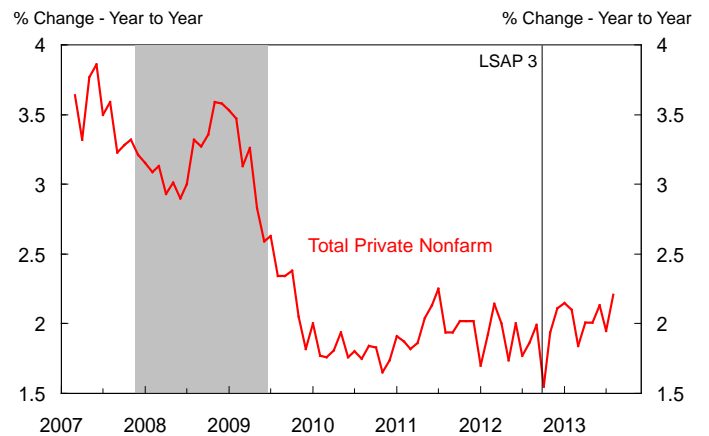
Source: Bureau of Labor Statistics, FRBNY Calculations

Beveridge Curve



Source: Bureau of Labor Statistics

Average Hourly Earnings

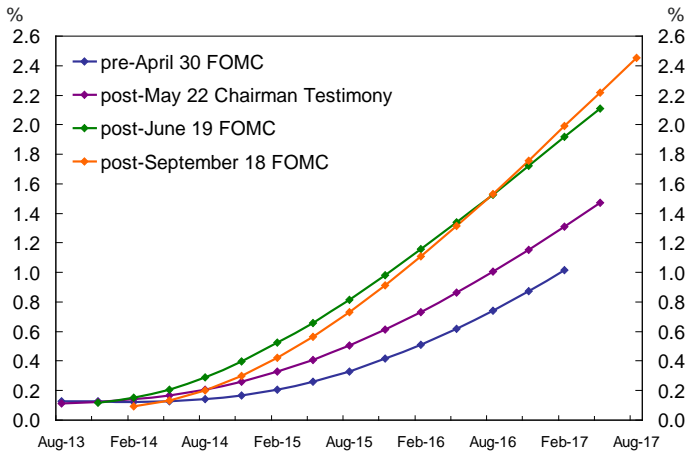


Source: Bureau of Labor Statistics

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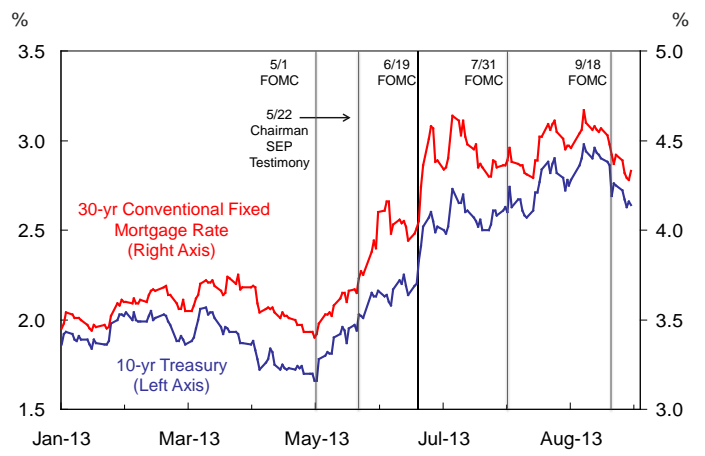
Figure 3: Financial Market Movements

OIS-Based Expected Fed Funds Rate



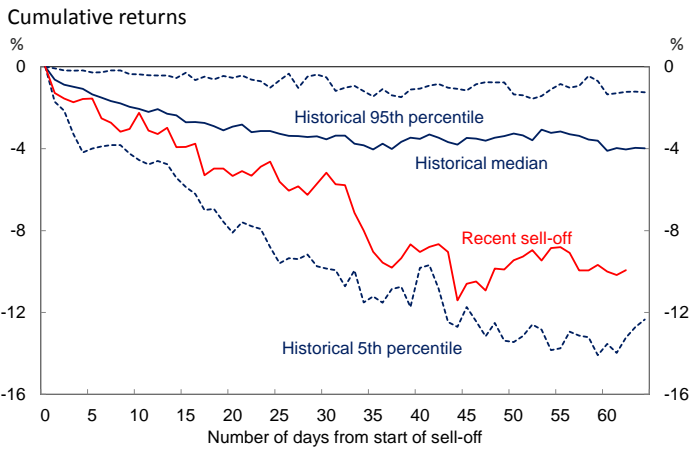
Source: Federal Reserve System

10-year Treasury & 30-year Fixed Mortgage Rates



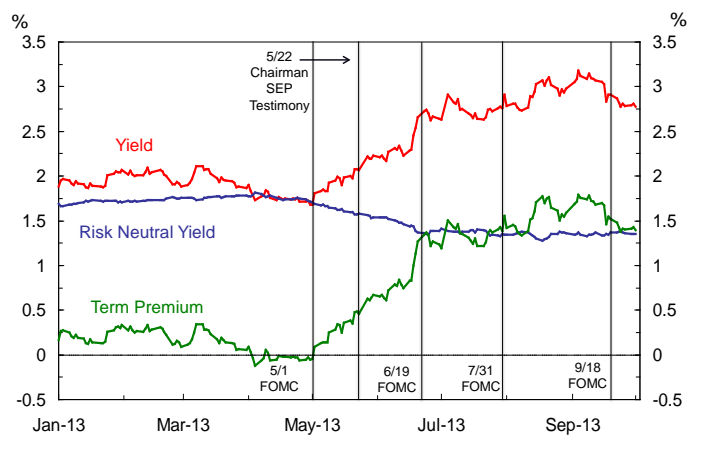
Source: Bloomberg, Federal Reserve Board of Governors

The Recent Bond Sell-off in Historical Perspective



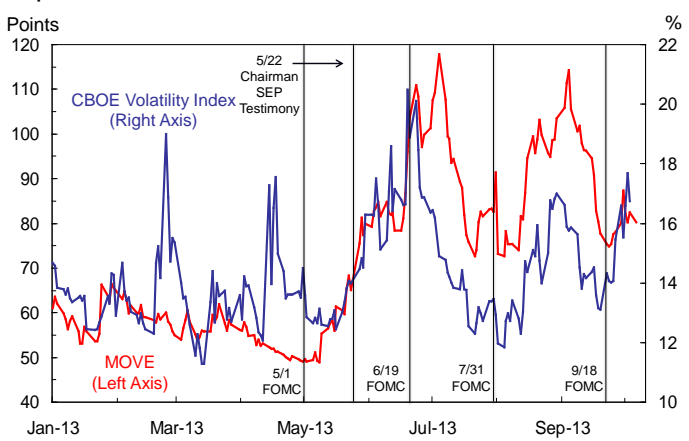
Source: Federal Reserve Board Note: Distribution of returns for sell-offs between 06/14/61 and 07/31/13

10-year Nominal Yield Decomposition



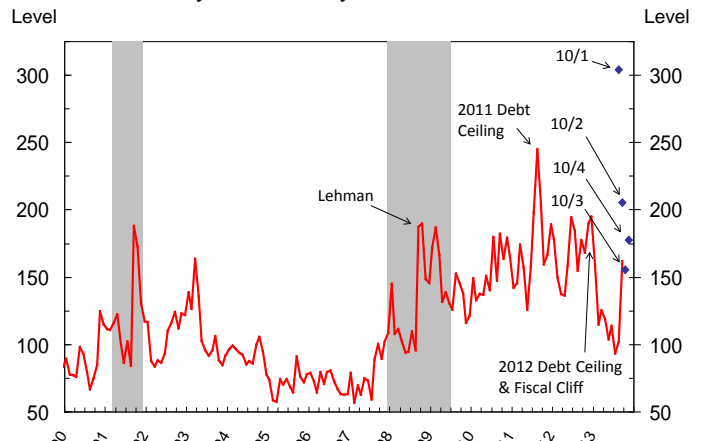
Source: FRBNY Calculations

Implied Volatilities



Source: Chicago Board Options Exchange, Bank of America Merrill Lynch

Economic Policy Uncertainty Index

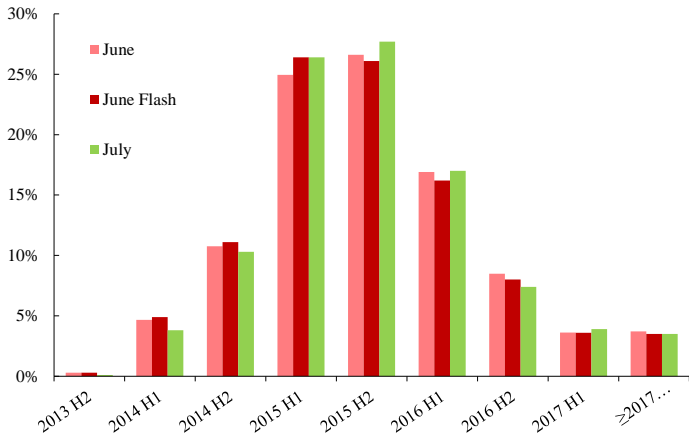


Source: Policyuncertainty.com

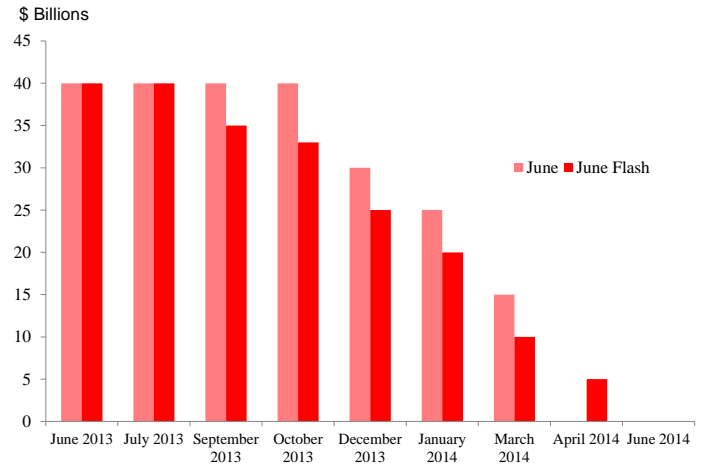
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Figure 4: Primary Dealers' Expectations¹

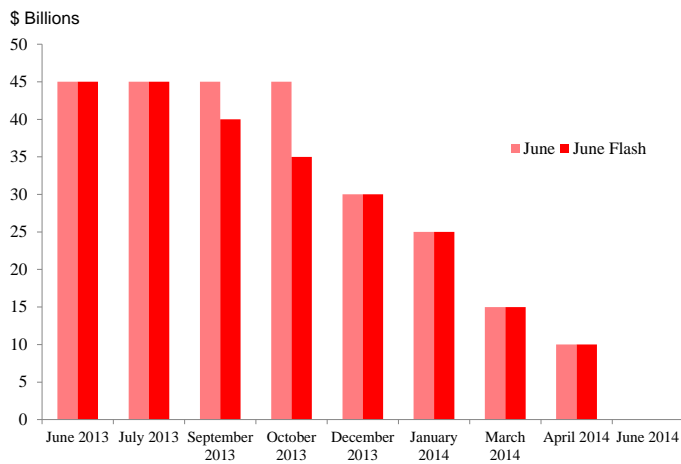
Average Probability Distribution of First Fed Funds Target Rate Increase



Median Monthly MBS Purchase Size



Median Monthly Treasury Purchase Size



¹ Survey of Primary Dealers, Markets Group, Federal Reserve Bank of New York
 June survey was taken on 6/10. June Flash survey was taken on 6/24.