Minutes of the MONETARY POLICY PANEL

Meeting of September 21, 2012

Present: External advisors: Markus Brunnermeier, Mark Gertler, Nobuhiro Kiyotaki, Frederic Mishkin, Ricardo Reis, Michael Woodford. Internal Staff: Tobias Adrian, James Bergen, Christine Cumming, Marco Del Negro, William Dudley, Gauti Eggertsson, Marc Giannoni, Krishna Guha, Tom Klitgaard, Jamie McAndrews, Jonathan McCarthy, Meg McConnell, Paolo Pesenti, Simon Potter, Argia Sbordone, Andrea Tambalotti.

The roundtable discussion developed around the main items laid out in the meeting Agenda, the reaction to the policy decisions laid out in the September FOMC meeting statement and the policy issues raised by those decisions, and possible alternatives for the FOMC to improve its communication.

Monetary Policy After the September FOMC Decision

The MPP members first discussed the September FOMC statement and its impact on markets. The panelists welcomed the shift in the statement's focus towards taking actions until there is sufficient progress in achieving objectives, as they believe it enhances the effectiveness of the policy stance. Many also noted approvingly that the policy strategy was multi-pronged. Looking forward, some panelists mentioned that optimal policy in many models may lead to a temporary overshooting of the long-run inflation objective. They thus noted that a policy challenge is to communicate such a possibility without allowing long run inflation expectations becoming unanchored. Panelists commented on options to meet that challenge, focusing on nominal income and price level targeting. There was also a more general brief discussion of time versus state contingent commitment. Some panelists argued that from the investors' perspective a time commitment is safer, in the sense that it removes uncertainty, but others pointed out that shifting the calendar date has possibly raised market uncertainty. Many agreed that time commitment can be useful when used together with state-contingent language.

The panelists then discussed whether the FOMC could be more explicit about the benchmarks to gauge whether labor market conditions have improved substantially, and whether explicit benchmarks are indeed desirable. Some panelists suggested that a single number – for example, a threshold for unemployment – would not be appropriate, and most panelists agreed that it may be better for the FOMC to focus on overall labor market conditions, including not only several labor market indicators, but also forecasts for variables such as GDP that are likely to related to labor market conditions.

The discussion then focused on policy options if economic conditions do not improve quickly enough. On the possibility of nominal GDP targeting, the panelists discussed the challenge in explaining to the public that the FOMC's objective is real rather than nominal growth, but noted that, relative to a price level targeting policy, nominal GDP targeting better reflects the FOMC's dual mandate. Panelists debated the extent to which the current FOMC statement has incorporated a nominal GDP target policy as well as the potential problems of an explicit nominal GDP targeting if uncertainty and variations in potential real growth lead to inflation straying well away from its longer-run objective.

Discussing other potential policy tools, one panelist proposed to consider programs to promote credit expansion, such as those recently implemented by the Bank of England. Other panelists noted that these programs imply that the central bank would take on some credit risk. Furthermore, it is also not clear which problems any such programs would address, since there currently do not seem to be term funding problems for banks in the US.

Panelists then debated why the state of the economy remains weak despite accommodative monetary policy, and in particular whether that is due to stronger than expected headwinds or to an impaired transmission mechanism. This debate also raised the issue of our understanding about how monetary policy operates in the current environment. Panelists generally agreed that policy has been effective, but growth after a financial crisis may remain weak for a longer period because of the enduring damage the crisis imposed on the economy.

Asked whether low interest rates policy is punishing savers, therefore undermining the recovery as these households reduce consumption, panelists noted that while demand may well go down for some households, aggregate demand should nonetheless increase. It was however noted that while low interest rates are hurting only savers that are not holding a diversified portfolio, there are re-distributional issues associated with the current policy.

Development of an FOMC consensus forecast

In the last part of the meeting the discussion turned to the desirability and feasibility of developing an FOMC consensus forecast. The panelists agreed that the Summary of Economic Projections (SEP) does not adequately express the view of the FOMC, and that developing a consensus forecasts could improve communication. There was general agreement that for a consensus forecast FOMC participants should express their outlook assuming a common policy path, rather than assuming a policy that each individual deems appropriate, as in current SEP practice. However, most of the panelists thought that the FOMC participants should have the opportunity to express their dissent both from the consensus forecast and from the policy stance underpinning it.