Minutes of the Investor Advisory Committee on Financial Markets

October 5, 2017

Federal Reserve Bank of New York

Committee attendees:

William A. Ackman, Pershing Square
James Chanos, Kynikos Associates
Mary Callahan Erdoes, J.P. Morgan Asset Management
Dawn Fitzpatrick, Soros Fund Management
Vicki Fuller, Office of the New York State Comptroller
Britt Harris, The University of Texas/Texas A&M Investment Management Company
Joshua Harris, Apollo Management
Bob Jain, Millennium Management
Scott Minerd, Guggenheim Partners
Rebecca Patterson, Bessemer Trust
Rick Rieder, BlackRock, Inc.
John W. Rogers, Jr., Ariel Investments
David Tepper, Appaloosa Management L.P.
Paul Tudor Jones, Tudor Investment Corp.

FRBNY and Federal Reserve Board attendees:

William Dudley, Chair
Sarah Bell
John Clark
David DeCarlo
James Egelhof
Michael Held
Beverly Hirtle
Matthew Lieber
Meg McConnell
Michael Nelson
Simon Potter
Matthew Raskin
Seth Searls
Kevin Stiroh
Michael Strine
Benedict Wensley

Domestic Developments

Committee attendees discussed the September FOMC statement, press conference, and Summary of Economic Projections, as well as how these communications shaped market participants' views on normalization of the Federal Reserve's balance sheet. Several committee attendees suggested that market participants believe the FOMC will proceed with a path of policy rate increases that continues to provide accommodation, even as it proceeds with normalizing the Federal Reserve's balance sheet. Several committee attendees also indicated that clear communication from Federal Reserve officials about the gradual and predictable reduction of its reinvestments would tend to reduce any upward pressure on interest rates from normalization. In addition, several committee attendees pointed out that continuing accommodation from foreign central banks would continue to put downward pressure on both foreign and domestic interest rates.

Global Developments

Committee attendees discussed the recent trend and outlook for U.S. and global inflation. Several committee attendees suggested that global inflation has been suppressed by an accelerating pace of technological improvement, which has increased the effective supply of goods and services. In addition, some committee attendees argued that technological improvements may be leading to increasing downward measurement bias on actual inflation. Several committee attendees suggested that both these factors would tend to reduce their outlooks for inflation over the next several years. However, some committee attendees pointed out that wage inflation in the U.S. has risen more than goods inflation, as the labor market has tightened. Some committee attendees also contrasted inflation for services, which has risen above the Federal Reserve's two percent objective for overall inflation, with goods inflation, which remains below the overall target.

Committee attendees next discussed how recent political and economic developments have changed their assessments of risk to their economic outlooks. Some committee attendees suggested that financial imbalances, such as nonfinancial corporate and government debt burdens, pose a downside risk to their economic growth outlooks. Some committee attendees also suggested that investors' complacency about central banks maintaining easy monetary policies or their complacency about low volatility in financial markets pose downside risks. Some committee attendees suggested that potential changes in U.S. tax and regulatory policies present upside risks to their growth outlooks. Other potential risks cited by individual committee members included: changes in the leadership of the Federal Reserve, the politicization of monetary policy, central banks tightening too quickly despite low inflation, central banks tightening too slowly despite financial imbalances, fiscal authorities crowding out private investment, a structural change in inflation dynamics, investor complacency about low oil prices, an increase in industry concentration, and cyber attacks.

Committee attendees also discussed factors driving the U.S. dollar's depreciation year-to-date. They generally attributed the dollar's depreciation to a flattening in the expected path of the domestic policy rate, which they saw as driven, in turn, by reduced expectations for fiscal stimulus in the U.S., as well as relatively subdued inflation pressures. Committee attendees noted that the dollar could strengthen if fiscal stimulus was passed and the expected path of the policy rate increased relative to expectations for interest rate increases in the rest of the world. In contrast, they suggested that the dollar could weaken further if no fiscal stimulus was passed and foreign central banks tightened monetary policy at a similar pace as the Federal Reserve.

Financial Landscape

Committee attendees discussed whether the prolonged period of historically low interest rates may have created distortions in financial markets. They discussed the current levels of U.S. corporate debt, equity market valuations, corporate credit spreads, U.S. households' net worth, and the U.S. federal budget deficit. Some committee attendees argued that central banks should aim to increase real interest rates in a fashion that is not entirely predictable to market participants; they suggested that less transparency over the path of rate increases would serve to increase market risk premiums to more sustainable levels.