

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Date: December 1, 2016
To: Federal Open Market Committee
From: David Wilcox, Steven Kamin, and Thomas Laubach
Subject: Two Memos on the Labor Market as it Approaches Full Employment

The attached two memos address issues that are relevant as the labor market approaches full employment. The first memo, “Ramifications of Allowing the Unemployment Rate to Undershoot Its Natural Rate,” prepared by Stephanie Aaronson (R&S), Andrea De Michelis (IF), Cynthia Doniger (MA), Charles Fleischman (R&S), Manuel Gonzalez-Astudillo (R&S), Stacey Tevlin (R&S), and Joyce Zickler (MA), examines issues related to the fact that, in both the Summary of Economic Projections (as summarized by the medians) and the staff’s Tealbook forecast, the unemployment rate falls below its assumed long-run sustainable level. One question examined in the memo is whether a “soft landing” (that is, a smooth return of the unemployment rate to near its sustainable level) has ever been achieved in history; another question is whether periods of undershooting in the past have been associated with undesirable consequences such as unwanted increases in inflation or increases in financial imbalances; a third issue is whether periods of very low unemployment have had demonstrable positive effects on the functioning of the labor market.

The second memo, “Labor Market Slowing and Supply Constraints,” prepared by Hie-Joo Ahn (R&S) and David Ratner (R&S), explores the role of labor supply constraints in contributing to the slowdown in labor market improvement in 2016.

If you have any questions about the contents of these memos, please feel free to contact the authors of the memo directly or any of the three of us.