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U.S. Economic Outlook and Monetary Policy

Remarks by

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at

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Thank you for the opportunity to participate in this CFA Institute conference on fixed-income management. Before we begin our conversation, I would like to share a few thoughts about the outlook for the U.S. economy and monetary policy.¹

The U.S. economy is in a good place, and the baseline outlook is favorable. The median expectation from Federal Open Market Committee (FOMC) participants' most recent Summary of Economic Projections is for GDP growth to be around 2 percent in 2019, for growth to continue near this pace next year, and for personal consumption expenditures (PCE) inflation to rise gradually to our symmetric 2 percent objective.² The unemployment rate, at 3.5 percent, is at a half-century low, and wages are rising broadly in line with productivity growth and underlying inflation. There is no evidence to date that a strong labor market is putting excessive cost-push pressure on price inflation.

But despite this favorable baseline outlook, the U.S. economy confronts some evident risks in this the 11th year of economic expansion. Business fixed investment has slowed notably since last year, exports are contracting on a year-over-year basis, and indicators of manufacturing activity are weakening. Global growth estimates continue to be marked down, and global disinflationary pressures cloud the outlook for U.S. inflation.

U.S. inflation remains muted. Over the 12 months through August, PCE inflation is running at 1.4 percent, and core PCE inflation, which excludes volatile food and energy prices, is running at 1.8 percent.

¹ These remarks represent my own views, which do not necessarily represent those of the Federal Reserve Board or the Federal Open Market Committee. I am grateful to Brian Doyle of the Federal Reserve Board staff for his assistance in preparing this text.

² The most recent Summary of Economic Projections is an addendum to the minutes of the September 2019 FOMC meeting. See Board of Governors of the Federal Reserve System (2019), "Minutes of the Federal Open Market Committee, September 17–18, 2019," press release, October 9, <https://www.federalreserve.gov/newsevents/pressreleases/monetary20191009a.htm>.

Turning now to monetary policy, at both its July and September meetings, the FOMC voted to lower the target range for the federal funds rate by 25 basis points.³ With these decisions, the current target range for the federal funds rate is 1.75 to 2 percent, which compares with the range of 2.25 to 2.5 percent that prevailed between December 2018 and July 2019. The Committee took these actions to provide a somewhat more accommodative policy in response to muted inflation pressures and the risks to the outlook I mentioned earlier.

Looking ahead, monetary policy is not on a preset course, and the Committee will proceed on a meeting-by-meeting basis to assess the economic outlook as well as the risks to the outlook, and it will act as appropriate to sustain growth, a strong labor market, and a return of inflation to our symmetric 2 percent objective.

Turning now to the framework under which the Federal Reserve operates in financial markets, in September of this year, shocks in the repurchase agreement (repo) market put upward pressure on money market rates, and these pressures spilled over into the federal funds market. In response to these developments, the Federal Reserve on September 17 initiated a program of repurchase operations to provide liquidity sufficient to keep the federal funds rate within the desired target range. These operations have been successful in achieving this goal.

As the FOMC announced in January 2019, the Committee seeks to operate with a level of bank reserves that is sufficiently ample to ensure that control of the federal funds

³ See Board of Governors of the Federal Reserve System (2019), “Federal Reserve Issues FOMC Statement,” press release, July 31, <https://www.federalreserve.gov/newsevents/pressreleases/monetary20190731a.htm>; and Board of Governors of the Federal Reserve System (2019), “Federal Reserve Issues FOMC Statement,” press release, September 18, <https://www.federalreserve.gov/newsevents/pressreleases/monetary20190918a.htm>.

rate is achieved primarily by the setting of our administered rates and is not, over the longer term, reliant on frequent and large open market operations.⁴ In July, the FOMC concluded the program of balance sheet reduction in place since October 2017 and indicated then that, after a time, it would commence increasing its securities holdings to maintain reserves at a level consistent with an ample-reserves regime.

The FOMC announced on October 11 that it would seek to maintain, over time, a level of bank reserves at or somewhat above the level that prevailed in early September, a level that we believe is sufficient to operate an ample-reserves regime.⁵ This week, the Federal Reserve Bank of New York began a program of purchasing Treasury bills in the secondary market. This program will continue at least into the second quarter of next year and is designed to achieve—and, over time, maintain—ample reserve balances at or above the level that prevailed in early September. In addition, the Federal Reserve will continue to conduct term and overnight repo operations at least through January to ensure that the supply of reserves remains ample even during periods of temporary, but pronounced, increases in our nonreserve liabilities, and to mitigate the risk that money market pressures adversely affect monetary policy implementation.

It is important to note that the open market operations we have announced are technical, “Central Banking 101” operations and should not be conflated with the large-scale asset purchase programs that the Federal Reserve deployed after the financial crisis. In those programs, the Federal Reserve was seeking to ease financial conditions by

⁴ See the Statement Regarding Monetary Policy Implementation and Balance Sheet Normalization, which is available on the Board’s website at

<https://www.federalreserve.gov/newsevents/pressreleases/monetary20190130c.htm>.

⁵ See the Statement Regarding Monetary Policy Implementation, which can be found on the Board’s website at <https://www.federalreserve.gov/newsevents/pressreleases/monetary20191011a.htm>.

lowering term premiums via its purchases of long-term Treasury bonds and mortgage-backed securities. By contrast, the program announced on October 11 will concentrate its purchases in Treasury bills. The technical measures we are undertaking do not represent a change in the stance of monetary policy, which we continue to implement by adjusting the target range for the federal funds rate.

Finally, I would like to say a few words about the monetary policy framework review we are undertaking this year. This review of our monetary policy strategy, tools, and communications is the first of its kind for the Federal Reserve. Public engagement, unprecedented in scope for the Fed, is an important part of this effort. Through our *Fed Listens* events, we have been hearing a diverse range of perspectives not only from academic experts, but also from representatives of consumer, labor, business, community, and other groups. We will draw on these insights as we assess how best to achieve and maintain maximum employment and price stability in the most robust fashion possible. In July, we began discussing issues associated with the review at our FOMC meetings. We will continue reporting on our discussions in the meeting minutes and share our conclusions when we finish the review during the first half of next year.⁶

Thank you very much for your attention.

⁶ Information about the review and the events associated with it are available on the Board's website at <https://www.federalreserve.gov/monetarypolicy/review-of-monetary-policy-strategy-tools-and-communications.htm>.