

Implementing Macroprudential and Monetary Policies: The Case for Two Committees

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The Issue:

- Revival of macroprudential policy in advanced economies
- Important interactions with monetary policy
- What is the best governance structure?
 - » Generally
 - » Within Federal Reserve

Monetary and Macroprudential Policies

- Shared long-term goal: sustained growth
 - » But different primary goals
- Both work through financial conditions
 - » But different tools
 - Monetary: interest rates and central bank portfolio
 - Macroprudential: capital, liquid assets, activities, terms of lending

And Different Focus

- Macroprudential policy
 - » Externalities and tail risks
 - » Financial cycle
 - » Particular market segments
- Monetary policy
 - » Central tendency for economy
 - » Business cycle
 - » Broad effects

Monetary Policy and Financial Stability

- Policy “leaning”
 - » But: Effectiveness? Cost?
- Cost-benefit
 - » Monetary: stable prices and full employment
 - » Macroprudential: financial stability
- Monetary policy: “last line of defense” for financial stability

Two-Committee Approach

- Two committees each focused on own mandate and own tools
- Facilitates accountability
- Dealing with interactions and interdependence

In the Federal Reserve

- Two committee structure
 - » Board of Governors: macroprudential
 - » FOMC: monetary policy
- Reinforced by reserve bank governance structure
- Potential complication: using the Fed portfolio to foster financial stability

In the United Kingdom

- Two Committees
 - » Monetary Policy Committee
 - » Financial Policy Committee
- Different primary objectives
 - » Price stability; financial stability
- Same secondary objective
 - » Support policies of the government

MPC/FPC Interactions

- Building resilience early in the recovery
- MPC forward guidance knockout
- Housing risks

Deficiencies in the United States: Where is the “Last Line of Defense?”

- Governance problems
 - » Disconnect: perceived responsibility and authority
 - » Coordination across Balkanized regulatory structure
 - » FSOC: helpful, but limited authority and subject to political pressures

Deficiencies (2)

- Tools
 - » Structural emphasis
 - » Lack of real estate tools
 - Sectoral capital requirements
 - Limits on LTV and LTI

What is to be done?

- Legislation unlikely
- Stock take
 - » What are the available authorities?
Gaps?
 - » Involve all key agencies
 - » Change the conversation