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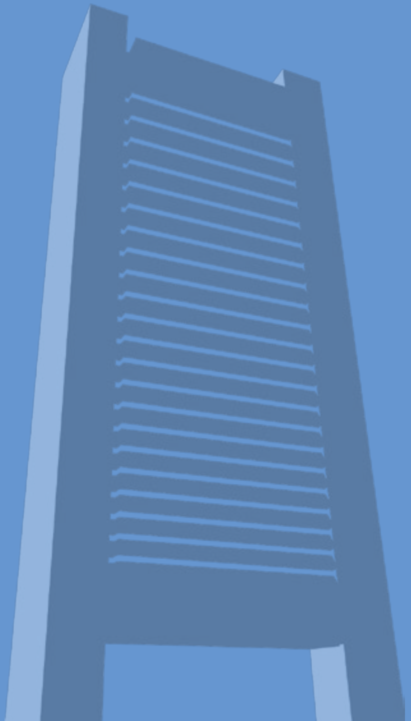

Current Economic Conditions and the Implications for Monetary Policy

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bostonfed.org

Evolving Views on Appropriate Monetary Policy

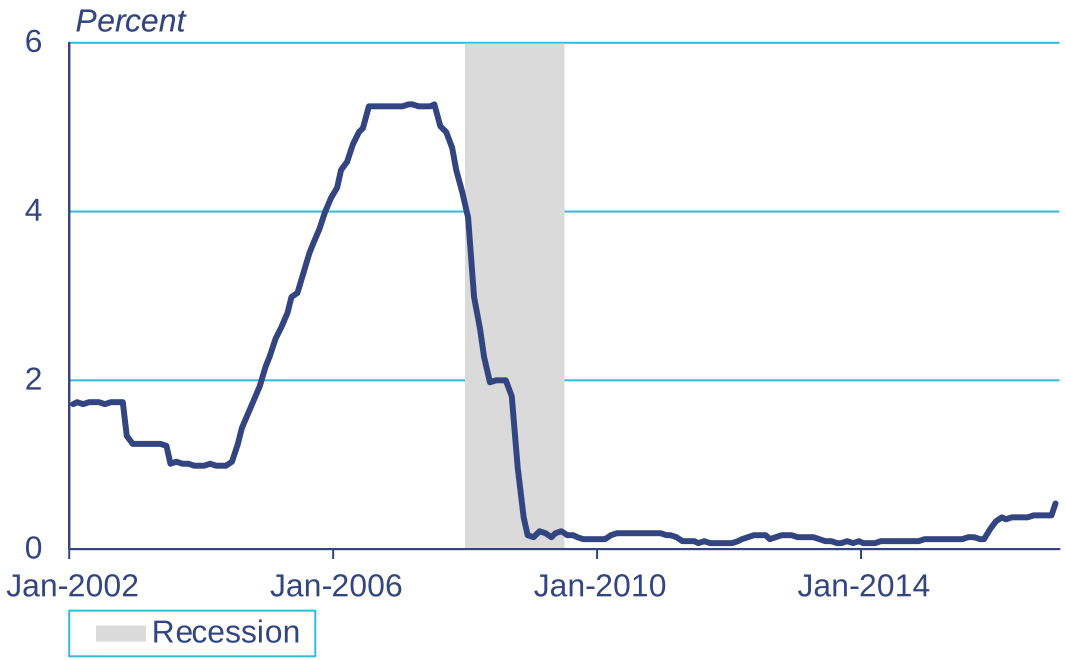
- From 2007 to 2014 when addressing this group I have been an advocate for accommodative monetary policy
- More recently, my comments have been advocating for a gradual return to a more normal monetary policy
- It is not that my underlying views or economic analysis have changed; rather, economic circumstances have evolved and now imply the need for a different stance of monetary policy

Approaching Our Mandate

- Appropriate monetary policy will need to normalize more quickly than over the past year, but certainly not as rapidly as in the last tightening cycle
- The unemployment rate is at my estimate of what is likely to be sustainable in the long run
- Total and core PCE inflation measures are approaching the Federal Reserve's 2 percent inflation target (which is defined in terms of total PCE)

Figure 1: Federal Funds Rate

January 2002 - December 2016



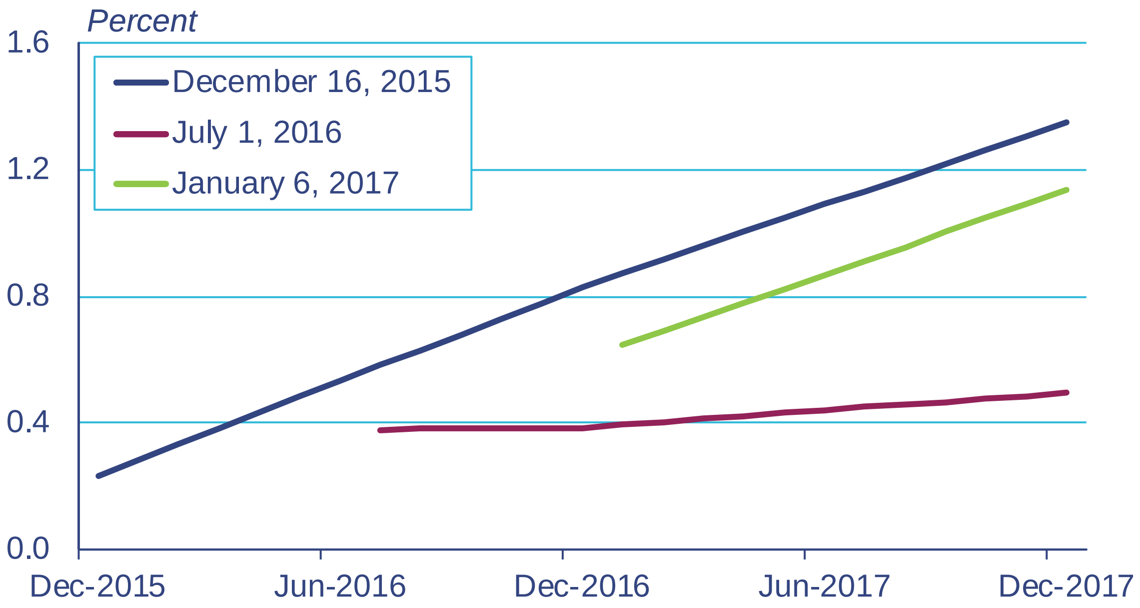
Source: Federal Reserve Board, NBER, Haver Analytics

Why Was Such A Slow Normalization of Monetary Policy Appropriate?

- The significant loss of jobs during the Great Recession ensured the recovery to full employment would not be quick
- Real GDP has been growing only slightly faster than potential
- Inflation rates both here and abroad have remained well below the inflation targets set by central banks
- Because policymakers consistently missed on the weak side, very patient and gradual approach to raising the funds rate has been entirely appropriate

Figure 2: Federal Funds Rate Projections Implied by the Federal Funds Futures Market on Selected Dates

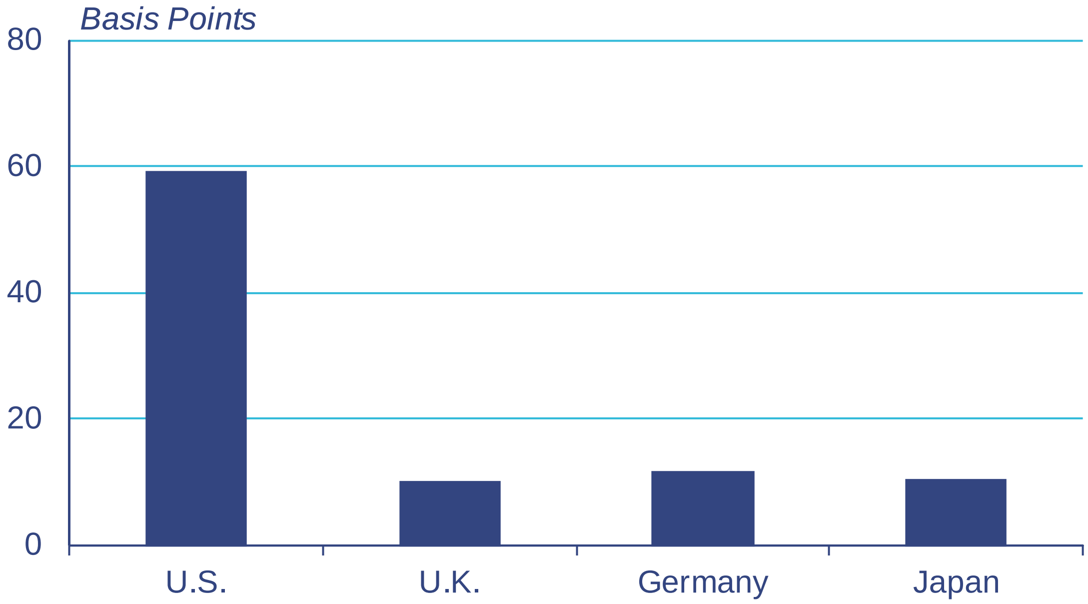
December 2015 - December 2017



Source: Bloomberg Finance L.P.

Figure 3: Ten-Year Government Bond Yields

Change, November 1, 2016 - January 6, 2017



Source: Bloomberg Finance L.P.

Figure 4: Five-Year Treasury Yield Minus Five-Year Inflation-Indexed Treasury Yield

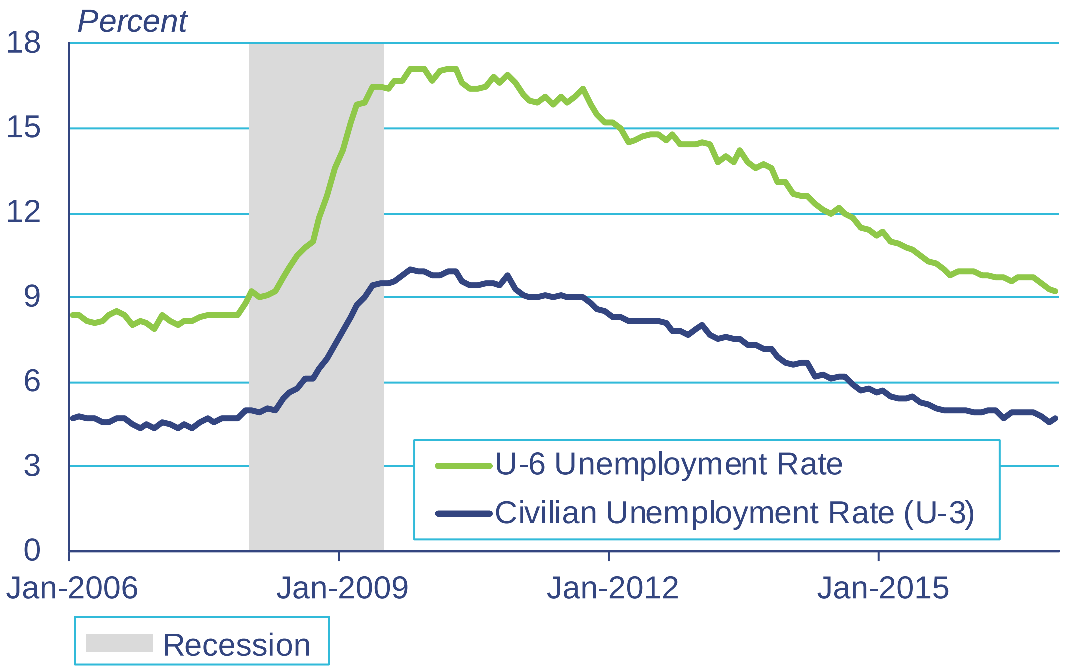
January 3, 2012 - January 5, 2017

Note: Yields at Constant Maturity

Source: Federal Reserve Board, Haver Analytics

Figure 5: Measures of Labor Underutilization

January 2006 - December 2016

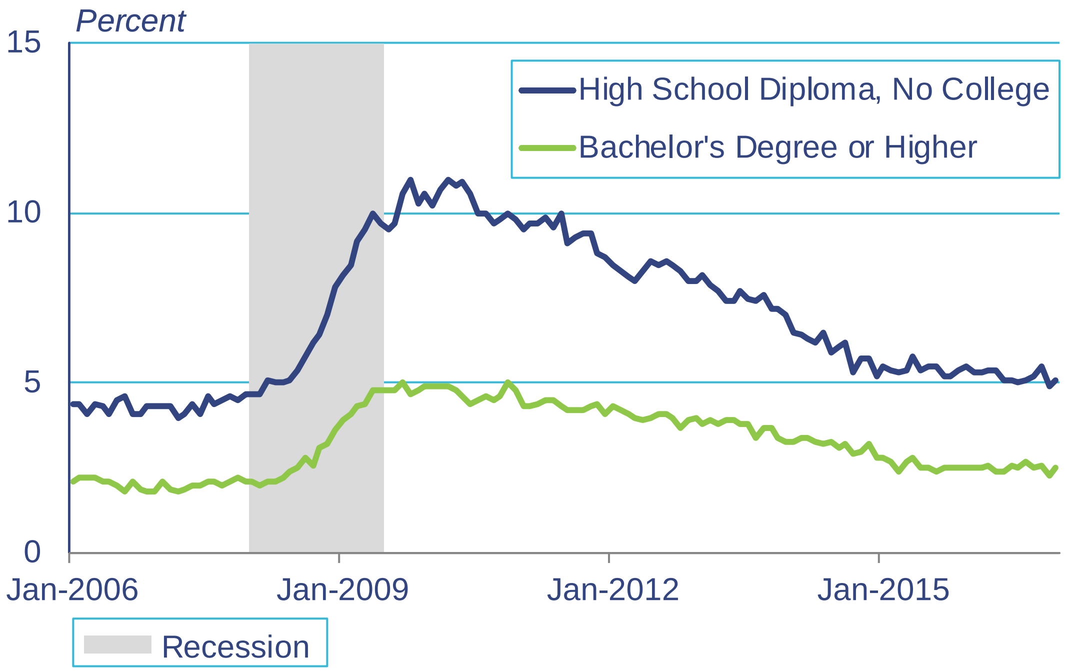


Note: The U-6 measure is total unemployed, plus all persons marginally attached to the labor force, plus total employed part time for economic reasons, as a percent of the civilian labor force plus all persons marginally attached to the labor force.

Source: BLS, NBER, Haver Analytics

Figure 6: Unemployment Rate by Educational Attainment

January 2006 - December 2016

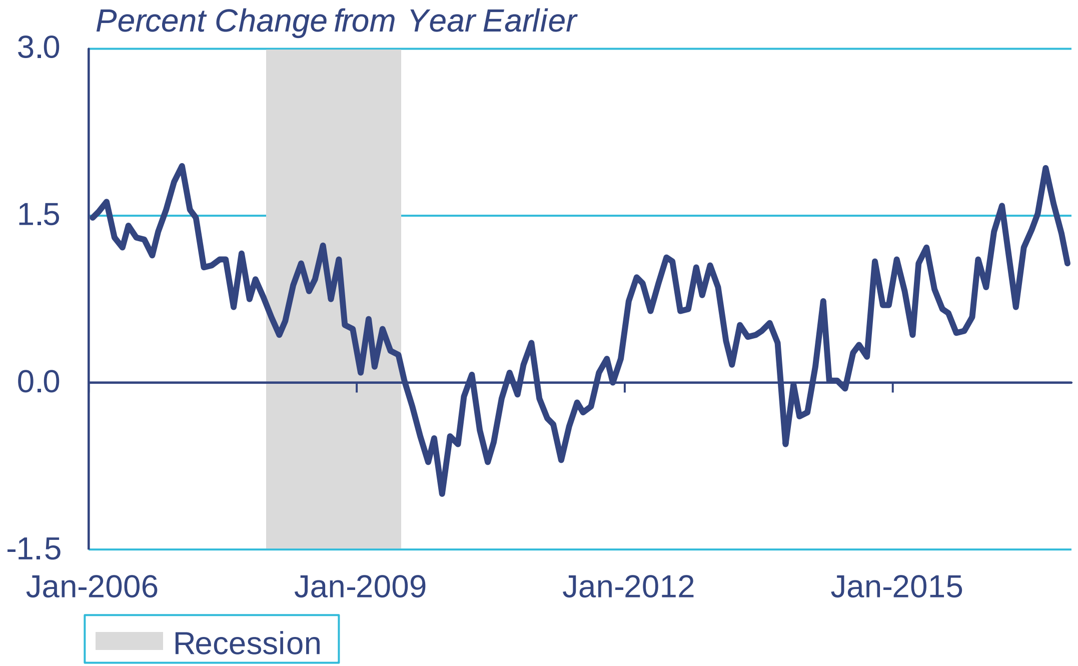


Note: For population age 25 and older

Source: BLS, NBER, Haver Analytics

Figure 7: Civilian Labor Force Growth

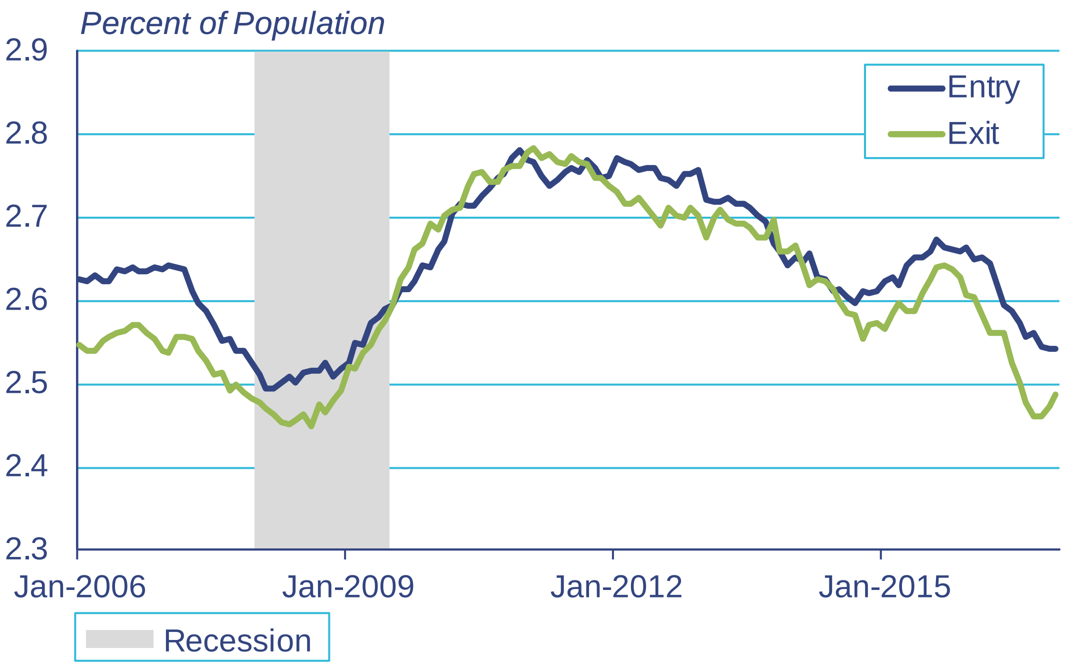
January 2006 - December 2016



Source: BLS, NBER, Haver Analytics

Figure 8: Labor Force Entry and Exit

January 2006 - December 2016

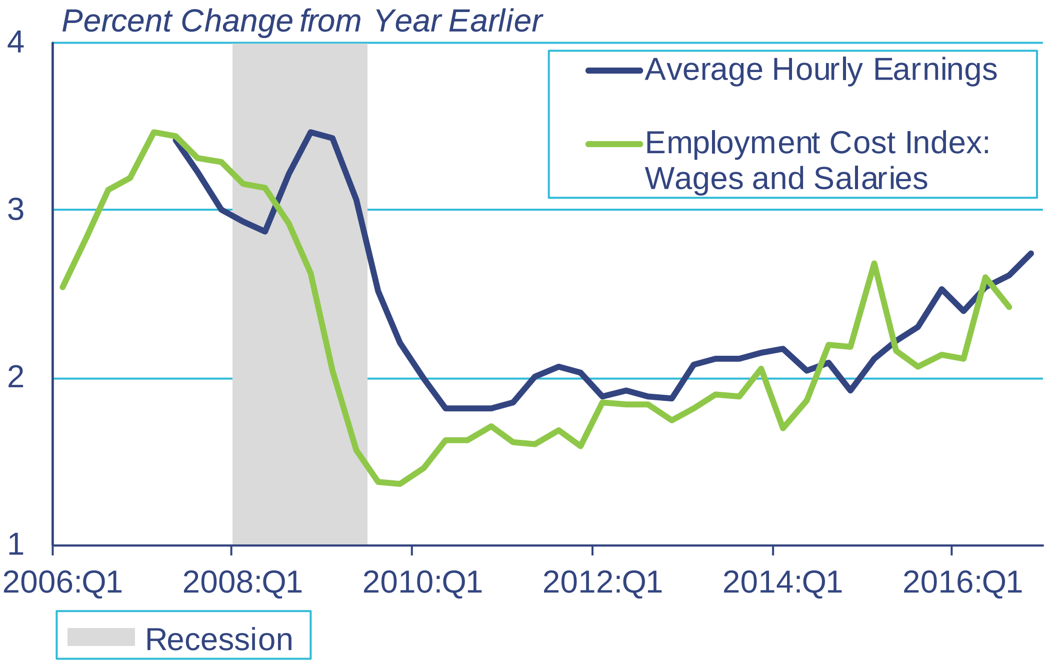


Note: Shares are twelve-month moving averages

Source: BLS, NBER, Haver Analytics

Figure 9: Wage Growth for Private Industry Workers

2006:Q1 - 2016:Q4

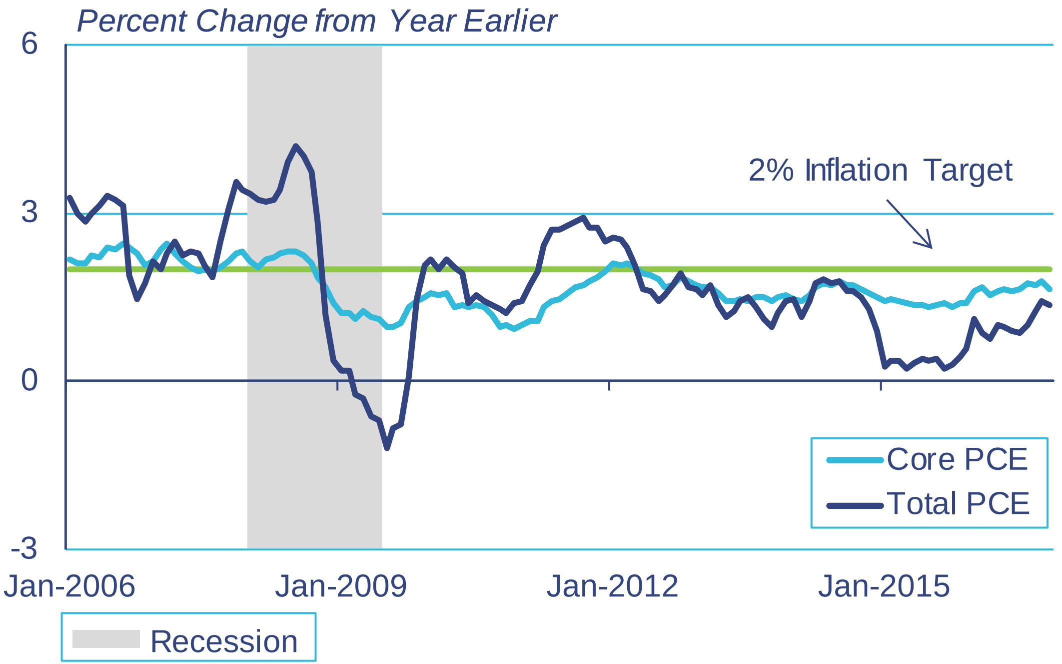


Note: The Employment Cost Index for the fourth quarter of 2016 has not yet been released

Source: BLS, NBER, Haver Analytics

Figure 10: Inflation Rate: Change in Total and Core Personal Consumption Expenditures Price Indices

January 2006 - November 2016

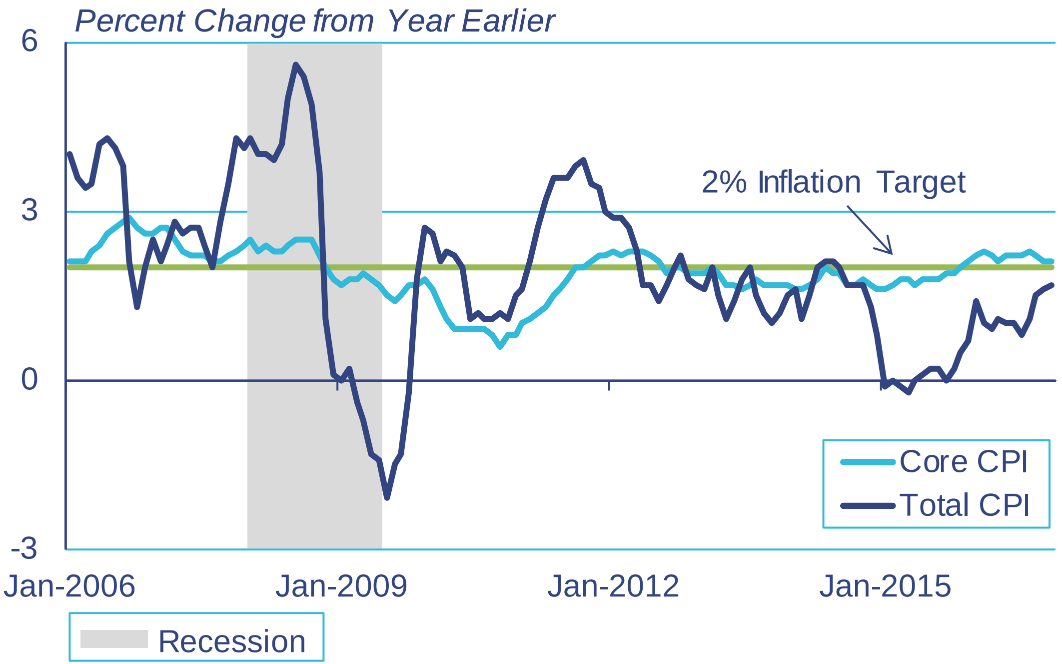


Note: Core PCE excludes food and energy

Source: BEA, NBER, Haver Analytics

Figure 11: Inflation Rate: Change in Total and Core Consumer Price Indices

January 2006 - November 2016

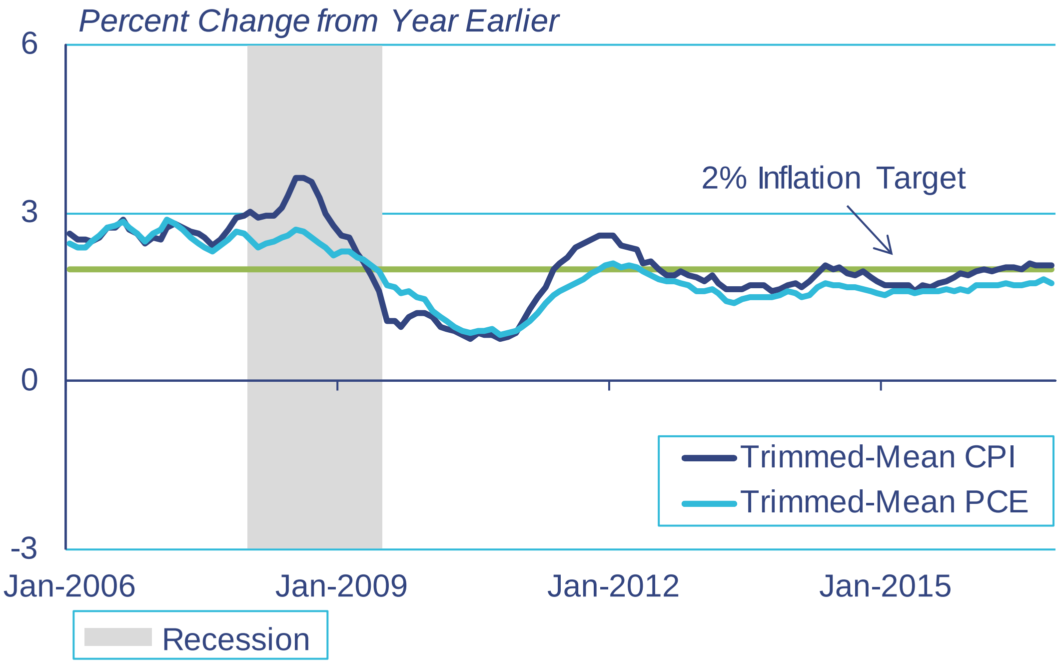


Note: Core CPI excludes food and energy

Source: BLS, NBER, Haver Analytics

Figure 12: Alternative Inflation Measures: Change in Trimmed-Mean PCE and CPI

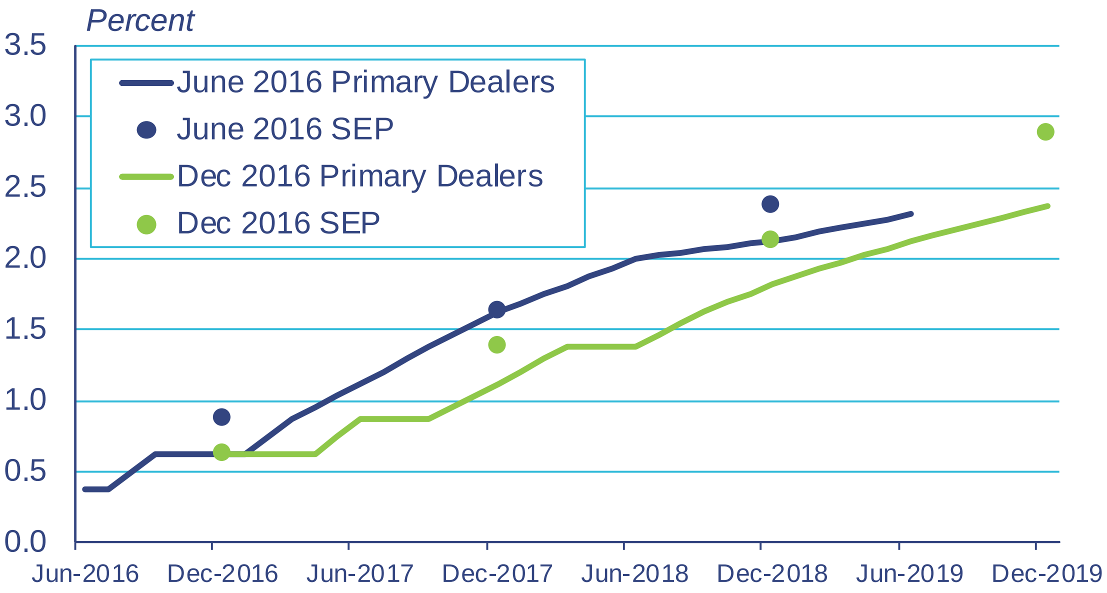
January 2006 - November 2016



Source: Federal Reserve Bank of Cleveland, Federal Reserve Bank of Dallas, NBER, Haver Analytics

Figure 13: Estimates for the Target Federal Funds Rate Path

June 2016 - December 2019

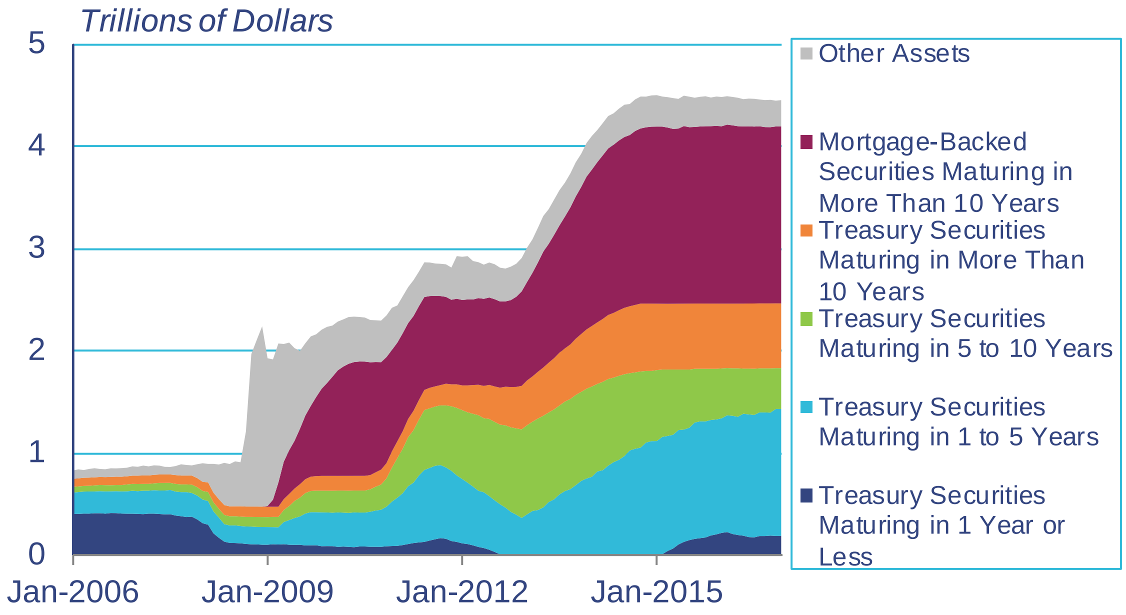


Note: Estimates from the Survey of Primary Dealers are median estimates for the target rate or the midpoint of the target range. Estimates from the Summary of Economic Projections are medians of the projections for the midpoint of the target range at yearend for 2016 -2019.

Source: FOMC, Summary of Economic Projections, June 2016, Dec 2016; Survey of Primary Dealers, June 2016, Dec 2016

Figure 14: Federal Reserve System Balance Sheet Composition

January 2006 - December 2016



Source: Federal Reserve Board, Haver Analytics

Concluding Observations

- We are now approaching both elements of the Fed's dual mandate – and my own forecast is we will achieve them by the end of 2017 – which calls for gradually normalizing monetary policy
- The aggressive policy actions taken by the Fed during the financial crisis and recession made a huge difference
- As a result, the U.S. is closer to achieving its goals for monetary policy than are most other developed countries