Monetary Policy Advisory Panel
Meeting of March 29, 2017
Minutes

Present: William Dudley, Michael Strine. Panelists: Markus Brunnermeier, Mark Gertler, Takatoshi Ito, Thomas Philippon, Kenneth West, Michael Woodford. FRBNY Staff: Ozge Akinci, Richard Crump, Marco Del Negro, Thomas Eisenbach, Domenico Giannone, Julia Gouny, Beverly Hirtle, David Lucca, Jonathan McCarthy, Paolo Pesenti, Julie Remache, Robert Rich, Argia Sbordone, Angela Sun.

The meeting began with a discussion of the economic outlook and the apparent new narrative that emerged following the U.S. presidential election. The panelists then turned to a discussion of policy normalization and issues related to the Federal Reserve's balance sheet.

The economic outlook: hard vs soft data

The discussion started with the panelists' views on the economic outlook. Panelists observed that there was a wide dispersion in output growth forecasts for the first quarter. They noted that this dispersion largely was associated with an apparent disconnect between "hard" expenditure data, which had signaled a continued moderate expansion of the U.S. economy, and "soft" survey data, which had pointed to a more upbeat outlook. Panelists debated whether the more optimistic expectations expressed in the survey data would eventually be reflected in the aggregate expenditure data. The general view was that business optimism had mostly been driven by expectations of corporate tax cuts and an easing of regulatory constraints under the new Administration and Congress. Some panelists expressed the view that corporate tax reform might increase capital inflows into the United States, which in turn could lead to a surge in investment. Other panelists were more skeptical about this argument, as they did not believe that many U.S. corporations are presently cash constrained, and thus anticipated that tax reform would provide little additional incentive for investment. Panelists also discussed the likelihood that the proposed border tax adjustment, which a number of panelists viewed as potentially having stronger stimulative effects, would be implemented.

Panelists also discussed the apparent signals coming from the financial markets and debated the reasons behind what they saw as rather subdued movements in longer-term Treasury yields in response to recent policy communications.

Policy normalization and the balance sheet

Panelists next discussed the criteria that should guide the determination of the appropriate longer-run size of the Federal Reserve's balance sheet. Referring to recent arguments by Jeremy Stein, they discussed whether it would be desirable to maintain a relatively large balance sheet, even when policy rates had moved well away from the effective lower bound, to help promote financial stability through the ample provision of government-supplied safe short-term claims. There was then some discussion of the degree of accommodation currently provided by the balance sheet and the potential effects of a reduction in its size. It was noted that it is difficult to infer these effects from existing studies of central bank asset purchases, as current economic and financial conditions are quite different from those existing when the programs were initiated. Panelists generally favored a passive shrinking of the balance sheet by ceasing reinvestment of maturing Treasury securities and principal payments from MBS, but did not express strong views on the longer-run size of the balance sheet. Some panelists raised the issue of whether the relevant factors guiding the Federal Reserve's balance sheet policy for the longer run are on the asset side or the liability side. Panelists continued to be largely in favor of using the balance sheet in times of crisis, which they saw as an argument against maintaining an overly large balance sheet in "normal" times.

Global economy issues

There was some discussion of Brexit and other political risk events in Europe. Panelists observed that the United Kingdom had just sent the Article 50 notification to the European Union, starting the two-year countdown for the U.K.'s exit from the EU. It was noted that financial firms located in London would probably need to begin to make decisions about staff location before the end of that two-year window.

Political events in Europe, particularly the upcoming French elections, were seen by panelists as downside tail risks at the moment.