No Exit?
Some Comments on Monetary Policy in Economic Transition

Prepared for the Georgia State University Economic Forecasting Conference

Atlanta, GA
November 18, 2009

The views expressed are mine, and not necessarily those of the Atlanta Fed or the Federal Reserve System.
The recent forecast of the Federal Reserve Bank of Atlanta remains on the modest-side of the consensus.

**REAL GDP GROWTH**

<table>
<thead>
<tr>
<th>Quarter</th>
<th>Actual</th>
<th>FORECAST</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1-06</td>
<td>5.6%</td>
<td></td>
</tr>
<tr>
<td>Q3-06</td>
<td>2.1%</td>
<td></td>
</tr>
<tr>
<td>Q1-07</td>
<td>2.2%</td>
<td></td>
</tr>
<tr>
<td>Q3-07</td>
<td>3.0%</td>
<td></td>
</tr>
<tr>
<td>Q1-08</td>
<td>1.4%</td>
<td></td>
</tr>
<tr>
<td>Q3-08</td>
<td>0.8%</td>
<td></td>
</tr>
<tr>
<td>Q1-09</td>
<td>-4.0%</td>
<td></td>
</tr>
<tr>
<td>Q3-09</td>
<td>-3.4%</td>
<td></td>
</tr>
<tr>
<td>Q1-10</td>
<td>2.1%</td>
<td></td>
</tr>
<tr>
<td>Q3-10</td>
<td>2.0%</td>
<td>FRBA</td>
</tr>
</tbody>
</table>

**SOURCES:** Blue Chip panel of economists, October 10, 2009, Federal Reserve Bank of Atlanta
The GDP turnaround is expected to be very subdued relative to the “typical” recovery experience.

**REAL GDP GROWTH**

- **Actual**
- **Avg. of past 7 recessions**

**FORECAST**

SOURCES: Bureau of Economic Analysis, Blue Chip panel of economists, October 10, 2009
Current forecasts are very pessimistic in historical context.

Source: BEA, Blue Chip
Unemployment is still rising and the share of joblessness attributed to permanent job loss has surged.

Source: Bureau of Labor Statistics (through October)
Underemployment is significantly higher than in past recessions.

**Part-Time for Economic Reasons**

Indexed to Start of Recession=1

Dots represent end of recession

Source: U.S. Bureau of Labor Statistics
Underemployment is significantly higher than in past recessions.

Source: U.S. Bureau of Labor Statistics
Employment at firms with less than 50 employees have been most affected by the current recession.
Policy changes usually lag unemployment peaks

Historical lag between end of recession, unemployment rate peak, and beginning of funds rate tightening cycle

<table>
<thead>
<tr>
<th>End of Recession</th>
<th>Unemployment rate peak</th>
<th>Beginning of funds rate tightening cycle</th>
<th>Months from end of recession to unemployment peak</th>
<th>Months from unemployment peak to beginning of funds rate tightening cycle</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nov-01</td>
<td>Jun-03</td>
<td>Jul-04</td>
<td>19</td>
<td>13</td>
</tr>
<tr>
<td>Mar-91</td>
<td>Jun-92</td>
<td>Feb-94</td>
<td>15</td>
<td>20</td>
</tr>
<tr>
<td>Nov-82 (Jul 1980)</td>
<td>Dec-82</td>
<td>Jun-83</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Mar-75</td>
<td>May-75</td>
<td>May-76</td>
<td>2</td>
<td>12</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(1)</td>
<td>(15)</td>
</tr>
</tbody>
</table>
President Lockhart says:

I do not think that time has yet come, and to be consistent with my outlook, I think it may well be some time before a comprehensive exit (from monetary stimulus) need be under way.

“Thinking About Recovery”: September 10, 2009 speech, University of South Alabama
Exit stage 1: The credit facilities wind down

Federal Reserve Assets (Uses of Funds)
$ billions

SOURCE: Federal Reserve Board
Exit stage 2: LSAP completed

Treasury and Agency MBS Purchases
Daily cumulative total, Billions $

MBS purchase commitment

Treasury purchase commitment

Agency MBS (lhs)  
Treasuries (rhs)
The Fed’s (really big) balance sheet

Federal Reserve Liabilities (Sources of Funds)

$ billions

Dec-07 Feb-08 Apr-08 Jun-08 Aug-08 Oct-08 Dec-08 Feb-09 Apr-09 Jun-09 Aug-09 Oct-09

SFP = Supplementary Financing Program
SOURCE: Federal Reserve Board
Exit stage 3: Sucking up the excess reserves

- We can just sell the assets we own (i.e. Treasury securities or mortgage-backed securities)

- We can rent out the assets we own (reverse repos)
Exit stage 4: Interest rates on the move

• Will the balance sheet still be big?

    --- Ans: Don’t know, but I wouldn’t rule it out

• Time to think about the interest paid on bank reserves as the new (or transition) policy instrument
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