

THE FEDERAL RESERVE SYSTEM

Date: October 11, 2019
To: Federal Open Market Committee
From: David Altig, Jeffrey Fuhrer, Marc Giannoni, and Thomas Laubach
Subject: Background Papers for Review of Monetary Policy Framework

Attached are two memos that will serve as the basis for the staff presentations during the Committee’s special topic discussion at the upcoming meeting continuing the review of the monetary policy framework:

1. “Issues Regarding the Use of the Policy Rate Tool,” October 11, 2019
2. “Issues in the Use of the Balance Sheet Tool,” October 11, 2019

Following the Committee’s discussion of alternative policy strategies at the September meeting, the two memos prepared for this meeting address several issues regarding the use of the Committee’s two principal tools, the federal funds rate and the balance sheet. The first memo reviews alternative forms of forward guidance (FG) and examines the empirical evidence on the effectiveness of these variants. It also discusses how different forms of FG resolve the key tradeoff between the degree of precision of the FG and the desire to preserve flexibility and optionality. It concludes with a brief discussion of the foreign experience with negative interest rate policy, and the limitations of the applicability of this experience to the U.S. financial context. The second memo reviews the evidence on the effectiveness and possible costs of large-scale asset purchases, and discusses the merits of flow-based and fixed-size programs. It also examines options for the use of asset purchases to impose ceilings on Treasury yields at certain maturities (aka yield curve control). It concludes with a brief discussion of the merits of MBS purchases as well as “funding for lending” programs.

Following the staff presentations and Q&A, there will be a full go-round. It would be helpful if, in your comments, you could address the questions on the following page.

**Questions for Discussion of Framework Review
at the October 2019 FOMC Meeting**

1. What do you see as the merits of the three types of forward guidance (FG) (qualitative, date-based, and outcome-based) in augmenting conventional monetary policy? How would you anticipate using the different types of FG to address different economic circumstances?
2. What do you see as the benefits and costs of negative interest rate policy in the context of U.S. financial structure, assuming that there are no legal impediments to using this tool?
3. What do you see as the benefits and costs of using different types of balance sheet policy (BSP), either “flow-based” or “fixed-size”? Do you see evidence of diminishing returns in the implementation of BSP, resulting from the low level of long-term rates?
4. What do you see as the benefits and costs of employing yield curve control—in particular, using BSP to cap rates on shorter-maturity instruments (perhaps to reinforce forward guidance about the near-term path of the policy rate) or on longer-maturity instruments (to lower the level and volatility of rates that are more closely related to economic activity)?