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- **February 14, 2013**. Presentation. "U.S. Monetary Policy: Easier Than You Think It Is," *Mississippi State University*, Starkville, Mississippi. Presentation (pdf) (bullardstarkville14feb2013finalpdf) | Press Release | Related news articles.

  U.S. Monetary Policy: Easier Than You Think It Is

  February 14, 2013

  St. Louis Fed President James Bullard discussed why he views the stance of U.S. monetary policy as considerably easier now than in 2012 during a special banking forum at Mississippi State University in Starkville, Mississippi.

  [Presentation (pdf)](https://www.stlouisfed.org/-/media/project/frbstl/stlouisfed/files/pdfs/bullard/remarks/bullardstarkville14feb2013final.pdf)| [Press Release](https://www.stlouisfed.org/news-releases/2013/02/14/st-louis-feds-bullard-says-us-monetary-policy-is-considerably-easier-today-than-in-2012)

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  • [Fed policy has put 'pedal to the metal' in 2013:

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• [Fed's Bullard: raising minimum wage will mean fewer people hired](http://www.reuters.com/article/2013/02/14/us-fed-usa-bullard-wages-idUSBRE91D1CB20130214), by Alister Bull, Reuters.

St. Louis Fed's Bullard Says U.S. Monetary Policy Is Considerably Easier Today Than in 2012

STARKVILLE, Miss. – Federal Reserve Bank of St. Louis President James Bullard gave remarks Thursday on [“U.S. Monetary Policy: Easier Than You Think It Is,”](https://www.stlouisfed.org/-/media/project/frbstl/stlouisfed/files/pdfs/bullard/remarks/bullardstarkville14feb2013final.pdf)at a special banking forum sponsored by Mississippi State University’s Department of Finance and Economics.

During his presentation, Bullard discussed recent changes to U.S. monetary policy and his view of how the stance of monetary policy has been altered. On the Fed’s nominal interest rate policy, he noted that the policy rate has been near zero since December 2008 and that the Federal Open Market Committee (FOMC) has promised to maintain the near-zero rate into the future, so-called “forward guidance.” In December 2012, the FOMC replaced the fixed-date forward guidance with a “threshold” approach. “The threshold approach has disposed of the ‘pessimistic signal’ that was a side effect of the date-based forward guidance. This should make the forward guidance more effective,” he said.

Regarding the Fed’s balance sheet policy, outright asset purchases have replaced the “Operation Twist” program, which Bullard noted may not have been as effective as hoped. “Open-ended outright purchases are a more potent tool,” he said. Furthermore, he stated that the FOMC has promised to maintain an aggressive asset purchase program, and he discussed some considerations for the future of this program.

Overall, “the current stance of U.S. monetary policy is considerably easier than it was in 2012,” Bullard said. “2012 policy was characterized by a relatively weak ‘Operation Twist’ program combined with somewhat counterproductive date-based forward guidance,” he said. In contrast, “2013 is characterized by a relatively potent open-ended outright asset purchase program combined with more effective threshold-based forward guidance.”

Thresholds and the Policy Rate

Before December, the FOMC stated that the policy rate would likely remain near zero until mid-2015. “This created a ‘pessimism problem’ for the Committee,” Bullard said. He explained that “the date could be interpreted as a statement that the U.S. economy is likely to perform poorly until that time,” which he has called an “unwarranted pessimistic signal.” However, he said, “The Committee did not intend to send such a signal.”

Rather than using a given date, Bullard noted that the FOMC has now changed its forward guidance to a description of economic conditions at the time of the first rate increase. Such a dependency on economic conditions is known as “state-contingent” policy.

“In December the Committee instead adopted ‘thresholds,’ values for inflation (2.5 percent) and unemployment (6.5 percent) that give an indication that the time for a policy rate increase may have arrived,” he explained. “Now, as data arrive on U.S. economic performance, private sector expectations concerning the timing of the first rate increase can automatically adjust,” Bullard said. “The Committee is no longer sending the pessimistic signal, because the threshold conditions can be met at any time.”

While the thresholds fixed the pessimism problem, they still have some challenging aspects. “The use of thresholds is not a panacea,” Bullard cautioned. He discussed several issues that the FOMC is likely to face going forward with this strategy. For instance, he said, “The FOMC cannot pretend to target medium- or long-term unemployment.” In addition, “The

Committee needs to reiterate that it considers many more variables in attempting to gauge the state of the U.S. economy." Finally, he said that "the thresholds will likely be viewed as triggers for action."

Balance Sheet Policy

Turning to balance sheet policy, Bullard discussed "QE3," which the FOMC adopted at its September 2012 meeting and extended in December, replacing "Operation Twist" with outright purchases. Unlike the FOMC's previous asset purchase programs, no end date was specified; this is so-called "open-ended" QE. The current approach is to purchase $40 billion in mortgage-backed securities and $45 billion in Treasury securities per month, which Bullard noted would be an annualized pace of more than $1 trillion.

The previous asset purchase programs had an "end-date problem," Bullard said, explaining that "these end dates tended to occur at times which were characterized by relatively poor economic data." As examples, he cited March 2010, when the European sovereign debt crisis was heating up, and July 2011, when the U.S. debt ceiling debate was occurring. "With QE3, the Committee instead seeks 'substantial improvement' in labor markets before pausing purchases," he stated.

Unlike the interest rate policy, the timing on the balance sheet policy is not associated with thresholds. "The Committee has maintained a qualitative approach to the state-contingent aspect of balance sheet policy," Bullard said, adding that "attempts to also put thresholds on the timing of asset purchases may be a bridge too far."

How Long Can QE Continue?

Bullard discussed four considerations for QE3 going forward. First, while substantial labor market improvement is a condition for ending the program, Bullard said that "the Committee could consider many different aspects of labor market performance when evaluating whether there has been 'substantial improvement.'" These include the unemployment rate, employment, hours worked, and Job Openings and Labor Turnover Survey

(JOLTS) data.

Second, “Without an end date, the Committee may have to alter the pace of purchases as news arrives concerning U.S. macroeconomic performance,” Bullard said, noting that “substantial labor market improvement” does not arrive suddenly. “This suggests that as labor markets improve somewhat, the pace of asset purchases could be reduced somewhat, but not ended altogether,” he explained. “This type of policy would send important signals to the private sector concerning the Committee’s judgment on the amount of progress made to that point.”

A third consideration for the QE program is inflation and inflation expectations, Bullard said. Current readings on inflation are rather low, which he said may give the FOMC some leeway to continue asset purchases for longer than otherwise. Although worries about rising inflation have so far been unfounded, “the lesson from QE2 is that inflation and inflation expectations did trend higher,” he said, adding that it is too early to know if that will happen with the current QE program.

Finally, he said, “The size of the balance sheet could inhibit the Committee’s ability to exit appropriately from the current very expansive monetary policy.” He explained that when interest rates rise, asset values will fall, which could possibly complicate monetary policy decisions.

“Considerations for the future of the QE program are multi-faceted and will require a careful judgment of the Committee in the coming quarters,” Bullard stated.

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