

Recent U.S. Economic and Financial Developments

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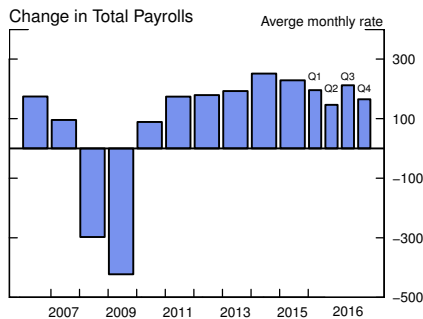
Federal Reserve Board

January 12, 2017

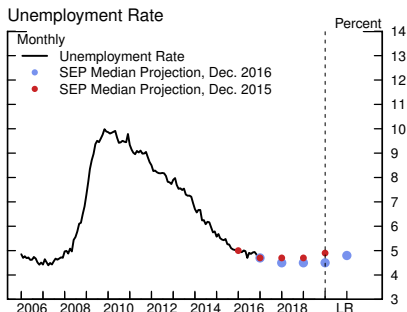
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The U.S. labor market has continued to strengthen

- ▶ Employment gains in 2016 somewhat above the pace consistent with LFPR trend and constant unemployment rate.
- ▶ Unemployment rate close to median longer-run normal rate in SEP, projections little changed since December 2015.



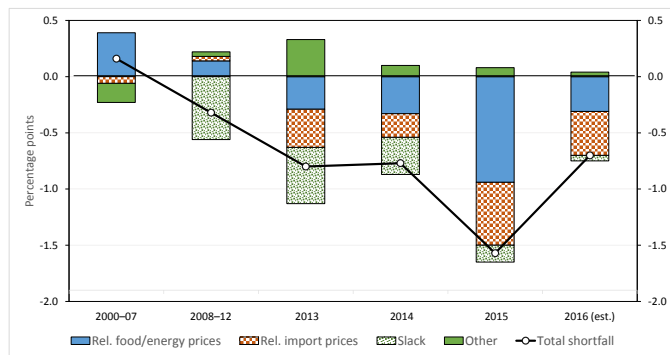
Source: U.S. Bureau of Labor Statistics



Source: U.S. Bureau of Labor Statistics and December 2015 and 2016 SEPs.

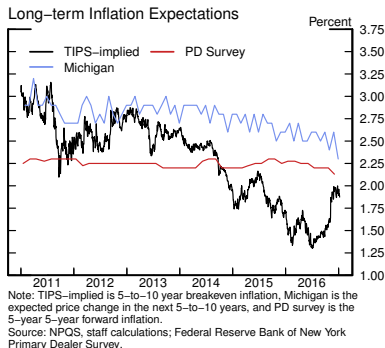
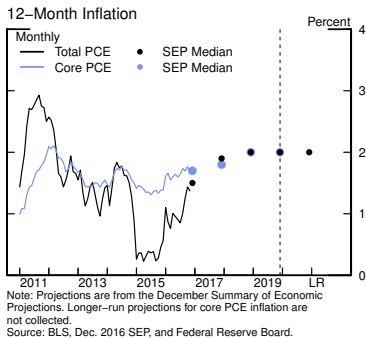
Inflation developments through the lens of the Phillips Curve

- ▶ Low PCE inflation in recent years mostly explained arithmetically by energy, food, and core import prices.



Inflation has increased somewhat since earlier this year

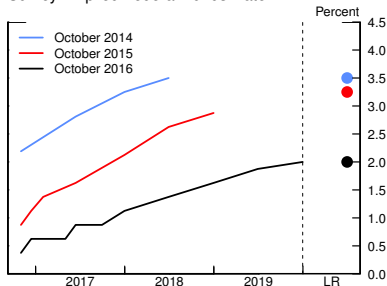
- ▶ In 2016, total and core inflation moved closer to 2 percent objective for total inflation, latest readings near 1-1/2 and 1-3/4 percent.
- ▶ Market-based inflation compensation remains low, most longer-term survey measures little changed.
- ▶ SEP projections little changed since December 2015.



Expected pace of policy normalization

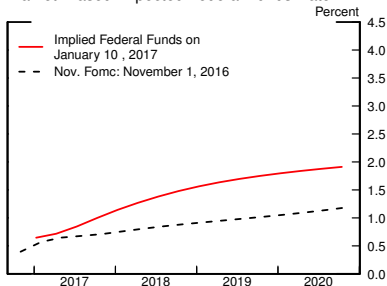
- ▶ Expected funds rate path shifted down substantially since 2014, even at very long horizons.
- ▶ Only a small part of downshift has reversed since early November.

Survey-Implied Federal Funds Rate



Source: FRBNY Primary Dealer Survey.

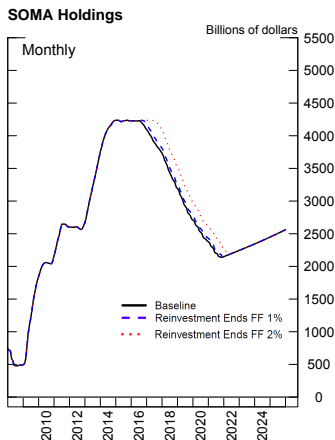
Market-Based Expected Federal Funds Rate



Note: Path is estimated using OIS quotes with a spline approach and a term premium of zero basis points.
Source: Bloomberg and staff calculations.

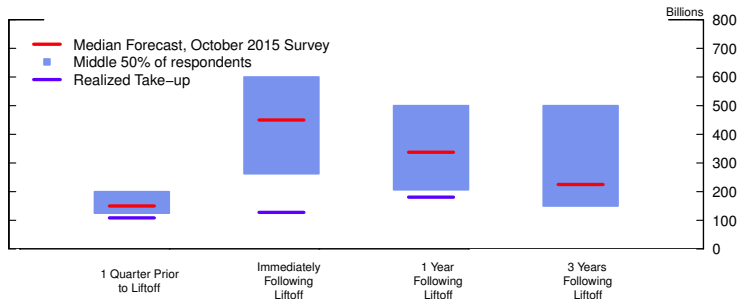
Policy normalization: Phasing out reinvestment

- ▶ In July and September 2015, FOMC discussed strategies for phasing out or ending reinvestments.
- ▶ Time-dependent (fixed time after liftoff) vs. state-dependent (e.g. level of funds rate) strategies.



Monetary policy operations after liftoff

- ▶ Despite large volume of excess reserves, fed funds rate solidly within target range, other overnight rates close.
- ▶ Surprisingly low ON RRP take-up with 25 bp spread between IOER and ON RRP rate. High take-up at quarter-ends, but no surges during periods of stress.



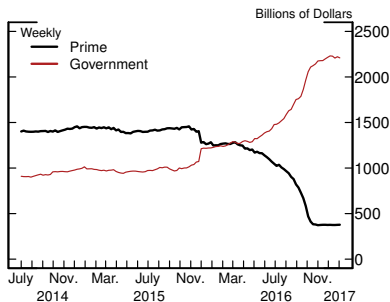
Note: Purple bars are average take-up excluding month-ends. Dec. 17, 2015 to Jan. 29, 2016 is the period used to calculate the immediately after liftoff bar. Oct. 22, 2016 to January 10, 2017 is the period used to calculate the 1 year following liftoff bar, following full implementation of the SEC's money market fund reforms.

Source: FRBNY, October 2015 Primary Dealer Survey and the Survey of Market Participants.

Market imprint of October 2016 MMF reform

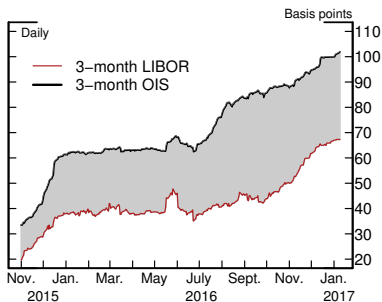
- ▶ MMF reform has led to dramatic reduction in prime MMF assets under management.
- ▶ Unsecured term funding costs have increased, and volumes have declined, but few strains elsewhere.

Prime and Government MMF Assets under Management



Source: Investment Company Institute and staff calculations.

LIBOR-OIS Spreads



Note: LIBOR is London interbank offered rate; OIS is overnight index swap.

Source: Bloomberg.