Monetary Policy in this Unusual Time

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Overview

• **2023: The golden path and inflation dynamics**
  - A great year for the dual mandate
  - Supply chains, labor supply, productivity growth
  - Are more favorable supply developments to come in 2024?

• **Inflation expectations barely moved: The role of the Fed**
  - Credibility was an anchor

• **(If time) Non-bank financial institutions (NBFIs) and monetary policy transmission**
2023: The Golden Path and Inflation Dynamics
Huge decline in inflation without a recession

Core PCE Inflation
(Percent change)

- 6-month (a.r.)
- 12-month

Source: BEA via Haver Analytics
Huge decline in inflation without a recession

Change in Core PCE Inflation vs. Unemployment Gap

Note: Core PCE inflation is the change from the previous year in Q4/Q4 core PCE inflation; unemployment gap is the difference between unemployment rate and CBO’s estimate of the noncyclical rate of unemployment.

Source: BEA, BLS, and CBO via FRED; staff calculations
Supply chain repair

Global Supply Chain Pressure Index
(Standard deviations from average)

Source: FRBNY via Haver Analytics
Note: Blue shading indicates 68% confidence band
Strong labor supply

Labor Force Participation Rate

(Percent)

64
63
62
61
60

Note: Trend reflects the labor force participation rate expected in an economy with unemployment at its natural rate given the age, cohort, gender, and education composition of the labor force.
Source: BLS via Haver Analytics; staff calculations based on Aaronson, Hu, Seifoddini, and Sullivan (2014)
Wage-price dynamics

• In long run, inflation = wage growth - productivity growth

• Is wage growth consistent with target inflation?
  - Wages stickier than prices, so be careful in making judgments

• In short- and medium-run, prices lead unit labor costs
Productivity recovery:Hints of the ‘90s?

**Nonfarm Business Sector Productivity vs. Trend**

(Index 2017 = 100)

- **Note:** Trend calculated from 2007:Q1 to 2019:Q4
- **Source:** BLS via Haver Analytics
Inflation Expectations Barely Moved: The Role of the Fed
Anchored inflation expectations – since the 2000’s

10-Year Inflation Expectations and Core PCE Inflation (Percent)

Note: 4-quarter percent change in core PCE and a PCE consistent series for average inflation expectations over the coming 10 years constructed from the Hoey Survey, Survey of Professional forecasters, and a statistical model.
Source: BEA via Haver Analytics, Federal Reserve Board
Rates are restrictive

Real Federal Funds Rate (Percent)

Note: Federal funds rate target midpoint less 1-year ahead inflation swap rate. SEP long-run equal to longer run federal funds rate projection in the December 2023 SEP less the 2 percent inflation target.
Source: Federal Reserve Board; Bloomberg
Nonbank Financial Institutions and Monetary Policy Transmission
Bank share of lending to nonfinancial business

Lending Share Excluding Real Estate
(Percent)

Source: Federal Reserve Board Z.1 Financial Accounts of the United States
Appendix
Core PCE inflation components

Note: Core goods are goods less food and beverages purchased for off-premise consumption and gasoline and other energy goods. Core services are services less electricity and gas. Food services are included, as is the case in BEA core PCE prices. Source: BEA via Haver Analytics; staff calculations
PCE housing detail vs. Zillow new rents

PCE Rent and Owner-Equivalent Rent Subindexes & Zillow Observed Rent Index
(12-month percent change)

Source: BEA and Zillow via Haver Analytics
Increased business formation

U.S. Business Applications with Planned Wages
(Number, seasonally adjusted)

Source: U.S. Census Bureau via Haver Analytics