November 15, 2024

Council Attendees:

Donald Kohn, Brookings Institute (Council Chair)

Gabriel Chodorow-Reich, Harvard University

Julia Coronado, MacroPolicy Perspectives LLC

Klaus Desmet, Southern Methodist University

Wenxin Du, Harvard Business School

Darrell Duffie, Stanford University

Karen Dynan, Harvard University

Daryl Fairweather, Redfin

John Haltiwanger, University of Maryland

Karin Kimbrough, LinkedIn

Nathan Sheets, Citigroup

Federal Reserve Bank of Dallas Directors Attendees:

Tom Falk, Kimberly-Clark Corporation (retired)

Peter Rodriguez, Rice University

William Serrata, El Paso Community College

Federal Reserve Bank of Dallas Staff Attendees:

Lorie Logan, Karel Mertens, Heidi Mitchell, Mike Schetzel, Sam Schulhofer-Wohl, Rebecca Zarutskie, Deborah Kilroe, Anthony Murphy, Chris Otrok, Alex Richter, Mark Wynne, Alex Chudik, Scott Davis, Jim Dolmas, Enrique Martínez García, Ali Ozdagli, Jody Stanley, Fang Yang, Xiaoqing Zhou, Anton Cheremukhin, Sewon Hur, Mike Plante, Sam Dodini, Lucie Lebeau, Tucker Smith, Reid Taylor, Tyler Atkinson, Ron Mau, Elizabeth Souder, Braden Strackman

Discussion of the Fed's Balance Sheet

The Council discussed issues around the ongoing normalization of the Fed's balance sheet, its implications for money markets, the effective transmission of monetary policy, and the challenges in gauging the ampleness of reserves. Council members noted that the time of day at which payments are made to the largest dealer banks was a potentially useful metric for gauging the scarcity of liquidity, with later-in-the-day payments being associated with widening spreads between repo rates and the interest rate on reserve balances. Discussion ensued regarding the failure of dealer intermediation capacity to grow in line with the size of the Treasury market, which was viewed as an important factor contributing to recurrent episodes of repo market volatility and widening spreads.

The Council discussed potential actions that could allow for more efficient use of dealer balance-sheet space for intermediation or otherwise reduce the need for such capacity, including reducing the importance of leverage-based capital regulations, adjusting the Fed's Standing Repo Facility, developing intra-day repo markets, and expanding the potential for a greater volume of direct repo transactions.

Members further raised questions around the impact of large recent increases in government debt on Treasury markets and rates. One council member noted that countries with high levels of government debt, like the U.S., tend to have negative swap spreads on long-term bonds. Additional discussion ensued regarding the convenience yield on U.S. Treasuries that has been in decline, despite strong demand for dollar funding. Given these developments, members argued that there are likely challenges for funding future debt, which will likely manifest in higher term premia on U.S. Treasuries. Moreover, council members opined that the role of levered non-bank investors in absorbing Treasury issuance has grown, particularly as the Fed's balance sheet has shrunk, presenting a potential financial stability concern.

Discussion of the U.S. Housing Market

Council members discussed developments in the U.S. housing market, seeking to understand the implication of mortgage rates on house affordability and the implications of house price and rent developments on inflation. Members discussed how mortgage rate lock-ins have contributed to historically low level of home listings and sales. Some members also noted potential adverse implications of mortgage rate lock-ins for labor mobility, and hence aggregate labor productivity, while others noted that those willing to move for work may be well compensated. Other members mentioned that mortgage lock-ins might also affect older households, who traditionally would downsize or move to rental housing, reducing the supply to younger households.

Council members also noted that higher mortgage payments are largely attributed to higher mortgage rates, less so to home prices increase over the past year. Others added that increasingly higher insurance costs may cause some to reevaluate housing decisions. Members noted that income raises being absorbed by higher housing costs might be weighing on consumer sentiment.

Council members also discussed the extent to which relatively high completions of new housing construction have eased the housing shortage; however, new construction starts have decreased. Moving forward, members discussed the extent to which potential changes in immigration might impact the supply of labor to the construction sector, leading to longer delivery times on new construction.

Council members also discussed current and future rent dynamics. Members noted that rents have largely been flat over the past year, partly reflecting overbuilding in the multifamily sector, and more households are choosing to rent than before. Members noted this could be due to both high mortgage rates discouraging housing purchase and rent prices being stable.

Members also noted that, unlike other periods of increasing housing costs, increases this time are more homogeneous across the U.S. geographically with some of the highest increases being in the interior of the country. Others noted that housing shortages have eased in some coastal areas, while the sun belt has grown rapidly and expanded housing offerings.

General Discussion on the Economy and Issues Relevant for Monetary Policy

The Council meeting concluded with a general discussion of the economic outlook, risks around the outlook, and near-term policy tradeoffs. The wide-ranging discussion touched on several issues including: the strength of the U.S. economy relative to the rest of the world and the potential drag on global growth from struggling goods-producing European economies and significant headwinds in China; uncertainty about future domestic policies on immigration, tariffs, taxes and deregulation, and the possible impact of policy changes on inflation; strong recent labor productivity gains, driven by higher capital utilization and by continued firm births in highly productive sectors, and technological innovation, though members were uncertain as to whether more rapid productivity growth would continue; and the difficulty of estimating the natural rate of interest. Council members emphasized again the importance of clear communication from the FOMC on the economic outlook and the path of policy.