

Monetary Policy Case Study

Predicting Federal Reserve Actions in an Era of Uncertainty

POLICY CONTEXT

In response to the 2008-09 financial crisis and subsequent recession, the Federal Reserve cut short-term interest rates effectively to zero and lowered long-term rates through multiple large-scale asset purchase programs (i.e., “quantitative easing”). This unprecedented use of monetary policy eased financial stress and improved rate-sensitive sectors of the economy. However, it also created uncertainty around the effects of both QE and the Fed’s exit strategy.

Keybridge’s clients across all sectors have become increasingly concerned about the implications of Fed policies for their businesses. Over the past several years, many questions have arisen. Would quantitative easing result in rapid inflation? Would massive injections of liquidity create financial imbalances? When will the Fed begin to unwind quantitative easing? Will the inevitable rise of interest rates stifle the housing market recovery? Who will be the next Fed chairperson, and what will that mean for monetary policy moving forward?

APPROACH

Keybridge’s economists provide a number of services to clients concerned with monetary policy and how it might affect their businesses. Through regular correspondence, Keybridge has delivered timely and insightful analysis and guidance to clients.

- (1) *Tracking the Federal Reserve*: Keybridge closely follows the Fed’s public statements, meeting minutes, and policy actions. Based on more than 30 years of experience, Keybridge’s economists use their knowledge of the Fed’s inner workings and the overall macroeconomic environment to help clients anticipate the Fed’s next moves.
- (2) *Custom “Fed Reaction Functions”*: In addition to studying traditional “Taylor Rules,” Keybridge has developed its own Fed Reaction Functions to estimate the appropriate level for short-term interest rates.
- (3) *Economic and Inflation Momentum Monitors*: Keybridge publishes monthly leading indicators on U.S. economic growth and inflation that provide clients with a 3 to 6 month outlook. These tools help anticipate the economic environment the Fed will be operating under in the near future.

RESULT

Keybridge’s analysis, forecasts, and strategic guidance have helped clients make smarter decisions and mitigate risks. Global investors have gained greater understanding of the timing and magnitude of interest rate movements that affect their investment returns. Chief Economists at Fortune 100 companies have garnered new insights that they have used to advise their executives on key strategic decisions; and trade associations have used Keybridge’s views on monetary policy to help shape their economic agenda.