GRADUATE SCHOOL of BANKING AT LOUISIANA STATE UNIVERSITY

2017 Bank Study Project
Class of 2019

MONETARY ECONOMICS

Brandon N. Cline

NOTES:

1. Please use 8 l/2" x 11" paper (or paper folded to that size).
2. Attach the **Freshman Cover Sheet – Class of 2019** from http://www.gsblsu.org/students-3/ as the first page of your project.
3. Please staple your project or use a binder clip. **DO NOT** use paper clips

Complete and mail by February 15, 2018

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Part I. Monetary Policy

Go to the website of the Federal Reserve Board of Governors at www.federalreserve.gov and click on "Monetary Policy" and then on "Reports" on the left hand side of the page.

Under the "Reports" tab click on "Beige Book". Note, alternatively, that you can go directly to the Beige Book website at http://www.federalreserve.gov/monetarypolicy/beigebook/default.htm.

After reading the most recent Beige Book Report, drawing on other indicators available from http://research.stlouisfed.org/fred2/ (be sure to spend time researching this site for relevant economic data and trends), and reviewing other resources provided in class:

a. Provide a through critique of the policy actions summarized in the most recent Federal Open Market Committee Policy Statement. Note that the most recent statement/press release is available from http://www.federalreserve.gov/monetarypolicy/default.htm (The latest press release is available under the "Related Information" heading by clicking on "Recent Statement".) Based on your review of the Beige Book and an analysis and summary of recent indicators, your critique should provide specific reasons why you agree or disagree with the actions taken by the Fed. Your analysis should be 2-4 double-spaced pages in length.

b. Do you consider the current policy actions by Federal Reserve to be potentially inflationary or deflationary? Explain.

c. Considering the global economy and the recent actions of the Federal Reserve relative to those of other central banks around the world (e.g. the ECB and China), 1) explain the movements in the value of the dollar during the past year. 2) Do you expect the dollar to continue its strength in 2018? Explain why or why not.

d. Based on your preceding analysis in parts a-c, would you have voted for or against the FOMC Policy Action as described in the most recent FOMC Press Release (Recent Statement)? Why or why not?

   Keep in mind that, because this statement is formed by a committee, it is reasonable that even those members voting in the affirmative may not agree with all aspects of the policy action. So, you must determine whether the analysis, summarized in part a., gives you sufficient reason to vote against the overall policy action described in the most recent FOMC Press Release. Since you have already provided an analysis in part a. (above), your response may be limited to 1-2 paragraphs addressing the specific reasons you support, or do not support, the consensus statement.

Part II. Policy Decisions for Changing Economic Conditions

Assume for the purpose of this exercise that the following economic conditions will exist at the time of your graduation from the Graduate School of Banking at LSU in May 2019 (assume that trends are reflective of 6 months of data):

GDP: 3.4% (stable)
PCE Inflation: 3.3% (trending slightly upward)
Core PCE Inflation: 3.1% (trending slightly upward)
Headline (U3) Unemployment: 5.0% (stable)
U6 Unemployment: 8.5% (stable)
Labor Participation Rate: 65% (trending slightly upward)
Consumer Sentiment (University of Michigan): 90 (stable)
Housing Permits (new privately owned): 1 Million Units
Case Schiller Index (20 City Composite): 180 (trending upward)
Term Structure of Interest Rates (Yield Curve as of May 2017): 3-month T-bill 1.25%; 1-year T-bill 2.0%; 10-year T-bond 4.25%; 20-year T-bond 5.50%
30-Year Mortgage Rate (Average for Qualifying Mortgages): 5.50%
Federal Funds Rate (Targeted Range): 0.75 – 1.00%
Interest on Reserve Balances: .75%

a. Based on this information and what you have learned about the various "tools in the toolkit" of the Federal Reserve, prepare a 2-page (double-spaced) monetary directive. While you might describe it as generally "accommodative" or "restrictive", be sure to address how you would adjust monetary policy through the use of interest on reserves and specific types of open market operations (recall our discussion of traditional purchases and sales, QE, and the purchase/sale of MBS as well as Treasury securities). Because policy decisions are made at the margin, please feel free to speak in terms of raising (or lowering) the targeted Federal Funds rate by 25, 50, etc. basis points and raising/lowering interest paid on reserves by a specific amount from the levels indicated above. Your response should also include specific types and associated maturities of asset purchases/sales. (Hint: This refers to the currently more targeted approach to monetary policy we discussed in class).

b. Would the level of debt and deficits, tax policies, bank regulatory policies (especially those related to capital requirements and lending regulations), or other government interventions have any bearing on the monetary actions discussed in Part a. above? Explain in detail but limit your response to 2 double-spaced pages.

c. Discuss how monetary policy actions can affect your specific institution's profitability and product and service offerings. This question is designed for you to consider the effect of interest rate and associated risks on your bank's lending practices, security portfolio decisions, liability mix, and service offerings. Consequently, you are encouraged to discuss this question with senior staff members at your institution. Please limit your response to 2-3 double-spaced pages.