More from the Cato Institute 30th Annual Monetary Conference

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Moderator: **William Poole**
Senior Fellow, Cato Institute

The Fed has practically given up its independence. It is independent with the confines in the government.

QE2 was a mistake — there were already excess reserves at the banks.

Current economic problems are not monetary in nature. ECB has violated or circumvented many strictures in its charter.

Current Fed has too much of a short-term focus. Dual mandate has been tilted too far toward unemployment.

Criticizes easy monetary policy in the late 90s and 2003-2004.

Kevin Warsh
Distinguished Visiting Fellow, Hoover Institution

Diminishing returns to monetary policy. Monetary policy can be really strong at some moments, and very weak in others.

What regime are we in? An important question when setting policy.

Argues that 2008 was a panic and Fed actions were justified. Today, that's not so, where monetary policy is weak.

Fiscal contraction would allow for more aggressive monetary policy, but that is not true today. Today the fiscal is aggressive, and the Fed is buying the Treasuries being issued, giving a feel (though not reality yet) of debt monetization.

Fed is weakening credibility by their current actions.

Communications matter, but they are not everything. What the Fed does is more important than what the Fed says. Communications policy has limits.

Price stability should be the main mandate. Maximizing sustainable employment is important, but outside the remit of the Fed. Bank regulation is not as effective as it should be.

Monetary policy can't make up for bad trade and fiscal policies.

Gerald P. O'Driscoll Jr.
Senior Fellow, Cato Institute

Believes that the Fed is *de jure* independent, but not truly independent.

1. History supports a dependent Fed. Inflation was a result of loose policy 1965-85.
2. Reading transcripts shows Fed members pay attention to politics.
3. Inconsistency literature suggests independent central banks will generate inflation at times.
4. Low correlation between central bank independence and inflation.
5. Central banks are creations of the State and cannot be fully independent.

De facto independence of Fed is questionable.

Volcker could only act independently because Reagan supported him.

Failure to forecast the Great Recession lessens the legitimacy of the Fed to engage in discretionary policy.

Policy rules when they lead to good results give a central bank more room to run, more discretion.

David Malpass
President, Encima Global

Argues that present monetary policy is contractionary. Hurts savers, end misallocation of capital…

The Fed is a giant, heavily leveraged SIV, borrowing short and lending long, w/only $55B of equity capital.

Fed is sucking duration out of the fixed income markets more rapidly than the Treasury is issuing.

Capital allocation is getting warped by the Fed, leading to higher prices for gold and corporate bonds, mortgage bonds, etc.

Favors corporate profits over wages… Government and large companies favored over small. M2 not growing rapidly, even though monetary base has gone up significantly. Traditional policy transmission mechanism not working.

Does a gold model inferior to Eddy's & mine.

Q&A

Malpass: stability of monetary policy/inflation would promote growth.

GDP growth tend to raise interest rates (DM: like the old classical view), as people bid for the ability to borrow to buy growth.

Warsh: Fed is a price-maker, not a price-taker, but it affects the risk-free rate, and it affects the pricing of all assets, distorting investment