Global Economy

Jackson Hole Economic Policy Symposium: At The Cliff Edge

Expansión (Spain)
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In the shadow of the spectacular Teton Mountains in Jackson Hole, Wyoming, the Federal Reserve Bank of Kansas City held its forty-third Economic Policy Symposium from August 22 to 24. The event, attended by bankers from prominent central banks, academics and representatives from both the government and the financial sector, aims to discuss key economic issues and their implications, and monetary policy options. This year, a decade on from the Great Recession, the discussion focused on "Challenges for Monetary Policy."

Given the global economic slowdown (Germany and China), the trade war between the US and China, and high levels of geopolitical uncertainty (Brexit, Hong Kong, Italy and Iran), attention was focused on the speech by Jerome Powell, Chair of the Federal Reserve (Fed), and his vision for the future direction of monetary policy in the US.

During his speech, Powell analyzed the history of monetary policy since 1950 and raised three fundamental questions: Can the Fed resist the temptations that lead to high inflation? Can long periods of growth lead to financial instability? What is the best way to promote prosperity in a world of slow global growth, low inflation, and low interest rates?

According to Powell, although inflation is low and risks point in this direction, the Fed has the ability to avoid price rises if this is the case. Powell also emphasized that while the Fed cannot prevent economic agents from taking excessive risks, the risks of financial instability are low and regulators have adequate mechanisms to monitor them and act appropriately should they pose a danger to the economy.

On the other hand, Powell highlighted that the current environment of slow growth and low inflation increases the risk that monetary policy will be trapped in a low-interest scenario over a prolonged period. In light of this, the Fed will continue to analyze the advantages and disadvantages of possible strategies to reverse the shortfall with respect to the inflation target, the unconventional tools available in times of prosperity and times of crisis, the possibility of adding new tools, and the communication strategy. The Fed will share its findings with the public in 2020.

The Fed will also maintain its risk management strategy in order to respond adequately to developments that impact its medium- and long-term forecasts. For example, despite strong growth in private consumption and the strong labor market, the Fed decided to cut the interest rate in July to mitigate the risks presented by the global slowdown, trade policy uncertainty and low inflation.

However, Powell emphasized that the current conditions are unusual, and that the greatest challenge is how to incorporate trade policy uncertainty into its decisions. In principle, given the deterioration in financial conditions and employment and inflation forecasts, the Fed could react in the usual way by reducing the interest rate to stimulate investment and consumption. However, there is no action plan that allows monetary policy to adequately accommodate all the consequences of a trade war, particularly the impact of uncertainty.

This last item has unleashed intense debate among Fed members as to how to balance the impact of the trade war in the business cycle, with a view to monetary policy and the independence of the institution. In order to limit risks and sustain economic expansion, the Fed is very likely to cut the interest rate further in September, even though some economic indicators might suggest otherwise. If uncertainty continues to rise, additional cuts in subsequent months cannot be ruled out. However, Congress and the White House are ultimately responsible for finding an appropriate solution to reduce uncertainty.

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