October 29, 2008—Morning Session

CHAIRMAN BERNANKE. Good morning, everybody.

PARTICIPANTS. Good morning.

CHAIRMAN BERNANKE. We have some data this morning. Dave, would you like to discuss this?

MR. STOCKTON.[6] Yes. You have at your place a table on orders and shipments of durable goods, one of the more inscrutable releases to actually make sense of, but the bottom line is very little effect on our basic outlook here. As you can see in that second set of numbers, the shipments area excluding the aircraft line was up 2 percent in September. That was actually a little stronger than we had penciled in, but only enough to add a few basis points to GDP growth in the third quarter. Then you can see that it has basically been averaging flat for the last two months. This is a September figure, so it's fairly dated at this point. The orders figures, the set of numbers above—again looking at the "excluding aircraft" line—have been coming down. I wouldn't say that they're collapsing, but they're certainly weakening some. So this really has no appreciable effect on our outlook for a small decline in equipment spending in the third quarter and a more appreciable decline in the fourth.

CHAIRMAN BERNANKE. Does the resolution of the Boeing strike have any macro implications?

MR. STOCKTON. We actually predicted that the strike would end this week. It did.

MR. PLOSSER. My, you're good.

MR. STOCKTON. It wasn't looking too good last week. [Laughter] But we're expecting that it would provide a small rebound effect on first-quarter GDP growth. It's going to take a little while to get production back on track here.

[6] The materials used by Mr. Stockton are appended to this transcript (appendix 6).

CHAIRMAN BERNANKE. Other questions for Dave? Okay. If not, let's continue with our go-round. Vice Chairman.

VICE CHAIRMAN GEITHNER. Thank you, Mr. Chairman. We expect a recession at least as bad as the 1990–91 recession, with a significant risk of a deeper, more protracted downturn worse than the '80s, and a very substantial rise in the unemployment rate. Inflation is decelerating quickly, and deflationary forces are ascendant around the globe. The huge decline in energy and commodity prices will add to a very substantial downward pressure on core inflation from increased economic slack around the world. We could see an abrupt change in inflation expectations into deflationary territory.

We've seen a lot of policy action over the past few weeks. One question is whether policymakers should wait to measure the effects of these measures before going further, and I want to talk a little about that question. My view is that I don't think so. The outlook has been deteriorating ahead of the policy response. This is true both here and around the world. The magnitude and speed of the tightening financial conditions, the erosion in business and consumer confidence, the fall in actual spending, and the shift in inflation risk together present very grave risks to growth and to the financial system. Mitigating these risks is going to require more monetary policy here but even more so in the other major economies. But in addition to the very substantial easing in the global stance of monetary policy ahead, the substantial damage that has already happened to financial intermediation globally suggests that a broad-based and quite large fiscal stimulus will be critical to prevent an excessive fall in aggregate demand.

How quickly and how far should we reduce the federal funds rate in the United States? The Greenbook and the Bluebook present a very strong case for moving down another 100 basis points quickly. In fact, if I read the pictures in the Bluebook correctly, they might imply a need to get real rates to the negative 3 to negative 5 percent territory relatively quickly, if we could do that. If we don't move another 50 today, we'll be behind again. Monetary policy has effectively tightened substantially since the summer, of course, because of the intensification of financial pressures and because of the rise in forward real interest rates that have come with the rapid deceleration in expected future inflation. Beyond this meeting and this choice, our choices are harder. I think we need to get real rates lower and, to make sure we get them there, we need to keep them low enough long enough. This requires that we get the nominal fed funds rate as low as possible as soon as possible. I don't see a good case for monetary policy gradualism in the current context. The risks are too great. If we're too tentative, the damage to the financial system and to the real economy could be much greater and much harder to correct. If we end up doing too much, we can always adjust. That's an easier problem to solve. It just requires will. With global financial markets placing progressively more weight on a very severe global recession, the "keep our powder dry" and "reserve our remaining ammunition" arguments don't seem that compelling to me. We don't have much ammunition left in the fed funds rate anyway. If we hold that back, it will likely be less effective when we ultimately use it. The more powerful escalation options we have left will probably involve communications, such as continued commitments to keep rates low enough long enough that we avert creeping expectations of deflation and can be confident that inflation will come in around our target level over the forecast period.

I don't have a strong view now about how low we can go with the nominal fed funds rate without causing too much risk of damage to the functioning of financial systems. We need to look at all possible options, though. I think the principal focus of our staff's work in the coming weeks will be to put together a set of alternative policy options going forward along with the analysis of their benefits and risks so that we're in a position to act quickly enough to be effective. Just a few final points. I think this basic risk-management choice really involves three dimensions of judgment. One is about the relative probability of alternative outcomes. The second is about the relative consequences of or the damage caused by those alternative scenarios. Importantly, it also involves a judgment about the ease of correcting, adjusting, or mitigating the consequences of being wrong.

This is just a stylized presentation, but in the staff notes yesterday, there was a nice way to think about those choices. I just wanted to point out one thing about this stylized framework of those choices, which is the consequence. If you look at exhibit 5, the bottom left panel, which shows the inflation outcome associated with the "more rapid recovery" scenario, in this presentation you don't have much risk of a very bad inflation outcome in the event that we end up doing too much with too much policy and have to take that back. Again, it's important to recognize that it's not just about the probability that we attach to the alternative scenarios. It's not just about the relative impact of the consequences of those scenarios. It's about the ease with which we can correct for a judgment that was wrong—in this case, a judgment that we did too much. This may understate the complications in correcting for that error and may make it look easier than it may ultimately be, but I think it's a nice framework.

Finally, I just want to point out, just to underscore the basic point: This is not going to be principally about monetary policy going forward. If you look at the broad framework of policies that are now in place, both here and globally, and the instruments we have to play with, along with the fiscal authorities: we have monetary policy; we have the liquidity arrangements and what we do with our balance sheet over time; we, the collectively integrated government, have the broad fiscal policy questions and the scope for either a broad-based substantial fiscal package or more-targeted fiscal measures, as the Chairman suggested, to focus on the credit markets; and we have the capacity to alter the framework of capital and guarantees that is now in place. Beyond that, the government here also has the ability to change what the GSEs, the FHA, and the FHLB can do. So when we think about escalating going forward, to go to President Fisher's question from yesterday, we have the ability on all these fronts to do more if that's necessary and prudent. But I think the mix has already changed substantially. It was probably mostly fiscal nine months ago. It is certainly mostly fiscal now in a broader sense, except that many of the major economies going forward will have to move monetary policy very substantially. Thank you.

CHAIRMAN BERNANKE. Thank you. Governor Kohn.

MR. KOHN. Thank you, Mr. Chairman. A number of the presentations yesterday talked about falling off a cliff in the middle of September. I think we need to remind ourselves that we were sliding downhill pretty fast before we hit that cliff. The third-quarter data, which aren't really affected by what happened in the last two weeks of September, indicate that the economy was weaker than we thought at the time of the last FOMC meeting. I think Dave Stockton or Norm Morin noted that about a third of their downward revision reflected incoming data rather than the credit tightening. That was especially true for consumption, with real consumption spending falling through the summer, responding to lower employment and tighter credit. Private domestic final purchases were revised down to a decline of 3½ percent in the third quarter after being flat in the first half.

Housing price declines picked up in August, and I think the deteriorating economy and concerns about the economy were reflected in increased nervousness in financial markets over the summer into the first half of September. It was really those worries about what the losses were going to be and how they would spread from mortgages to loan books generally—that deepening pessimism—that doomed the marginal institutions like AIG and Lehman and the GSEs. They just didn't have a chance to recapitalize or stabilize themselves when so many of the other market participants were worried about what their own positions would be. The resulting flight to liquidity and safety, the loss of confidence that followed, the deepening gloom, and the failures and near failures and associated losses triggered a tremendous tightening of financial conditions over the intermeeting period—President Yellen and others discussed this—despite the 50 basis points of easing. Even after the 900 point increase yesterday, equity prices are down about 20 or 22 percent over the intermeeting period. The dollar is up 10 percent. Corporate borrowing rates are up for investment-grade corporations 200 to 250 basis points. Banks tell us that they're tightening across every dimension of their lending; and other lenders, like finance companies, are also cutting back very, very sharply. You can see this in autos clearly, but the stress is much broader than just the auto finance companies.

We have good programs in place to deal with many of these problems—the capital, the FDIC guarantees, and the Federal Reserve balance sheet facilities—and they are having some effects relative to the freezing up of markets that we had in mid-September. We can see that interbank spreads and LIBOR have come down some. Commercial paper rose, I guess, on Monday with the introduction of our facility. Declines in money market mutual funds have abated, though they're still there, and there are some signs that maturities are beginning to lengthen in funding markets. As these programs are more fully implemented, we'll see some greater effects—including, I hope, some greater willingness to extend credit. I also assume that the fiscal package is necessary, as in the Greenbook "fiscal stimulus" alternative.

But we need to remember that the improvement we've seen over the last couple of days is relative to a situation in which funding markets were in effect frozen beyond a very short term, and although a sharp snapback is possible, as President Plosser was noting yesterday, I think further gains are more likely to be gradual. In the past few days, the declines in LIBOR have seemed very grudging and gradual, and LIBOR remains quite high—I think close to 75 basis points higher—relative to what it was in mid-August, before we even cut rates. This was three-month LIBOR that I looked at this morning. In an environment of economic weakness, spreading credit problems, falling house prices, a number of false dawns in this episode so far, and death and near-death experiences, lenders and investors are going to continue to be very cautious and conserve their liquidity and capital. So despite further improvements, financial conditions will remain quite tight. The effects of lower wealth, higher borrowing costs, the stronger dollar, and tighter nonprice terms of credit will play out over the next few quarters, putting downward pressure on an economy that was already in recession.

At the same time, heightened uncertainty and fear of future problems caused a sharp deterioration in attitudes and spending even apart from the effects of credit. Judging from the Conference Board index, regional purchasing manager surveys, and anecdotes—including what we heard around the table yesterday—it feels like a recessionary psychology, as I think Charlie Evans called it. Others talked about pulling back and curtailment of discretionary spending in train, and this is not just caused by credit effects. This is just fear. So we've had a downward shift in aggregate demand as well as a movement along the aggregate demand curve, and this downward shift in aggregate demand will propagate through multiplier–accelerator effects even if attitudes begin to improve some.

The global dimensions of the shock are important. As we talked about yesterday, heightened risk aversion has had a pronounced effect on emerging market economies as well as on industrial economies. Net exports cushioned domestic weakness in the first half of the year, but with the dollar strong, if anything we'll be absorbing weakness from abroad, not exporting it, as the rest of the year goes on and we get into next year. Growing credit problems abroad will only add to pressures on many large global lenders who might have thought they were diversified geographically. But a little like our U.S. housing market, they will find that diversification doesn't really work when there's a global recession.

The net effect of all of this is a much weaker growth path for the economy. In my forecast, I had a somewhat steeper near-term decline in economic activity and a slightly sharper bounceback than the staff, including my fiscal assumption, but I also have the unemployment rate peaking at over 7 percent, as the Greenbook did. With commodity prices plunging, the added slack maintained through several years, and declines in inflation expectations, inflation will be on a clear downward track. In the Greenbook, this downward track for inflation obtained even with the assumption of some rebound in commodity prices and the resumption of dollar weakness. In my forecast for inflation from next year on, inflation was at or below the 1½ to 2 percent rate I would like to see as a steady state consistent with avoiding the zero bound when adverse shocks hit.

Critically, the downside risks around activity forecasts are huge and tilted to the downside. I think they're huge because we've never seen a situation like this before, certainly not in my experience dating all the way back to 1970, and have only the vaguest notion of how it will play out in financial markets and spending. I think they're tilted to the downside because I, like the staff, assumed a gradual improvement in financial markets. That could be delayed or even go in the wrong direction for a time, further tightening financial conditions. In addition, the effect on spending of the heightened concerns and tighter credit conditions could be larger and longer lasting than I assumed. For some time an important downside risk to the forecast has been a sharp upward revision to household saving as wealth, job availability, and borrowing capacity eroded. I assumed a moderate increase in the saving rate, but I can definitely see the possibility that adverse developments will galvanize a more thorough rethinking by the household sector of what saving is needed, and that will affect investment as well as consumption. We'll get to the policy implications of all of this in the next round. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Thank you. Governor Warsh.

MR. WARSH. Thank you, Mr. Chairman. The first sentence of the Greenbook said that "recent economic and financial news has been dismal"; and the last sentence on page 1 of the Bluebook said that "markets generally remain extremely illiquid and volatile." I can't do better than that, but I can certainly do worse; so let me give that a try. [Laughter]

Market prices and official and corporate data confirm an additional leg down in mid-September, which has been much discussed. I think it is going to become increasingly clear that October, particularly the first 20 days of the month, was materially worse. So if we fell off the cliff in the middle of September, I think that once the data come out and find their way into the marketplace in October, the Greenbook forecast might look a bit more positive than the facts on the ground would suggest. As a result, my own forecast is less optimistic than the Greenbook, but there is plenty of uncertainty, as I think Dave Stockton talked about yesterday.

Let me make a few comments about financial markets before turning to the broader economy. I expect a prolonged period of significantly strained credit markets, and that strain is likely to be exacerbated between now and year-end and I suspect even well into 2009. The credit intermediation process that we've talked about is fundamentally broken. I talked six months ago about the financial architecture that was fundamentally being changed. I think that has all happened faster than I could have anticipated. Confidence, not just in counterparties but in basic rules of doing business across financial markets, has been lost, and my own sense is that loss of confidence is not easily fixed, even by well-intended government programs. We should all be quite patient in terms of seeing the benefits of the rather dramatic actions taken by the official sector, both here in the United States and overseas. Corporate bond rates and other risk spreads may well fall from their recent peaks, as suggested in the Greenbook, but spreads across asset classes are likely to stay far wider than historical norms throughout the forecast period. I think these new spread relationships are uncertain. So what we thought would be sort of normal spreads of LIBOR and normal spreads of corporate bonds, all have to be reassessed not just by us but also by market participants. Even if credit is now made more available to businesses through some of these new Treasury and other programs, I suspect the all-in cost of capital is likely to materially impede business investment, particularly given expectations by businesses for a weaker economy in the upcoming period. As Vice Chairman Geithner suggested, monetary policy might be able to do a bit about this, but it is not going to be able to change it very much.

Let me turn to three points on the economy before closing. First, in the near term, given my sense of how October is tracking, it's likely to be extraordinarily weak. I expect weaker fourth-quarter consumption than the Greenbook, weaker labor markets going into 2009, and a materially weaker fourth-quarter GDP print. Some labor surveys—including some of my own preferred measures, like the JOLTS—seem to be holding up; but I'm not sure that that's going to hold for another couple of months. So I'd expect the labor markets to trend more materially in the direction that I've discussed.

Well, what about beyond the near term? What about 2009 and beyond? It strikes me that the catalysts for marked improvement are lacking. When I think about fiscal policy, regulatory policy, tax policy, and trade policy, which I talked about previously, it's not obvious to me that any of those are going to provide some kind of catalyst for a marked change in the contour of the economy. On the fiscal front, I assume that the fiscal stimulus is likely to be larger, maybe even materially larger, than in the Greenbook alternative simulation, but my own conclusions are similar to the Greenbook's, which is that I'm not sure it's going to be terribly effective. I'm not sure it's going to be constructed in that way, and I'm not sure it will do nearly as much as it will inevitably be advertised to do. A more disturbing trend probably even than the efficacy of a fiscal package—which in my own view is absolutely necessary, but again I query whether it's going to be structured in a way to do what it needs to do—is that potential output in the forecast period is likely to fall. Trend growth rates are coming down, and I expect productivity to fall perhaps even more than in the Greenbook projection. The vaunted resilience of the U.S. economy, which I've talked about for a long time, is certainly going to be tested during this period. Business investment, it strikes me, will be a useful gauge as we get into the first quarter of 2009 to see how tough an economic period we have in front of us, and I worry about the decisions that business people will be making. Now, of course, against all of this, markets could snap back, as we saw a little yesterday—2009 could look better. We have to remain open minded about the possibility that the economy will continue, as it has over the past ten or fifteen years, to outperform model-based expectations.

Let me turn to foreign growth. These decouplers, which were so prominent for so long, are somehow hard to find these days. Foreign growth strikes me as likely to fall faster and stay lower than in the Greenbook projection. The road back is not likely to begin as early as the first quarter of 2009 for our major trading partners. The "more financial fallout" alternative simulation strikes me as significantly more likely for foreign growth. In light of a growth trajectory that is better here in the United States than outside the United States, at least relative to current market expectations, I'd expect the foreign exchange value of the dollar on balance to strengthen against a basket of foreign currencies.

So let me turn finally to inflation. The trend on import prices, the broad measures of commodity prices, and the expected dollar strength all suggest that inflation problems are abating markedly. I think an open question, which isn't likely to be dispositive but is likely to be interesting, is how sticky prices are, particularly from the consumer product companies during this period—how long the various surcharges and increases in prices we've seen can stay high and the companies attempt to keep profit margins. My guess is that they can make profit margins look decent for another quarter or two; but beyond that, prices across a broad set of products and services are likely to retrace some of the gains in recent periods. I'll save the balance of my remarks for the next round. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Thank you. Governor Kroszner.

MR. KROSZNER. Thank you. Well, the autumnal bonfires have really sort of heated up since the last FOMC meeting. I think we have evidence in the United States and now worldwide of what emerging market literature calls "sudden stops"—a sudden stopping of the flow of capital, the so-called flow of hot money, into Latin America or other countries and the devastating impact that could have when suddenly credit is no longer available. I've been talking about the slow burn of the problems in the credit markets, but I think we saw that move up to a different level globally over the past six weeks. This is the concern that we had earlier in the year about a regime shift. We seem to have moved from a growth regime to a sliding-by-with-some-growth regime and now to a contractionary one and the nonlinear effects that we had been concerned about.

As we always say, it's particularly difficult to predict where the economy is going to go. But there's evidence of why it's so difficult because almost any measure of volatility is up dramatically. That's true on the financial market side, on the real side, as well as just in movements of consumer confidence. So I think that we can say with some confidence that it is particularly difficult to predict which way things are going to go. As many people have said before, a few spreads have come down, but given the extent of our actions and those of other governments around the world—central banks, fiscal authorities, et cetera—it is surprising that there has been so little effect.

Now, maybe it's just because so much is going on that there's a fair amount of confusion and uncertainty about what the programs mean, how they will actually be implemented, and to whom they will be applied. I think that's perhaps part of the reason for some of the spreads not coming down with respect to interbank borrowing—there is a lack of clarity about exactly how the FDIC program will operate and exactly how the TARP will operate. We'll hear more about that in a bit, but I think it's going to take time for people to feel confident about how that will work. Also, I think there is real uncertainty because after thirty days some banks may not get the guarantees or may have the guarantees pulled back. I think there is also a lot of uncertainty about who will get TARP funding and who is qualified for TARP funding. As information comes out about people not being qualified or markets being concerned that individual institutions are not going to be qualified, that could put on a lot of pressure. Unfortunately, that's going to be coming in addition to the end-of-the-year pressures. So I see a number of looming risks, particularly in the financial services sector, as we fully implement and clarify some of the programs that I think on balance can be helpful but that can actually cause some uncertainty at individual institutions. Others have also mentioned broader challenges in the emerging markets and the insurance companies and certainly we have the hedge fund redemptions that are looming. I'm very concerned about trying to get over the end of the year with so many different pieces putting additional pressure on. Even some of the pieces that we thought would be helpful potentially have a lot of downside risk to them.

But even if we get through this—and the government guarantee programs, the special liquidity facilities, and the negative real rates that we have and potentially may make even more negative would provide some support—the fundamental uncertainty is not going to be resolved until we see what is going to work in the financial sector, what's going to be the successful business model, and what are going to be the new sets of activities that can be undertaken. Will certain funding markets come back and at what spread once you take away all these special programs? Until that is worked out, I don't see how the markets can figure out who will survive and who won't, who is going to be there in three months and who isn't. I think that the programs are very valuable in providing a time out—a time for people to reassess. But until there's greater clarity in those financing markets going forward, I don't think the markets will actually be able to recover. That why the alternative simulation that puts things off a bit more seems quite sensible to me.

Some specifics on consumption. As I often do, I talked with some of the largest providers of consumer credit in the United States. They are reporting, exactly as Governor Kohn said, that consumption or spending growth was decelerating through the summer, but it did seem to get much more rapid in September and October. One of the large companies actually reported significant contraction on the consumer side of spending. On the small business side, it was still positive but down from double-digit growth in the second quarter to basically flat. They also looked across income categories. This is not a phenomenon of just the people at one or the other end of the spectrum. It seemed to be across the board for what they looked at. All of them have reported, just as the Senior Loan Officer Opinion Survey did, a significant reduction of credit lines. So even if we're not seeing credit in and of itself having contracted yet, the ability to get credit down the line is going to be much, much more difficult. Also the funding markets for the credit card companies have effectively closed. They may reopen. Things may come back, but I think it's going to take time for that to happen, and they were certainly not optimistic about that.

As virtually everyone has mentioned, inflationary pressures for a variety of reasons are much lower, and I think that fits into what the Vice Chairman said about thinking about the costs of moving now and perhaps moving "too quickly." There seem to be lower costs now in being a bit more aggressive than, let's say, six months ago because much less inflationary pressure seems to be out there. I think a prudent risk-management point of view would certainly take into account those costs and benefits. We need to use our monetary policy tools as effectively as we can and then work with the other tools that a number of others have mentioned to try to get the markets to be more comfortable with where things will go and then be able to lend to each other—to have the unlocking of the credit markets without government guarantees, without negative interest rates, and without extraordinary liquidity facilities. Thank you.

CHAIRMAN BERNANKE. Thank you. Governor Duke.

MS. DUKE. Thank you, Mr. Chairman. I focused on the "more rapid financial recovery" scenario, not so much because I thought it was the most likely but just trying to think what it would take to bring that about. I'm not sure that the policy changes we have done recently will do that, but I am fairly certain that we are going to keep at it until we find something that restores confidence.

I was shocked when I was looking at the Bluebook at how short a time has passed since the meltdown of all these major financial institutions—Fannie, Freddie, Lehman, AIG, WaMu, and Wachovia. There is a sense among those who were affected, who lost from it, that they just really didn't see it coming, at least not at this speed, and that all of them had adequate regulatory capital, and the bankers at least were used to watching a sort of gradual burndown of that capital before institutions failed. They had a sense of being unable to predict who was going to be saved, who was going to get whacked, and who would be the winners and the losers. So subsequently both the banks and their customers froze, and there has been very little activity since then. All the banks I talked to reported having stopped doing business with one or more counterparties and that one or more counterparties had stopped doing business with them, and they were shocked by both of those things.

So, first and foremost, it is clear that we need to restore confidence and predictability. In this sense, the recent moves to increase deposit insurance, to guarantee interbank short-term debt, and to provide capital on the same terms to banks of all sizes should be helpful—but only as long as we can do this without creating new uncertainty about who is going to benefit and who is not. Without being too subjective or too cute, we need at this point just to create confidence in our entire system. The demonstrable and preemptive support of the nine largest financial institutions; our public support of AIG; similar support of globally important banks by their home countries; and the resolution of Wachovia and National City, the two largest troubled institutions, without loss should help us avoid shocking surprises while everybody calms down.

In this light, my conversation with the banks centered mostly on their reactions to the recent policy changes. All thought the deposit insurance increase was helpful. They varied in their estimates of the importance of the increase to $250,000, with a lot of them pointing out that for consumers they had already really restructured deposits to insure fairly large amounts, and several were using the CDARS (Certificate of Deposit Account Registry Service) program for larger depositors. They were even more enthusiastic about the coverage of transaction accounts, although one banker felt as though this coverage really hadn't gotten as much visibility as it should, particularly with corporate treasurers, and many had already seen corporate and institutional deposits move into Treasuries and felt as though it was going to be difficult to get those back. There was even much more confusion about the guarantee of short-term debt. One banker questioned how they would know whether the fed funds sold to another bank actually fell inside the 125 percent cap. Another one thought that the all-or-nothing structure of the guarantee was a little difficult to work with. Interestingly, and as I pointed out yesterday when I asked about interest on reserves, nobody had even focused on it. They had bigger fish to fry. So I wouldn't read anything into those early results.

As for capital injections, most were taking a hard look at it. Two large community banks had just issued private capital to support growth that had been attracted from competitors, but they thought that they could profitably deploy the new capital. Other banks were interested in having the capital just in case they had the opportunity to buy weaker competitors, particularly deposits or branches in problem resolutions. None was really concerned about the announced restrictions, but a number of them were somewhat suspicious of the possible restrictions that might come later. Some small banks with already high levels of capital somehow felt pressured to apply anyway just to show that they would qualify, although they didn't think it would give them much growth. In all cases, capital is only part of the story. They also need reliable funding if they are going to expand lending. This will have to come either from reliable deposit growth or from the reopening of secondary markets because all of them were reluctant to increase borrowing from any source. The loan-to-deposit ratio is growing new fans. In terms of lending, all reported that they were still lending to their relationship customers, and they were cutting back on credit to credit-only customers. As one defined it, if 90 percent of the revenue is coming from credit, then that was a customer relationship they wanted to exit.

They still report no significant deterioration in the C&I book. I asked about drawdowns from companies, and across the board they said they had seen it in a couple of instances but really they had not seen an awful lot of that, so that might be some posturing rather than actual drawdowns on the credit. They are, however, exercising strong pricing discipline, and the pricing decisions, more than credit decisions, are being escalated up the approval chain, actively outreaching to customers that they want to keep and assuring them of credit availability. But because they have no pricing power on the funding side and pricing became very skinny on loans in recent years, there is a high level of sticker shock going on, which might explain some of the complaints about unreasonable terms. They also report very high levels of caution from their customers, with the descriptions ranging from "hunkering down" to "wait and see." There were more anecdotal reports of companies riding trade credit by trying to accelerate receivables or extend payables. Now, whether this is due to the actual or to the perceived unavailability of credit from banks is not yet clear.

Real pressure is on commercial real estate lending. They are very selective in new projects. They are processing renewals for only one year, using the opportunity to shore up pricing and underwriting, and no longer writing mini-perms. Nobody is doing those. So far, the performance is holding up on commercial properties, with strong performance on apartments and weakness showing up in retail. Residential construction and land development continues to be a problem. In visiting the San Francisco and the Kansas City Banks, I was shocked to hear the same story from large builders about land sales. One builder had a 300-acre parcel with a cost of $75,000 an acre, listed it for $15,000 an acre, and sold it for $10,700. Another reported a property with a cost basis of $120 million selling for $12 million. Apparently, the impetus for both of these transactions was a judgment that the cash received from tax refunds was more advantageous than holding out for better pricing. So the outlook for lending in residential construction or commercial real estate is dim far into the future, and I would say the same thing for syndicated or participated lending. However, to the extent that banks can exit those segments, it should free up funds for normal lending for businesses and consumers. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. President Fisher.

MR. FISHER. Mr. Chairman, I would like to ask Governor Duke a question. Do you sense in this deep dive into the institutions that you talked to that they are benefiting from cuts in the fed funds rate? Are they enthusiastic or not about the prospect for a lower fed funds rate?

MS. DUKE. Actually, I have heard a couple of reports that, when we did that last 50 basis point cut, banks did not lower their prime. A lot of banks still have prime-related credits. As we lower the rates, whether it makes a difference on anything else, it affects the prime, and there are still an awful lot of 5 percent CDs out there. So as we lower rates, we are cutting into those margins, and it is likely to turn some of them negative.

MR. LACKER. Mr. Chairman?

CHAIRMAN BERNANKE. President Lacker.

MR. LACKER. I would just echo that. I have heard the same thing from bankers in our District—just vociferous complaints about lowering rates because their loan rates go down but their cost of funds doesn't.

MR. FISHER. Mr. Chairman, if I could just add one other thing. We are hearing more and more about people switching to LIBOR, trying to shift their lending contracts to LIBOR rather aggressively, obviously, because they are higher rates. But I'm wondering if you're picking that up as well.

MS. DUKE. Well, I don't know. But just as soon as they get them switched over there, maybe we'll be successful at bringing LIBOR down.

CHAIRMAN BERNANKE. Okay. Thank you. Let me try to summarize all that I heard today and yesterday, and then I'll try to add some new comments to that. The outlook for economic growth appears to have deteriorated quite significantly since the last meeting. Data on consumer spending, production, and employment had weakened more than expected even before the recent intensification of the financial crisis. Over the past six weeks or so, however, financial conditions have greatly worsened, and risk aversion has increased, despite actions here and abroad to stabilize the banking system. Equity values have declined sharply amid conditions of low liquidity and extraordinary volatility.

Credit market conditions have improved modestly since the global actions to recapitalize banks and guarantee their deposits, assisted also by additional central bank liquidity actions. However, in almost all credit markets, spreads remain much wider, maturities shorter, and availability more constrained than was the case before the intensification of the crisis. Firms face continued funding risk and rollover risk. Banks have probably not reserved sufficiently for the credit losses to come, and hedge funds will be hitting their net asset value triggers in greater numbers, forcing them to liquidate assets. The duration of future financial turmoil is hard to judge, but it could be lengthy.

The worst thing is that financial conditions appear already to have had a significant and remarkably quick effect on activity and consumer and business expectations and plans. Most Committee participants see us in or entering a recession and have marked down significantly their expectations for near-term growth or for the pace of the recovery. The difficulty of predicting the course of the crisis or its effects on the economy has also increased forecast uncertainty. In particular, the ultimate effects of some major policy actions, such as the creation of the TARP and the bank guarantee, are not yet known. Uncertainty about future policy actions, as well as uncertainty about the economy, has affected behavior in markets and the broader economy.

Consumer spending has weakened considerably and probably fell sharply in the third quarter, reflecting in part a recessionary psychology. Consumer durables, such as automobiles and discretionary expenditures, have been particularly hard hit. This weakness reflects the same set of negative influences on consumption that we have been seeing for a while, now compounded by losses of equity wealth and confidence effects on prices, although lower oil prices may provide some relief. The labor market continues to decline, with many firms reporting that they are cutting back workers. The housing sector has not been noticeably worse than expected, and reports are somewhat mixed. But on a national basis, the contraction is continuing, and recent developments in the economy and credit markets are likely to have adverse effects. Inventories of unsold new homes remain high, putting pressure on prices. Nonresidential construction continues at a moderate pace; but backlogs are falling, and the sector is looking increasingly vulnerable to weakening fundamentals and tighter credit conditions. Whether a new fiscal stimulus package will be passed and to what extent such a package would be helpful remain open questions. Manufacturing production has weakened significantly as have expectations of demand, including export demand. Credit is becoming more of a problem for many firms and their customers. Spending on equipment and software appears to have slowed, reflecting greater pessimism and uncertainty. Falling commodity prices may reduce mining activity and cool the boom in agriculture. On the plus side, firms are reporting fewer cost pressures, and inventories do not appear excessive.

Deterioration in global growth expectations has been marked. Industrial economies had already shown signs of slowing, and they have been hit hard by recent financial developments. Emerging market economies, until recently evidently not much affected by the U.S. slowdown, have in recent weeks also been hit hard by the spreading financial crisis. Together with the stronger dollar, these developments are likely to restrain future growth of U.S. exports.

Inflation risks have declined materially, reflecting the fall in the prices of energy and other commodities, the stronger dollar, and the prospect of considerable economic slack. Firms report much reduced pricing power and lower markups. Inflation expectations have come down, both in the surveys and in the TIPS market, though it wasn't noted—but I will note—that the TIPS market is distorted by illiquidity and other problems there. Most participants see both overall and core inflation moderating in the coming quarters toward levels consistent with price stability, with some seeing a risk of undesirably low rates of inflation. Some note, however, that financial dislocations affect aggregate supply as well as aggregate demand and may reduce the extent to which slower growth damps inflation. So that's just my sense. Any comments? Additions?

Let me make just a few additional comments, none of which will be radically different from what we have already discussed. I do think it is overwhelmingly clear that we are now in a recession and that it is going to be a severe one. To give some sense of perspective, the postwar record for duration is 16 months. If the NBER sets this experience as having begun early this year, I think we have a reasonable chance to break that record. The largest increase from peak to trough in unemployment rate was in 1981. It was 3.6 percentage points. Starting from 4.4 percent, I think we have a chance to come close to that number. Yesterday's drop in consumer confidence in one month from 61 to 38 shattered the previous low of 43 in December

1975. So I think we are talking about an episode here that could easily be among the largest postwar recessions.

We don't know how things would have evolved without the developments in September, but obviously we have to deal with that reality. It was just a few weeks ago that we were dealing with what might have been a true systemic crisis, in the week leading up to the G-7 and IMF meeting. I think it has been very fortunate that Europe, the United States, and other countries have adopted vigorous responses to that, including bank capitalization, bank guarantees, and other measures. That has been very important in calming the situation somewhat and reducing the systemic aspects of investor concerns. That being said, concern about counterparties remains very strong. Risk aversion is intense, spreads remain high, and I think that this has now become really pervasive. It isn't just a question of junk bonds and weak borrowers or weak credit histories. The spreads on GSE debt, on high-grade corporate debt, and other areas have also widened, leading to a very broad based tightening in credit conditions. So I think that, overall, any reasonable reading of financial conditions suggests that the tightening of credit or financial conditions in the last six weeks or so has been quite substantial and overwhelms the effects of our coordinated rate cut.

Now, normally you would expect to see a tightening of credit conditions affect the economy with some lag. It takes time for people to borrow money and to use the money they borrow to make expenditures. But compared with that prediction, we have instead seen a sudden stop—a remarkable and very rapid effect on economic activity. It is possible this is due less to the direct effects of credit availability and more to the psychological impact of these events. One possible analogy is the 1980 Carter credit controls, when the government announced what seemed to be a tightening of credit. There was a very sharp response in economic activity, probably based more on expectations than on actual credit availability. Unfortunately, the credit controls could be removed by government fiat; we are not able to do that today.

One interesting development is that the labor market has not yet shown as much weakness as one would expect. Unemployment insurance claims and other indicators do not yet show a marked deterioration. I expect that we will see more deterioration of the labor market.

Besides the intensification of the financial crisis that has markedly increased the restrictiveness of financial conditions, I think the other very important development since our last meeting has been the internationalization of the crisis. We had already seen weakening in Europe before the most recent intensification, but it has become much more severe. There is little doubt that the United Kingdom and Europe are in or about to enter recession. My sense is that their monetary policy responses will be stronger than what the Greenbook anticipates. I believe they will be very aggressive in responding to that.

A new and particularly worrying development is the fact that the crisis has now spread beyond the industrial countries to the emerging markets. The G-7 weekend was quite an interesting one. It was a striking experience. I heard over and over again from the Indians, from the Brazilians, and from all over the world that, until the middle of September we were fine, we were not being much affected, we didn't see much effect on our trade flows, and suddenly everything changed; and now we are under severe stress. We are seeing tremendous outflows. Our currencies are plummeting. Commodity price declines are hurting many countries. I think that is going to be a very significant development as we go forward.

Just to give some data, in just a few weeks the EMBI spread, the emerging market sovereign debt spread, went from 280 basis points to 850 basis points; and the emerging market equity index has fallen about 40 percent since the last meeting. It is not obvious that these changes were justified by economic fundamentals. Many of these countries are very well run and had shown a lot of progress in their domestic policies and their domestic economies. Instead, I think they are suffering contagion from us mostly. Unfortunately, the implications of this will be not only the usual trade and commodity price type of implications but also, and even more important, financial implications. We are now seeing that the adverse feedback loop, which we've been talking about for a long time in the United States, is becoming a global phenomenon. In particular, European banks are very heavily exposed to emerging market debt. So we are going to see yet more of this interaction between the financial markets and the broader economy, except at a global rather than a national level. These developments, obviously, are very disturbing and don't bode well for U.S. growth or now for global growth. Somewhat ironically, all of this deterioration in the global outlook has led the dollar to appreciate very sharply, which is interesting to say the least. For us that obviously also has important implications for inflation, and as Governor Kohn mentioned, it means that we will be less a recipient of foreign strength and more a supporter of foreign weakness than we have been until now.

On inflation, I know there is some discomfort in talking about a 1 percent policy rate and promising to keep it low for a protracted period—and all those things. We have seen this movie before, and I think we all have to recognize the importance of watching the implications of that for our economy and for asset prices and to take quite seriously the responsibility for removing accommodation in a timely fashion once the crisis has begun to moderate. That being said, I don't think that there is really any case in the near term to be worrying very much about inflation—or, perhaps even less so, the dollar—as we look at our policy. Pricing power is evaporating. And given what is happening in the global economy, I don't see a commodity price boom any time soon, although I think as the economies do begin to recover in the next year or so that we might see some recovery in commodity prices.

So I think that, as everyone has indicated, this is a very worrisome situation. I don't think we have control of it. I don't think we know what the bottom is, so we have to remain very flexible and very open to new initiatives as they become necessary. There has been some comparison of this to the Japanese situation. I'm beginning to wonder if that might not be a good outcome. The advantage of the Japanese was, first of all, that they were isolated. The rest of the world was doing okay, and they were able to draw strength from their exports and the rest of the global economy. Although they had very slow growth, they never really had a deep recession or big increases in unemployment. I think we are looking at perhaps a much sharper episode, and our challenge will be to make sure that it doesn't persist longer.

I do think that one lesson of both Japan and the 1930s as well as other experiences is that passivity is not a good answer. We do have to continue to be aggressive. We have to continue to look for solutions. Some of them are not going to work. Some of them are going to add to uncertainty. I recognize that critique. I realize it's a valid critique. But I don't think that this is going to be a self-correcting thing anytime soon. I think we are going to have to continue to provide support of all kinds to the economy. Let me stop there and, unless there is any question or comment, ask Brian to introduce the policy round.

MR. MADIGAN.[7] Thank you, Mr. Chairman. I will be referring to the version of table 1 that was distributed to you on Monday. It is reproduced in the package before you labeled "Material for Briefing on Monetary Policy Alternatives." Changes in the language relative to the Bluebook version are shown in blue.

Starting on the right-hand side of the table, even though members saw the economic and financial information that became available over the intermeeting period as worse than expected, they might be inclined to leave the stance of policy unchanged at today's meeting, as in alternative C. As noted yesterday, your

[7] The materials used by Mr. Madigan are appended to this transcript (appendix 7).

economic projections reveal that many of you anticipate that inflation pressures will diminish less quickly than the staff anticipates, and several of you noted explicitly that you thought less easing would be appropriate than was assumed in the Greenbook forecast. Also, the Committee already reduced rates in early October, responding to at least some of the adverse economic news. Moreover, the Federal Reserve has put in place additional facilities to support credit intermediation, and the Treasury and the FDIC are moving quickly with the implementation of other programs that should, with time, help stabilize financial institutions and markets and enhance the flow of credit to households and businesses. Finally, you might believe that the Congress is likely to enact a second fiscal stimulus package, possibly reducing the need for additional monetary policy accommodation.

The rationale section of the statement suggested for alternative C would acknowledge the intensification of financial turmoil and the weakening of the economic outlook. However, it would also cite the range of policy actions taken in recent weeks as factors that should help over time to improve credit conditions and promote a return to moderate economic growth. The language on inflation would be essentially identical to that used in the Committee's statement earlier this month, noting that the upside risks to inflation have been reduced. The risk assessment would state explicitly that the Committee's primary concern is the downside risks to growth, suggesting a predilection for lowering rates. Nonetheless, with market participants anticipating an easing today—a 50 basis point move is seen as most likely—an announcement along the lines of alternative C would point to a much higher trajectory for the federal funds rate over the next few months than investors had expected. Short- and intermediate-term Treasury yields would likely jump, credit spreads probably would increase further, and equity prices might decline sharply.

If the Committee is of the view that further policy accommodation is appropriate at this time but is also quite uncertain about the extent of rate reductions that will ultimately be required, it might be attracted to the 25 basis point easing of alternative B at this meeting. Members might have a less pessimistic outlook for the economy than that presented as the baseline in the Greenbook or might at least be quite uncertain as to the extent of the negative forces at work in the economy. At the same time, you may view the incoming information as suggesting that the 50 basis point easing earlier this month is unlikely to be sufficient to adequately balance the risks to economic activity and inflation. Given these considerations, you might see modest further easing today as appropriate and be prepared to cut rates again in coming months should developments warrant.

The statement proposed for alternative B would note that the pace of economic activity appears to have slowed markedly, and it would repeat language from your early October statement indicating that the financial market turmoil is likely to exert additional restraint on spending. The announcement would also indicate that, in light of the decline in the prices of energy and other commodities, the Committee expects inflation to moderate in coming quarters to levels consistent with price stability. As noted in a box in the Bluebook, we think that, in view of your previous policy communications, outside analysts would interpret such a statement on the inflation outlook as indicating that the Committee anticipates that overall inflation will drop to around 1½ percent to 1¾ percent before long, a indication that would be consistent with the central tendency of your inflation projections for 2009. The risk assessment in alternative B, paragraph 4, would cite the same broad range of policy actions that was proposed in alternative C, paragraph 2. It would indicate that the predominant concern of the Committee is the downside risks to economic growth. Market participants see a 25 basis point easing at this meeting as possible, but at this point they seem to place significantly higher odds on a 50 basis point reduction. The explicit citation of downside risks to growth would suggest that further easing could be forthcoming after this meeting, but this announcement still would suggest a higher path for the federal funds rate than they anticipate. Consequently, short- and intermediate-term rates might tend to edge up after such an announcement, credit spreads might widen somewhat further, and equity prices might decline.

Under alternative A, the Committee would ease policy 50 basis points at this meeting. An economic outlook along the lines of the Greenbook forecast would provide one rationale for choosing this alternative. The Greenbook forecast for aggregate demand has been slashed dramatically, importantly reflecting a sharp decline in equity prices, a steep rise in credit risk premiums, and a considerable climb in the foreign exchange value of the dollar. One metric for this revision is the Greenbook-consistent measure of the short-run equilibrium real interest rate, r*, which has been cut nearly 3 percentage points since the September meeting to a level of about minus 3 percent. That level is about 2 percentage points below the actual real funds rate defined on a consistent basis. The staff outlook for a protracted period of substantial economic slack, together with the recent plunge in energy prices, points to a considerable diminution of inflation pressures, with overall inflation falling to 1½ percent next year in the Greenbook forecast—even with the Greenbook's assumption of 100 basis points of further easing by early next year. But even those who are somewhat less pessimistic about the outlook than the Board staff might view the modal outlook as having deteriorated enough, or the downside risks as having increased enough, to warrant a 50 basis point rate cut today.

The rationale language for alternative A in the revised version of table 1 is similar to that for alternative B, but alternative A, paragraph 2, notes additional factors that are restraining growth. The risk assessment, too, is similar to that for alternative B, but it references the rate reduction that would be implemented today under this alternative and notes that downside risks to growth remain, without saying that the downside risks are the Committee's predominant concern. An announcement along these lines seems largely consistent with market participants' expectations, and the market reaction would likely be relatively small. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Thank you. Questions for Brian? All right. If there are no questions, why don't we begin our go-round. President Lockhart.

MR. LOCKHART. Thank you, Mr. Chairman. I think that this is a tough call. I support alternative B, with the statement wording as presented. In my thinking, a 25 basis point cut today is part of a total 75 basis point action, including the October 8 move. I believe the deterioration we have seen in September and October and the resulting downward revision of the outlook merit a cumulative response of this magnitude. That said, I am sympathetic to the view that we would be well advised to keep some powder dry to respond to shocks or developments ahead. I anticipate that, because a number of the dynamics in the markets have not really played out, we will have more shocks and they could come from further financial institution failures, corporate failures, a sovereign debt crisis, and market disarray; and in other markets, such as the municipal market, there is always a chance of a geopolitical event. In all likelihood these things come in combination or in rapid fire. So, as I said, I am sympathetic to the "powder dry" view, but I see the powder dry objective as being in conflict with responding to the recent deterioration. Therefore I come to 25 basis points or alternative B to some extent as a compromise, combined with the 50 basis points of October 8. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Thank you. President Yellen.

MS. YELLEN. Thank you, Mr. Chairman. I favor alternative A, a 50 basis point cut in the funds rate. This action, and even more, is justified by the dramatic developments since our last meeting—a deepening of the recessionary outlook worldwide, the near meltdown of the global financial system, and the abatement of inflationary pressures. Frankly, it is time for all hands on deck when it comes to our policy tools, and the fed funds rate should be no exception. Although we cut the funds rate 50 basis points a few weeks ago, the Greenbook inflation projection was revised down more than that, so the ex ante real funds rate actually edged up over the intermeeting period.

We need to do much more and the sooner, the better. One might argue against such a policy move in favor of a wait-and-see approach to better gauge if the recent flurry of policy initiatives will turn things around. In normal times, I would have some sympathy for this argument, but these are about as far from normal times as we can get. We are in the midst of a global economic and financial freefall, and the confidence of households, businesses, and investors is in shambles. The adverse feedback loop is playing out with a vengeance. Lenders continue to ratchet up terms and standards, sapping the ability of households and businesses to spend. As the economy weakens, further loan defaults will mushroom.

I think strong, clear action is needed. Historical precedents, such as the case of Japan, teach us that it is a mistake to act cautiously as the economy unravels. I think the clear lesson from both economic theory and real-world experience is to lower rates as quickly as possible to avoid a deeper and more protracted recession, not to keep our powder dry or to wait to use tools until later if they are available to us now. The more medicine we give and the sooner we give it, the better. The Bluebook optimal policy simulations tell us that, absent the zero bound, the funds rate should be lowered well below zero next year. Since that is not an option, we should do the most with what we've got and cut the funds rate aggressively now.

CHAIRMAN BERNANKE. Thank you. Governor Kohn.

MR. KOHN. Thank you, Mr. Chairman. Like President Yellen, I support alternative A, the 50 basis point cut. I think it's the right response to the very, very substantial change in the economic outlook since the last meeting. We would have cut the nominal federal funds rate by 1 percentage point and real federal funds rates by something less than 1 percentage point depending on what you think is happening to inflation expectations. But surely inflation expectations are coming down—and coming down substantially.

I think the incoming information, the weakness before the shock hit in mid-September (which to me suggests that we didn't have any insurance against that weakness at the time), the extraordinary tightening of financial conditions, and the downshift in spending that we've seen since mid-September all suggest that a 1 percentage point cut in the real rate, and even a little less than a 1 percentage point cut, would seem a very modest and moderate response to the shock. It's probably a down payment. If the staff is right, we will need more. I built more into my own forecast. But even if the economy is not as weak as the staff has built into the Greenbook, I think a substantial cut in the federal funds rate is entirely appropriate.

All of us—without exception, I think—said that there were downside risks to their forecasts, and a number of us have cited the possibility of a very deep recession here. So I think we need to take action. We are starting with a situation in which the economy is declining. We are in recession. The unemployment rate is rising. Inflation is falling. There is a global recession in train. It seems to me, from a risk-management perspective, that the costs of not doing enough—the costs of being reluctant to lower rates and making that situation worse—are far larger than the costs of going a little too far because things turn around faster. I think we are in a situation in which it is almost impossible at this point to go too far. Mr. Chairman, we may have to take it back at some point in the future, but right now I think the 50 basis points is absolutely justified by the conditions in which we find ourselves.

I was drawn, as the Vice Chairman was, to the staff simulation having to do with a more rapid financial recovery. I myself think that's a very small probability. But even if that's what happens, we'll know by December whether the financial markets are recovering faster. We can stop at 1 percent, if we're getting that recovery; and the outcomes, as the Vice Chairman noted, really aren't that bad in that recovery. So I think that even the small probability of a very sharp turnaround in the markets is still consistent with cutting rates another 50 basis points at this meeting.

The fact that we are already low is not a reason to hold back. I don't agree with the "keeping the powder dry" kind of argument. I think the lessons of history, including from Japan, are that the closer you get to the zero lower bound the more aggressive you should be. If you let weakness build, that weakness will overwhelm your policy tools. The most effective use of the limited scope for policy easing is to be preemptive and stop weaknesses from building.

I think a 50 basis point easing will have beneficial effects. I don't think that the markets will react very much. We won't see those beneficial effects. But if I can compare it with doing 25 or nothing at all, I think doing 25 or nothing at all would have adverse effects. With 25 or nothing, you'll get longer-term rates up, you'll get stock prices down, and you'll get an erosion of confidence at a time when we don't need it—that the central bank doesn't get how serious this situation is. I agree that the last easing was largely offset by the loss of confidence and the rise in uncertainty. I also agree that it might not feed through as directly and completely as it often does because banks are trying to rebuild and lenders are trying to rebuild profit margins. But I still think it will be effective. As I say, I convinced myself of that by asking about what would happen with the alternatives, and I think the alternatives would be far worse. We need to keep fine-tuning the TARP and the liquidity provision. We need fiscal stimulus. I agree with all of that. We need to move on lots of dimensions. But these things will not be sufficient in and of themselves to counter this. Monetary policy is a fairly blunt instrument, but we need to stimulate the spending wherever we can to do this.

Some have expressed concern about circumstances forcing us to ease between meetings. We have done 50. Will that take us further? I think we need to make clear in our statement and our minutes—particularly in our minutes—that we do expect a weak economy going forward, at least a moderately softer economy, and that the process may call for further easing. I think it will call for further easing at the next FOMC meeting, but we can get to the next FOMC meeting and see. But it should take a substantial and unexpected deterioration relative to that path to justify an intermeeting action. So I think we are absolutely right to have a prejudice toward taking actions at meetings, when we can sit around and discuss things. The odds are high that we will need to go further, but we should do that at a meeting if we can. If we do have a very strong and substantial deterioration even relative to our weak outlook and we do end up moving between meetings, surely that move would not put us at a level that is unjustified by the circumstances. So I think we can deal with the intermeeting situation and not have the pressures of the market, the pressures of expectations, get us to a level at which we're ultimately uncomfortable. In short, I think it's a very serious situation. We need to do all we can to counter this situation. Now is not the time to hold back. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Thank you. President Rosengren.

MR. ROSENGREN. Like the Greenbook forecast, our forecast predicts a significant recession. Further easing will likely help mitigate the severity of the recession. Coupled with improvements in short-term credit spreads, a reduction in the federal funds rate should lower rates on home equity lines of credit as well as business and consumer rates tied to LIBOR, easing cash flow for consumers and businesses. We are facing problems of historic proportions, both here and abroad. A 50 basis point easing, as in alternative A, is both necessary and appropriate. Even with the easing assumed in the Greenbook, the unemployment rate remains too high for too long. The inflation rate falls enough to be well below my target. To avoid a severe and prolonged recession, we will very likely need further monetary easing and a significant fiscal package, even after this 50 basis point reduction in the federal funds rate.

I would just note in terms of the language that, although I am comfortable with the alternative A language, my actual views would be closer to saying "the predominant concern of the Committee is the downside risk to growth" rather than "nevertheless, downside risks to growth remain."

CHAIRMAN BERNANKE. Okay. Thank you. President Evans.

MR. EVANS. Thank you, Mr. Chairman. After thinking about this for quite some time, I cannot convince myself that alternative A is not the right way to go.

MR. KROSZNER. Let the transcript reflect that. [Laughter]

MR. EVANS. You were very effective in listing a number of dire circumstances. The fact that we may challenge the maximum duration of a recession in the postwar period, any mention of the 1981-82 recession is very frightening, you even mentioned 1975 in terms of the reduction in confidence, and the 1980 credit crunch also—you were able to do that without any mention of the 1930s, and that's quite compelling, I would say.

So for the reasons that have been already discussed, the outlook is quite unfavorable, and I think that this will help improve matters. But as I thought about the concerns that I have, one concern is whether this will actually be viewed as effective today. I'm not sure about that. The last time we cut rates, financial stress intervened to swamp any beneficial interpretation of that. Whether that affects our credibility, I think that Don Kohn was very effective in mentioning that there will be credibility hits in the other direction if we don't take some action like that. I do think that eventually things will subside and the beneficial effects of lower policy will be seen. About the dry powder argument, we are not going to have many more actions left after this, but I don't see what the alternatives are other than to go ahead and put this in place. I don't subscribe to the view that inflation is likely to be too low, although that is a risk. Inflation concerns, the financial stress, all of those issues, even taking into account the risk that President Bullard mentioned the other day, I think speak strongly to the fact that we're running out of normal monetary policy options and that fiscal actions are going to be strongly important. So I do favor alternative A. Thank you.

CHAIRMAN BERNANKE. President Hoenig.

MR. HOENIG. Well, Mr. Chairman, I certainly understand how serious this matter is, and I guess I am of the view that alternative A is not going to solve much. There is a psychology, I understand, in the market that is going on, and I am not convinced that our continuing to take these actions and then having adverse outcomes is necessarily going to inspire confidence. I think we need to let our actions work their way through. Part of the problem is that the credit mechanism is stuck right now because of the tremendous uncertainties. Then I look at all of the things we have done over the last month, and the ramping up of the liquidity facilities has really exceeded even our ability to sterilize. So we have had, in effect, a funds rate that is well below our target. We have excess reserves in that period that were over $280 billion when they are normally $2 billion, and that was before we added more swap lines and more liquidity into the market. Frankly, I think we are at a point now where the liquidity mechanisms that we're trying to use, not our interest rate targeting, are really our monetary policy. As we go forward, perhaps we need to think about how we are going to conduct monetary policy under a quantitative easing environment. That is what I think we will effectively be at if we move again today. So how we think about liquidity and about the credit mechanisms is really where more of our attention will have to be spent. Lowering the rate may have some positive effects, but I doubt it. So I would just stay where we are, let some of these past actions begin to work through, and see what the effects of those are before we then take another move because I think the market would just appreciate some stability over time in our actions so that they can see these things begin to work. It isn't a problem of the interest rate level right now, in my opinion, so that's why I would wait and see. Thank you.

CHAIRMAN BERNANKE. Thank you. President Plosser.

MR. PLOSSER. Thank you, Mr. Chairman. Clearly, forecasts have been marked down since our September meeting—mine included. This reflects the weaker data that we have obtained on the real side, especially consumer spending and manufacturing, but also worsening conditions in the financial markets. Accordingly, in an intermeeting move on October 8, we cut the funds rate 50 basis points. Yet the additional effect on the economy of financial turmoil during the last month remains highly uncertain. Spreads in many markets remain higher than at the time of our September meeting, but some have started to decline. If our new facilities have the desired impact, we may well see spreads continue to fall back to September or lower levels. It is very difficult to say at this time. Although I dislike intermeeting rate cuts, I supported the October 8 cut because it was part of a coordinated effort among central banks around the world and it seemed justified given that our growth outlook had deteriorated and inflation expectations had remained stable.

We may well have to do more, but I think we are near the end of what we can do with monetary policy. Of course, it's difficult to determine the appropriate level of the funds rate, and I want to draw your attention to the Greenbook, which showed that, whether we cut today or don't cut today, the paths of GDP, employment, and inflation over the next year or two are not much different. In fact, in most models, cuts of that magnitude do not show up very heavily in real variables. I would also note that, according to the Greenbook, we could cut the rate to zero and have no effect on inflation, apparently, for the next four years. However, given the fact that rate cuts don't have much effect, even in the Greenbook simulations, we have cut rates. It may not make much difference, as President Hoenig was saying. My preference at this meeting would be to stand pat and see how the data and financial markets improve. We are already engaged in extraordinary quantitative easing, even at this point, and we are hearing from bankers that the funds rate will do little to stimulate lending on their part or improve their balance sheets. Now, delaying necessary rate cuts is not desirable. But given the considerable uncertainty around our forecast, it is not clear that further cuts are either necessary or desirable or are going to be effective. And doing so for purely psychological reasons, from my standpoint, is a dubious way to conduct policy.

A comparison of the baseline Greenbook forecast with the alternative scenario involving more-rapid improvement in financial conditions suggests that the appropriate policy path is very much dependent on knowing whether the increase in financial stress in September will be lasting. If conditions deteriorate further, which they might, we may want to cut in December. If conditions improve, this may not be necessary. Given the decline in confidence in our markets and institutions, I think the Fed can play a positive role by being a steadying hand. That's another reason to wait a bit longer before moving again.

I do not believe that we inspire confidence by appearing to react to market fluctuations. Even though that's not what we're doing, I fear that we often give that appearance. Moreover, although we have gotten positive reactions to the creativity of our liquidity programs, I think we have missed opportunities for raising confidence by rolling out our liquidity facilities in a piecemeal fashion. We had announcements made every day between Monday and Wednesday, on October 6, 7, and 8. I think it would have been far better to announce these actions as a well-thought-out package, explaining the intention of the individual pieces and how they related to one another. For example, we now have three different lending programs designed in whole or in part to support money market mutual funds. I have concern that we have been looking reactive rather than proactive, even though I know that some of these programs had been in the works for a while.

I have argued that it is important that we think about our policy choices in terms of policy paths—that is, a dynamic path. The principles of dynamic programming suggest that we think about our policies in a backward-looking way. This, I believe, applies not only to monetary policy but to our liquidity programs as well. In this spirit, I believe that we must think hard about our exit strategies both from the liquidity programs and from our very low funds rate. I think we have dug ourselves a very deep hole in terms of the breadth and depth of our lending to the private sector. We seem, at times, to be the lender of first resort as well as the lender of last resort. We must make sure that we have a sturdy ladder that will enable us to climb our way out of this hole. This is especially important given the interaction between the programs and the differences across the programs in their current expiration dates.

On the monetary policy side, we have added significantly to liquidity in the economy, as I alluded to earlier. Given the uncertainty surrounding our forecast, we may very well find ourselves in a position of having to reverse those injections sooner than expected. I am even more concerned with this planning process than I have been when I have raised this point before. The baseline funds path in the Greenbook is quite extraordinary from my perspective. It suggests that we can keep the funds rate low, below 1 and even close to zero, throughout most of the forecast period. Indeed, in 2011 the funds rate is still below 2 percent, even though the economy is growing at 4.4 percent. We may disagree somewhat on the magnitude of the contributions of our low interest rate policies in the 2003–05 period to the current problems, but I don't think many of us want to repeat that episode. Yet looking at the baseline forecast and where the funds rate remains—below 1 percent or certainly below 2 percent for the next four years—it strikes me as a risky strategy at best and perhaps even a dangerous one. We have previously expressed views around this table that this Committee historically has been reluctant to raise rates in a timely fashion, and I believe that fear is reinforced by what I see in the baseline forecast in the Greenbook. That projection worries me a great deal. We must not act in a way that sows the seeds of the next crisis.

Despite the pressure of the here and now, we cannot and should not ignore the consequences of our actions in the intermediate term. Managing our way from point to point, dealing with immediate problems, can very easily lead us to a place in which we do not wish to be—thus the importance of thinking in terms of a path. I think it would also serve us well to think about the process we will follow to unwind our liquidity programs in advance, so that we avoid unintended consequences across markets, and about the communication strategy that will ease the transition back to a more market based provision of liquidity.

In sum, Mr. Chairman, although I would prefer not to move today, I recognize that my forecast is more optimistic than most. Moreover, I also accept the notion that there is a great deal of uncertainty about the outcomes and fragility in the marketplace, and your concerns are well noted. Thus, I will not dissent against a 50 basis point cut. But I would like to remind the Committee of our earlier discussions and the general agreement I thought I heard that, when the time comes, we will have to raise rates and we may have to do so aggressively. In all likelihood, that will occur before lagging indicators, such as the unemployment rate, are firmly on the decline. This is not the projection offered in the Greenbook baseline. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Thank you. President Bullard, you have a handout?

MR. BULLARD. I do have a handout.

CHAIRMAN BERNANKE. Everybody have a copy? President Bullard.

MR. BULLARD.[8] Thank you, Mr. Chairman. I guess before I start, I just want to say that I generally agree with everything everyone is saying. This is a dire situation, and I am perfectly comfortable with that assessment. What I want to do with my comment here is just put on the table one idea about why a rate reduction might be counterproductive. That is what I'm trying to do here.

The U.S. economy now appears to be in recession. Intensified financial market turmoil and very fluid expectations have created a very difficult situation. A key question for the Committee is what to do with the monetary policy piece of the policy response to the situation. We know that monetary policy is a blunt instrument that does not directly address fundamental problems in financial markets. We have other programs in place to try to address those problems more directly. We also have important fiscal actions, which are probably having the largest effect in trying to stabilize the current situation. Unlike the ECB, we already lowered nominal interest rates aggressively earlier this year in anticipation of the possibility of weak macroeconomic performance. We are now in the middle of a further round of easing, which is threatening to send nominal interest rates to zero, given the force of events.

Is this the optimal policy, or could it backfire on the Committee? I want to at least lay out the possibility that a very low nominal interest rate policy may be counterproductive. My key worry is that housing markets remain at the core of the current turmoil. Mortgage markets—

[8] The materials used by Mr. Bullard are attached to this transcript (appendix 8).

\$14 trillion or so, about one GDP—are based on nominal contracts. Deflation tends to be very destructive in an environment of nominal contracting. I want to stress that macroeconomic expectations are very important for the way the economy actually evolves and will evolve going forward and that those expectations are very fluid in the current environment. The Japanese experience, while it is not an exact parallel, represents an important reference point for the current situation. Japan's problems were very real. Some have described the outcome as a lost decade.

So let's turn to the graph here for just a second. This is what I was talking about yesterday. This is an argument put forward by Jess Benhabib, Stephanie Schmitt-Grohé, and Martín Uribe. On the vertical axis is the nominal interest rate. On the horizontal axis are the inflation rate and inflation expectations, which in this graph are going to be the same thing. The diagonal line labeled "Fisher" is just a Fisher relationship. The nominal interest rate is the real interest rate, *r*, plus inflation expectations. Then policy is described by the line with the kink in it. The policy line means that, when medium-term inflation expectations are above target, we raise the nominal interest rate and, when medium-term inflation expectations are below target, we lower the nominal interest rate. That works beautifully around the targeted equilibrium, the π^* in this environment, and all goes well. It's just that, when you go to low nominal interest rates, strange things start to happen because you have to do something with policy as you come to very low nominal interest rates. You could just go to zero, and then you would have the horizontal line labeled "policy" that would go across all the way to the minus *r* there. Or you could stop at some earlier level. I chose something here to illustrate what the Greenbook seems to have in mind, say ½ percent.

But any way you cut it, this is going to create another crossing of the Fisher relation and create a second steady state. This is the main point of the Benhabib analysis. You can layer on top all kinds of other stuff that you would like to include in your model, but most models are going to have a Fisher relationship, and most models are going to have the policymaker reacting by adjusting the nominal interest rate. So this other steady state, the steady state with low nominal interest rates, has deflation. If you get stuck there, in our current environment, this would exacerbate the housing problem a lot and make our problems much more severe. So this is just one caution about going to a very low nominal interest rate environment. When I saw this six or seven years ago, it had some influence on me. Before this, I was not worried about any of the zero bound issues. But then, this does make me a little nervous, given the core problem in our situation, which is the housing problem. That's the argument. So let me set that aside then.

One thing this line of research pointed out—and a whole bunch of papers have been written since this paper—is the existence of this second steady state and that the deflation associated with the trap steady state is a worrisome phenomenon. There are two steady states here. You can just argue that you don't think the lower one is going to be the one the economy coordinates on and that eventually we are going to go back to the high one and that is perfectly fine. However, the Japanese case seemed to be zero nominal interest rates and a moderately low rate of deflation for quite some time. You could say that, if we coordinate on this low nominal interest rate steady state, we can somehow take fiscal policy actions to move off that to the other steady state. That is a more complicated issue. That has been addressed in the literature, and that is also a reasonable thing to say. I guess my main concern about this is, since it is a very dire situation and I think we are going to go very close to zero very soon, I want us to do it with our eyes open. It has some possibility of creating a worse environment. That is the only thing I wanted to say here.

So my preference based on this would be to leave rates alone and say, "Let's use fiscal policy." I don't think what we have now is an interest rate problem. What we have now are problems in credit markets, and I think they are being fairly well addressed by the most recent fiscal actions, including capital injections into the banking sector. So that would be my preference at this point.

CHAIRMAN BERNANKE. Thank you. Let's see, President Fisher.

MR. FISHER. Mr. Chairman, if you had kicked around in the streets of Hong Kong in 1997, then you would have wandered into elementary schools and seen what we called at that time "Quotrons"—children trading stocks on the lunchroom floor. It was the surest indicator that the market was out of control. This morning I opened the *Wall Street Journal,* and on the front page they describe an exercise run by the Securities Industry and Financial Markets Association, which you know is Wall Street's biggest trade group, with a similar program in American schools. It says that a 13-year old in Wilmington, Delaware—Michael Ashworth—is slumped by his computer, weary from another rough day in the stock market with all his favorite picks—Domino's Pizza, the Hershey Company, and Gap—surprise! [Laughter] "I'll be honest with you," he confided, "before all this I asked my Mom to give me stocks for Christmas. But then, I told her not to do it. I asked for a parakeet instead." [Laughter] Now, this is not as exotic or thoughtful a handout as the one from my colleague from St. Louis, but here's the point. He may not get that parakeet because the pet store may not have access to credit. This is, to me, the fundamental issue that I think President Plosser—and I won't repeat his arguments—and President Hoenig were referring to. The concern I have is not about the price of money. In fact, I think we are not seeing that kind of transmission mechanism—Governor Duke gave testimony to that earlier. All of us are aware that it is not moving as quickly through the IV tube as we would like it to because of the crimped nature of the tube.

I have no problem with the language in alternative A, except for the first paragraph, and the phrase "including today's rate reduction." I have an open mind. I do think the issue in terms of restoring the system comes back to credibility and predictability. You cannot have a functioning capitalist system if you have total uncertainty. These are the issues that I believe President Plosser, President Hoenig, earlier President Lacker, and others were referring to in the first intervention. I thank President Geithner in particular for addressing the questions I asked yesterday, and there was reference to them earlier.

We have done so much so quickly. We are in a quantitative easing period. The question is whether it actually makes a difference if we cut rates or not and whether the price of money is actually the issue or the fact that money is not flowing, that there are counterparty risks and rollover risks, and all the things we have talked about at this table and each of us has articulated in our public speeches. To be very honest with you, Mr. Chairman, I am open-minded about this because I could make that argument both ways. If it doesn't matter, why not cut 50 basis points? Or why not hold? I am not convinced yet—and I'd like to listen to the rest of the arguments—that alternative A, in terms of the action, is the right way to go. I do think it's very important that we be very clear and articulate in laying out how we see the world, and I do believe that the language in alternative A does the best job of all the columns that have been presented.

But I come back to the question I asked before. What are the next steps? I'd like to know. What is the end game? I'd like to know before I cast my vote. I will conclude with actually once again agreeing with President Yellen, as I think I have done twice in history.

[Laughter] The last time was at the last meeting. I think it's very important that we have all hands on deck, that we have a unanimous decision. But, still, I would like answers to my questions. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. President Fisher, I promised you answers, and I will deliver them. President Pianalto.

MS. PIANALTO. Thank you, Mr. Chairman. I strongly favor alternative A, a 50 basis point cut in our fed funds target rate today. I think it is important for us to move aggressively and quickly to offset the strong forces that are acting to depress economic activity. I know that some prefer a more measured response, especially as we move closer to the zero bound, but the lesson I take from history is that more and sooner is better than taking smaller steps over time. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Thank you. President Lacker.

MR. LACKER. Thank you, Mr. Chairman. The economic outlook has definitely deteriorated. On top of the slowing at the beginning of the third quarter, a sequence of policy actions and statements has spread an inchoate fear. In response to that, a wide variety of economic agents have delayed outlays. The breathtaking credit market interventions that we have undertaken in the last several weeks are going to make it hard to judge whether those markets are stabilized. It is going to make it even harder to judge how and when to withdraw.

Governor Duke asked rhetorically what it would take for recovery to begin. I think it is not going to be a very healthy recovery unless we have made substantial progress toward withdrawing these interventions. I know it's probably premature in the midst of a crisis to be talking about the recovery, but a number of people did, and I think it makes sense on the grounds that President Plosser advanced for us to be thinking ahead. President Geithner talked about the will and the desire and that it amounts to a matter of will to reverse course later on. I think that in withdrawing these subsidies and these credit market interventions is where we are going to need the will. It is going to be really hard to disenfranchise somebody who now has access to one of these programs.

The inflation outlook has improved. Expected inflation has come down. A couple of people have noted that. That brings the real rate where the interest rate is now—to about zero. So I can favor a 50 point reduction in the federal funds rate target at this meeting. I think a funds rate that is, in real terms as best as we can measure it, about minus 1 percent is how we should see our way through here, at least in the near term. Like President Evans, I will mention the 1930s. What I take from my reading of the Great Depression is that this is what central banks should do in times like this—keep real interest rates low.

Let me make a couple of brief observations. As I mentioned yesterday, I think we are going to face a challenge communicating about our strategy. If we need to reduce interest rates to the lowest practical level to which we feel we can reduce them, I think yesterday's discussion suggests that the Committee could use a refresher course on the monetary economics of the zero bound. I applaud President Bullard for his breaking new ground by providing a figure from the *Journal of Economic Theory*. [Laughter]

I want to put something on the table about the federal funds rate. We are voting today on the target for the federal funds rate. The way our operations are conducted now, we are leaving so many excess reserves in the system that we are driving the federal funds rate down to the interest rate on reserves. The interbank risk premium is likely to become small as the FDIC guarantee becomes well understood and more broadly effective. The GSEs are likely to catch on that they deserve more on their funds. Small banks, as Governor Duke says, that haven't really paid attention to what this new regime is about are going to find that brokers are going to be able to find them placements at closer to the interest rate on reserves. So I think that the sloppy trading below the interest rate on reserves is going to fade over time. As long as we have excess reserves at the scale that we do, as long as the Desk has added that many reserves, we are going to have the effective federal funds rate at the interest rate on reserves. Because we are voting on the federal funds target rate, I think that the Committee ought to have some understanding from the staff that either excess reserves are going to be drawn down to the point that the effective rate is lifted off the interest rate on the reserves floor or—and this would be my preferable course of action—we raise the interest rate on reserves to equal the target rate. Otherwise, we are voting on something, but we are actually doing something else. I can understand the desire to err on the side of soft rates. This is what we did in August 2007. But as rates go down, we need to be more and more careful about what the Committee is actually voting on.

CHAIRMAN BERNANKE. Just to support what you said, we are obviously still trying to find our way in how to use this in the new regime with the excess reserves interest rate. It is possible that at some point we might decide to target that interest rate. That might be the most straightforward thing to do. But as I understand it—and, in fact, I'm quite confident—the intention of the staff and the Board is to try to figure out what the relationship is between the excess reserves interest rate and the federal funds rate as normally measured. If we can establish a reliable relationship, then we should try to—and we will—use that to hit the target. It's coming close to it. We certainly are not trying intentionally to come under the target. If that fails, then we will go to what you are suggesting, which is effectively what I'm saying, and make them the same. Then, effectively, there is no difference between targeting the interest rate on excess reserves and targeting the federal funds rate. We are certainly open to that, and there is no intention to do anything other than to try to figure out a way to take the FOMC's decision and put it into practice in the money markets. President Stern.

MR. STERN. Thank you, Mr. Chairman. Well, financial headwinds continue to be a major part of my thinking about the economic outlook. Reasonable people can differ about that issue, but it seems to me that the headwinds are significant and they are likely to persist. Partially as a consequence and partially for other reasons, the economic outlook has deteriorated, and the inflation outlook, fortunately, has improved. So I favor alternative A, and I am satisfied with the language associated with it.

Let me make just one additional comment. One way of thinking about lowering rates at this juncture and its potential effectiveness is that it is important to reduce the price of liquidity in this environment. I think that's what lowering the target would do. That said, if I think about policy a bit beyond this meeting, I start with an observation that Governor Kohn made. We are probably going to receive a batch of pretty negative economic news over the next several months. At the same time, a lot of programs are in place, as everybody is aware; and perhaps my optimism is ill-conceived, but I actually think that they have the promise of being effective over time. So it's not just a question in my mind of the nature of the news we get, but are we also seeing signs that all these programs are getting some traction and being effective? If they are, that ought to temper our desire to go further. Obviously, a lot of things are in play, and a great deal of uncertainty is present here and abroad. But we will simply have to assess all these developments as best we can as time passes. I think I'll end my remarks there.

CHAIRMAN BERNANKE. Thank you. Governor Warsh.

MR. WARSH. Thank you, Mr. Chairman. Let me begin by agreeing with Don Kohn on two things. This is the toughest economic period I can remember in his lifetime, [laughter] and I support alternative A. I think the inflation trends and the trends in the global economy give us flexibility, which six months or so ago I did not think we would have. I think that gives us some degree of freedom that, given all of the negative tone, including my own, around the table, gives us at least some source of comfort.

Next I would say that I agree with the consensus around the table, which is that these problems are not principally about monetary policy. But I also think that monetary policy isn't irrelevant to this, and all agencies of governments around the world are making tough decisions, and the marginal benefits of further monetary policy changes strike me as not high but not irrelevant. I think President Plosser talked a bit about the alternative policy paths in the Greenbook that range from keeping the fed funds rate constant where it is to taking it to zero percent and the surprisingly small differences in output, employment, and core inflation there. In some ways, in the discussion that we're having about 25 or 50 or moving or not, it would not be fair for any of us to overstate the importance in terms of directly affecting the economy in the short term.

That goes to my final point, which is that the most valuable asset that we have isn't what at the end of this meeting might be 100 basis points left of monetary policy. Frankly, it is the credibility of the institution and the credibility of the FOMC. If I compare our credibility now to virtually any other organization in the United States or maybe even globally, I think our credibility is holding up quite well, particularly relative to the degree of difficulty we have in front of us, relative to the trauma in financial markets and the weaknesses in the economy. So it is that asset, that credibility, that we need to continue to protect more than incremental basis point moves on the fed funds rate. I think that credibility will be tested over this period as it will for our counterparts. We don't want to find ourselves in a corner come December or come a couple of brutal days in the markets where we feel compelled to continue to act and make 50 basis point moves unless and until we know where we want to end up on this. So I'm sympathetic to that point of view. We need to tell the story before the story is told for us of what our lower bound is, why it's there, and what our diagnosis of the economy is. I think that the Chairman and the rest of us will have ample opportunity to do that between now and December and that it is quite important to make sure we come out of this as strong as we have been through this period so far. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Thank you. Governor Kroszner.

MR. KROSZNER. Thank you very much. Well, I've not been able to convince myself not to agree with President Evans. As everyone has said, we have this very significant global shift that has stepped down real activity and financial activity. The inflation environment has changed dramatically from a number of months ago with the change in commodity prices, the change in the value of the dollar, and the change in not just U.S. but also global resource utilization. I think we've seen just an enormous change there. Also, when you look at the expected federal funds rate path—we have to be careful in looking at anything in the markets these days because of liquidity, risk premiums, or term premiums that we're not quite sure about—the markets are expecting significant cuts from us. They are not expecting any immediate or near-term significant increases in inflation, and I think all of the indications are that it will be going down.

In a cost–benefit analysis, the costs seem relatively low in terms of the potential for inflation of doing this. Now, we have to think about it in terms of benefits, and a number of people have touched on the transmission mechanism. I do think that there are forces that mute the extent to which a 50 basis point cut translates into 50 basis points or lower on costs, but I don't think they completely offset it. It still has the effect of reducing the cost of liquidity, reducing many people's borrowing costs. I think it still does have an effect even if there's an offsetting risk spread and even if there's an offsetting bank action that affects that. So in terms of costs and benefits, at this time it seems that the costs are relatively low or muted, and the benefits are positive and potentially high.

In particular, as I mentioned before, I'm concerned about the confluence of forces that may make things very difficult around the end of the year. If you look at a lot of these LIBOR or forward markets, they're not coming down either in the United States or around the world. We have a lot of uncertainties with hedge funds, with the potential for other institutions getting into trouble, and with just the implementation of our policies—in particular, as I mentioned, the way the FDIC guarantee program and the TARP program work may end up singling out institutions and bringing them down more quickly than otherwise. So I think it makes sense in terms of cost–benefit analysis, even more so given the tail risk around the end of the year, to act now. We have another opportunity to act in December and obviously an opportunity to act at any point if we do see a dramatic change. We are getting near as much as we can do, but I don't see the costs of acting more aggressively and more quickly here outweighing the benefits. So I support alternative A with the language as drafted. Thank you.

CHAIRMAN BERNANKE. Thank you. Governor Duke.

MS. DUKE. Thank you. I confess I find myself torn between the position of President Plosser and the equally compelling arguments of Governor Kohn, and that makes alternative B quite attractive as a way, not because of any optimism about the economic outcome, but I really do question the effectiveness of any move in the fed funds target given the actual trading of the fed funds rate right now. When we set the interest rate on reserves, at that point I was concerned that our interest on reserves would disrupt the market for fed funds between banks because of the risk premium. With the FDIC insurance, I think that goes away, and so probably President Lacker's suggestion deserves some strong consideration. I am also painfully aware of the operational and financial difficulties that banks experience at a 1 percent fed funds rate and the likely difficulties of other intermediaries as the absolute level of rates falls further.

As I stated in my earlier remarks, I'm also most concerned about the importance of predictability in returning confidence to the markets, and in that light, I am concerned about market expectations. But having recently been an expecter rather than a decider, I'm going to suggest that most of those doing the expecting don't understand at all the issues that we've discussed here today. There's a thought that, if the fed funds rate just comes down, it would maybe make this pain go away. So I agree with Governor Warsh that the public statements in the intermeeting period and as we approach the point where we simply can't meet market expectations anymore are critically important to shape market expectations. So I do think it's important that the markets focus on the other efforts, and with that I would support alternative A.

CHAIRMAN BERNANKE. Thank you. Vice Chairman.

VICE CHAIRMAN GEITHNER. Mr. Chairman, I support alternative A, both the action and the language for the reasons I said earlier. I just want to make a couple of other points. I think the only way to be predictable in a crisis like this is to be predictably inert or to be late. I don't understand the basic argument that you add to confidence by being inert or by being late or, as the Chairman said, by being passive despite overwhelming evidence about changes in the outlook and risks to financial stability. The argument that makes me most uncomfortable here around the table today is the suggestion several of you have made—I'm not sure you meant it this way—which is that the actions by this Committee contributed to the erosion of confidence—a deeply unfair suggestion.

Now, a lot of things happened over the last three months and the last year, and a lot of things happened in terms of policy over the last six weeks. There is no doubt that communication about policy by all the arms of the U.S. government and the uncertainty created by the actions by all the arms of the U.S. government contributed in ways to uncertainty about the policy response going forward. There is also no doubt that inevitably in a crisis like this, when policy moves forcefully, it is scary because a lot of people are not yet at the point of assessing or understanding the forces driving our decisions. But I think it's just unfair to suggest that the actions by the Chairman and this Committee were a substantial contributor to the erosion in confidence and to uncertainty about further policy actions, even though it's true that when we move with force and drama it has the risk of adding to uncertainty.

I'd be very careful to look more broadly at the full range of other things that happened in that period of time, including, for example, the confusion established by the range of different choices for interventions in Lehman, AIG, the GSEs, WaMu in particular, and Wachovia and what that meant. Look particularly at the damage to confidence created by the Congress's actions in the weeks after the legislation was first proposed. Compare that, for example, with the announcement effect of the initial thing. Look also at the uncertainty created around what the package was designed to do and how it was designed. But please be very careful, certainly outside this room, about adding to the perception that the actions by this body were a substantial contributor to the erosion in confidence. I think that Don Kohn said it best. The whole framing, which seems to have hardened now, that the world ended with the Lehman bankruptcy is just deeply unfair to the basic truth. Independent of whether there was an option available at the time, the erosion in underlying economic conditions and in confidence in the future outlook was powerful and substantial going into August and early September. So I just offer that.

You know, everyone wants to quote FDR. FDR said at one point, "If I judge the mood of the country right, what this calls for is bold experimentation." I do not believe that this Chairman and this Committee have been irresponsibly experimenting at the cost of predictability and confidence going forward. What we have done is a relatively well designed series of escalations in monetary policy and liquidity intended to be preemptive against what we knew was substantial risk of a very adverse economic and financial outcome. The risks were not broadly shared, not just in this room but outside. But I think the judgments by the Chairman were largely correct in weighing those risks appropriately at that time, and I think we all owe him a substantial amount of deference for the judgments he made and his wisdom. Both here in this room and in the effect he had on the policy choices that the fiscal authorities also ultimately made look very good now and will look even better over time as people understand how grave and substantial the risks were that we were facing in the economy and the financial system.

One last point to President Fisher's question. President Fisher asked the obvious question, which is, What next? I think a very good approach to decisionmaking is to say, "I don't want to know so much about this. I want to know about the next three things." I know the Chairman is going to give a nice, thoughtful, and complete answer to this. But I would just say the following: We don't need to know today what is next on the monetary policy front. We know there may be some arguments for going lower than 1 percent. We have to think through very carefully the collateral damage consequence in terms of what that does to market functioning and behavior. We have to look at the alternatives to that, including in communication. A range of other policy options are within our capacity to influence and effect that will give us the ability to minimize downside risk going forward. But I don't think that we need to know—and we cannot know with precision—what the optimal mix of those things is now before deciding what to do, although I'm very sympathetic to the basic judgment. The question really is, In moving today, are we going to do more harm than good to our ultimate objective? It's very hard to make the case that we do damage to any of our basic fundamental objectives and mandate. I can see a much stronger case that we do a lot of damage to those if we don't act today, even though we all recognize that ultimately this is going to require more than monetary policy to address the risk here.

CHAIRMAN BERNANKE. Thank you. President Plosser.

MR. PLOSSER. I'd just like to just take a moment to react. I'm not sure whom you heard saying that the result was primarily a result of this Committee's actions or the Chairman's actions or anyone else's actions. If those were words you were putting in my mouth, that was not what I said, President Geithner. I do think I have been supportive of almost all the actions in terms of liquidity facilities; I supported the actions. I also was supportive of the Lehman Brothers decision. But I think it's a far cry from saying that uncertainty about policies contributes to uncertainty—which you agreed to—it's a far cry from that to saying we lay the blame at the feet of this Committee or the Chairman. So I don't know what straw man you were setting up, but it certainly didn't apply to this member of the Committee. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Okay. Thank you. Let me just offer some thoughts that may be somewhat more expansive than usual in response to the questions that have been raised. Some of this is extemporaneous, so you'll have to bear with me. Let me first talk about the strategy we pursued thus far and where we are and then think about where we might go as a country as well as an institution going forward.

Without going through all of the familiar discussion about how the crisis began, what the sources of it were, I think that the Federal Reserve's responses are essentially three. First, we were relatively early and aggressive in our monetary policy easing, particularly compared with other countries. Second, we have been creative and expansive in our use of liquidity tools, including a wide variety of lending programs. Third, we have used our available, but not always adequate, tools to try to stabilize systemically critical failing institutions and to try to mitigate systemic risk.

Without sounding too defensive, I will try to argue that I think on all three of these we have been more or less in the right direction. First, on the early and aggressive monetary policy easing, obviously there was a lot of concern—a lot expressed abroad that we were going to create a stagflationary 1970s type of situation and that we were going to destroy the dollar and its role as an international currency. Our response essentially was that we thought that the increases in commodity prices were mostly a relative price change induced by changes in real demand for commodities and in the supply of commodities across the globe and that, at some point, those commodity price increases would stabilize, which would lead to a moderation of the inflationary effects and concerns. It took longer than we had expected; but once it began, it was more pronounced than we had expected. Inflation has not become the problem that was anticipated by many early on, and the dollar, of course, is now stronger than it was before we began our cutting of interest rates. So in retrospect, I think our monetary policy, although not perfect certainly—and our communication was not always perfect—broadly speaking was appropriate given what has turned out to be a very severe economic situation.

Liquidity expansion also received some criticism early on. There was a view that this was inducing moral hazard. There was also some question of whether this was an effective approach. We were helped in this respect by the fact that the ECB joined us very early in this type of aggressive policy. I don't know the counterfactual. It has obviously not solved all of the problems. But I think there's a strong perception in the markets and in the general public that these actions have been supportive, and they helped mitigate the effects of the crisis on the functioning of the financial system. So I feel comfortable also with that approach.

The attempts to stabilize failing systemically critical institutions, beginning with Bear Stearns, have obviously been very controversial. There have been criticisms from the right and from the left. From the right, the initial criticism was that we have no business interfering with the market process. We should let them fail. The market will take care of it. What are we doing? We heard this as recently as Jackson Hole. I never took this seriously. I just don't believe that you can allow systemically critical institutions to fail in the middle of financial crises and expect it to be not a problem. I don't want to get into the issue about the inconsistency. It's true that we treated senior debt differently between Fannie and Freddie and WaMu and Wachovia, but I don't think that that is the reason we are having the financial crisis we're having. I think there was a panic brought about by the underlying concerns about the solvency of our financial institutions. That panic essentially turned into a run. Companies like Wachovia that had adequate Basel capital faced a run on their deposits, which was self-fulfilling. The investment banks essentially faced runs. We did our best to stabilize them, but I think that it was that run, that panic, and then the impact the panic had on these major institutions that was the source of the intensification of financial crisis. So I don't buy the argument that we should stay out of the business of protecting the financial system, and I think that the major factor was, in fact, the panic that was generated by the underlying uncertainties and the effect that had on critical institutions.

Also more recently we have heard more of a critique from the left, which is, What in the heck were you guys doing letting Lehman fail? This is interesting given that the critique had been the other one for quite a while. I think that critique is unfair at a narrow level in that, first, Lehman was a symptom as well as a cause of the recent crisis and, second, the Fed and the Treasury simply had no tools to address both Lehman and the other companies that were under stress at that time. I think that criticism is appropriate, though, as directed toward the United States as a whole. We did not have—as the Europeans have or as we have FDICIA for banks—a system that was set up to allow a reasonable and responsible orderly resolution of nonbank systemically critical institutions. I think we now have made a lot of progress there. The TARP will provide a good interim solution. It is very important that in the future we address the too-big-to-fail problem that we have, that we find ways to reduce that problem, and that we find ways to deal systematically with firms that are in crisis. So given the fog of war—which has, of course, been intense going back for more than a year—I would defend what we've done in terms of the general direction, acknowledging that execution is not always perfect and that communication is not always perfect.

Now, what about the future? History suggests that, whenever a financial crisis becomes sufficiently severe, ultimately the only solution is a fiscal solution, and we will have a fiscal solution. There are two possibilities. One is that the financial system will muddle through, in which case the fiscal solution will be of the sort we've already seen: injections of capital, support for critical firms, support for the credit markets in general; Keynesian-style demand support. That's one possibility. I hope that's where we're going to be. In my own testimony, I argued that we should try to focus whatever stimulus we have in solving the underlying problems rather than simply handing out money and that we could do that, again, by addressing credit markets. I would add, foreclosure, homeownership, and some of those issues as well. So I hope that's where the fiscal policy will be. I hope that will take the lead from us going forward. Obviously, we'll have to continue to play a supporting role in a lot of different ways.

The other possibility, of course, is that things get much worse and that we are in the same situation as Sweden or Japan, in which case a massive recapitalization of the banking system will be necessary. That will eventually happen, but I just note that, in all of these fiscal dynamics, there is a political economy overlay. You have to get to the point that it is not only the right policy to induce fiscal support but also that it is politically possible. That's one reason that I think the TARP was not possible before the most recent period. In fact, it was barely possible recently. So, again, I believe that fiscal policy will have to be a critical part of the solution going forward.

Another part that we should not forget about is the international response, which is now just beginning really to become serious. The responses after the G7 weekend on banks and bank guarantees were important and suggested a commitment by other countries to stabilize the system. That's very important. I think we will see aggressive monetary policy going forward, and I think we'll see increasingly aggressive fiscal policy in other countries because they recognize that the decoupling is no longer a realistic story. So that's going to be important as well.

With respect to the Federal Reserve, just generally speaking—and I'll come back to the specific recommendation for today—again, I think that our liquidity provision has been constructive. It has allowed the use of our balance sheet to help push in the deleveraging process that's been going on now for more than a year. My guess is it will probably expand some more, but I don't see it expanding a lot more, if for no other reason than we are reaching the limits of our operational capacity as well as balance sheet capacity. I think we have been reasonably successful in staying on the side of liquidity provision and not straying into credit or taking credit risk. I want to stay on that side of the line both for legal reasons and because that's the way monetary policy and lender-of-last-resort policy are supposed to work. Again, I hope that the fiscal interventions will now be able to take away some of these responsibilities from us, but we'll have to see how they play out.

I confess that I hear President Plosser's concerns about reversing these programs. I recognize that it's something we'll have to do carefully. But I just don't see it as being something that will be a huge problem if the economy begins to recover and credit markets begin to function more normally. I think we'll be able to do it. Japan was able to get out the quantitative easing without too much difficulty. But I acknowledge the point that it is something we're going to have to plan for and think about.

On monetary policy, I think it is important for us to be responsive. Even if we stipulate for the moment that the interest rate changes we might make today have a minimal effect on the cost of capital—and I don't necessarily agree with that, but let me stipulate it—there is still the importance of the signaling and what we're trying to tell the markets about what we plan to do in the future. Frankly, I don't think that we should try to signal that we are going to stand pat, that we are reluctant or refuse to move lower. We have to be prepared to move as low as makes sense. By that I mean in part that there are institutional factors that affect the efficacy of monetary policy at very low interest rates. We're all aware of that. I asked yesterday, and I'll ask again, for the staff to go back to the 2003 work, to update it, and to think it through and help us understand what I would call the effective zero. What is the real zero? Is it zero? Is it 50 basis points? Is it 75 basis points? We have to recognize that if we do go to literal zero, it would have very substantial effects on a number of financial markets, and we would have to ask ourselves whether the benefits from that are worth the dislocations. The Japanese thought they were, and for example, they did shut down the interbank market for a long time. Maybe doing it is worth that. Those are decisions that we need to make before the next meeting, and we will have opportunities to talk about this together and in public as well. But I do think that monetary policy needs to be proactive and to continue to be part of the solution here going forward.

What about today's action? I essentially accept the general change in outlook as proposed by the Greenbook. Since our last meeting there has been an effective tightening in financial conditions, which has overwhelmed the 50 basis point cut that we did with the other central banks.

The outlook has become much worse. So it is important for us to act aggressively and to signal essentially that we're willing to do whatever is necessary to support the recovery of this economy. There has been a lot of talk about confidence. I think the best thing we can do for confidence is to say that we're going to do whatever it takes, even if it involves extraordinary actions, to get this economy back onto a path where it can begin to grow in a reasonable way again. Signaling coyness, being cute, is not a safe strategy right now. We just need to be straightforward and say that we're going to do what it takes. In my view, just to be specific, 50 basis points is the right step today.

Now, a number of concerns and objections have been raised. Let me address just a few of them. One is President Bullard's very interesting presentation on the inflation trap, and intuitively it's clear that, for a given real interest rate, you can have an equilibrium at which you have a high nominal rate and a high expected inflation rate or you can have a low nominal rate and deflation. Both of those things are possible. That was the trap that Japan got into. We obviously want to avoid the deflation trap. The question is, How do you avoid it? As far as I can see—obviously we can get further into this—the best two ways to avoid it are, first, as President Lacker suggested, reaffirm our commitment to price stability defined as 1½ to 2 percent or whatever our Committee's general view is. We're going to try to do that with our projections and potentially with the trial projection that we're doing, and I think we can continue to strengthen our commitment to maintaining a positive inflation rate. The other thing, in terms of the dynamics, is to be aggressive in trying to avoid getting to a deflationary situation, where those expectations move in that direction. I don't think deflation expectations will arise spontaneously because we're cutting interest rates. I think they'll arise because the economy is expected to be extremely weak, and anything we can do to eliminate that expectation in my view would be helpful.

The second objection I've heard is the question of whether or not these actions are effective. I think they are effective. Maybe they're not as effective as under normal circumstances, but let me put it to you this way. If we cut 50 basis points today and the LIBOR–OIS spread rises 50 basis points tomorrow, I will accept that there's a problem. But if the LIBOR spread doesn't move much and the overall LIBOR drops 50 basis points, then I think that we're having an effect. If you look at LIBOR over the past year, you'll see a dramatic decline even though the spreads have widened. I don't think you can argue that we're not having any effect. To the extent that we're having a muted effect, you can just as well argue that we should be more aggressive because you need to do more to get the same impact. So I understand those concerns, and I reiterate, responding to Governor Duke and others, that as we get very low, there are side effects on certain institutions and financial markets. We need to understand those, and that's part of our decision process. But I don't think it's the case that monetary policy has zero impact.

The third argument I've heard is the "keep the power dry" argument. Unless you think that movements in the rate are entirely psychological in their effect, I don't think that that's a strong argument in this particular circumstance. Again, we analyzed this quite a bit in the 2003 episode, and the general outcome from the literature and from simulations done by our own staff—Dave Reifschneider, John Williams, and others have published research on this—is that the best way to avoid the zero bound is to be more aggressive than normal to try to avoid the accumulation of weakness and try to avoid getting into that trap. So more-preemptive strategies are, in fact, consistent with what we've done for the last year.

My recommendation for today is 50 basis points and the language in alternative A. I do think that it will be at least moderately beneficial both in terms of psychology and in terms of reducing the cost of funding and giving some additional support to funding markets. I hope that in these remarks, which again are somewhat extemporaneous, I have addressed to some extent the future steps. We ought, again, to think very hard in the next six weeks about what the real zero is and what the implications are of going below, say, 75 basis points. Then we ought to make a determination, and it may be that we can sit still in December. It may be that things improve quite a bit in the markets, for example. It's possible. One advantage of doing 50 today is that we almost certainly will not have to do anything intermeeting because we will have done this significant step today. So in December we'll be able to look at the situation. We may be able to do little or nothing—it is possible. But if we decide that further action is needed, at that point we should be prepared to decide what the regime is going to be, how far we're going to go, and what the effective zero is, and I think that we shouldn't hesitate to do that if that's what the situation calls for. So I think there is a way forward. I understand the need to withdraw all these policy actions at an appropriate time. But I don't think that focusing on the near term for the moment is at all inconsistent with the fact that at some point these things will have to be reversed. So, any further questions or comments? President Fisher.

MR. FISHER. First, I would like to thank you, Mr. Chairman, for that very thorough and clear elucidation. I meant to mention earlier that I actually agree with President Evans. It's worthwhile now and then evoking Ronald Reagan. What I mean by that is not his "Where's the pony?" comment, but more important, the reason he was so successful as a leader was that he had clear objectives, they were limited, and they were well articulated. It doesn't matter if you're a Democrat or a Republican. I think it's very important for us to understand what our objectives are in order for us to be fully supportive. By the way, Tim, as Mr. Plosser has been, I have been fully supportive of all of these initiatives. Again, I want to thank you, Mr. Chairman, for helping us understand better the cognitive road map because it is critical for all of us to do what Janet suggested, which is have all hands on deck and make sure we're all fully supportive. Against that background I would support alternative A. Thank you, Mr. Chairman.

CHAIRMAN BERNANKE. Thank you. Other questions? President Plosser.

MR. PLOSSER. Just a question or thought. As the staff prepares the review of the 2003 studies and memos and thinks about what zero effectively means and how we might operate in those circumstances, one thing I think would be useful to include is a discussion of whether or not when that time comes we announce that publicly and say, "Okay. This is it. From now on we have to do X, Y, or Z," and make it part of the communication strategy. Maybe they would anyway. But if we get to the point where we now as a group have some concerns that, well, effectively we really don't want to go below X, we will have to do some other operational actions as a substitute for that.

CHAIRMAN BERNANKE. I think there's no problem doing that. I can do that. That is not a problem. President Lacker.

MR. LACKER. Yes, I also strongly support your charge and direction to the staff to assemble with all due haste updated information for the Committee about what the effective lower bound on nominal interest rates is. But I'd urge you, along the lines of what President Plosser suggested, to include in that charge what we would do once we got there, what we could do, and what would be open to us. I emphasize again the relevance even if we don't get there because analytically we're effectively doing that right now with interest on reserves. The classic economics of this is that, when you get down to effective equivalence between a monetary asset and a government bond of one-day duration or whatever, to be effective monetary policy needs to be fiscal policy. It needs to acquire other assets that we wouldn't normally otherwise acquire. We're doing that right now. So I'd emphasize the importance and relevance of that.

VICE CHAIRMAN GEITHNER. Mr. Chairman.

CHAIRMAN BERNANKE. Vice Chairman.

VICE CHAIRMAN GEITHNER. I also think it would be helpful, as the staff looks at the policy options going forward, that they do other parts of the communication options, too—not just those but also other ways to think about how to make policy for looking at and communicating a path that are different from what we did in 2003. It would be good to look at options for how we talk about policy going forward in that context along with just the operational choices and the policy choices.

CHAIRMAN BERNANKE. President Plosser.

MR. PLOSSER. Just to follow up on that—I think that's a very excellent suggestion, President Geithner. To be very specific about that, in our trial run, one thing that we did was to look at what we thought was the steady state. One way to engender some communication about the longer run might be to include what the Committee thought the steady-state neutral level of the funds rate would be in that environment. I'd describe the path by which we got there; it would convey some sense to the marketplace of what we thought would be in some normal world a reasonable level of the funds rate consistent with those targets. I just throw that on the table as something to think about.

CHAIRMAN BERNANKE. Okay. Other comments? Would you call the roll, please, Debbie?

MS. DANKER. Yes. This vote encompasses the language of alternative A that was in the package passed out earlier today as well as the directive from the Bluebook, which states the following:

"The Federal Open Market Committee seeks monetary and financial conditions that will foster price stability and promote sustainable growth in output. To further its long-run objectives, the Committee in the immediate future seeks conditions in reserve markets consistent with reducing the federal funds rate to an average of around 1 percent."

Chairman Bernanke	Yes
Vice Chairman Geithner	Yes
Governor Duke	Yes
President Fisher	Yes
Governor Kohn	Yes
Governor Kroszner	Yes
President Pianalto	Yes
President Plosser	Yes
President Stern	Yes
Governor Warsh	Yes

CHAIRMAN BERNANKE. All right. I'll need the governors to join me in my office for just a moment. Everyone else, let's all take a twenty-minute coffee break. When we come back, maybe we can start at that point with your briefing, David, on the TARP, and around 12:15 we'll break and get lunch and hear the end of the briefing, if that all works for everybody.

VICE CHAIRMAN GEITHNER. The expected duration of the next part of our meeting is four hours, three hours? [Laughter]

CHAIRMAN BERNANKE. We should be done by 1:00.

MS. DANKER. It's not part of the meeting.

VICE CHAIRMAN GEITHNER. The nonmeeting part of the meeting?

CHAIRMAN BERNANKE. It's only a briefing, not a meeting, once we come back. Okay. A twenty-minute break now and then we'll have a briefing and lunch.

[Recess]

CHAIRMAN BERNANKE. Well, let me officially get to the point of adjourning the FOMC meeting just by first noting that the next meeting is Tuesday, December 16. Put that on your calendar.

VICE CHAIRMAN GEITHNER. That's a long way away. [Laughter]

MR. PLOSSER. Can't we meet before then? [Laughter]

CHAIRMAN BERNANKE. I'd like to remind you that you have until 5:00 p.m. on Thursday to submit revisions to your economic projections, in case the markets change your views.

MS. DANKER. Only through today's meeting.

CHAIRMAN BERNANKE. Sorry—using information only through the end of today's meeting. All right, the FOMC meeting is adjourned. Thank you.

END OF MEETING