NEWS RELEASE

The Federal Reserve Bank of St. Louis
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Media Advisory:
November 4, 1998

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St. Louis Fed's *Review:*
Monetary Theory in the Laboratory
The FOMC in 1997
Price Stability and Financial Stability: The Historical Record
A Policymaker Confronts Uncertainty

ST. LOUIS — The September/October edition of ***Review***, the Federal Reserve Bank of St. Louis' journal of economic and business issues, features the following articles:

- **"Monetary Theory in the Laboratory."** Empirical tests of macroeconomic and monetary theories are typically conducted using non-experimental field data provided by government agencies. Modern theories, however, have increasingly imposed restrictions on individual behavior that are not embodied in any available field data. John Duffy, a professor at the University of Pittsburgh and a visiting scholar at the Federal Reserve Bank of St. Louis, surveyed the recent papers that have used laboratory methods (specifically, experiments with paid subjects) to test modern monetary-theory predictions.
- **"The FOMC in 1997: A Real Conundrum."** Although the U.S. economy performed very well in 1997, the Federal Open Market Committee (FOMC) was concerned that the traditional signals of inflation — rapid money growth and high levels of economic activity — were not accompanied by higher inflation. Rather, inflation fell steadily throughout the year.

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The committee put forth several hypotheses, but still found the situation puzzling. Peter S. Yoo, an economist with the St. Louis Fed, surveyed the committee's minutes from last year. He noted that in the end the FOMC changed the intended federal funds target once and members searched anxiously for the answers to the conundrum they faced in 1997.

• **"Price Stability and Financial Stability: The Historical Record."** Many countries mandate inflation control as the paramount objective for monetary policy. Critics, however, argue that such a narrow focus compromises a monetary authority's responsibility to preserve stability of the financial system. Thus, the criticism goes, a limited focus on inflation control could increase financial instability. An alternative view holds that a monetary policy directed at controlling inflation would lessen both the incidence and severity of financial instability. Michael D. Bordo, a professor of economics at Rutgers University, and David C. Wheelock, an assistant vice president of the St. Louis Fed, examined the histories of the United States, the United Kingdom and Canada. Their research determined that most episodes of severe financial instability occurred during disinflationary periods that followed sustained inflation. As a result, the evidence appears to support the claims of those who argue that control of inflation could enhance, rather than detract, from the stability of the financial system.

• **"A Policymaker Confronts Uncertainty."** This article is a reprint of a speech given by William Poole, the president and chief executive officer of The Federal Reserve Bank of St. Louis, to the St. Louis Gateway Chapter of the National Association for Business Economics. In this article, Poole discussed the five categories of uncertainties facing today's monetary

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policymakers: 1) the data; 2) future events, shocks and disturbances; 3) how the economy works; 4) market reactions to Fed policy; and 5) the market's anticipation of Fed policy. Poole also discussed the Federal Reserve's role in dealing with each of these uncertainties and their impact on today's policy environment.

Subscriptions to ***Review*** are free and can be obtained by calling (314) 444-8809. The publication is also available on the St. Louis Fed's website: www.stls.frb.org.

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