

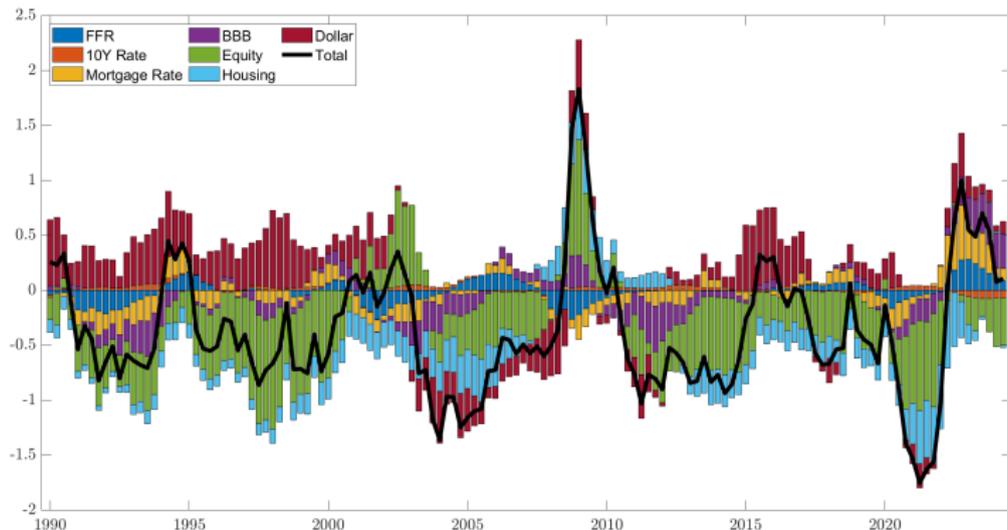
# FCI-Targeting

Ricardo J. Caballero (MIT)

Chicago Fed Council Meeting, Fall 2024

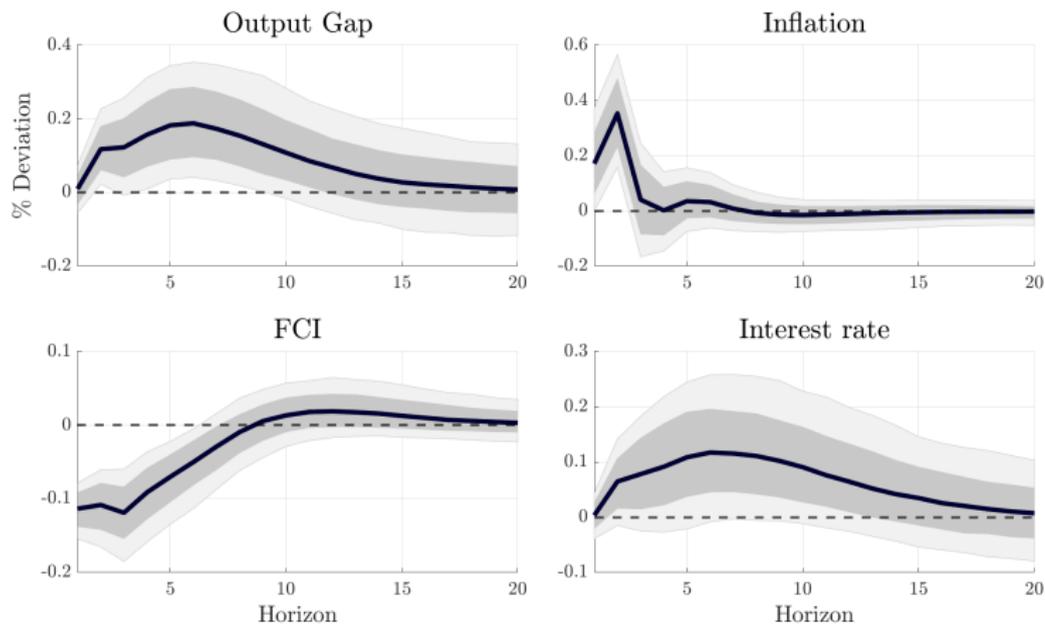
Based on: "Financial Conditions Targeting" Caballero, Caravello, and Simsek (2024)

# US FCI is driven by stocks, FX, house prices (and bonds)



- ▶ FCI-G by Ajello et al: FRB/US implied output effects of various  $\Delta P$
- ▶ Sign convention: Negative FCI  $\Rightarrow$  higher  $\Delta P$  and output

# Financial noise shock affects financial conditions and gaps

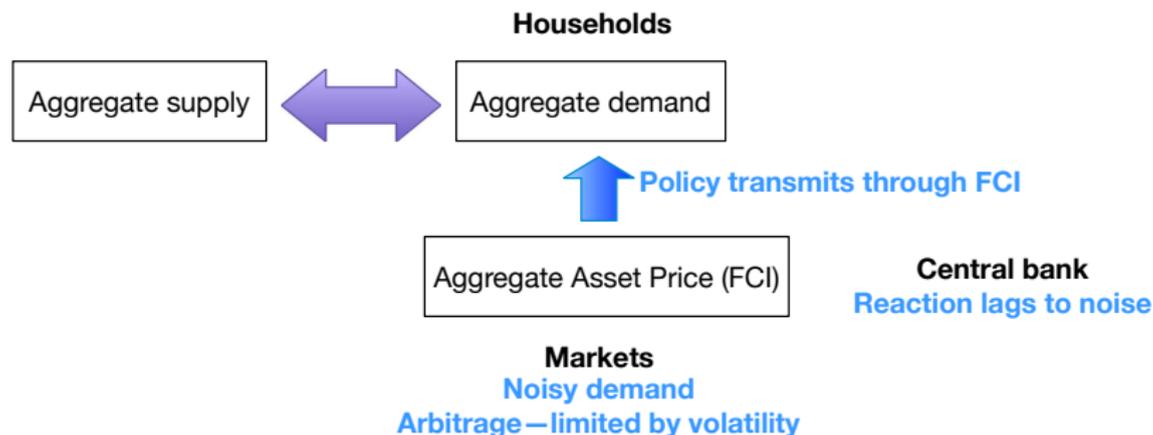


**Figure:** Impulse response to financial noise shock. Sample 1990Q1-2019Q4. Shaded and light shaded grey bands indicate 68 and 90 confidence sets.

# What should the Central Bank do about this noise?

Received answer: focus on macro variables... *“There is no significant additional benefit to responding to asset prices”* (Bernanke and Gertler, 2000, 2001)

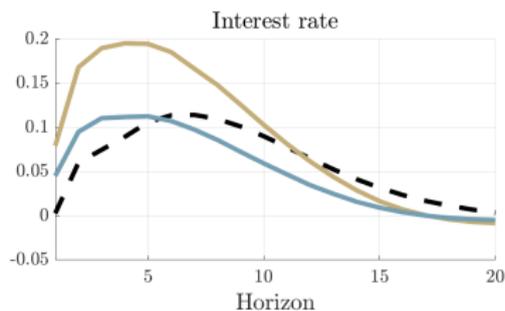
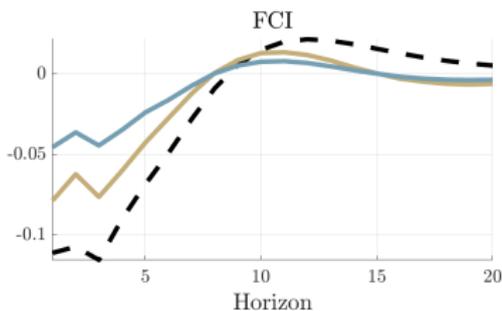
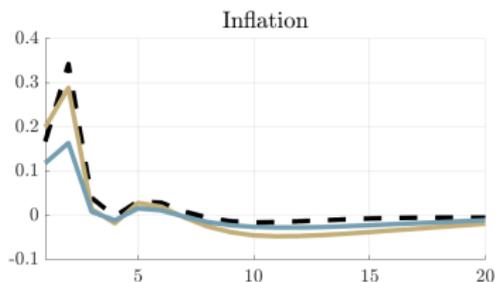
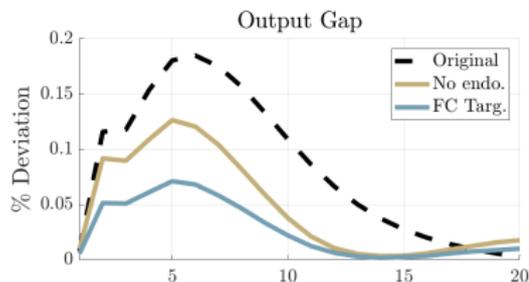
**This paper:** response to asset prices **lowers macro volatility.**



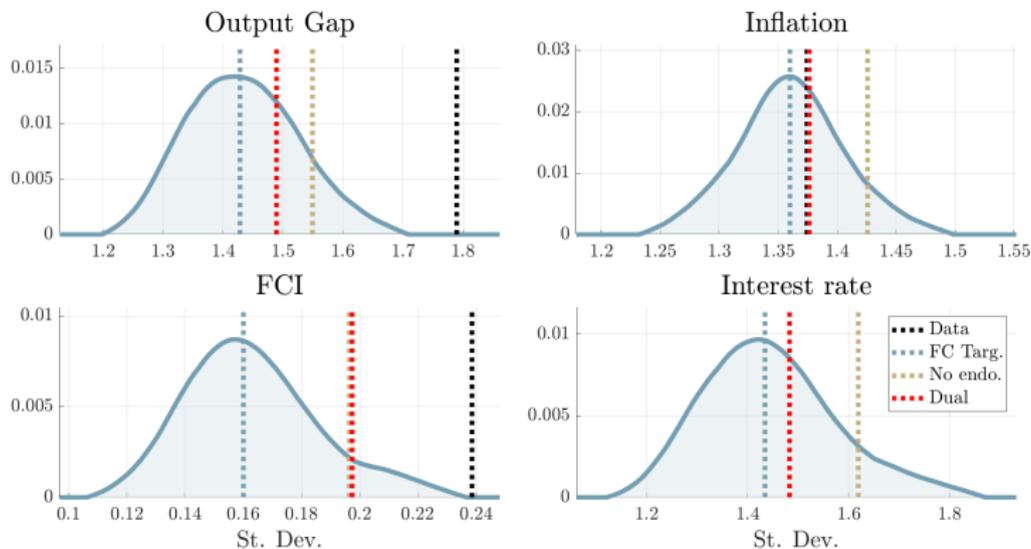
- ▶ **Recruitment effect:** FCI-targeting increases the market's elasticity

# FCI targeting would mitigate the macro impact of noise

$$\mathcal{L} = \sum_{t=0}^{\infty} \beta^t [\pi_t^2 + \tilde{y}_t^2 + \lambda_{\Delta i} (i_t - i_{t-1})^2 + \psi (\overline{FCI}_t - FCI_t)^2]$$

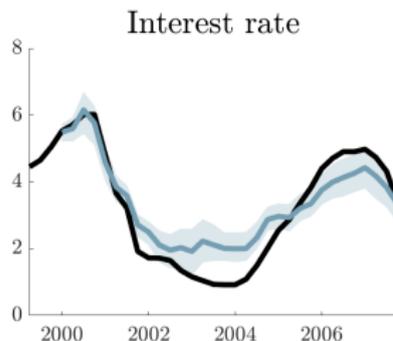
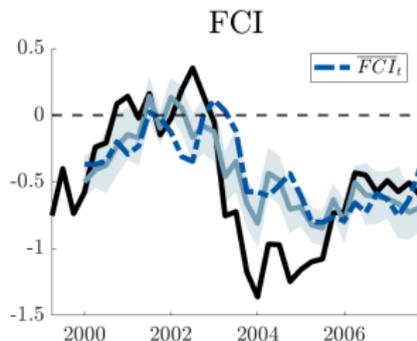
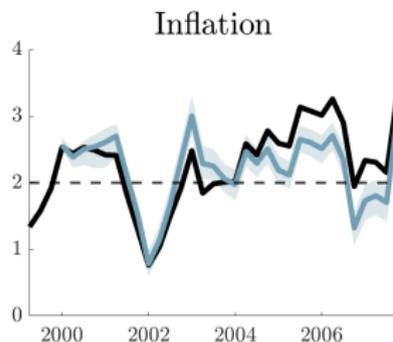
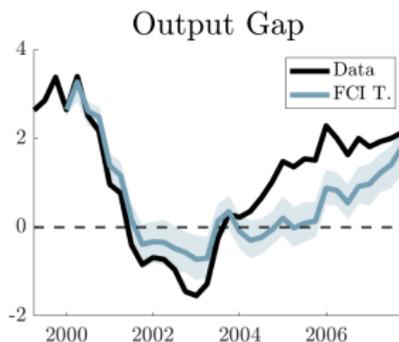


# FCI targeting would reduce overall macroeconomic volatility

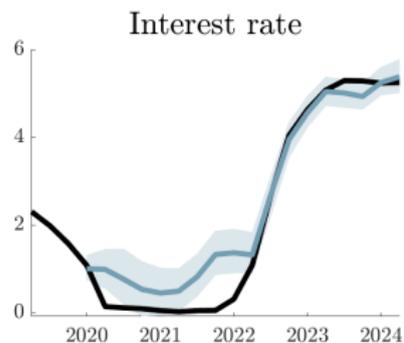
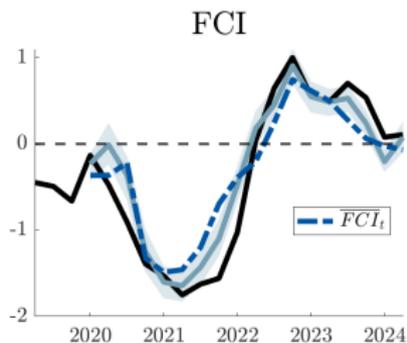
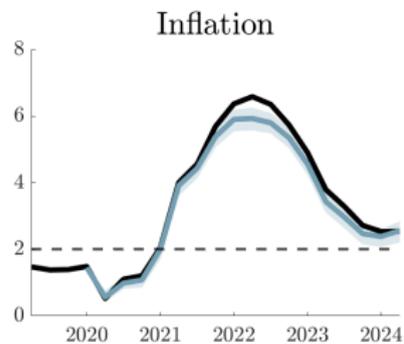
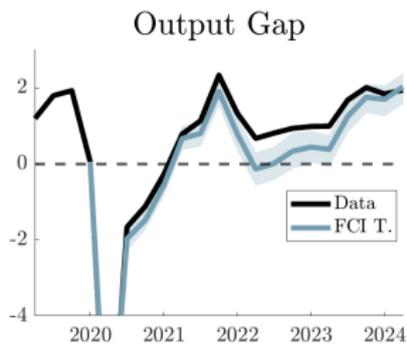


**Black:** data. **Red:** Flex. Dual Mandate ( $\psi = 0$ ). **Blue:** FC targ. with  $\psi^* > 0$ .  
**Beige:** FC targeting, no endog. vol reduction .

# FCI Targeting, Dot-com to GFC

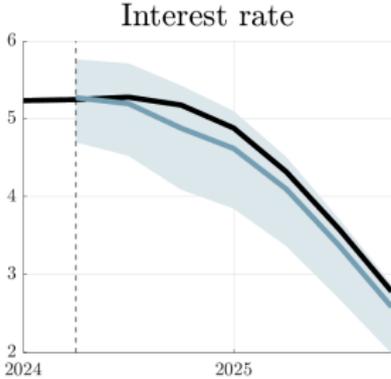
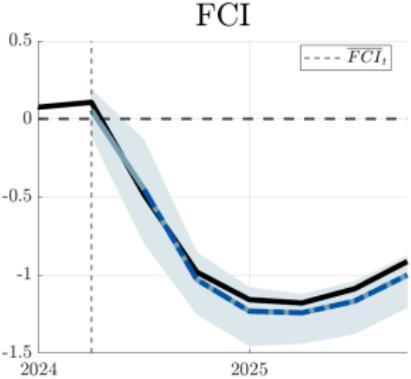


# FCI-Targeting 2020-2024



# Conditions at the end of 2024Q2

Details



# Final Remarks

- ▶ Financial Dutch Disease:

In a sense, Fed has been a hostage of NVDA....

Aggregate vs distributional effects

- ▶ Is rstar a useful concept?

Less so than pstar

But... “rstar may be lower than you think” ....

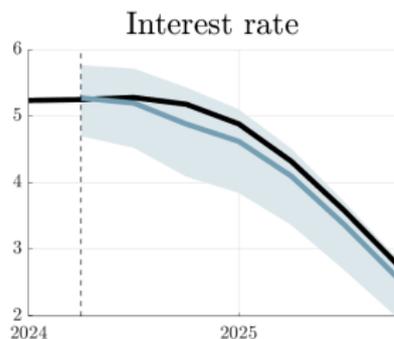
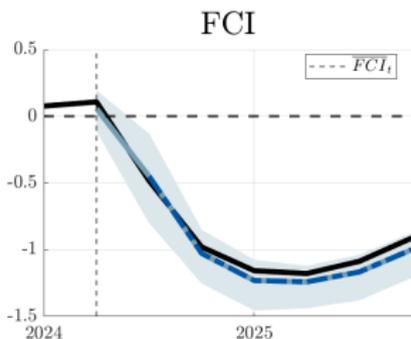
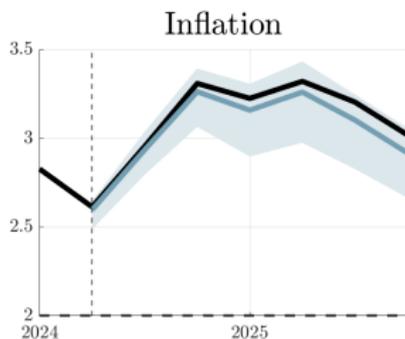
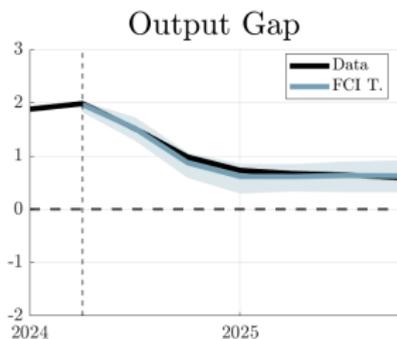
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Ricardo J. Caballero, Tomás E. Caravello, and Alp Simsek. Financial conditions targeting. *MIT Economics Working Paper*, 2024.

# Conditions at the end of 2024Q2: Details [Back](#)



# Longer Horizon Forecasts

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