Fed to roll over Treasuries as they mature

By Editorial Staff *Thu, Jan 21, 2016*

'Market participants desire certainty, but in the uncertain world in which we live, that desire is not consistent with the policy that would best achieve our objectives,' said William C. Dudley, president of the New York Fed, in a speech last Sunday.

About $216 billion in U.S. Treasury securities will mature in 2016, but according to a **speech** this week by New York Fed president William C. Dudley, the Federal Reserve will roll them over rather than let its $2.4 trillion inventory of Treasuries shrink.

The reinvestment policy is designed to be interest-rate neutral. While the Fed won't increase its overall Treasury holdings, it will still be acting as a buyer of Treasuries, thus maintaining demand, establishing a desired price floor and preventing upward pressure on yields.

Addressing the Economic Leadership Forum in Somerset, NJ, last Sunday, Dudley said:

"As we noted in the December FOMC statement, we anticipate that we will continue reinvestment 'until normalization of the federal funds rate is well underway.'

"I think this policy makes sense not only because the decision to end reinvestment will represent a further tightening of monetary policy, but also because it is difficult to assess ahead of time the impact of such a decision on financial market conditions given the lack of historical experience.

"I also believe that continuing reinvestment until the federal funds rate reaches a higher level makes sense. We want to ensure that we have the ability to respond to adverse shocks by easing monetary policy by lowering the policy rate. Having more 'dry powder' in the form of higher short-term interest rates seems more desirable than less dry powder and a smaller balance sheet.

"My view is that we should not set a numerical tripwire for ending reinvestment. If the economy were growing very quickly and the risks of an early return to the zero lower bound for the federal funds rate were deemed to be low, then I could see ending reinvestment at a relatively low federal funds rate.

"In contrast, if the economy lacked forward momentum and the risks of a return to the zero lower bound were judged to be considerably higher, I would want to continue reinvestment until the federal funds rate was higher.

“In my view, good monetary policy-making requires ongoing assessment and judgment, not the adherence to mechanical rules. I know market participants desire certainty, but in the uncertain world in which we live, that desire is not consistent with the policy that would best achieve our objectives.”