FINANCIAL CONDITIONS AND THE REAL ECONOMY

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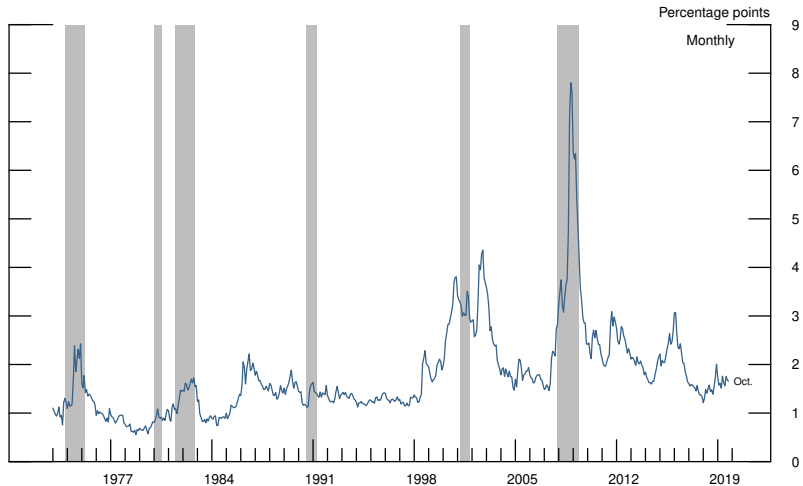*— Economic Advisory Panel Meeting —*
Federal Reserve Bank of New York
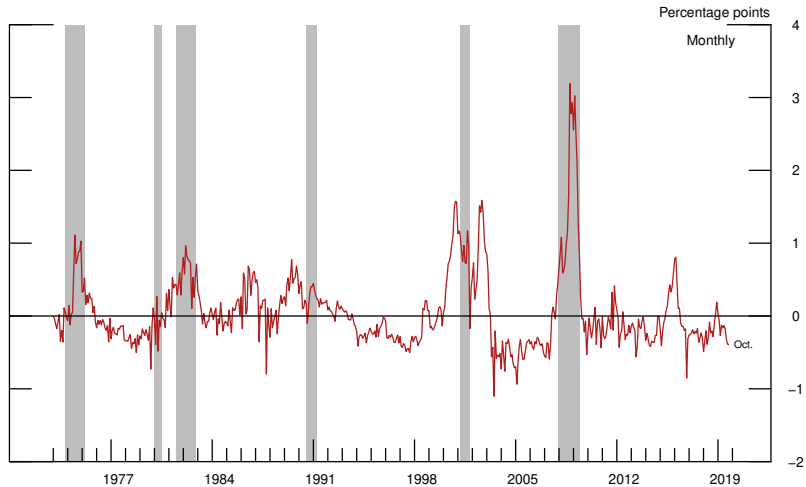November 15, 2019

GZ Credit Spread

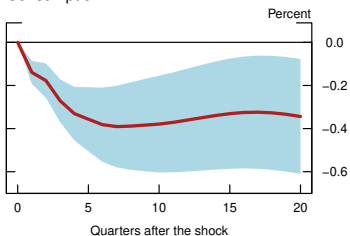**Sample period: 1973:M1–2019:M10**

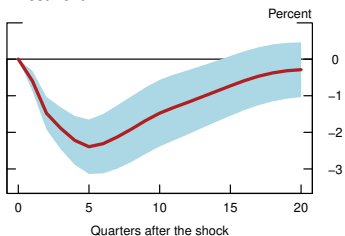# Excess Bond Premium (EBP)

Sample period: 1973:M1–2019:M10

Percentage points
Monthly

Oct.

Macroeconomic Implications of an Adverse EBP Shock

Sample period: 1973:M1–2019:M10
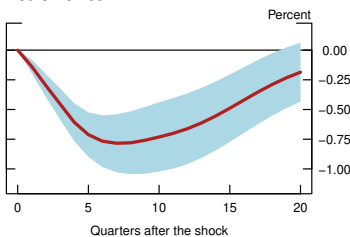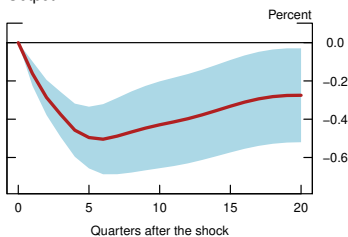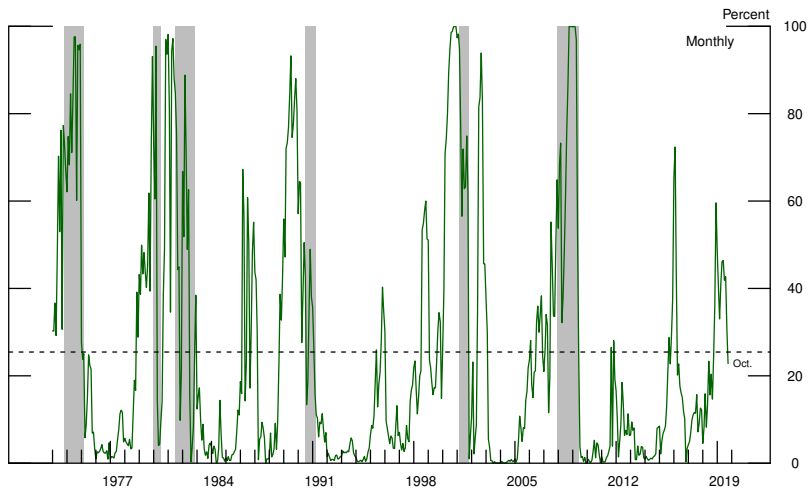

NOTE: Shaded bands represent 90% confidence intervals.
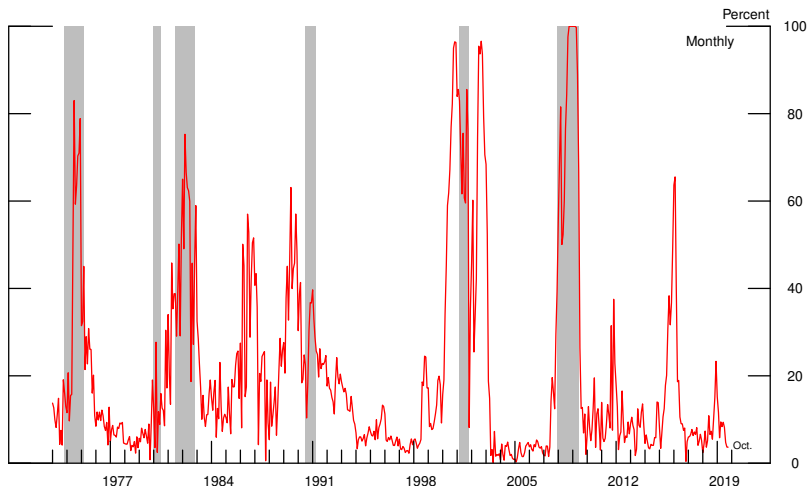
12-Month-Ahead Recession Risk

Probit model with EBP and (10y/3m) term spread

NOTE: The dashed line denotes the unconditional probability of an NBER-dated recession over any subsequent 12 months.
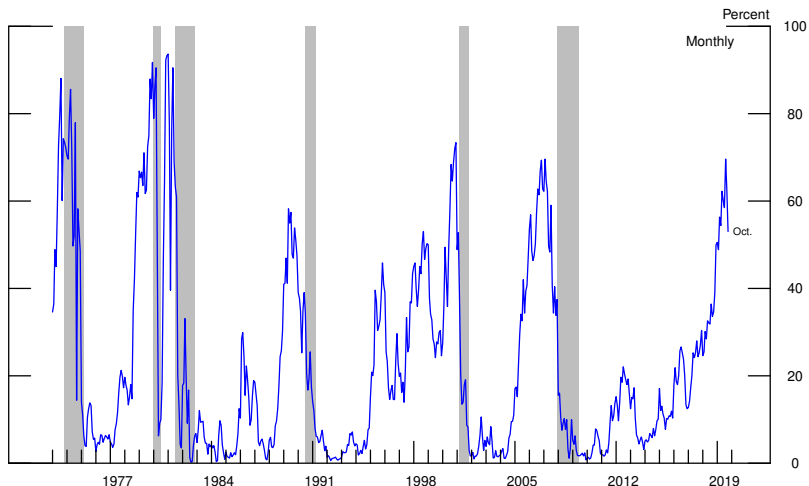
Contribution of the EBP to Recession Risk

Sample period: 1973:M1–2019:M10

NOTE: Contribution of the EBP is evaluated at the average level of the (10y/3m) term spread.

Contribution of the Term Spread to Recession Risk
Sample period: 1973:M1–2019:M10

NOTE: Contribution of the (10y/3m) term spread is evaluated at the average level of the EBP.

Summary

- EBP captures broad movements in financial conditions that determine credit supply.

- Increases in EBP have large contractionary effects on the real economy:
  - ▶ 25 bps. increase in $EBP_t \Rightarrow$ 50 bps. contraction in GDP_{t+6}.

- EBP is a robust predictor of recessions on par with, but independent, of the term spread.

- Further evidence suggests that monetary policy easing has significant effects on economic activity through its impact on EBP.