LV13021

Changing the monetary policy game using quantitative easing: Is it doing the job?

Ray M. Valadez
Pepperdine University

Abstract

For the past five years (2008-2013) the United States and the rest of the world have embarked upon a new approach to quantitative easing (QE) by central banks. Previously, the Federal Reserve's (Fed's) monetary approach was focused on the so-called overnight bank rates or the Federal Funds rate in the United States. The intent has been to stimulate economic growth through several channels by attempting to lower the interest rates in the financial system. Among several assumptions is the belief that interest rates drive investment and mortgage rates, which in turn will ultimately lower the unemployment rate working through these channels.

The U. S. monetary policy's effort to curb unemployment in the United States, presents an interesting twist on the Fed's role in the economy. The buying of mortgage backed securities (MBS) by the Fed's appears to be a new unchartered path to reduce not only the mortgage rates but the unemployment rate as well. The conceived idea that by buying long term treasuries and MBS will create a stimulus for growth with employment opportunities assumes a significant relationship between mortgage rates and the unemployment rate in the United States.

The purpose of this paper is to explore the main research question: Is there a significant relationship between the unemployment rate and mortgage rates? Subsequent questions related to this question were raised and tested for statistical significance. An attempt was made to develop a formula based on regression analysis results and the QE's alleged impact on the unemployment rate. The variables used were the unemployment rate, the 30-Year fixed mortgage rates, the Case/Shiller housing index, and the 10-Year Treasury rate with the last three being the independent variables and the first being the dependent variable.

This study examines the relationship between the unemployment rate and the other selected variables from before, during, and after the period known as the *2007 global financial meltdown* precipitated by the housing bubble burst followed by the greatest recession since the great depression of the 1930s. There appears to be an inverse relationship that is statistically significant between the unemployment rate and 10 year treasury rate, a lever for mortgage rates. Additionally, a short formula was developed using three variables to attempt to predict the unemployment rate effect using this type of quantitative easing.