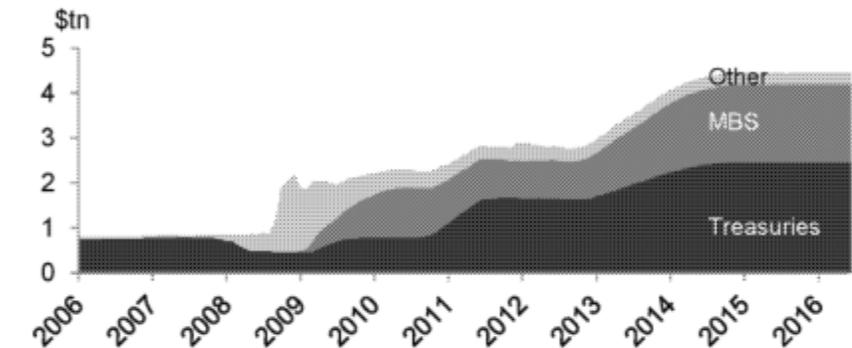


This is especially true if the Fed decides to taper its reinvestment policy and this leads to a tightening of financial conditions



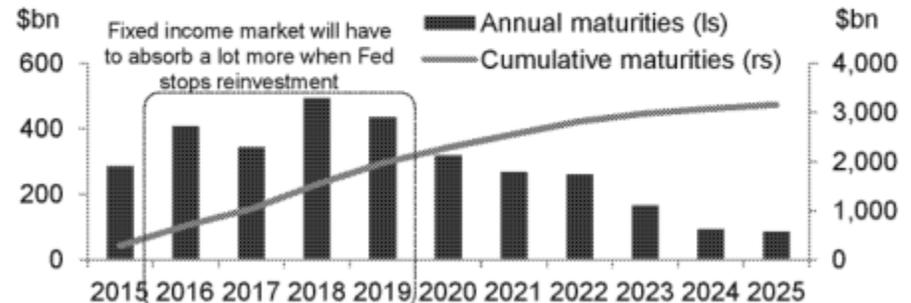
- The Fed is currently reinvesting proceeds from its maturing securities keeping its balance sheet stable
- Altering this reinvestment policy would equate to a monetary policy tightening
 - Fed can stop, or more likely taper reinvestments
 - Opposite effect to QE, i.e., higher long-term rates
- As such, the decision and the tightening of financial conditions it would bring about may affect the Fed's assessment of the pace of rate hikes
 - At \$300-500bn per year through 2019, the amount of maturing securities is considerable
- The Fed has so far given little guidance on when or how this will happen
 - Fed would like to be confident that economy is weathering rate hikes well
- We expect Fed to begin reducing its reinvestment some time in the second half of 2016

The size of the Fed's balance sheet is currently kept constant via the reinvestment of maturing assets



Source: Haver Analytics, Deutsche Bank Research

A wave of maturities from the Fed's portfolio could put upward pressure on long-term rates when the Fed stops reinvesting



Note: projections based on a speech by the Fed's Stanley Fischer in February 2015
Source: Fischer (2015), FRBNY, Deutsche Bank Research