

policy tool during the period of near-zero policy rates, and that the FOMC has not set a timetable for ending the current reinvestment policy.

“Now that the policy rate has been increased, the Committee may be in a better position to allow reinvestment to end or to otherwise reduce the size of the balance sheet,” he said. “Adjustments to balance sheet policy might be viewed as a way to normalize Fed policy without putting exclusive emphasis on a higher policy rate path.”

In conclusion, Bullard said the St. Louis Fed’s recommended policy rate depends mostly on the safe real rate of return, and such rates are exceptionally low and are not expected to rise soon. “This, in turn, means that the policy rate should be expected to remain exceptionally low over the forecast horizon,” he said. “The new administration’s policies may have some impact on the low-safe-real-rate regime if they are directed toward improving medium-term U.S. productivity growth.”

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- **December 5, 2016.** Presentation. ["The Low Real Interest Rate Regime Post-Election: Is There a Switch?"](#) 53rd Annual Economic Forecast Luncheon, W.P. Carey School of Business, ASU, Phoenix, Ariz. [Presentation \(pdf\) \(bullard_asu_dec_5_2016pdf\)](#) | [Press Release](#).

The Low Real Interest Rate Regime Post-Election: Is There a Switch?

December 5, 2016

New policies that are being developed in Washington in the aftermath of the election could impact the current environment of low real (inflation-adjusted) interest rates on such safe assets as short-term government debt, President James Bullard said in a presentation at Arizona State University in Phoenix. He singled out three efforts being discussed by legislators in

Washington, saying they have the potential to affect productivity growth and, therefore, real interest rates; those three are deregulation, tax reform and targeted infrastructure spending. Bullard also explained his reasoning for recommending an increase in the fed funds rate of 25 basis points, which would bring it up to 63 basis points, still exceptionally low.

St. Louis Fed's Bullard Discusses Low Real Interest Rates and New Policies in Washington

PHOENIX – Federal Reserve Bank of St. Louis President James Bullard discussed [“The Low Real Interest Rate Regime Post-Election: Is There a Switch?”](https://www.stlouisfed.org/-/media/project/frbstl/stlouisfed/files/pdfs/bullard/remarks/bullard_asu_dec_5_2016.pdf) on Monday at Arizona State University’s annual economic forecast luncheon.

In his presentation, Bullard discussed how the current state of the U.S. economy and monetary policy might be viewed in terms of a “low-safe-real-interest-rate regime” and whether the proposed policies of the incoming White House administration could impact this regime.

“Bottom line: Whether the new policies being developed in Washington represent a ‘regime shift’ depends on whether these policies will impact productivity,” he said.

Low-Real-Interest-Rate Regime

The St. Louis Fed recently changed to a regime-based approach to near-term projections of the U.S. macroeconomy and monetary policy. Under this approach, the macroeconomy could visit a set of possible regimes, and monetary policy is regime-dependent.

Bullard described two real interest rate regimes, noting that a high-real-interest-rate regime prevailed in the 1980s and 1990s, but a low-real-interest-rate regime prevails today. He explained that the real returns on safe, short-term assets, such as short-term government debt, are

exceptionally low and are unlikely to return to their historical levels over the next two to three years.

Bullard noted that the St. Louis Fed's recommended policy rate (i.e., the federal funds rate target) depends mostly on the safe real rate of return.

"With inflation and unemployment close to longer-run levels, a standard recommendation is to set the policy rate equal to the real interest rate plus the inflation target," he said.

"Because we are in the low-real-rate regime, the St. Louis Fed's policy rate recommendation comes out to a low number," he explained.

The current policy rate setting is 38 basis points, or 0.38 percent. "I conclude that a single 25-basis-point increase in the policy rate – from 38 to 63 basis points – will get us very close to the standard recommended value over the forecast horizon," Bullard said. (The forecast horizon runs through 2019.)

The Impact of New Policies Brewing in Washington

In discussing whether President-elect Donald Trump's new policies being developed could impact the current low-safe-real-rate regime, Bullard said that if they are properly executed, the new set of policies may have some effect. In particular, he focused on their potential impact on productivity growth.

Bullard explained that low productivity growth is one of several factors that may be putting downward pressure on safe real rates of return. "U.S. productivity growth is low and could conceivably be improved considerably. This could help to increase the real rate," he said.

Of the new policies being developed in Washington, Bullard said deregulation, infrastructure spending and tax reform could have some impact on the low-safe-real-rate regime over the next several years, but any impact from immigration and trade policy reforms will likely take longer.

He then discussed the potential impact of the first three policies:

- Regarding deregulation, he said to the extent that some areas of regulation are excessive, deregulation could improve productivity.
- Regarding infrastructure, he said spending directed to the right public capital could improve productivity.
- Regarding tax reform, he said changes that encourage investment in the U.S. could improve productivity.

He concluded, “New policies brewing in Washington may have some impact on the low-safe-real-rate regime if they are directed toward improving medium-term U.S. productivity growth.”

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- **November 18, 2016.** Panel Discussion at Frankfurt European Banking Congress.
[Video and Summary.](#)

President Bullard on Panel at Frankfurt European Banking Congress

November 18, 2016

The video is no longer available.

St. Louis Fed President James Bullard participated in a panel discussion at the Frankfurt European Banking Congress in Frankfurt, Germany. He shared his views on multiple topics, including the potential impact of proposed legislative action on the U.S. economy, the St. Louis Fed’s regime-based approach to near-term U.S. macroeconomic and monetary policy projections, and whether he currently sees a bubble in the U.S. economy.

Other panelists included John Cryan of Deutsche Bank; Pentti Hakkarainen of the Bank of Finland; Andréa M. Maechler of the Swiss National Bank; and