to-make-of-market-measures-of-inflation-expectations.html)" Liberty Street Economics, New York Fed, Aug. 15, 2011.

4The drop since 2014 has been highly correlated with oil prices. For more on this topic, see my presentation on Feb. 24, 2016, " [More on the Changing Imperatives for U.S. Monetary Policy Normalization](https://www.stlouisfed.org/-/media/project/frbstl/stlouisfed/files/pdfs/bullard/remarks/bullard-money-marketeers-nyu-24-feb-2016.pdf)."

Additional Resources
• Regional Economist: [Inflation Expectations Are Important to Central Bankers, Too](https://www.stlouisfed.org/publications/regional-economist/april-2016/inflation-expectations-are-important-to-central-bankers-too)
• On the Economy: [What Future Oil Price Is Consistent with Current Inflation Expectations?](https://www.stlouisfed.org/on-the-economy/2016/march/oil-prices-inflation-expectations-cpi-assumptions)
• On the Economy: [How Accurate Are Measures of Inflation Expectations?](https://www.stlouisfed.org/on-the-economy/2015/may/how-accurate-are-measures-of-inflation-expectations)

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- **April 14, 2016**. Article. "President's Message - The Road to Normal: Necessary, Even if It Means Going It Alone," Federal Reserve Bank of St. Louis *Annual Report 2015*.

  President's Message

  The Road to Normal: Necessary, Even if It Means Going It Alone

Until about seven years ago, the U.S. had not seen short-term nominal interest rates basically at zero since the Great Depression and World War II. [Historically, macroeconomists looked at that era as an aberration—a situation that was not the normal state of affairs for either the U.S. economy or most economies around the world. But that view is now challenged. Recent encounters with zero rates here in the U.S. and around the globe suggest that zero-interest-rate environments are long-lasting and that the macroeconomic experience in a zero-rate environment is not particularly good. Returning to a macroeconomic equilibrium that includes somewhat higher nominal interest rates may lead to better outcomes for the U.S. economy. 1](https://www.stlouisfed.org#endnote1)

During the 2007-2009 crisis, the Federal Open Market Committee (FOMC) set a target range for the federal funds rate at 0-0.25 percent. It remained there from December 2008 to December 2015, when the FOMC increased the target range by 25 basis points (to 0.25-0.5 percent). This step is ideally the first of many steps in the process of normalizing U.S. monetary policy.

From a global perspective, however, normalization is not occurring. While the U.S. has started increasing interest rates, most of the other major economies outside of China are still at zero (or even at negative interest rates) and are not planning to come off zero anytime soon. In fact, in addition to low interest rate policies, the European Central Bank is currently in the middle of an aggressive quantitative easing (QE) program, as is the Bank of Japan. If one believes that global markets are well-integrated, then global interest rates overall likely will remain close to zero for a long time.

Even if the Fed continues to raise interest rates, U.S. monetary policy will remain exceptionally accommodative through the medium term. In addition to stressing that policy decisions will be data-dependent, [the FOMC's statement following its Dec. 16, 2015, meeting said, "The Committee expects that economic conditions will evolve in a manner that will warrant only gradual increases in the federal funds rate; the federal funds rate is likely to remain, for some time, below levels that are expected to prevail in the longer run." 2](https://www.stlouisfed.org#endnote2)

[Furthermore, the FOMC has stated that it expects to wait until normalization is well-underway before starting to normalize the Fed's balance sheet, which increased from about $800 billion in 2006 to about $4.5 trillion due to the Fed's QE programs. (As a result of the exceptionally large balance sheet, the Fed has had to change tactics on how it operates in short-term interest rate markets. See the main essay in this annual report for more details.)](https://www.stlouisfed.org#endnote3)

Why is normalization expected to take so long, and why isn't the world normalizing monetary policy along with the Fed? The lack of inflation pressure helps address both questions. Inflation has been very low in the U.S. and in other major industrialized economies that are part of the Group of Seven (G-7), in part because of a commodity cycle in which energy prices have declined dramatically since mid-2014. Low inflation has been the major surprise of the era, given that central banks in these countries have implemented zero-interest rates and other supplemental types of monetary policy. Why higher inflation has not occurred so far despite these aggressive monetary policies is a topic of debate, causing macroeconomists to revisit their models.

But with inflation still low, one might ask, "Why normalize at all?" Although headline inflation remains low, inflation net of the decline in oil prices is reasonably close to the Fed's 2 percent target. Moreover, forecasts suggest that headline inflation will move back to the target once oil prices stabilize. On the employment side of the Fed's dual mandate, labor markets are now close to normal. Thus, a key reason for normalizing policy is that the FOMC's goals regarding inflation and employment have essentially been met, while the policy settings remain far from normal.

Another reason to normalize is that staying at zero could cause distortions in the economy. For example, a major bubble in asset prices could result, and if the bubble bursts, a recession could follow—much like we saw during the mid-2000s. A second example of a distortion is that the very low rates of return on saving may be creating disincentives for saving. Tilting policy toward borrowers for such a long period of time, however, may not be optimal. Furthermore, the low returns on saving are hurting retirees and others who are counting on that income. 4

A third reason for wanting to normalize policy goes back to the U.S. experience during 1984-2007. The U.S. had long expansions and relatively mild recessions then. That era was characterized by less volatility and faster growth than occurred in the 1970s. In addition, monetary policy was relatively well-understood in the 1984-2007 period, and policy was adjusted in both directions in response to economic shocks. In short, the U.S. macroeconomic equilibrium during that period—when nominal interest rates were higher—was associated with good economic outcomes. If we are unable to return to such a situation, it would be unclear how monetary policy would be implemented and what the new equilibrium would look like, specifically in terms of macroeconomic volatility. [Prudent monetary policy, therefore, suggests moving monetary policy settings closer to normal. 5](https://www.stlouisfed.org#endnote5)

James Bullard President and CEO Federal Reserve Bank of St. Louis

Endnotes

1. The rate on three-month Treasury bills was near zero for much of the 1930s and early 1940s and was pegged at 3/8 percent from early 1942 to July 1947. See Carlson, Mark; Eggertsson, Gauti; and Mertens, Elmar. "Federal Reserve Experiences with Very Low Interest Rates: Lessons Learned," FOMC Memo Dec. 5, 2008, at [www.federalreserve.gov/monetarypolicy/files/FOMC20081212memo02.pdf](https://www.federalreserve.gov/monetarypolicy/files/fomc20081212memo02.pdf). [[back to text](https://www.stlouisfed.org#1##1)]
2. For more on data dependency, see my column in the January 2016 issue of The Regional Economist, "What Does Data Dependence Mean?" at www.stlouisfed.org/publications/regional-economist/january-2016/what-does-data-dependence-mean, and in the January 2015 issue, "Liftoff: A Comparison of Two Normalization Cycles," at www.stlouisfed.org/publications/regional-economist/january-2015/presidents-message. [[back to text](https://www.stlouisfed.org#2##2)]
3. See the FOMC statement on Dec. 16, 2015, at

www.federalreserve.gov/newsevents/press/monetary/20151216a.htm. [[back to text](https://www.stlouisfed.org#3##3)]
4. See also my speech on June 26, 2014, “Income Inequality and Monetary Policy: A Framework with Answers to Three Questions,” at [www.stlouisfed.org/~/media/Files/PDFs/Bullard/remarks/Bullard_CFR_26June2014_Final.pdf](https://www.stlouisfed.org/-/media/project/frbstl/stlouisfed/files/pdfs/bullard/remarks/bullard_cfr_26june2014_final.pdf). [[back to text](https://www.stlouisfed.org#4##4)]
5. For more discussion, see my speech on Nov. 12, 2015, “Permazero,” at [www.stlouisfed.org/~/media/Files/PDFs/Bullard/remarks/Bullard-Permazero-Cato-12Nov2015.pdf](https://www.stlouisfed.org/-/media/project/frbstl/stlouisfed/files/pdfs/bullard/remarks/bullard-permazero-cato-12nov2015.pdf). [[back to text](https://www.stlouisfed.org#5##5)]

- **April 6, 2016**. Welcoming Remarks. Given at the *Homer Jones Memorial Lecture*, Federal Reserve Bank of St. Louis.
  Remarks (pdf) (welcoming-remarks-homer-jones-2016pdf) | Event Videos.

Welcoming Remarks: 2016 Homer Jones Memorial Lecture, Featuring Lawrence Summers

April 6, 2016

St. Louis Fed President James Bullard delivered welcoming remarks at the 27th Homer Jones Memorial Lecture. He introduced this year's speaker, Lawrence Summers—one of the country's most influential economists and policymakers—who discussed "Secular Stagnation and Monetary Policy." The annual event honors the St. Louis Fed's former Research director, Homer Jones, who played a major role in helping the Bank become a leader in monetary research and statistics.

Full text of remarks:

Welcoming Remarks by James Bullard, President and CEO The 2016 Homer Jones Memorial Lecture Federal Reserve Bank of St. Louis April 6, 2016