THE FEDERAL RESERVE SYSTEM

Date:	October 13, 2015
То:	Federal Open Market Committee
From:	David Altig, Stephen A. Meyer, and Daniel G. Sullivan
Subject:	Background Material for r* Discussion

During the April FOMC meeting, a number of participants suggested that the Committee should have a discussion of the meaning of r*, of its current level and how its level might be expected to evolve, and of its implications for the Committee's policy decisions. The attached four memos, listed below, address these issues.

- 1. r*: Concepts, Measures, and Uses
- 2. Real Interest Rates Over the Long-Run
- 3. Estimates of Short-Run r* from DSGE Models
- 4. Monetary Policy at the Lower Bound with Imperfect Information about r*

The first of the four memos identifies various concepts of r^* ; it also discusses the connection between r^* and simple policy rules such as the Taylor rule. The second memo focuses on factors that have contributed to persistent, longer-run, movements in r^* , and on empirical estimates of longer-run trends in r^* . The third memo focuses on shorter-term variations in r^* using insights derived from research on dynamic stochastic general equilibrium (DSGE) models; this memo emphasizes the effect of economic disturbances on r^* at business cycle frequencies. The fourth memo addresses the policy implications of uncertainty about the level and persistence of movements in r^* ; it includes a discussion of the implications of adjusting simple rules by incorporating a time-varying intercept term that proxies for movements in r^* . Staff will provide short briefings on these four memos at the upcoming FOMC meeting. Participants will have an opportunity to ask questions and to provide comments (not a full go-round). If you would like to comment, it would be helpful if you would address some or all of the following questions:

- 1. What does your estimate of the current level of r* imply for the degree of accommodation provided by current monetary policy?
- 2. How, in your view, has r* been affected by recent changes in financial conditions, especially by movements in the exchange value of the dollar?
- 3. How do you expect r* to evolve, and what are the implications for the appropriate path of policy going forward?