The New Normal for the U.S. Economy

The Philadelphia Fed Policy Forum

Philadelphia, PA

December 4, 2015

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President and CEO
Federal Reserve Bank of Philadelphia

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Good morning and welcome to the 11th Philadelphia Fed Policy Forum. This is my first Policy Forum as President and CEO, and I have been looking forward to it since joining the Bank in July.

Our Policy Forums are held only once every two years. They provide a unique opportunity to bring together some of the most renowned leaders in economic research and focus on long-term issues and their implications for monetary policy.

As someone who has spent much of his career at academic institutions, I am particularly thrilled to lead an organization that provides a forum for the sort of wide-ranging discussions and debates we will hear today.

I want to thank Mike Dotsey, director of research, and his staff for organizing today's program. They have brought together an all-star lineup of thought leaders from across the country. I am excited for you to hear them and so appreciative that they could join us.

Our theme today is "The New Normal for the U.S. Economy." What is the "new normal"? As the saying goes, "It depends who you ask." But I believe most would agree that the question is complex and that there is scope for different viewpoints. Today, we will hear several views on the U.S. economy's current and long-term economic prospects.

Our goal is to delve into some of the different issues and perspectives that are influencing our nation's economic growth. We will cover a wide range of topics, broadly divided into three areas that have an impact on our economy: technology/innovation, social factors, and monetary policy.

Here at the Philadelphia Fed, economist Leonard Nakamura has been researching how the evolution of information and communication technology is creating measurement issues for our statistics. One example is that some innovations, such as free apps and social media, are widely used but may not generate revenue, at least not right away. Leonard calls this URL — "Ubiquity now, Revenue Later."

In a "URL world," is productivity growth truly as low as it appears in the official statistics? It is possible that new disruptors to the economy, like free apps and social media, are making our progress harder to capture in current economic measures. This is a special concern for monetary policy because it is possible that we are not fully capturing rising quality in our price measures and that inflation is even lower than we think it is.

These issues have a direct bearing on the conduct of monetary policy. This is why today's discussions on the economic impact of technology and innovation are relevant for central bankers. I am honored to welcome Robert Gordon and Joel Mokyr from Northwestern University, and Erik Brynjolfsson, whose book *The Second Machine Age: Work, Progress, and Prosperity in a Time of Brilliant Technologies* was one of the highlights of my summer reading.

I am also very pleased to have leaders like Daron Acemoglu, Darrell West, and Eric Hanushek with us to address issues surrounding immigration and income inequality.

All of these issues have critical implications for the new normal. Our day will conclude with thoughts on monetary policy from two of my respected colleagues: James Bullard, President of the St. Louis Fed, and Narayana Kocherlakota, President of the Minneapolis Fed. Narayana has served the Federal Reserve with great distinction for the past six years. It has been a pleasure getting to know him, and I want to wish him the best for his future endeavors.

We all know that what the new normal will mean ultimately depends on the growth rate of worker productivity, the key determinant of our standard of living. Most of you are familiar with Paul Krugman's statement that while "Productivity isn't everything, but in the long run it is almost everything."

The recent slowdown in productivity growth and the continuing downshift in labor force growth are prominently influencing our views of the new normal. But trends are not destiny — or at least they needn't be. The growth rate of productivity is influenced by a range of factors, many of which we can influence. These include the rate of discovery of new knowledge, the incentives for businesses to adopt new technologies and to provide the needed on-the-job training for their workers, the effectiveness of our educational institutions in providing formal schooling, and the growth in the size of our domestic and international markets. Last but not least, it also includes the whole gamut of economic policies that interact with all of those factors.

Our nation's growth is one of the most important issues we face as policymakers. We know that incremental changes in the standard of living will determine our future prosperity. We need to be thinking about what we can do to positively influence growth rates five, 10, and 15 years down the road.

While prospects for long-term growth in the United States remain solid, the medium-term outlook has been revised downward in recent years. My view, which is my own and not necessarily that of the Federal Reserve System or my colleagues on the Federal Open Market Committee (FOMC), is that we will see steady and modest growth going forward.

GDP growth has averaged 2.2 percent since the Great Recession ended in June 2009, and the most recent FOMC projections show the central tendency for long-term growth to be in the 1.8 to 2.2 percent range. Economic fundamentals have been improving, and we are approaching normalcy.

Accordingly, I would like to see rates raised sooner rather than later. With an early start, we can better ensure that monetary accommodation is removed gradually and that inflation returns to the Fed's 2 percent target smoothly. My fear is that the Federal Reserve risks losing its credibility and only adds uncertainty to the economic landscape the longer the Committee waits to begin normalizing policy.

Therefore, raising rates this year will, in my view, serve to reduce monetary policy uncertainty and to keep the economy on track for sustained growth with price stability.

One of the highlights of my first four months at the Fed has been the opportunity to meet with people across the District. I have heard firsthand about small business challenges, innovative community programs, new housing models, and much more. People's pride, commitment, and resilience are empowering. As someone who has dedicated much of his life to education and developing our future leaders, I am inspired by the great potential I see.

Our challenge is to ensure that we have the resources, the vision, and the leadership to make full use of our District's potential.

We don't know exactly what tomorrow will look like, but we do know it will be different. We need to stay attuned to, and ahead of, those changes.

I think you can see why I am so excited to have you here in Philadelphia for today's program. I hope that it raises many questions and inspires more discussion and research on these pressing issues.

Thank you for joining us. I look forward to the presentations and the discussions they will generate. Please enjoy today’s program.