The St. Louis Fed's New Characterization of the Outlook for the U.S. Economy

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President James Bullard and his co-authors explain the St. Louis Fed's new characterization of the U.S. macroeconomic and monetary policy outlook, which more explicitly takes into account uncertainty about possible medium- and longer-run outcomes. The new approach is based on the idea that the economy may visit a set of possible regimes instead of converging to a single, long-run steady state. As such, the new approach does not include projections for long-run values for U.S. macroeconomic variables or for the policy rate.

Paper (pdf) | Media Call Audio (below)

Some details:

- The idea that the economy will converge to a single, long-run steady state (with key macroeconomic variables returning to long-run averages) is being abandoned.

- In its place, a new narrative emerges—one that considers medium- and longer-term outcomes in terms of regimes. Examples of regimes would include periods of no recession and recession, periods of low productivity growth and high productivity growth, and periods of low returns on government debt and high returns.

- Regimes are generally viewed as persistent, and optimal monetary policy is viewed as regime-dependent.

- This new approach delivers a simple forecast of key macroeconomic variables that are likely to persist over the next 2.5 years: real output growth of 2 percent, unemployment of 4.7 percent and inflation of 2 percent. Under this regime, the appropriate policy rate path would be 0.63 percent over the forecast...
For the longer run, the new approach does not contain forecasts for macroeconomic variables or the policy rate, as predicting exactly how and when a regime will change is difficult. The best path today is to forecast that the current regime will persist and set appropriate policy for this regime.
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