



Normalization: A New Approach

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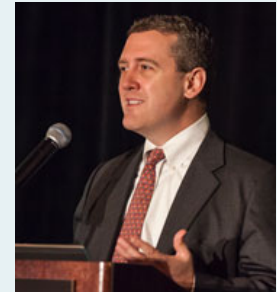
August 17, 2016

While addressing a research conference in St. Louis on wealth and asset management, President James Bullard explained the reasoning behind the St. Louis Fed's new approach to near-term U.S. macroeconomic and monetary policy projections. The old narrative assumed that the economy is converging to a single, long-run steady state, with key macroeconomic variables tending toward an average of their past values. In the new narrative, the concept of a single, long-run steady state is abandoned. Instead, there is a set of possible "regimes" that the economy may visit, which are generally viewed as persistent. While switches between regimes are possible, they are not forecastable. Bullard said that the projected policy rate path is the main difference in the new approach: The policy rate under the old narrative would likely rise over the forecast horizon to be consistent with its steady-state value, whereas the policy rate under the new narrative would likely remain essentially flat over the forecast horizon to remain consistent with the current regime.

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"Rationally, let it be said in a whisper, experience is certainly worth more than theory."
Amerigo Vespucci

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