LEXINGTON, Ky. — Federal Reserve Bank of St. Louis President James Bullard presented “Remarks on the 2018 U.S. Macroeconomic Outlook” Tuesday during the Annual Economic Outlook Conference at the University of Kentucky.

“U.S. real GDP growth surprised to the upside during 2017. The natural prediction from here would be that growth will now slow toward trend during 2018 and 2019,” Bullard said. “The possibility of a tax-driven investment boom in the U.S. leans against this type of forecast.”

Despite such growth, and relatively good labor market performance, inflation remains low. “Continued strong labor market performance is unlikely to translate into meaningfully higher inflation because Phillips curve effects are weak,” Bullard added. However, he said that “inflation expectations have moved more in line with the 2 percent inflation target of the Federal Open Market Committee (FOMC).”

**The Modest 2017 Economic Growth Surprise**

Bullard noted that the U.S. real GDP growth rate in the fourth quarter of 2017 was 2.5 percent, measured from a year earlier. In December 2016, the FOMC’s median projection for 2017 growth was 2.1 percent. “The upside surprise in 2017 was arguably modest,” Bullard said.

He also noted that other large economies had better-than-expected growth in 2017, which fed into the profits of U.S. multinationals and helped U.S. equity prices rally last year.

“The natural forecast to make at this point would be that growth will slow toward the trend pace during 2018 and 2019,” he said, adding that the St. Louis Fed's estimate for the trend growth rate is about 2 percent.

**An Investment Boom in 2018?**
Recent changes to the U.S. tax code have been made to spur investment, which has been relatively low during the past eight years. “If investment returns to its average from past expansions, growth in the U.S. will improve,” Bullard explained.

“Most forecasters seem to be hedging their bets on whether or not an investment boom will materialize,” he said. “An investment boom is not my baseline case, but I am keeping a close watch on this issue.”

**Inflation Remains Low**

Inflation remained low during 2017 against a backdrop of relatively good labor market performance and a still historically low policy rate (i.e., the federal funds target rate), Bullard noted.

While the employment report released on Friday was good, with 200,000 jobs created and the unemployment rate holding steady at 4.1 percent in January, “I caution against interpreting good news from labor markets as translating directly into higher inflation,” Bullard said. “The empirical relationship between these variables has broken down in recent years and may be close to zero.”

He also discussed inflation expectations, which may give a signal of future inflation. He noted that market-based measures of inflation compensation have increased recently. “The measures today are closer to being in line with the FOMC’s 2 percent inflation target, but remain a bit low,” he said.

**Monetary Policy Closer to Neutral**

Turning to the stance of U.S. monetary policy, Bullard noted that the FOMC has begun to gradually reduce the size of its balance sheet. In addition, the range for the policy rate has been increased gradually and is currently 1.25-1.50 percent.

He also noted that current estimates of the neutral real rate (or $r^*$) are near zero, and that core PCE inflation (measured as the year-over-year percentage change in the core personal consumption expenditures price index) is 1.5 percent. Therefore, the current policy rate setting minus core PCE inflation is near $r^*$, which suggests that “the current policy setting is closer to neutral than in previous years,” Bullard said.