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Macro Roundup Artcile

Headline: Have Interest Rates Risen Fundamentally?

Article Link: https://blog.rangvid.com/2023/11/19/have-interest-rates-risen-fundamentally/

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Tweet: Jesper Rangvid finds that the NY Fed's estimate of low underlying interest rates seems robust and that the resilient economy is likely due to post-pandemic savings and expansionary fiscal policy.

Summary: The underlying level of interest rates cannot be observed but must be estimated. There are two well-known estimates. One, from the NY Fed, suggests that underlying interest rates are still very low, while the other, from the Richmond Fed, suggests that they have been rising recently. My reading of this is that the estimate from the NY Fed – at least for now – appears more robust. Low equilibrium interest rates have important implications. Let me conclude by mentioning at least two of them. If underlying equilibrium real interest rates had risen, monetary policy would not be tight right now and would explain why we have not yet experienced a recession. On the other hand, if r* has not risen, monetary policy is tight. I'm leaning towards the latter. I think the economy has been amazingly resilient because people saved a lot coming out of the pandemic, coupled with a very expansionary fiscal policy that is also supporting growth, not that monetary policy is not tight. Second, if underlying real interest rates are low, interest rates should fall when inflation is under control and monetary policy rates are lowered. Perhaps interest rates will not become quite as low as before the pandemic (e.g. negative interest rates in Europe), but should be significantly lower than today. Related: Measuring the Natural Rate of Interest After COVID-19 and In Search of Safe Havens: The Trust Deficit and Risk-free Investments! and What Have We Learned About the Neutral Rate?

Primary Topic: Financial Markets

Topics: Financial Markets, Fiscal Deficits, Fiscal Policy, GDP, Government Spending, Op-Ed/Blog Post, Weekly

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