General Discussion

GENERAL DISCUSSION Olivier Blanchard commented that he agrees with Gregory Mankiw on the uncertainty of whether there are dynamic efficiencies or inefficiencies—there are many distortions that matter, but the welfare cost is probably lower than it was in the past. Blanchard argued that the effective lower bound was missing from the discussion and that it matters because it may come into play to sustain demand. Blanchard disagreed with Carmen Reinhart that the decrease in real rates is largely a result of monetary policy. The decrease started long before quantitative easing, the financial crisis, and COVID-19 and while quantitative easing allowed banks to achieve lower de facto interest rates, the causality comes from real factors, not policy. Quantitative easing is not monetization in the usual sense; it is a swap of two liabilities: bonds and interest-paying central bank reserves, he concluded. On Phillip Swagel's remarks, Blanchard noted that he suspects the scenarios presented were benign relative to what we may expect would happen; he went on to suggest that the scenarios should be ranked by the difference between the interest rate and inflation rate, which is what matters for debt dynamics.

Steven Davis remarked that safe government debt provides a convenience yield for many holders of collateral that supports other transactions. He pondered whether we should use the total return, inclusive of the convenience yield, when we evaluate the long-term forces that determine the safe real interest rate. He further posed the question whether convenience yields have risen enough in recent decades to account for much of the decline in pecuniary return on safe government debt.

Austan Goolsbee was struck by the view in Mankiw's presentation that suggests an increase in savings and a lack of investment opportunities as

Brookings Papers on Economic Activity, Spring 2022: 250–252 © 2022 The Brookings Institution.

the cause of low interest rates. He argued that if one takes the view that the savings glut is caused by financial repression in China or other emerging markets, the risk of the saving rate going down and driving the interest rate up seems like a substantial risk worth considering as one scenario related to what will happen to the debt.

Mankiw responded to Davis and confirmed that the convenience yield is indeed left out of the neoclassical model; he indicated that it is not straightforward to calibrate. He agreed with Goolsbee that some of these forces can reverse but noted that the increase in the saving rate is likely the least important of the three—an increasing saving rate, lower growth, and higher markups. On Swagel's presentation, Mankiw said that he appreciated that there were multiple contingencies, multiple paths instead of just one. He was not convinced that figuring out the contingencies by looking at the tails of the *Blue Chip* forecasts is the best approach; instead, he suggested, by running an autoregression one could look at the standard errors and then find the outcome for the 10th percentile, the 20th percentile, and so on, and use those as scenarios. Mankiw concluded that such an approach would likely lead to a vastly more uncertain outlook for the future than the scenarios Swagel presented.

Reinhart argued that the big reserve accumulation of China has had a global impact on the savings glut and the lower interest rates. Reversal scenarios are not implausible and should be considered, for example, declining saving rates as demographic and housing problems in China accentuate. She speculated that the issue of the use of the dollar in sanctions could reduce the appetite for Treasuries over time. Reinhart moved on to address Blanchard's comment, saying that real factors do indeed matter, but she argued that Blanchard grossly underestimates the impact of monetary policy. The peak in real interest rates was in the early 1980s, she noted, following Paul Volcker raising the federal funds rate by almost 600 basis points. The cluster of exceptionally high real interest rates around that time was driven by monetary policy and inflation stabilization, marking the turning point for the secular decline. She asserted that she would not be convinced that monetary policy does not matter.

Blanchard clarified in the virtual conferencing chat that he agreed that central banks can affect the actual rate, something which was certainly the case with Volcker, but he argued that the decline since 1990 reflects a decrease in the real neutral rate.

Swagel noted that, in his comment, he showed two different scenarios, not two different economies, and he added that he and his colleagues will be working on more extreme scenarios in future research. In response to a question in the chat, he clarified that the data he presented were publicly held debt.

Robert Hall emphasized the importance of the point made by Blanchard that when the government buys securities from the Federal Reserve, they are doing two things: funding the operation by borrowing and holding the corresponding securities. He pointed out that it is a matter of shifting between agencies and that there is no financial principle suggesting that it carries any importance beyond that. In addition, the Treasury tends to offset what the Federal Reserve does by switching to longer maturities when quantitative easing is in effect, he continued, revealing a huge coordination failure between the agencies but having no material effect on the capital market. He concluded that we do not need to worry about quantitative easing.

Chris Sims expressed uncertainty about any analysis that focuses on the period between 1980 and the present. He reiterated what Reinhart pointed out: the peak of real rates was in the early 1980s and the rise lasted about as long as the subsequent fall. He argued that it is not clear the rise can be explained by the same factors that some are invoking to understand the subsequent fall in rates.

Mankiw agreed with Reinhart that the period in the early 1980s was related to Paul Volcker's Federal Reserve policy and suggested that the decline up to about 1995 was at least partly related to monetary policy, but he contended that subsequent years were likely driven by real factors. He concluded by noting that what we are facing now—basically thirty-year Treasury inflation-protected securities at zero percent—is probably historically unprecedented.