Research Working Papers

How Optimal Was U.S. Monetary Policy at the Zero Lower Bound?

by: Brent Bundick, Logan Hotz and A. Lee Smith

December 01, 2023

Forward guidance and large-scale asset purchases effectively offset disinflationary effects from the zero lower bound.

RWP 23-14, December 2023

The zero lower bound on nominal interest rates can generate substantial downward pressure on longer-term inflation expectations. We use data on interest rate options and inflation compensation to estimate how the probability that the zero lower bound will bind in the future has weighed on inflation expectations in the United States. Over the 2008-19 period, we estimate that the zero lower bound imparted only a small drag on longer-term inflation expectations of around 10 basis points. We argue that the Federal Reserve's forward guidance and large-scale asset purchases largely offset the potential disinflationary effects of the zero lower bound, even prior to the formal adoption of an average inflation-targeting framework.

JEL classifications: E32, E52

Article Citations

- Bundick, Brent, Logan Hotz, and A. Lee Smith. 2023. “How Optimal Was U.S. Monetary Policy at the Zero Lower Bound?” Federal Reserve Bank of Kansas City, Research Working Paper no. 23-14, December. Available at https://doi.org/10.18651/RWP2023-14

Related Research

- Mertens, Thomas M., and John C. Williams. 2021. "What to Expect from the Lower Bound on Interest Rates: Evidence from Derivatives Prices." American Economic Review, vol. 111, no. 8, pp. 2473-2505.

Authors

Brent Bundick

Sr. Research and Policy Advisor

Brent Bundick is a Senior Research and Policy Advisor in the Economic Research Department of the Federal Reserve Bank of Kansas City. He rejoined the Department in 2014 after completing his Ph.D in Economics from Boston College. Prior to graduate school, Brent worked in the Department as a Research Associate and Assistant Economist. He also holds a M.S. in Mathematics and Statistics from the University of Missouri – Kansas City and a B.A. in Economics and Mathematics from the College of William and Mary. Brent's research interests are macroeconomics, monetary policy, and computational economics.

A. Lee Smith

Senior Vice President

Andrew Lee Smith is a Senior Vice President and Economist at the Federal Reserve Bank of Kansas City. In this role, Lee has oversight of macroeconomic research and serves as an advisor on monetary policy matters.Lee’s research has focused on the effects of expanding and unwinding the Federal Reserve’s balance sheet, the impact of forward guidance on financial markets and the economy, and, more generally, how central bank communication can influence expectations and economic conditions.Prior to joining the Bank in 2014, Lee received a Ph.D. in economics from the University of Kansas. He also holds a B.A. in economics and mathematics from Drury University in Springfield, Missouri.