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ACCEPTED MANUSCRIPT

Short-run Effects of Lower Productivity Growth. A Twist on the Secular Stagnation Hypothesis☆

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1. Introduction

Since 2010, U.S. GDP growth has been anemic, averaging 2.1% a year, and this despite interest rates very close to zero. Historically, one would have expected such low sustained rates to lead to much stronger demand. But this time, they have not.

For a while, one could point to plausible culprits, from a weak financial system to fiscal consolidation. But, as time passed, the financial system strengthened, fiscal consolidation came to an end, and still growth did not pick up.

We believe that this is largely due, not to legacies of the past but to lower optimism about the future, more specifically to downward revisions in forecast potential growth. Put simply, the anticipation of a less bright future is leading to temporarily weaker demand.[1]

If this explanation is correct, it has important implications for policy and for forecasts. It may weaken the case for secular stagnation, as it suggests that the need for very low interest rates may be partly temporary. Put another way, to the extent that investors in financial markets have not taken this undershooting into consideration, the current yield curve may underestimate the strength of future demand, and the need for higher interest rates in the future.[2,3]

Our paper is organized in three sections:

The first section looks at the historical relation between revisions in long-run potential growth forecasts and unexpected movements in consumption and investment. It finds a

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