**Negative Interest Rates Are a Dead End**

They won’t spur growth, but will divert attention from reforms that can.

The Federal Reserve building in Washington, D.C. *PHOTO: GETTY IMAGES*

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The [Bank of Japan](http://quotes.wsj.com/JP/XTKS/8301) recently [announced](http://www.boj.or.jp/en/announcements/release_2016/k160129a.pdf) that it would follow the European Central Bank’s lead and implement a “negative interest rate” policy. Reducing interest rates is supposed to increase spending and investment, spurring growth.

It won’t work. Negative central-bank interest rates will not create growth any more than the Federal Reserve’s near-zero interest rates did in the U.S. And it will divert attention from the structural problems that have plagued growth here, as well as in Europe and Japan, and how these problems can be solved.

Part of the impetus behind a central bank’s negative interest-rate policy is a desire to devalue the currency. With lower market interest rates, holders of euros, for example, may sell them to flee to countries with higher interest rates—driving down the euro’s exchange rate, boosting European exports and growth. But it is impossible for every country in the world to depreciate its currency relative to others. If the European Central Bank hopes to force euro depreciation against the yen and the Bank of Japan hopes to force yen depreciation against the euro, one or both of the central banks will fail.

They might both be successful for a time in depreciating against the dollar, which we are witnessing now. But should the Federal Reserve respond by reversing its December rate increase—or heaven forbid, following Europe and Japan into the abyss of negative rates—then even the depreciation against the dollar will disappear. What will take its place is a damaging currency war that will undermine all three currencies.

Moreover, commercial banks and investors in economies with negative central-bank interest rates will prefer to hold safe debt, such as government bonds, instead of cash deposits. But consider the recent yields on 10-year government bonds in Japan, nine basis points, or in Germany, 32 basis points. Isn’t it amazing that those living in the eurozone cannot find ample capital investment projects with a (risk-adjusted) yield above 0.32% that are worth doing?

The situation in the U.S. is not much different. The interest rate on a 10-year T-bond is a bit below 2%. Can any informed person believe that the cost of borrowing is holding back capital formation in the United States?

Nonresidential investment in the U.S. actually fell in the fourth quarter, and year over year is up by a paltry 2.9%. Central banks are part of the problem, because their monetary-policy gimmicks are promising to citizens and legislators alike what they cannot deliver. Honest central bankers know that policy gimmicks will not deliver growth, but admitting as much is politically verboten.

Where central banks can help is by identifying the structural impediments to growth and recommending a way forward. In the U.S., Congress should force the Federal Reserve to come clean about why growth has been so slow. The forthcoming congressional monetary policy oversight hearings—Feb. 10 for the House Financial Services Committee and Feb. 11 for the Senate Banking Committee—are the right place to explore what is wrong with the U.S. economy.

These committees ought to insist that the Fed, with its large and expert staff, present relevant studies by mid-June, in time for the annual oversight hearings in July. At the July hearings, the Fed can discuss its research. Academic and other experts can offer their analysis of the Fed’s findings. Instead of vague Fed statements about “headwinds,” the nation deserves solid empirical work on the problem.

I recommend two studies. One would examine regulatory constraints on business investment. The second would examine disincentives in U.S. tax law holding back business investment.

There may be other topics worth studying, but it would be a mistake to burden the Fed staff with more than it can reasonably handle. We need high-quality studies, with substantial empirical content. There is nothing unprecedented in congressional committees requesting the Fed to conduct studies and report back to them. As a young Fed staffer, I wrote two such papers on housing in 1972.

It is terribly important that advocates of limited government understand what is at stake. If the U.S. economy stalls—not my best guess, but possible—we will hear desperate demands that the federal government “do something.” The logical response will be calls for a return to near-zero or even negative interest rates, combined with fiscal “stimulus.” Like lower rates, higher spending or tax cuts will do little in the short run to boost growth, but it will dig the federal government into a deeper fiscal hole, further damaging long-run prospects.

It needs to be repeated: Monetary policy today has little to offer to raise growth in the developed world. Central banks, however, have much to offer. Their expert staffs can provide the insights necessary for legislatures around the world to act.