

Nominal Interest Rates Can be Negative

In the text we stated that although *real* interest rates can be negative, *nominal* rates cannot. That is nearly true, but not quite. In January 2012 the German government sold €4 billion of 6-month bills at an interest rate of $-.012\%$. This was the first time that yields on newly issued German government debt had fallen below zero, although German short-term debt had been trading at negative yields in the secondary market for some weeks. Bills for six-month debt had hit a low of minus 0.3 percent shortly after Christmas 2011.

It would not have made sense for most individuals to lend money at a negative interest rate. They would have done better to keep their money under the mattress and earn nothing. But what about large German corporations with millions of euros to invest? No mattress was large enough or safe enough to accommodate their needs. They could have placed the euros in a deposit account with a bank. But in the middle of the Eurozone crisis in 2012, no bank was totally safe. Many corporations were content to pay a small sum in the form of a negative interest rate to have the German government look after their money.

Was there nothing better that corporations could do? Siemens, the electrical engineering giant, had one answer. It used a banking licence, which entitled it to deposit money with the European Central Bank and earn an interest rate of $.25\%$.

Negative nominal interest rates are not wholly unknown in the United States. In December 2008 three-month Treasury bills traded briefly at a negative yield of $-.01\%$. It seems that in this case also investors did not completely trust banks. Anyone investing \$1 million in three-month bills was prepared to pay the government \$25.56 to guard their money.