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Trump has ramped up calls for negative interest rates. Here's what they are and why they matter.

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Reuters / Aly Song

As economic growth around the world slows, central banks are turning to their weapon of choice as a defense: interest-rate cuts.

- **Interest rates have been historically low in the decade since the 2008 financial crisis, which sent a shock through global economies.**
- **Negative interest rates were once touted as a short-term remedy for sputtering growth in regions like Europe, but over the past few years they've shifted toward becoming the norm.**
- **Now, about \$16 trillion worth of the global debt market has negative yields, meaning some investors are becoming so risk averse they're willing to pay to hold bonds.**

- **Here's everything you need to know about negative interest rates, from how they work to why they matter.**
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The global economy is set to dive deeper into the realm of negative interest rates as central banks look for new ways to spur growth amid signs of a looming slowdown.

The issue hit a fever pitch Wednesday morning as President Donald Trump **tweeted** (<https://twitter.com/realDonaldTrump/status/117173569176992972>) that the Federal Reserve should lower interest rates "to ZERO, or less," for the US to refinance its debt.

The tweet puts the onus further on the Fed to lower rates, something most economists already expected the central bank to do — though not to the extreme degree Trump appears to want.

Still, while the US remains far from negative-rate territory, other major economies have already taken the plunge.

Initially expected to be a short-term solution for economies struggling to spark growth and hit inflation targets following the 2008 financial crisis, negative rates are increasingly becoming a staple of monetary-policy tools. For evidence of that, one need not look further than Japan and countries across Europe.

That activity has pushed the global market value of negative-yielding debt to \$16 trillion, according to Bank of America. That means investors have to pay money to hold bonds in more than a quarter of the debt market.

With that established, it must be noted that negative interest rates aren't necessarily a bad thing. What they suggest about the broader economic outlook, however, is **much more concerning** (https://www.businessinsider.com/negative-interest-rates-killing-banks-says-investor-peter-boockvar-2019-9?utm_source=markets&utm_medium=ingest).

Read more: Global central banks are making investors pay to stash their money. An investment chief overseeing \$4.5 billion explains why that would be a disaster for the US. (https://www.businessinsider.com/negative-interest-rates-killing-banks-says-investor-peter-boockvar-2019-9?utm_source=markets&utm_medium=ingest)

Bonds are typically considered safe-haven assets, and investors often shift toward them when they see macro risks on the horizon. If those traders are growing so concerned about the long-term outlook that they're willing to pay to put their money in bonds, it indicates they're not very optimistic about the future.

Here's everything you need to know about negative interest rates, from how they work to why they matter:

How do negative interest rates work?

Interest rates are established by central banks and flow down to commercial banks and other financial institutions. Central banks set a benchmark range for borrowing costs, and commercial banks then take direction from that range to set rates for savings accounts, mortgages, and loans.

Typically, commercial banks will pay account-holders a small interest rate for storing their money with the bank. With negative interest rates, account holders get charged a nominal rate instead, so they lose money by keeping it in the bank.

The idea behind negative interest rates on savings accounts is to encourage people to spend. If savers have to pay for their money to be stored, ideally they'll be more likely to spend it instead.

But negative interest rates don't just affect savers — they also affect how governments issue debt. Central banks around the world have dragged down bond yields by keeping interest rates historically low.

Read more: \$2.9 trillion State Street is sounding the alarm on years of lower market returns. Its deputy investment chief identified where the strongest income could be found in this new world order. (https://www.businessinsider.com/how-to-invest-recommendations-when-returns-are-lower-lori-heinel-2019-9?utm_source=markets&utm_medium=ingest)

Bonds have a negative yield when the total amount of interest an investor receives over the life of the bond is less than the premium they paid for it. Investors who purchase bonds with a negative yield and hold them to maturity end up losing money on their investment.

In the event that they need a safe place to park their capital when other investment vehicles — like stocks — become too volatile, they become more willing to do so.

Where did negative rates come from?

The European Central Bank cut rates below zero for the first time in 2014 in response to the region's dire debt crisis and dangerously low inflation following the 2008 financial crisis. Several countries across Europe, including Sweden, Denmark, and Switzerland, followed in the ECB's footsteps and lowered rates below zero shortly after.

The Bank of Japan adopted negative rates in 2016, setting short-term borrowing costs at -0.10% and buying huge amounts of government bonds in the open market to lower long-term yields. The process of a central bank buying long-term bonds is known as quantitative easing, and it often puts downward pressure on bond yields.

Negative rates at the time were seen as short-term jolts to struggling economies, but the phenomenon has slowly evolved into something analysts and investors are prepared to grapple with for the long term.

What are some examples of countries with negative rates?

Five central banks have interest rates set below zero:

- **Japan:** -0.10%
- **Sweden:** -0.30%
- **European Central Bank:** -0.40%
- **Denmark:** -0.70%
- **Switzerland:** -0.80%

While Germany doesn't have negative rates, it recently issued the world's first 30-year, zero-coupon bond last week. The auction flopped, selling less than half the amount that was issued and signaling the negative yields across Europe could finally be dragging down demand.

The ECB is expected to roll out a large stimulus package in the coming months that includes a bond-repurchase program and further cuts to its already-negative rate.

Are negative rates bad?

Negative interest rates aren't necessarily a bad thing. Taken at face value, it seems strange that a saver could actually lose money by storing it in a bank or that an investor might have to pay to hold a bond.

What's more concerning is what negative interest rates signal. The idea that some investors have become so risk averse that they're willing to pay money to store capital in a safe-haven investment like a bond suggests a bleak outlook for the global economy.

Read more: 'Abrupt and severe market losses': One expert explains why stocks are on pace to underperform the safest government bonds for the next 20 years
(https://www.businessinsider.com/next-stock-market-crash-equities-lag-treasurys-for-20-years-2019-9?utm_source=markets&utm_medium=ingest)

There's also the worry that countries with negative rates have less flexibility to respond to an economic downturn with monetary stimulus. Central banks usually look to cut rates to jump-start growth in the economy, as lower rates will encourage savers to spend. If rates are already low, and in some cases negative, then central banks might have less or no flexibility at all to help fend off a recession.

According to Bank of America, investors can still make money on negative-yielding bonds. While negative-yielding bonds typically pay very low or zero in coupon payments, investors can still make money by selling

them before they mature. Bond prices rise when yields fall, so even if negative yields continue to drop, the bond's price will appreciate.

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