

# Policy Regimes versus Economic Regimes

## Binary classifications can be too simplistic

It is tempting to think of regimes like flipping a switch from on to off. We give regimes names like recession, fiscal discipline, or zero interest rate policy (ZIRP), and we look for signposts marking each period’s beginning and end.

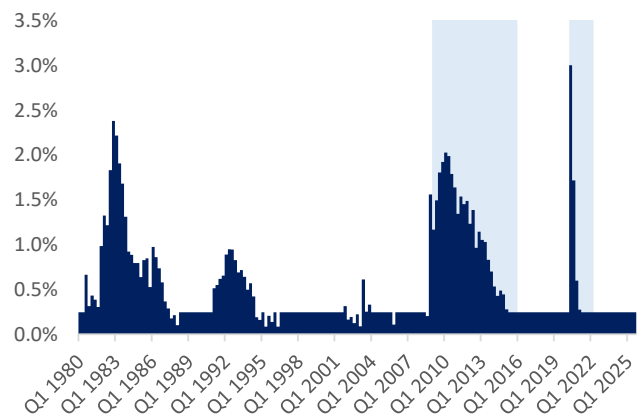
While this type of crisp categorization is helpful for narratives, it can be difficult for analysis. Even something as simple as identifying “inflationary” periods requires setting a threshold and splitting events into being completely inflationary or not. These binary choices are forced and potentially misleading. Adding more categories does not

solve the problem, because forcing history into 3 or 4 buckets forces the same borderline calls.

What if we reframe the problem? Instead of asking which regime we are in, we measure the degree to which each historical experience resembles the current environment (or any environment of interest). We use a statistic called relevance to capture this degree of “regimeness” quantitatively. For example, if we characterize the US economy by its average characteristics in the ZIRP policy regimes of recent decades, we find that even though ZIRP as a policy was not active previously, there are still economically related episodes further back. Moreover, the periods that align with these prototypical ZIRP circumstances are the beginnings of crisis recovery as opposed to the ends.

Beyond just building intuition, we use these precise relevance weights to create regime-specific forecasts of expected returns, risk, and correlations across major asset classes, and we build portfolios optimized for ZIRP and non-ZIRP periods. Interestingly, embracing this ambiguity actually leads to clear portfolio conclusions. Credit risk shines more in ZIRP periods, pushing allocations towards Treasuries over corporates as we move into higher rate environments. Commodities also become more compelling, offering both higher expected returns and better diversification than in ZIRP times. The bigger takeaway, though, is that mapping policy dictates to their many historical echoes can be helpful.

**Exhibit 1: Zero interest rate “regimeness”**



Source: State Street Markets. Chart shows the relevance of historical periods to typical zero interest rate policy (ZIRP) economic conditions (dark bars) versus strict ZIRP definitions (light shading).


For more on this topic, see our 2026 journal paper: “**Policy Regimes versus Economic Regimes: Implications for Portfolio Construction**” by Mark Kritzman and David Turkington, The Journal of Portfolio Management, Vol. 52, No. 7, May 2026

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