Fed Unfiltered, Transcript
2/10/22 – Tom Barkin, Interview: Stanford Institute for Economic Policy Research

Mark Duggan:

Hello everyone, and welcome to today's event featuring Tom Barkin, sorry for one sec, President and CEO of the Federal Reserve Bank of Richmond. I'm Mark Duggan, the Trione Director of the Stanford Institute for Economic Policy Research, and I'm grateful that so many of you are able to join us here today online.

Mark Duggan:

We're only six weeks into 2022 and we're already making some impressive strides here at SIEPR in the new year. Our affiliated scholars have been producing a tremendous amount of policy relevant research, writing policy briefs, and placing op-eds on a wide range of issues, including working from home, COVID's impact on the economic gains made by Black Americans, the Biden Administrations move to curtail hidden junk fees, and ways in which Medicare can go about saving lots of money in the payments that it makes to the nursing home industry. And in exactly three weeks from today we'll be kicking off this year's SIEPR Economic Summit, that will feature US Treasury Secretary Janet Yellen, US Commerce Secretary Gina Raimondo, and an impressive slate of many more policymakers, business leaders, and academics. You can get more details about the summit, and learn more about our research, on our website at SIEPR.stanford.edu.

Mark Duggan:

Today I'm thrilled to have Tom Barkin with us, and we couldn't have him at a better time. For me personally the timing is perfect since in my econ one class we are right now switching from micro to macro, so I'll be taking careful notes during today's event to use in the upcoming few weeks in my class. But at a more systematic level, there's a great deal of uncertainty and expectation now with regard to the labor market, inflation, the feds potential moves in the coming months to potentially raise interest rates, and the overall health and direction of the US and global economy. Tom is going to start things off with a presentation that will touch on these issues, and then we'll move into a Q&A where we'll be able to take your questions, and you can submit them through the link that should be appearing now on your screens.

Mark Duggan:

Before we get started, I'm truly honored to introduce Tom Barkin and welcome him to SIEPR. He's been leading the Richmond Fed since 2018, where he's responsible for an area that covers the Carolinas, Virginia, Washington DC, West Virginia, and my old stomping grounds, Maryland. In the simplest sense, the bank is charged with fostering strong economic growth and stability in the region. Of course doing that requires some complex policy decisions that Tom will discuss with us today. Tom also serves on the Federal Open Market Committee and is responsible for bank supervision and the Fed's technology organization.

Mark Duggan:

Before he came to the Richmond Fed, Tom was a senior partner and CFO at McKinsey & Company, a worldwide management consulting firm that I'm guessing many of you have heard of, where he also oversaw McKinsey's offices in the southern United States. Tom earned his bachelor's degree, his MBA, and his law degree from Harvard, and despite being trained exclusively at one of our biggest east coast rivals, we are incredibly happy to host him today at this Stanford event. So with that, please join me in offering up a warm welcome to Tom Barkin to SIEPR, and Tom, take it away.

Tom Barkin:

Thanks so much, Mark, and thanks everybody for joining. I wish I could be there with you in person, but when this pivoted it's at least good to see your names and hopefully eventually faces of so many friends I have here on this conversation. So as I was prepping this talk I was in my library, and I saw a book that was written by Robert Rubin when he retired from government service. It's his memoirs titled In An Uncertain World, and it just seemed to me like that was a pretty good title for this talk, because the Fed is very much in the news these days, and I thought it might be timely to speak about forecasting and policy in the uncertain world we are all experiencing during this pandemic. These are my views, not that of anybody else in the FOMC, and that frees me up to be as direct as I want to be.

Tom Barkin:

Now you might rightly say that the world is always uncertain, after all Rubin wrote his book in 2003, after 9/11, after the internet bubble, after multiple developing country debt crises, things hardly seem stable then. But I think it's worth, when we think about the economy today, remembering that this pandemic came after an extraordinary decade of extremely low economic volatility by historic standards. The recovery in the 2010s was record length, GDP grew in every year of the decade averaging a little over 2%. Monthly job gains averaged 195,000 a month over the nine years before the pandemic, they were negative in only one year during that time, only one month during that time period. Core PC inflation on a 12 month basis moved in the extremely narrow range of 1.1% to 2.1%. The Dow Jones moved steadily up from a little over 10,000 in January 2010 to 28,000 at the end of the decade.

Tom Barkin:

In that context of economic stability, the Fed did a monetary policy review in 2020. It asked a bunch of questions that seemed relevant for the times, was employment at our maximum at 3.5% unemployment, or could a lengthier upturn move participation and therefore employment even further? Would less preemptive monetary policy nudge inflation, which was then hovering in the 1.8% range, back up to our 2% target? Was the Phillips curve, which describes a trade off between unemployment and inflation, less responsive than we had previously believed?

Tom Barkin:

Well, those days of stability now look as far back in the distance as the Clinton Administration. We've been living through a massive shock. COVID has risen and fallen and risen and fallen and risen and now is falling again. Over 6 trillion of fiscal stimulus has been injected in multiple waves. Demand has shifted from services to goods. Supply chains have broken. Fewer people are working. Employers can't fill jobs. Inflation has spiked to levels not seen for 40 years now.

Tom Barkin:

Now, I'm not complaining, but making policy in that context hasn't been easy. As a reminder, our tools take some time to have impact, so we set policy based on our forecast of where the economy is headed. Pre-pandemic you wouldn't have been far off if you had said, jobs will grow about 150 to 200,000 a month, inflation will be just under 2%, and so we should set policy rates to be just a little bit under neutral to allow inflation to rise to our target. But the last two years have been completely novel, they've challenged our forecasting, our tools, and our policy stance. And I thought it might just be interesting to go through maybe some of the key dates of the last two years.

Tom Barkin:

In March 2020, of course, the virus hit, communities shut down. The Fed foresaw the coming recession and move quickly to take rates to zero in two unscheduled meetings, and we began significant asset purchases in an effort to calm financial markets. The country closed and then reopen, 3 trillion in fiscal stimulus, hit with force, but in September 2020 COVID had spiked again. With core inflation having fallen to 1.6%, and about 11 million fewer jobs, we committed to keep rates at zero until inflation moved over 2% for some time, and we reached maximum employment. We were still at that time forecasting coming to 2% inflation from below.

Tom Barkin:

Now December 2020 was in the midst of last winter's COVID spike. Core inflation was still 1.6%, we now had 10 million fewer jobs, and we committed to continue our asset purchases until we saw substantial further progress against our mandated goals of unemployment and inflation. It's actually hard to believe just 14 months later, but I think it's helpful to remember we were at that time nowhere near either of those goals.

Tom Barkin:

In spring 2021, vaccinations had proven effective and were being successfully rolled out. Congress passed 1.9 trillion in stimulus in March, on top of 900 billion in December. Consumers were freed from isolation, and funded by stimulus and excess savings, and they spent with abandoned. Supply chains struggled to catch up, employers couldn't find workers. Inflation started its increase, but most of the escalation was in a few categories that we saw as temporary, like automobiles, which were short of chips, and travel, which was returning to normal. So we stayed the course.

Tom Barkin:

Frankly I thought, and maybe you did too, that the economy still had a lot of slack last March. I thought that this past fall, when schools reopened, and enhanced unemployment insurance expired, the workforce would return to normal, and many inflationary pressures would ease. But in the context of the Delta variant, neither happen. So in our November meeting, with labor markets still quite tight, and inflation well over our target, we began the process of normalization by tapering our asset purchases. In our December meeting, we accelerated tapering, and projected we would begin raising rates this year. We last met two weeks ago.

Tom Barkin:

So where are we today? We're 20 months into the fastest recovery in any of our memories. The economy is today well above pre-pandemic levels, and will likely return past the pre-COVID trend line this quarter. Underlying demand looks to remain robust, fueled by healthy personal and business balance sheets, and the need to replenish low inventories. Labor markets are tight, unemployment has dropped to the historically low level of 4%, even though there's still about 3 million fewer people employed than before the pandemic. Wages are up, inflation is elevated with core PCE inflation at 4.9%, in recent readings, like today's CPI, showing inflation both broadening and more persistent.

Tom Barkin:

Omicron has pressured workforces and threatened supply chains in ways that likely increased labor market and inflationary pressure. One number I saw that I just think is fascinating is the Census Household Pulse Survey. In mid-January it reported that 12 million workers were home with COVID because of fear of COVID, or having COVID, or taking care of someone with COVID, or being quarantined because they'd been exposed to COVID. During the holidays we learned people still wanted to fly, we just didn't have enough flight crews.

Tom Barkin:

Now forecasting looks like it's going to continue to be a challenge. The path and impact of future COVID variants isn't known, nor is their effect on global supply chains, like China's. Ukraine presents political uncertainty for sure, but imagine for a second a Russian energy or cyber response. Further congressional stimulus is still being discussed, consumer sentiment is weak at a time when consumer spending is strong, markets have been volatile. There's a lot of noise on inflation, yet TIPS indicators on inflation compensation appear largely unaffected.

Tom Barkin:

So it's actually quite hard to know if we're going to return to the relatively stable and healthy world of the 2010s or not. I asked myself two questions, first, is labor force participation going to rise to the above trend levels we saw in the last upturn, or was that the aberration? Now without meaningful additions to the workforce in this time of low immigration and declining demographics, we're likely to see ongoing wage pressures, which in turn would be inflationary. So will absenteeism decline as COVID fears subside? Will parents come back to work when schools and childcare stabilize? Will retirees rejoin the workforce?

Tom Barkin:

Second, and I think related, once current inflation pressures ease, will we return to core PC levels of around 1.9% like the last 30 years, 3.2% like the last two years, or 5.4% like the last nine months? Now I expect that elevated goods prices are going to ease as supply chains are repaired, which means we're going to see months over the next year where inflation looks quite muted. But I'm watching service prices closely as they're quite vulnerable to wage pressures, which make up a big percentage of the cost structure, and as I said, wage pressures look like they're going to be ongoing. And it's of course hard to know what impact this whole inflationary episode's going to have on people's expectations for inflation going forward.

Tom Barkin:

Now the uncertainty on both questions means the word of the day needs to be humility. Probably that should be the word every day in the policy arena given the forecasting challenges I discussed. A classic Fed dove might be optimistic, forecast to return to the 2010s, and move slowly on rates to ensure inflation doesn't slip back below our target. A classic Fed hawk might fear a wage price spiral and raise rates well above neutral levels to control inflation. Either one of these views could be right, but it's hard to know who.

Tom Barkin:

You saw in our last meeting we said the time to raise rates is coming soon. We also published our principles for reducing the balance sheet back to our normal levels. Liftoff doesn't take rates to levels that constrain the economy for some time, it just gets us better positioned if the answers to my question suggests we will need to. I see both the rate and the balance sheet announcements as signaling that the worst of the pandemic's passed, the economy's growing strongly, and we can start to put our monetary policy stimulus tools away, without yet needing to take any lean toward or against restrain. I hope we can get rates back to pre-pandemic levels relatively quickly, and when we do, policy will then be ready in whatever way is required in an uncertain world, that seems to me like the best path forward.

Tom Barkin:

So with that, Mark, I'll take any questions you got.

Mark Duggan:

Terrific, and we've already got some good questions coming in, feel free, if you have questions, to send them in. I'm going to start with some of my own, then pull some from the audience, and alternate a bit. So as you think about, I know none of us have a crystal ball, but as you look ahead, and I don't know, when the pandemic ends, I hesitate to use that language having seen the various waves, but if we get to a place where COVID is to a large extent behind us, or at least more contained then we currently feel like it is, do you think we're going to get back to a healthy labor supply, or do you think that we're going to be permanently below this, and just, do you anticipate an end to the labor shortage anytime soon? I'm hoping that my daughter's school, for example, will have bus drivers next year, because tons of parents are driving their kids to school every day because there are no bus drivers. Anyway, so maybe you can answer this.

Tom Barkin:

I think it's a really interesting way to ask the question because first of all, the human capacity to declare COVID over in your minds is amazing. I mean, we've all got it over in our minds right now, even though the case counts are higher than they were in many places last winter. But we've been placing, I'd say collectively, as an economy, a bet over the last year, year and a half, that it would be behind us, and when it is behind us you'd see people come back to the workforce, as I described. At this point though, since March, labor force participation's been basically flat. And so at some point you have to say, wow, I'm a little nervous about whether it's going to happen.

Tom Barkin:

Of course I believe if we truly have COVID behind us that some retirees who are out of the workforce because they're worried about their health will return, that some parents who don't have stable childcare situations, or school situations, will feel more comfortable getting back to the workforce, absolutely. And of course the people, the 12 million I talked about, even who are absentee at home with COVID will feel more comfortable being there. So I believe there is upside to the workforce, you just can't find it in the numbers yet.

Tom Barkin:

There's a good paper in Jackson Hole this year that says labor force participation always lags, unemployment comes down first, and then as people get more confidence in the job market they're willing to come in, so I think we'll see some of that, but I suspect it's going to be slow going, and that will have implications, because I think for the last 30 years we've been living in a world where we were long labor, not short labor, and that gave employers power to, and that was driven by baby boom generation working, women participating in the workforce at higher levels, access to offshoring and outsourced labor, people being healthier and working longer, and that freed employers up to manage wages and salaries, but also reduce pensions, maybe reduce union bargaining, all those things happened.

Tom Barkin:

And there's been predictions for years that that was going to turn, and the demographic numbers would make it look like it's going to turn, but until this pandemic it really didn't turn. And so then the question is, are we now back to the trend line that people have been predicting and going forward labor's going to be short? And I have an instinct that is where we're headed, that it's going to be shorter, and it's going to require folks to invest in working conditions, and productivity, and automation, and by getting people off the sidelines and into the labor force you might not otherwise be in, intensifying search efforts, and a bunch of those things.

Mark Duggan:

I guess policy, this might be more in the fiscal policy arena, but policy could play a role improving incentives to work in various ways as well. Okay, so let me ask you a bit about supply chain challenges, which have caused headaches for businesses all across the country. Do you anticipate businesses, and for that matter households, shifting strategies in the long term as a response? We're going to have a session on this at the summit in a few weeks, just also just get your sense of what's driving. I know it's very complicated, there's no one thing that you can point the finger at, but yeah, are businesses going to shift strategies, and what do you see as the most likely culprits to this? And I know we don't everything yet.

Tom Barkin:

Well, it is amazing, and certainly I was stunned at the amount of supply chain dislocation. Every executive I talked to almost describes it as Whac-A-Mole, you think you've solved one problem and another one comes along. And I think, I go back to how stable the prior 10 years were, and with the exception of the great recession, maybe the prior 30 years. But I think businesses were geared for a much smaller range of potential demand than in fact hit us. When demand shifted from services to goods, when stimulus and excess savings hit and propelled demand, goods demand in this country went up in the high teens, and the supply chains just weren't ready to manage that, partly because they were closed at the beginning and they just could never catch up. And so that's been a continuing issue, and it feels to me is going to take the greater part of this year, still, to catch up to it. So that's, in my mind, what happened.

Tom Barkin:

When you talk to businesses, I do think resilience has become a conversation that's much more significant than it was two years ago, and frankly four years ago, because I think a lot of this started with the whole tariff situation with Japan, where we found businesses, I'm sorry with China, we found businesses overexposed in their mind to a supply base that was getting tariffed. Then you come with the pandemic and you start to say, boy, any one country feels like a lot of risk to take. Wait a second, shipping supply chains, that feels like a lot of risk to take. Wait a second, just in time inventory, that feels like a lot of risk to take. And so I'm talking to a lot of people who are rethinking it.

Tom Barkin:

Now I don't really smell yet that the way they're rethinking it is bringing a lot of manufacturing on shore, which is what a lot of people ask, and I think the number one issue there is just they can't find workers. So it's hard to open a new plan if you don't have confidence you've got a workforce. But you hear a lot about nearshoring, you hear a lot about different inventory models, and different logistics models, so I think those are very much going to be in play.

Mark Duggan:

Sorry, great, thanks so much. So we're now coming up, I guess we're about a month out from being at basically two years of working remote, obviously not for all occupations, but for quite a few, millions and millions and millions of workers in the US, some have been working remote straight for two years, others to a large extent remote. And I'll just say, I have a friend recently who was lamenting that people weren't going into the office even though they could start going back to the office, and then I said, "Oh okay, well are you going in?" And they said, "Well no," and I said, "Well, why not?" And they said, "Well, because no one else is going into the office." So there is a little bit of a coordination, and they also made the point, "Well, also my commute now is 30 seconds as opposed to 30 minutes."

Mark Duggan:

And so I think that, I don't know what your sense is, is this remote work being here to stay? And I think people have mixed feelings about it because they've gotten used to this easy commute, no commute kind of thing, but on the other hand they're not getting the chance to network with their colleagues, and I think it's especially hard for newer workers. So I don't know, we have actually in our lineup of speakers Nick Bloom, who's done a lot of work on the productivity effects of working remotely, really great work. But yeah, I'm just curious to hear your take on how you think, and using also your McKinsey hat, because you were in [inaudible 00:21:38] companies all the time.

Tom Barkin:

I mean I've lived, in my former world, and even in my current world, in a hybrid world for my entire career. I've been in my office one or two days a week, I've never been in my office five days a week ever, and I think you can get a lot done that way. At the same time, if you're never in the office, I believe there are all of the issues that people talk about, collaboration, culture building, values inspection, mentoring, sponsorship, that just doesn't work the same way remotely. I think there are a lot of people, a lot of companies, who just believe passionately everyone needs to be back in the office, there are a lot of individuals who believe passionately they get everything done well at home. I just don't think the market has had a vote yet. I mean I'll just speak for our shop, we're still not back in the office, we will be soon, and I think the market's going to have a vote.

Tom Barkin:

From the company side, I don't know, there's some law firm somewhere that's going to insist that everyone come to the office, there's another law firm of the same size with the same capabilities that's going to say it's okay for everyone to work at home, they're going to attract different talent, this one might invest in culture building and collaboration and feel like they've got an advantage, this one may not have a lot of real estate expense and might be more attractive to a certain generation of talent, and they're going to go out in the market, they're going to compete. And I don't know who's going to win, but I'm pretty confident five years from now it'll be obvious that one of these models is better, if it is in fact better. They're going to compete it out.

Tom Barkin:

Same thing with talent. I've got two kids who are in the workforce and I tell them, "You want to go to the office, because you want to get noticed and you want to build relationships, you want to build a network." But there's going to be a bunch of talent that works from their home in a very nice location, there's another talent that's in the office every day, and they're going to have two different experiences, and we'll see where it falls out. So I just think the market hasn't really spoken, and I think all the people who think the way to go is flexible haven't really thought fully about career building, and all the employers that say, no, we're going to bring everyone back, haven't really thought about talent. I think there's some answer in the middle.

Tom Barkin:

I should add one more thing, hybrid isn't actually a good experience yet. Now I believe technology can make it that, but I assume you've tried, like I've tried, to have a meeting with four people in person and four people on the video, it's not a good experience. Maybe that's an innovation idea.

Mark Duggan:

Yeah, I agree with that. I think the slight challenge is, I feel like everyone has a different view on this. Some people wanted to be back to the office the instant that the office opened back up, other people would feel comfortable if there were fewer people going in, because then their risks are lower. Still other people would feel good about going in if there are a lot of people, because then... So it's just I think people are coming at this from a lot of different directions, so it'll be interesting to see, like you said, how it shakes out. So I have a bunch of questions but I'm going to interrupt my questions for a second because I have a question from your college roommate, who you know who that is.

Tom Barkin:

Okay, mutually assured destruction, let's go.

Mark Duggan:

Your college roommate is asking, "What is your outlook for US productivity improvement, and how did the pandemic affect that outlook?"

Tom Barkin:

Lenny, thank you, that's Lenny, presumably, and Lenny, that's much nicer than you normally are. So the productivity thing's really interesting. US in the 90s, 2.5% a year, but then around the first decade in the 2000s it dropped to about 1% a year, and for the 15 years after that productivity was 1%, which just isn't a very good number if you want to grow the economy. And all papers were written and theories were that it's all gone, and when I joined the Fed in 2018, again, having spent 30 years in McKinsey, I was shocked by that, because I knew in my heart that every day I woke up and helped companies become more productive, and I saw American businesses working night and day to become more productive, so I couldn't quite get my mind around why you weren't seeing the productivity.

Tom Barkin:

I will say over the last four years you've seen a big tick up, and at what point do you declare a trend isn't clear? But it was about 1.5% in '18 and '19, it was about 2.5% in '20 and 2% in '21, and those may not seem like big numbers versus 1%, but actually on the scale of the economy it's a huge number. And I think there's a lot more there, and if you buy what I'm saying, which is that demographics are taking us in a place where labor is going to be tight, then I think the incentive to invest is going to be high, and maybe you get the most out of it when you've got the most need to get the most out of it, so I'm pretty bullish on productivity.

Mark Duggan:

That's good. I do want to throw out that, on the productivity point, it's getting harder and harder to measure it as we get more and more services. So my main area of research is the healthcare sector, 18% of GDP, 2.5 times bigger than manufacturing, it's pretty hard to measure productivity in the healthcare sector, just as things go. But it's, yeah, I think to the extent that that is just a persistent factor, then the changes that we're seeing I think do reflect real changes in the economy.

Mark Duggan:

So let me, a lot of jobs where employers can't find... A lot of jobs that are out there have some, let's say, special training and technical skills, and employers can't find these workers. How do you think these jobs are going to be filled going forward? Do you think that higher ed should be more proactive in this space? Or do you think that corporations are going to do more general skills training for potential workers? Because there does seem to be a little bit of a gap, or mismatch in terms of the skills and the needs, at least in some sectors.

Tom Barkin:

Well, I'm going to pause, I'm going to hit exactly on what you said, but I divide the labor market these days into three different types of segments, one which may be what you're talking about is skilled trades, carpenters, plumbers, welders, but truck drivers I'd put in there, nurses I'd put in there, certain types of teachers. They have to go through a program, they have to get certified, many of those certification programs or community college intensive, and that segment was tight before COVID, and now it's massively tight. Demand has spiked in those professions, we're not producing anymore.

Tom Barkin:

Community college enrollment is actually down significantly in this country, presumably because as entry level pay increases a bunch of people are making choices, rather than go invest in their future they're taking advantage of the situation now, but we are not producing the numbers in those segments that we need. Now that's an addressable problem, it's about expanding manufacturing capacity of those people, but I think it's doable, we just got to invest in doing it. And I hear all kinds of issues of constraints on clinical placements or licensing, or spots in programs, and I think we've got to do a very aggressive job there.

Tom Barkin:

The second place, as I'll call it, lower income service workers. Those were always the last people in the economy, and four or five million of them have left the lower income service worker space, maybe they're working at an Amazon warehouse, or maybe they're home with their kids. But that's not a skills issue in the way we classically think about it, but is absolutely soft skills, getting into the workforce, pass a drug to, and so there's another set of issues around getting people in off the sidelines, getting them prepared and ready and interested and excited about work, and all that, that's a second set of skills.

Tom Barkin:

And then you might be talking about in the professional class, which has been in more balance, you absolutely have skilled categories, cloud engineers, cyber professionals, artificial intelligence, where they're incredibly tight, but I think we can know how to manufacture more of that, that's just an education, we've got lots of people who could do it, it's just a question of opening those professions. So that's how I'd segment it, depending on which set you are.

Mark Duggan:

Yeah, no, that's super helpful. So I'm going to pull a few questions, I've got tons of questions, I've got so many questions come in from the audience I want to be able to hit more than usual. So one is, is the Fed still following its flexible average inflation targeting strategy?

Tom Barkin:

Well, we have been following it, it's why we put forward the forward guidance that we put earlier, it's why we've kept rates as low as we have. We're going to go through the process, as Jay said his last press conference, of steadily moving rates up, I'm hoping toward neutral, and then we'll see where inflation lands at that point. But the objective of 2% over time is absolutely still the objective, and I hope we'll get back there. I'll say more to that, I hope to get back there, and we have the tools to get us back there.

Mark Duggan:

Terrific. Okay, another question. So have the wage gains and the increased costs that we're seeing changed the percentage of GDP going to labor and to corporate profits, do you think?

Tom Barkin:

It's a little early to land that, because there's a lag effect between wages going into prices and then prices going into wages, and all the rest of it. My impression is if you looked at 2021 you would see very significant wage gains, you will see that, that numbers already in there, but you'll also see, at least in the large corporate segment, pretty significant profit gains. And so I think the numbers I've seen show a modest tick up in the share going to labor, but there's also a pretty significant share going to profit, so I think it's a little early to declare victory on that.

Mark Duggan:

Okay, great. So there's obviously a meeting coming up next month, and there could be a decision about interest rates. I have a number of questions about the March FOMC meeting, so I'll just say March FOMC meeting, your thoughts on what will happen there. I'm just trying to aggregate and be respectful of your-

Tom Barkin:

No, I got it, I got it. So we had a meeting in January, the memo came out, Jay did a press conference afterwards. I think he was pretty clear that the time to begin raising rates is soon, that we'll be raising rates steadily toward neutral, and that we make those decisions on timing and size and scope as we got the data. And so we're now two weeks into a seven week period, so we've got a bunch more data to get before March, but data, we'll get a PCE, we'll get another CPI, we'll get a labor report, and so we'll see where we get by the time we get to March.

Tom Barkin:

But as I said in my talk, I do think it's time to start normalizing policy, I do think the extreme pandemic episode, even if we have waves of this coming back, is now much more clearly, in my mind, in the rear view mirror. I think we are at at least an interim level of maximum employment, and inflation is well over our target. So I'm certainly supportive of beginning what Jay said, the steady process of normalizing.

Mark Duggan:

Great, sorry for that, I just was having trouble unmuting. Okay, so this is a question about thinking ahead, not just to the March meeting, but going forward later in the year. So apparently St. Louis President James Bullard said today he supports raising rates by a full percentage point by the start of July in response to the hottest inflation in four decades. I mean, maybe it's just hard to think that far ahead, because we're going to get lots more data, but where do you see on that, and how do you see rates evolving in the meetings through July?

Tom Barkin:

I mean, I think you've answered the question, which is we'll see how the data comes out. We have a new president in Boston and someone quoted something that she allegedly said which I really liked which was, "You can't be both data dependent and entirely predictable, those two things don't actually go together, you have to see where the data takes us." But where I am I think of... Well, I think about this more as a bigger picture conversation.

Tom Barkin:

I think I would like a year from now, when we are, I think, in a much better situation to look at what a post-COVID level of inflation pressure looks like, what a post-COVID labor force participation situation looks like, I'd like to be in the position to move if we need to move. If inflation doesn't settle to where it might settle and settles well above our target, I'd like to be in a position to move, and that means getting back to where rates were before the pandemic. So over the next year or so that's where I'd like to move. What pace, what movement at each time, I think that's very much for the decision in a meeting, and there's certainly enough uncertainty, as I talked about, in the mega environment that you could imagine things that would make you move slower and things that would make you move faster. So I think about that.

Tom Barkin:

I'll also just make the point that the way our tools work is we don't have that much impact on inflation today. If we move rates a little bit here, a little bit there today, inflation today is being driven heavily by cost pressure, supply chain pressures, those types of things. What we do do is we change expectations on the future. The fact that the Fed, that moves over the medium and long term, so that's why I try to think out, as opposed to think today, so I'm a lot more focused on where we're headed than any particular choice at the next meeting or two.

Mark Duggan:

Great, okay. So we had talked a little bit before this meeting, and we're going to Zoom back in on national level issues, but as you obviously know there are 12 Fed bank presidents, 12 regions in the US, Stanford is located in the region for the San Francisco Fed, but you cover Virginia, Maryland, the Carolinas, West Virginia, Washington DC, and so forth. Can you just talk a little bit about just the industrial structure in your region, and how that influences your day to day relative to your 11 counterparts at the other Feds?

Tom Barkin:

So you described our district well. The way I think about it is we have Washington DC and suburbs, that's a pretty unique market in this country, and of course it's heavily government, government contractors and defense contractors, and the like, that's one big swath of our economy. We have Baltimore, which is actually an older industrial city that has its own unique set of situations. But if you took the entire rest of our district I'd split it into two segments, one is, I'll call them thriving new south cities. You would put Richmond in there, you'd put Charlotte in there, you'd put Raleigh in there, you'd put Charleston in there, Greenville, Spartanburg, Columbia, Asheville, they're very strong business climates, people are moving there, they're exciting place to be. They're big in the growing, they have their set of issues, but that's a common set of markets.

Tom Barkin:

And then you've got a bunch of really small towns, and West Virginia is full of those small towns, but if you took the big, thriving, new south cities out of North and South Carolina and Virginia, you'd have a lot of small towns that look not that much different than the eastern shore of Maryland, or West Virginia, or western Maryland. And so that's a whole nother segment, and we've put in, our bank actually, a lot of work into this situation in these small towns, because their economic performance lags the performance of the bigger cities by 10 or 12 points, I'm thinking now in labor force participation, employment to population, but you could look at it in many different ways. The health is less good, the income's less good, the growth is less good.

Tom Barkin:

And I think there's a lot that needs to be... Sorry, that was a call that came in, there's a lot that needs to be thought about in terms of how we enable those places to grow, for example, there's a ton of money in the most recent stimulus program that's targeted at smaller towns, and one of the challenges is getting the money deployed, because there aren't actually, in many of these places, entities that have got the capability, the track record, that the government entities require to deploy money. And so we are trying to think through, what are the things that are actually hitting these small towns and how's that different? So hopefully that gets you a bit of a feel for our district.

Mark Duggan:

Yeah, that's super helpful. As I said, I lived there for eight years, so I'm very familiar with it, and yeah, big fan of the area. But government looms larger there, the federal government looms larger in your district than it does out here.

Tom Barkin:

For sure.

Mark Duggan:

For sure, yeah. Okay, so the next question that I want to ask, I'm tweaking a little bit a question from one of our attendees, has to do with the monetary stimulus that's been put in place during the past couple of years. There's been a lot of debate in the media and among academic economists about, did we get the Goldilocks just right amount of fiscal stimulus? Did we do unemployment insurance just the right way, state and local fiscal support, tax cuts, one time checks to people, lots of different methods of fiscal stimulus, there been considerably less about the monetary stimulus, which was also quite significant. We actually have a session in a few weeks at the summit looking mainly, I think, my guess is, given the speakers, we're going to talk mainly about the fiscal side, perhaps you can just help us think through a little bit how you think about the stimulus by the monetary policy stimulus, which is not trivial over the last two years, and its effect, and what effect it's had on the real economy.

Tom Barkin:

Well, I guess I'd start with March of 2020, as I said before, I think taking rates to zero and making significant asset purchases in the context of some very real issue in government funding markets, I think was absolutely critical and provided a ton of value in terms of starting the process of getting to the other side. I also think we're equipped by our tools and our mandate to move relatively quickly, and I think the fact that we moved as quickly and as decisively as we did sent a pretty strong signal that I think was a good leading edge thought for the fiscal players to say, okay, this is big and we've got to do something about it. So that I feel good about, and also the impact we had.

Tom Barkin:

As I suggested, you could go then through to February of 2021, and say you've got very strong asset purchases, very low rates, that seems to be stimulating the economy you would want to, whenever you do policy the future's a little uncertain. So you're working against an uncertain set of outcomes. And I think if I knew now, if I knew then what I knew now, I'd be making different judgements, as I suggested, about the slack in the labor force last summer, just for one good example, the breadth of inflation right now, for another example. But you don't really know that. I do think, like fiscal, it's provided a lot of stimulus. Like fiscal, if you had 2020 hindsight right now I think you'd do it a little bit differently and you'd probably target it at those markets that it turns out needed it more, versus the other way around.

Mark Duggan:

So this is a question from an audience member, it may make a little more sense to you than it does to me, I'm a micro economist, not a macro person, but what would be the implications of the Fed raising rates at every meeting, as they did prior to 2000, as opposed to every quarter? Do they need the flexibility?

Tom Barkin:

Well, I think the implications are rates would get closer to normal, neutral, faster. What I heard from Jay's press conference is that there's no particular reason why you have to go on a predetermined path here, and so we did in the 2000s, 2000, I think, '04, '05, '06, move rates up at every meeting. I think in 2013, or I guess 2016, '17, '18, we moved it every other meeting. I just say today's environment is different than 2017. Inflation then was 1.8, 1.92, inflation today is, as I said, 4.9 on the PCE and higher, core PCE and higher on the CPI. There were, I think, bigger questions about the growth potential of the economy, certainly in the 2013, '14 than there are today, we seem to be growing extremely strongly. Unemployment's lower now than it was then. So I just think you're in a different environment, and that different environment does support, I think, a more forward leaning notion of how to normalize rates.

Mark Duggan:

Okay, so this is now asking you to draw from a little bit your conversations or communications with people in your district. I'm curious, have you heard much about the infrastructure bill, the bipartisan infrastructure bill that was passed late last year, and I think that we certainly heard a lot about it in the news, and there is clearly a significant uptick in what the federal government is spending on infrastructure, that's obviously not the Build Back Better Plan, but can you get a sense of, is it your sense from connecting with people that people in the district are thinking, wow, this is going to be terrific, we've got some infrastructure that really needs this improvement, it's going to really enhance the economy. Do they anticipate challenges? Have you heard much about it from people in your district?

Tom Barkin:

In our district it's widely supported, people are very supportive of putting money into infrastructure. They would note it hasn't been funded yet, and so while the House and the Senate are still thinking through the continuing resolution there's no funds for it, so nothing's been distributed, is what they say. They're not necessarily negative on it not being distributed, because I think one of the big concerns is this issue of infrastructure workers, and then the construction and the trades, people are really nervous about where you're going to find people, and or if more demand comes into the economy in these sectors, how are we going to either get the work done or handle it without raising wages to levels that'll be unsustainable? And so people are happy with it.

Tom Barkin:

To the extent there's concerns, there's, I'll call it, a fair share concern. I mentioned that in the smaller towns, am I really going to get what I need given some of the requirements? And then, like I said, there are infrastructure worker concerns, I think that is quite predominant in my markets.

Mark Duggan:

Thanks, that's helpful. Apparently I have not, I've gotten several questions since I asked what I thought was the question, but people are not satisfied with how I asked it, so I'm getting more 50 basis point type questions. Is raising rates 50 basis points instead of 25 basis points a tool that you are open to? I'm getting a number of questions in that vein, so apparently I didn't do justice to it before.

Tom Barkin:

Am I open to it conceptually? Sure. I mean, there will be times where we'll need to do that, there have been times in the past where we have done it. Do I think there's a screaming need to do it right now? I'd have to be convinced on that.

Mark Duggan:

Okay, this question just came in, and it was one that was on the tip of my tongue, so I'm glad that it came in from an audience member, when do you think the Fed should begin, or will begin reducing its balance sheet, and how fast, is this a substitute for a rate increase?

Tom Barkin:

Yeah, so balance sheet is another really interesting conversation because we now have a $9 trillion balance sheet, which where I grew up feels like a lot of money, and if you believe as I believe, that it's time to normalize policy, then you'd also say it's time to begin the process of normalizing the balance sheet. And so as Jay talked about at his press conference, and we're in the last set of minutes, we've begun the process of thinking about how exactly to do that.

Tom Barkin:

I'd say the balance sheet is not as tried and true a tool as rates. I mean, people know how rate increases work and how they market. We've only reduced the balance sheet once, and we're the only central bank in the world that I think did that, at least at some scale the last time. And so the track record's just lower. And so I think you do want to spend a little more time just thinking about how do you that? What's a good way to do that? And what's the right way to do it for this situation? Because this situation is different than the last situation, for the reasons I've talked about. Inflation is more elevated, the workforce is tighter, we have done this before. We've also got standing facilities now to help reduce the volatility around it, and the Standing Repo Facility and the overnight RRP facility.

Tom Barkin:

And so what we said in our principles, which I entirely subscribed to, are it's time to do a substantial reduction in the balance sheet. I think we've said because the language change it'll be less gradual than the last time, and that we would lead with rates and then go to balance sheet, but hopefully we could do it somewhat soon after we start working rates. And I think the last question that was asked was do I think it affects the economy? I do. If you believe that buying assets reduces interest rates, and therefore stimulates the economy, then I think reducing the balance sheet has some impact on the interest rates, and therefore helps constrain the economy in the way that rate increases to, I think it works alongside rates.

Tom Barkin:

But I will say there's a bunch of academic literature on this, it's wildly varying, the confidence interval on what the estimate of the impact is is extremely wide. My personal impression is it's on the more modest side than the more extreme side, but again, there are a lot of academics that are studying this.

Mark Duggan:

This is an interesting question here. Workers seem to have more power than they have for a long time. Do you expect this to last?

Tom Barkin:

I think there's a very good chance it lasts, for the reasons I've talked about. There's a book I really enjoyed by a professor named Goodhart, The Coming Demographic Reversal that makes this point, I think, even better than I'm going to make it, but which is the demographics are a fact, they're not going to change anytime soon. It doesn't look like immigration is going to be happening at scale, it's not happened yet under either of the last two administrations, and so you've got a workforce that's headed south.

Tom Barkin:

I think there's a potential to get more workers into the workforce, I'd note that Japan's workforce participation of people 60 and up is 14 percentage points higher than ours is, I'd note that Canada's participation of women in the workforce, which was the same as ours in 2000, has gone up four points while ours has gone down four points, so that's an eight point gap. So I think the potentials there to get more folks in the workforce, but it feels like pretty hard work, and so I think the slope's headed in a direction where you're going to have to work against that slope.

Mark Duggan:

Very interesting. Okay, so you mentioned the demographics, and this is, I never miss an opportunity to just express my sadness about how Washington DC deals with entitlement programs, and the challenges that are on the horizon. So in about 10 years, give or take, 12 maybe, there's uncertainty about it, projections are that the Social Security trust fund will hit zero, and what that means depends on who you ask, because it gets us somewhat into uncharted territory. In your role you talk with people who are thinking about these issues, can you give me reasons for optimism that policy makers might try to tackle this sooner than the day before the trust fund is going to reach zero? That's just Social Security, Medicare is an even more complicated beast, and I've done a lot on Medicare too, but it is just [inaudible 00:52:23], I mean, for examples-

Tom Barkin:

You really flipped me by starting a question about deficits than asking for me to be optimistic, you really put me on my head. So I could answer your question narrowly, which is I think there's so much political support for Social Security that it's going to remain funded, and as you know, if it's not funded by the trust fund, it gets funded out of general revenues.

Tom Barkin:

But I think your real question, which I totally subscribe to, is do trees grow to the sky when it comes to deficits, yes or no? And my belief is no, trees don't grow to the sky, and if our debt-to-GDP was in the high thirties in 2007, and it's in the 106% range, or something, today, do you like that trajectory? And answer is no. And then you might ask, well, what gives you some optimism? And I don't think it's the willingness of folks to pass, I don't know it. I mean, it has to be growth, it has to be growth.

Tom Barkin:

And so if you wanted to get optimistic, I guess the way to get optimistic is to say I do think we're back at the start of a run on productivity, as we were talking about earlier. I'd like to think that we could tackle, as an economy, this workforce issue, because it's in nobody's interest for the workforce to shrink in this country, and we're well ahead of many, many parts of the developed world, even at our relatively anemic population and workforce growth. And even if you look at the last four or five months in the budget receipts, they're significantly better than anyone had forecasted, or then prior year end, because we're growing, and if we grow at these kind of rates, you can make some progress. But of course you're going to have to grow and then restrain yourself from spending what you earn, so that's going to require a lot of focus.

Tom Barkin:

Another piece of optimism, on the Today show in 2011 they got together eight members of the American public, they had one from every segment, they had a retiree and a student, they had a liberal and a conservative, they had a tea partier, they had a union member, they picked one of everybody, and they gave them flashcards in terms of handling the deficit, and the group of the eight of them actually bounced the budget in 20 minutes. So it's not like there aren't things you could do, I just think it's about prioritizing them.

Mark Duggan:

Yeah, it would be good, it would be nice if someone could make a, is it a moral case? It would be good to leave to our, I don't think any of us would want to leave to our kids our big credit card bill, and so it's not that much different from them. And I guess, I don't know, I'm just waiting for someone in Washington DC to take that. You mentioned Bob Rubin at the beginning, and I'm not trying, but when he became a force in DC in 1993, in the Clinton Administration, they really decided to go after deficits, and that, you may remember that the fiscal situation got on a much better trajectory there.

Tom Barkin:

Well, you may remember that in that era. I think it was actually President Clinton who said when he dies and comes back he wants to come back as a bond market vigilante, because the case that Rubin made, if

I read the same books you did, is if you do this you're going to have a huge benefit in the bond market, which will then stimulate the economy, and one could argue that's what happened in the 90s. There's probably more to that story. But look at what's happened with the deficit and look at the long bond here, so you're not seeing that same situation, at least not yet. But maybe that is the kind of thing that would happen at some point and stimulate some action.

Mark Duggan:

Great. Okay, so I think we've got time for another couple of questions, and I know I'm not going to be able to get to all the questions, I've reduced the number I asked from my list, and we've had tons of them, but how, if at all, does the Fed consider differential labor force participation and wage growth by demography, eg., gender, race, ethnicity, that kind of thing?

Tom Barkin:

Very much part of the data set we're looking at, very much interested in the experience of the last upturn, which showed at the end that the last people into the workforce were those who were most disadvantaged, and there seemed to be room in the workforce for them to grow. And our framework, as I discussed earlier, talks about broad inclusive as part of the impact that our employment mandate can have.

Tom Barkin:

We do have a challenge in that our tools are reasonably blunt instruments, and so you can raise interest rates or lower interest rates, it's hard to raise interest rates for any particular group. You can buy assets or sell assets, it's hard to do that for any particular group. And it's also true that a lot of the differences among groups have their basis in issues that are far beyond monetary policy, whether they be education, or discrimination, or whatever. And so I think it is something that the profession increasingly is aware of and pays attention to and tries to normalize, but I just think it's important to recognize we don't have the fiscal tools, we've only got the monetary tools, and they're relatively blunt instruments.

Mark Duggan:

Okay, my final question is, and we've got some great questions, so apologies for those who didn't get their question.

Tom Barkin:

I assume you're just going to ask 25 or 50 basis points again.

Mark Duggan:

No, no, no, no, no, no, this one is, so a bunch of my econ one students are watching this, and many of them are literally 18 years old. And for many of them you're living the dream. You've gone out, you went into the private sector, you crushed it in the private sector, you worked at McKinsey, you climb the ladder, now look at you, you're working in economic policy and serving your country, and all this. Do you have any words of wisdom for some of the people who are just starting out as they embark on their careers in this uncertain world that you talked about?

Tom Barkin:

Oh, that's a pretty interesting question. So I think that it is good to go find something that you're excited about doing and put your head down and try to do it well, and not try to solve all the problems you don't have, but just solve the problem of trying to do something you're excited about doing well. At the same time, I think it's incredibly helpful to get to know people. And so one thing I've always gotten energy from my entire life is building a network of friends, and while I was working, and trying to do a good job at work, I was also building relationships and friendships outside of the workplace. And not in a transactional way, not in a careerist way, but genuinely I would meet somebody and have breakfast with somebody, and then if they needed some help, I would try to help them.

Tom Barkin:

And I think there's a part of building a career that is taking seriously what you do, and doing well at it, but I think far too many people focus only on that, and don't focus on the rest of their lives. And part of it is the network you build and the relationships you build and the friendships and how they can help you, part of it's actually your relationships at home and how you nurture those.

Tom Barkin:

There's something about whole life to me that's important in this, but you can do A plus B plus C, my last thought, the key to doing it is you actually can't do everything. You actually have to say, this is important and this is not important, and you have to work to get more productive in what you do at work. You have to move the work you have away from the time that's costly toward the time that's costless, so you don't piss off your spouse or friends. And so it actually takes a lot of work to be able to have the capacity to do all the stuff you want to do, and you have to work that, I'll call it resource allocation problem, like it's also a job.

Mark Duggan:

Perfect. Well, thank you so much for that, Tom, and you probably would also say that they should take more econ classes. I'll just throw that in there. So in any case delighted, it was so great to connect with you today, I'm so grateful to you for spending time with the SIEPR community and sharing your insights, really wish you could have been here in person, here in the SIEPR building, but hope we can have you back here in the SIEPR building in the not too distant future.

Tom Barkin:

Love too.

Mark Duggan:

But I know if everyone were here we'd be hearty applause right now, so thank you so much, Tom, again, President Barkin, thank you again for making time.

Tom Barkin:

No, Tom, thank you. Appreciate being with everybody, have a good evening.

Mark Duggan:

Okay, everyone. Okay, have a great, and thanks everyone, and you'll be seeing lots more from SIEPR in the coming days about the things that we have on the horizon, including our events and our research, so please be on the lookout, and thank you to all of you for tuning in and for your support of SIEPR, I really look forward to seeing you very soon. Bye-bye.