Fed Unfiltered, Transcript
3/23/22 – Tom Barkin, Interview: Montgomery County Chamber of Commerce

Lowell Yoder:

This might be your third time with us, so I think most of the folks really have a sense what you're all about. Your bio, I'm not going to read your bio because it is so strong, you're so qualified. I would just say just on a personal note, every interaction I've had with you, I've been so impressed with your genuine curiosity, interest, and commitment in the region that you serve, all the way from what's happening in the rural parts of your region. You have a special affinity for that as well, all the way to places like Montgomery County, and the more urban areas, so really appreciate all the work you've done. There's probably ... I can't think of any more possible variables we could put on the Federal Reserve right now. I'm sure that the folks that are listening in today are very curious about your thoughts, so I'm going to turn it over to you now to make a presentation. I got a feeling there'll be lots of engaging questions as well. Please, Tom Barkin.

Tom Barkin:

Good. Thanks. Great to be back. I call you guys my favorite chamber now because we're together so often, but also, I really am dying to be back with you in person. I'm about 85% of the way there because I'm in the Board of Governors in DC today, but I'll get all the way there for the next time. We could talk about whatever, I'll gladly take questions, but I thought I might just talk a little bit, to start with, interest rates, because the Fed's been in the news a lot lately, and a lot of people are asking me a lot of questions around how does this all work. There's a range of questions, so I'll just talk about interest rates. These are going to be my views, not anybody else's, as always, I can be as direct as I want.

Tom Barkin:

We had a meeting last week. We announced we're going to raise interest rates 25 basis points. That's not the biggest thing in the world. But also, we said that ongoing increases in the rate of interest will be appropriate in order to get inflation back to our 2% objective. We forecasted every meeting. The average member forecasted seven rate hikes this year, and three to four next year, which would move rates modestly above what most people think is the neutral rate. In his press conference, Jay also said we're going to start to reduce the size of our balance sheet at a coming meeting, which could be as early as May.

Tom Barkin:

So just taking a step back from that, I mean, it's time to normalize rates. The worst of the pandemic is behind us, we're 22 months into the fastest recovery in our memory, by the end of this quarter, GP is not only going to exceed the pre-pandemic level, it's likely to catch up to its pre pandemic [inaudible 00:02:51]. Consumer spending is strong, business investment is healthy, the housing market is hot, underlying demand looks like it's going to remain robust, that's fueled by healthy business balance sheets, healthy, personal balance sheets, low inventories, which are going to need to be replenished, state governments that are flushed with cash. I don't want to declare COVID over but ... and we will probably see more variance like the one rising in Western Europe, but we are learning to live with it, and I think that's good for the economy.

Tom Barkin:

The challenge we face now isn't the pandemic anymore, it's inflation, and we've talked about it before, demand for goods exploded in the middle of the pandemic, supply chains struggled to keep up. Labor markets also did not respond the way we all thought, so unemployment is low, the pool of those looking for a job is also low. There are 2 million fewer workers in the workforce, and immigration is almost another 2 million below its pre COVID trend. So, consequently wages are up, average hourly earnings are up 5.1%. Prices are up, core PCE inflations up 5.2%, that's the highest since April 1983. A year ago, you would've looked at it and said, "All this is temporary, it's chips in cars," but these issues have persisted and broadened, so inflation's the headline of the day, and that runs the risk of more and more firms looking to raise their own prices.

Tom Barkin:

So all of this means that the economy no longer needs aggressive Fed support, at some level that's good, but on the downside, we need to put ourselves in a position to contain inflation, and as you know, that's the Fed's job. So, maybe two or three questions that I get asked a lot, first is, how does raising rates actually contain inflation? I think it's worth just spending a little bit of time thinking about that, because the answer is different over different time horizons, and I just want to say, in the short-term, inflation is largely driven by things other than the Fed.

Tom Barkin:

The best analogy I can come up with is a hurricane, if a hurricane hits a coastal city, and people need to rebuild their homes and their businesses, lumber prices are going to go up, and there's really nothing rates can do to stop lumber prices going up if people need to rebuild their homes. Actually, rates shouldn't try to do that because eventually homes are going to get rebuilt, and lumber prices will come back down, and you don't want to constrain an economy where prices are only up because a hurricane hit the coast. So if you like that analogy, think about the pandemic, it had a lot of destructive impact, and I didn't even mention geopolitics, which of course are having their own destructive impact, and you've got inflation continuing to be impacted by supply chain shortages, fewer people in the labor force, the ebb and flow of the virus, most recently in China, and of course Russia's invasion of Ukraine, which affects prices of things like energy, and aluminum, and wheat and nickel.

Tom Barkin:

I don't expect much of any impact of rate increases on inflation in the short-term, I just don't think that's a very logical way to think about it. On the other hand, in the medium and the long-term, the Fed's rate moves definitely do matter, and in two ways, one is tangible, and one's less tangible. On the tangible side, we raise rates that reduces demand, when demand drops that eventually reduces prices. So deposit rates increase, that creates more incentive to save rather than spend, the dollar appreciates, that increases demand for ... that lowers the price of imports, and that lessens demand for exports. The borrowing rates rise, that reduces capital investment, and that reduces consumer spending, particularly in interest sensitive sectors like housing, and auto, and consumer durables. You're already seeing mortgage rates go up, for example.

Tom Barkin:

The less tangible part is inflation psychology, and the way I'd put it is both individuals and firms build expectations about what inflation's going to be. Firms then make their pricing decisions and their compensation decisions, and then individuals make their purchase and their employment decisions in the context of those expectations. If you expect inflation to be low and you see a big price increase, you're not going to pay for it. If you expect inflation to be high and you see a price increase, you go, "Well, that's happening everywhere." So if the Fed does its part to control inflation expectations, then consequently price and wage increases are going to stay stable and anchored. If we don't do our part, that's what's happening in Turkey.

Tom Barkin:

I'll say now, as best as we can measure it, and it is hard to measure, expectations seem to be pretty stable, if you look at the TIPS indices, the 5 to 10 year inflation expectations still look about where they looked a year ago. The Michigan survey of 5 to 10 year inflation expectations has only increased a little bit, both of them are at 2013-2014 levels. The metrics haven't broken out and that's good, but that also, I would suggest, requires people think that we're going to do our part. Now, some of you may think that doing our part to control inflation is going to drive us into a recession, and of course with the surge in energy prices since the Ukraine invasion, some are even raising the word stagflation, a word which a few of us remember from the 70s. I'll just say that we're not on a rate path right now to drive the economy into a ditch, we're actually still very far from the rates that most people think constrains the economy.

Tom Barkin:

My colleagues on the FOMC actually project that rate, estimate that rate, and most of them are within the range of 2% to 3%, so call it 2 1/2%. This week's move still leaves us 9 to 10 rate increases away from 2 1/2%, so we're not putting our foot on the brakes. We're just taking our foot off the gas, and I think that's a pretty good way to think about it. We're not taking our foot off the brakes, we're just taking our foot off the gas. The extraordinary support of the pandemic era is starting to unwind, I think that's a good thing. I think by doing that it puts us back into a position to do something, if we need to put the brakes on the economy in time, it's awfully hard to put the brakes on the economy when rates are at zero, but if you get rates back to normal, then you do have the ability to do that.

Tom Barkin:

Now on the other side, I get questions from people asking whether the Fed ought to move faster. We have moved at 50 basis points at a time in the past. We've even moved faster than that, and we certainly could do it, again, if we felt like it was necessary to prevent either expectations from an anchoring, or because we starts seeing inflation accelerating. But I guess I'd just say this is all a balancing act, you normalize rates to contain inflation, but if you overcorrect, you start to affect employment, which is the other part of our mandate. I just think that both inflation and employment are still being heavily influenced by the combination of pandemic era, supply and participation pressures, and the war on Ukraine. I just think it's going to take us a little while to meet the dynamics of whatever the post-pandemic economy looks like.

Tom Barkin:

Now, one piece of good news markets and monetary policy actually work pretty well together, that's a innovation Ben Bernanke brought to us. If you surprise markets though, in contrast, you can tighten financial conditions in ways that cause the real economy to pull back, so it's just worth noting where the bond market is. We signaled a pivot in our posture about four or five months ago, the two year treasury yield was 28 basis points at the end of September, it was 218 basis points this morning. The five year was 98 basis points, at the end of September it was 239 this morning, so we could move faster but when you look at that, you might say, "We're actually having a lot of impact we want to have right now."

Tom Barkin:

On the balance sheet, a reminder that I think rates are our key tool, but in the background, the balance sheet can reinforce the rate path. As a reminder, we started buying treasuries and mortgage backs in March 2020 in an effort to stabilize financial markets, we then continue them to support the economy. Our balance sheet is now 9 trillion in assets, that's up from 4.2 trillion pre pandemic. I just think if we're going to normalize rates, it's appropriate to normalize the balance sheet as well, and as I said, we're going to begin to do that soon. A lot of people ask what the impact is, I'll just say that the economists have a range of impact that is so wide it's not helpful. But the way I think about it is, if you're participating in the market buying assets, then you're lowering yields, and if you're not participating in the market, but instead you're rolling off assets, you're going to lower yields.

Tom Barkin:

I don't think in a big way. I don't think in a big way, and you can see we've started to announce these things, and the markets aren't moving that big in the medium to long-term, but I do think that any kind of movement in yield supports our desired rate trajectory. I think the questions of where this thing goes from here are big and broad. On the demand side, I do think demand is going to calm down as we get through the pandemic era, as rates increase, as excess savings are spent, and as these oil price shocks have the natural impact you would expect on demand, but I don't think it's clear how quickly it's going to calm down, and how we're going to settle out in terms of the mix of goods and services. I believe supply chains are going to recover as COVID recedes, as people remediate shipping and other barriers, chips will get back in cars, and workers are going to rejoin the workforce, but I think it's really unclear how much upside the labor force has, and how long it will take to clear these supply chain issues.

Tom Barkin:

Inflation will move toward target, because I think these pandemic and geopolitical pressures will ease in time, and policy will help, but I think it's unclear what the impact of this period is going to be on inflation expectations. We've had 39 years of 2% inflation in one year of 5 1/2, so I don't know what does 2024 look like, 2 or 5 1/2? I think that's a pretty interesting question we don't know the answer to. We do have tools which are flexible, so we're going to learn over time what pace we need to use them. The higher inflation lasts, the more aggressive you need to use the tools, and the more it receives the less aggressive you do, because we are very much committed to keeping inflation on a medium term path to 2%, and keeping inflation expectations anchored. I hope that's helpful, just a quick view of what's going on, what we're doing, and why we're doing it. Gigi, as always, I'm totally open to questions, comments, insults, and advice.

Gigi Godwin:

Thank you, Tom. I'm really excited to have you here. I did want, and I love the fact that we are your favorite chamber. Thank you for that.

Tom Barkin:

I don't tell everyone that, I just want you to know that.

Gigi Godwin:

We do have the best board of directors of any chamber anywhere on the planet. That said, one of the things that when you, and Lowell, and I got on a call recently together, we discussed what's the impact of all this on some of the issues that our companies, our employers are dealing with along the lines of adopting, and expanding their commitment to ESG. If you recall, we touched on that, and I don't know the degree to which the Federal Reserve is going to be involved in setting any kind of standards, or having a conversation about that, and of course we wondered about ESG a few months ago, even as we were wondering if there would be an invasion by Russia, because it was talked about before it happened. Then, of course the concerns about Taiwan, will China go in and disrupt the computer chips, and all that sort of thing.

Gigi Godwin:

We were using that as examples, and I'm just curious the degree to which you will or will not be involved in ESG-related conversations, which is the environment, social, and governance issues as a reminder because we've had speakers address that issue. Could you comment?

Tom Barkin:

Well, there's a lot to that question. So ESG, the Fed has a very narrow remit when it comes to ESG, we oversee the banks, and so we regulate the banks. We have the ability to put forth standards for the banks to live to. We've said that we're doing a lot of work to try to understand what climate transition and climate change has to do with the risk profile of banks, so that's on our list. The SEC announced, I think it was a couple days ago, a bunch of reporting requirements. I think the SEC has a much broader remit than we do, and so they're able to do a bunch of reporting, that's not our world, and of course there are a huge number of things that Congress could choose to do in the environmental space that would be well beyond our mandate.

Tom Barkin:

We're focused on prices. We're focused on employment. We do our little part to oversee the risk profile of banks. What would be an example of that risk profile? I talked about hurricanes earlier. We do look at banks and see what their concentration risk is on coastal properties, that would be a basic example, but I don't think you should imagine the Fed is the lead actor on climate change. Now, I do think there's a lot of work being done on climate transition, I do think that work is going to affect the economy. I think it's going to affect it in ways we don't fully understand, but the increase in oil prices over the last few weeks, in the context of the Russian invasion kind of brings that into stark focus. We all know that the leading harbinger of recessions is actually increasing oil prices, much more than the yield curve, much more than Fed rate things, that is, if you look at recessions over the last 50 years, that's what's driven them.

Tom Barkin:

Now, that doesn't mean it has to happen in the future, but to the extent you care about the health of the economy, you do worry if oil prices go up. I'd say it's quite striking when you see the administration engaging with Venezuela, and you start seeing some of the challenges Europe is having on oil price to say, "Wow, that's going to make the question of how we transition from a climate thing in a way that doesn't either, A, influence the health of the economy, or B, lead to price increases at some scale." That's an important question. I say from a monetary policy standpoint, we don't drive any of those decisions, but we're going to have to understand where that's headed as we try to influence the outcomes on health of the economy and inflation.

Lowell Yoder:

Gigi, I think we can, maybe just logistically, if someone would like to ask a question, they can just raise their hand, and maybe Juliet can monitor that and see who that is, and bring them on. But in the meantime, until we do get some of those questions-

Gigi Godwin:

Oh, we do. I see one. Ron raised his hand.

Lowell Yoder:

Okay, very good.

Gigi Godwin:

The first guy up, and he gets ...

Ronald T. Piervincenzi:

I didn't mean to jump in quickly, but I'll do it anyway. Thanks, Tom, I appreciate this. I just want to share something. USP is 200 years old, so it's certainly seen a lot of recessions, but of course organizations are not [inaudible 00:18:45] organizations. We had a discussion just a couple days ago, that for all of our senior leadership team, nobody had to role in any form of management the last time there was a significant inflation. In other words, nobody making decisions about our prices, relationships with distributors, whatever, all the things, has any previous experience. I wonder, not how this affects rates of course, but rather is there a discussion about the naivete of people, even consumers and behaviors? There's so little to base it on. Does it make it more difficult to take a look at those sentiments about what people's perspectives are for 5, 10 years out, and kind of calibrate that to the fact that most people are experiencing this for the first time in the form of their leadership, or even in their households?

Tom Barkin:

Yeah. I mean, I think if we've learned anything in the last three or four months on inflation, it's that people hate inflation. I think there were questions about that three years ago, five years ago, you might have conversations about, "Why do we fear inflation so much? Why is your target 2%? Why isn't it 3% or 4%? What if we had a little higher inflation in an effort to get more jobs, wouldn't that be good?" But if you look at consumer sentiment right now, people really despise inflation. If you look at business sentiment, most businesses had a great year last year, but they're very unhappy because they don't like unpredictability, they don't like uncertainty.

Tom Barkin:

I like to say that if you raise your own prices, it's because your products deserve it, but when your costs go up, it's because of that damn inflation, and if your wages go up, it's because you deserve it, but if the price of gas goes up, it's that damn inflation. So people are not symmetric in how they see those two, and so they see those two pressure, so that's pretty important to know. I think that certainly emboldens me in the firmness of how I think about what we've got to do about inflation, of course the Fed has been studying the 70s, 60s and 70s for its entire lifetime. There are trucks full of people waiting to go to battle here, that we've been doing these training exercises ever since, so I've got a lot of confidence in us on this.

Tom Barkin:

But I do think it's going to be a lot harder than we think it is to put the genie back in the bottle, and again, I use that exact analogy, the 39 years of 2% followed by the one year of 5 1/2%, because when I talk to businesses they do tell me, "Oh, yeah, this year we're going to have to raise prices." "Well, what's it going to be two years from now?" "Oh, no, no, we're not going to be able to do it two years from now." I think there is a curve back to where we were, but I don't think ... We talked a lot in June of 2020 about whether it was a V or a U, or a swoosh, or a square root sign or whatever, I don't think inflation is upside down V. I don't think you go up and you go down, I think you go up and you fade down, whatever letter of the alphabet that is.

Ronald T. Piervincenzi:

Thank you, Tom. I agree, and of course you've made decisions, people have already given raises to the workforce, and then the price increase comes a few months later, and they're committed in their price increase already so the V is sort of impractical. Thank you, appreciate that.

Tom Barkin:

Thank you.

Lowell Yoder:

I don't know if we have another one yet, but I will ask one, because I think it's been something that it's in the front of all of our minds, and has been for sometime, even prior to the pandemic, it's this whole thing around labor and finding people. Is this something we're just going to, as a ... just demographically, just we have to live with this kind of issue and adapt, or is there something else fundamentally that may change that dynamic?

Tom Barkin:

Well, I've been thinking a lot about this, because if we're honest with ourselves, for the last 30 years, we've been living in a world where we were long labor. Baby boomers went in the workforce. Women participated at much higher percentages. People lived longer lives, and stayed healthier, and worked longer careers. We opened up a global labor pool throughout offshoring, and so businesses lived in a world where we were long labor, and that led to doing a bunch of stuff. Some of it was being a little bit tighter on wages and benefits, cutting pensions, but also things like outsourcing, turning your labor force over to somebody else with confidence they could deliver. The demographers, 10 years ago, started saying, "Hey, the ship is turning here," because baby boomers started to retire, and the fertility rates were going down.

Tom Barkin:

Then you could even say immigration in the last five years has dropped, but we didn't see it so much in the workforce because participation increased, and it increased at the end of a very long upturn where a lot of people on the sidelines finally got in, which was great. But we really didn't ... It was a little tight in 2018 and 2019, but it wasn't tight like it's tight today, it didn't really take its measure on wages the way it is today. So, now we're on the other side of this, you want to be wary of overreacting to what's happened, but immigration has continued to fall. So that's another 2 million people not in the workforce, who would have been if immigration had stayed standard, and I'm not confident it's going to come back up. I haven't seen a lot of moves from this administration, certainly not the last administration, to move that, so it's a question mark, but that's down.

Tom Barkin:

Fertility has stayed down, the demographic tide has turned, and then coming out of COVID you just see participation drops, that importantly don't take participation down below the trend line, they just take it to the trend line. The question you have to ask yourself is, "What's the aberration? Is the aberration today? Or was the aberration 2018 and 2019?" The trend line's just going to go down. We may actually be living in a world where we're going to be short labor for a while, and if we're short labor for a while, that in the first instance, of course has implications for wages and benefits. But it also has, I think, implications for things like investments in automation and productivity, because businesses aren't going to stay neutral in this thing. It's going to have implications for how one invests to build [inaudible 00:25:17] in a workforce.

Tom Barkin:

One thing that I like to think about, because I do spend a lot of time, Lowell, in the small towns, is pensions and company towns, and if you go back to the 50s, all these small towns were built around one company, and that company built housing, that company built schools, that company took care of people for a lifetime, and then in the 90s we were able to get out of all that. Well, I don't think we're going back to pensions, but what's going to bind employees to the workforce going forward? I think you're going to see people experiment with childcare again, because I think that is a way. You're not really going to willy-nilly take your kid into a different situation, and quality childcare at the work site, I think, is the kind of benefit people are going to start investing in for loyalty.

Tom Barkin:

I'm rambling on, but I think it's going to be tight for a while. I think we're going to get to equilibrium in time, but that equilibrium's going to be a different pay and benefit model, and maybe a more creative pay and benefit model, but also a different productivity and automation model, and of course that has implications as well.

Lowell Yoder:

Great.

Tom Barkin:

I saw Kking with his hand up.

Lowell Yoder:

Yes, there. Yes.

Kking:

Bob, can you ... I'm sorry, Tom, can you hear me?

Tom Barkin:

Yeah.

Kking:

You know, this obviously is a very difficult time, and we're sort of in the middle of the perfect storm, not a good storm, a bad storm. It certainly is a combination of things, the war, what's going on in Ukraine right now has had major impact, certainly gas prices are a major impact, and some of the concerns, and if I understood you correctly, you're saying by raising interest rates, that will slow the curve down in terms of people wanting to buy, and less people that are buying as many things will drive pricing back down. Is that kind of the thought that, and by the way-

Tom Barkin:

I'm too clever to agree to any premise before I get the rest of your question.

Kking:

Okay, so if you're raising interest rates, and it's going to take a period of time before whatever you're raising, and I can see why some people will say, "Well, why aren't you increasing interest rates higher quicker as opposed to doing it very slow over a period of time?" I think initially, as you raise interest rates, that's going to have a bigger impact on inflation. I think inflation's going to go up initially before it'll start coming back down again. So in my mind I'm seeing inflation continuing to go up significantly, even though the Fed may be raising interest rates, and if that's ... to that extent, what happens to companies? By the way, it also goes into hiring, and how companies, if they have to hire would have to pay more to individuals because of the lack of or shortage of workers. Then, in many cases, these companies have to borrow money to be able to stay in business, so there's kind of an impact with all of these different things that are going to take place.

Kking:

The other last thing that I would comment on is, I think as a country, we need to look at what we can do internally here to help reduce inflation by increasing maybe ... when you look at gas prices, what could we be doing? I realize that we are concerned about our Earth and what's changing with the weather conditions in the world today, but at the same time, what can we do even on a shorter term to help reduce some of the inflationary costs?

Tom Barkin:

There was a lot in that. So here's the situation we're in today, demand is very strong. You described we're in the perfect storm today, and I think from an inflation standpoint, we're in a perfect storm, but we're in a really big boat. Demand is very strong, and that's a combination of the health of the US economy, walloping large amount of fiscal stimulus, a very strong monetary stimulus package, a very strong financial markets and housing markets, which have increased net worth at epic proportions. It's businesses that have paid down debt, and emerged to the other side with actually a lot of energy. Most people had their best year ever. State local governments that are flushed, inventories that are low. I mean, demand is very strong. We could argue, but that's what I believe.

Tom Barkin:

Prices are quite high, now they're not 1979 high, but they're too high for me, so I'd like to have prices down. We have our foot, collectively I would say, fiscal and monetary, on the gas, so I don't know, I can't really make a case in my mind to keep having the foot on the gas. The only way to make the case that I think you were making is that you think your foot's on the gas, but it's not. The second you take your foot off the gas, the economy's going to collapse, that's the risk profile you have to put in. I think the foot's still on the gas because of huge budget deficits, that's the fiscal side rates at zero, that's the monetary side. If we can't get rates off zero as an economy, we have a whole another set of problems, which again, you could argue, but I'm going to suggest I'm still hopeful, and confident that's not where we are.

Tom Barkin:

To me, it's a no regrets move to take your foot off the gas. You know this, but when you take your foot off the gas, the car doesn't stop, and so the car's going to glide a little bit slower, and then let's see how the economy responds. There are absolutely things that could happen. You talked about Ukraine, just imagine a wave of cyber attacks in a tit for tat escalation between us and Russia, that would change the story I'm telling, but [inaudible 00:31:19]. You also mentioned there are other things we could do, and I totally agree, because fiscally, we have got our foot on the gas as well too. You could take your foot off the gas fiscally by spending less or taxing more, that's one way to do it, but the other way is to think about how you ease supply, how you create more supply, whether that be of labor, or materials, or energy or the like.

Tom Barkin:

I think there's a set of things that we can do in our job, for sure there's a set of fiscal things that can happen, they would include thinking about our deficits. I'm not against that, but they would also include freeing up the supply side of the economy so that some of these pandemic era pressures were less pronounced.

Kking:

What do you think about with gas prices going up significantly? What do you think about ... I mean, look at the state of Maryland, where they've dropped the tax on gas to bring down the costs so people aren't as impacted. How does that really help the overall economy? Does that keep inflation up, or does that help reduce inflation?

Tom Barkin:

Well, you could put tariffs into this equation too. A lot depends on how you do it, so if you lower the gas tax, you lower the cost of gas to those who are spending it. Question one is, do BP, do they pass it on to consumers or do they keep the price the same? That's an important thing, same with tariffs, if you take off steel tariffs, do steel companies keep price the same or do they bring it down? That's an important question. If they do bring it down, then at least in theory, you've got lower gas costs for consumers, which should free up some amount of their wallet to spend on other things, which would be good for them, and good for the economy of course. In most states, and I'm pretty sure it's true in Maryland, the gas tax funds things, funds infrastructure, so how are you going to replace the money in there?

Tom Barkin:

Now, most states these days have excess funds because the stimulus programs from the Federal government were well in excess of what they needed, in part because the projections of what would happen to states in the pandemic didn't come to pass, because of the huge rebound we had. So that would be a interesting place to use the money, because a lot of states are talking about using these excess funds for tax cuts. It's on a docket in Virginia, where I'm living, and tax cuts can be regressive or they can be progressive. A gas tax cut is one of the more progressive tax cuts, just because of how people spend money.

Tom Barkin:

So it's not that it's ... I'm not criticizing the idea at all, but it's got to get executed. It's got to get executed in a way that don't take money away from future infrastructure funding because that's not rational, in ways that don't fund those people providing the gas at the expense of the people you're trying to help. It can be done that way. I'm not close to exactly how it's going to be done in Maryland, but it can be done that way.

Kking:

One last point and I'm done. I just have another question about the housing market, because I see ... certainly, right now the housing market is at a peak, not only is the resales extremely high, you have a lot of investors buying property so that he can rent them because rental rates have gone up significantly. As you continue to raise rates, and rates have increased significantly in the last 30 days, they're up to almost on a quarter 4 1/2% percent on 30-year fixed loans right now, which is going to either discourage people from buying, or they won't be able to afford the monthly cost as part of their mortgages, and whether that will drive the pricing down on housing, I don't know if that will help reduce the cost or the pricing. But again, to me, that's also adding to inflation for them because these people that are already feeling the bite of inflation, now they can't afford to buy, let's say a home, because the real estate or the interest rates are going up significantly.

Tom Barkin:

Well, so mortgage rates are up, and I talked about that earlier as a positive thing, because we've only raised rates 25 basis points, and you've got mortgage rates up a 100 in a quarter or something like that, and you have to be ... There are different ways to define inflation. I mean, housing prices are up a lot, if you like that, good, but if you don't like that, then raising rates is one way to control the rise in housing prices, and so maybe that's more ... it costs you more to buy a house and so your price comes up.

Tom Barkin:

You have to think about whether that's inflation or not, but I think the way I'd put it on housing is, first of all, everyone live in their house 24/7, and there's no better way to understand the flaws of your house than living in it 24 hours a day. So all these people decided they needed another house, whether they were people in cities who were looking for a second house, or people who thought their house didn't have a big enough office, or the people just couldn't stand the furniture anymore so they bought furniture, or rebuilt the patio. I mean, that's a huge part of what's happened into an economy where we had underbuilt housing for 12 years because of the aftermath of The Great Recession. So huge demand, low supply, and I should also say people like my mother, who are 87, and maybe should have left their house, they weren't going to go to a multi-family facility in the middle of COVID. So the supply down, the demand up, that's why you've got the prices increase.

Tom Barkin:

I do think one of the direct things when you raise interest rates is you will affect demand for housing. Now, I'll tell you, one thing you're going to see is a move from fixed to variable rate housing mortgages. So, if mortgage rates go up too much, people are going to start using ARMs, not fixed rate. You just have to be careful because there is a mix shift that goes on, and people will go for a five-year fixed ARM or whatever. You'll remember that from the mid-2000s. I'm not suggesting that's the environment we want to go back to, so it'll affect the price of houses. I think that's a good ... I think housing prices have increased so much in the last two years it's a good idea to put a little dent on it, because if you don't do that we know what happens, right? People go crazy, and they start financing more and more, and more, and you end up in 2008, so this is one of those. I'm not saying take the punch bowl away, but I think we need to just stop spiking the punch.

Kking:

Thank you, Tom, very much for your response.

Tom Barkin:

No, no, good questions.

Lowell Yoder:

Until we get another question I'd like to ask another, and it has to do ... We all heard supply chain, right? I mean, whoever coined that term made a lot of money in the last six months or so. But I'm curious as a business owner or as a business person, banker, whatever, we manage risk, and you balance that with costs and things, so I'm curious, do you see a long-term change? Meaning that people will say, "You know what? It's a lot cheaper to get it from somewhere else, maybe overseas somewhere, but you know what? This whole supply chain thing makes me think about risk and cost maybe in a little different way. Maybe I should look for a more domestic source for my product. I'm going to pay more, it's probably inflationary, but the certainty of that product outweighs the risk of getting it." Do you see that, or is that not a ... will that fade away?

Tom Barkin:

Well, two thirds of it. So everybody's looking at their supply chain and saying, "Holy cow, I've been grinding out the costs for a generation, and I have been underthinking resiliency." Everybody now is thinking about resiliency in the supply chain in a fundamentally different way, how that plays out, depends on the business. But by and large you're seeing increases in inventory, because just in time now is a little bit, or it was a little too lean, so they're thinking hard about, "What are the key parts that are at risk, and how do we make sure we've got enough supply to do it?" Especially in a world that still is relatively low interest rate.

Tom Barkin:

The second thing we're seeing is one country sourcing. People are saying, "I got to have a more diverse supply because countries can get shut down through tariffs, countries can get shut down through war, countries can get shut down through pandemics so I got to have diversification in my sourcing." The third thing you're saying is, "I love China, it's efficient, it's low cost, but I can't be totally tethered to China." So people are asking themselves questions on China. It's hard though with China because, especially when it comes to manufacturing, they are so efficient because it's low labor cost, but also very productive. There's been a lot put into that, and so people are struggling with that, because as you suggest, it does cost you a little bit more to make out of some other place, but they're going, "I can't be totally dependent on China." Now, and I'd say freight is now being valued in a different way, ocean freight, what that means is the guy who's winning right now is Mexico, relatively low cost, relatively close, you can put it on a truck or even on rail, and your risks are significantly less.

Tom Barkin:

I talked to an apparel manufacturer today who was talking about Haiti, same kind of thing. The folks who aren't really winning yet is American manufacturing, and I think that's because if you can't find workers for your core business, what convinces you you can open up a plant and find a bunch of workers? So there are a lot ... There are some industries, obviously defense is already almost entirely US manufacturer. I think there's a good chance healthcare manufacturer, mass gowns, pharmaceuticals is going to massively come, ships, you see a little bit of it. But I just think until we can get to a place where we've got a surplus of labor, it's going to be hard to convince people to open up and go into an auction.

Lowell Yoder:

Very good. I see a couple of questions.

Gigi Godwin:

I see Ron up again. Board member Ron. Ron.

Ronald T. Piervincenzi:

Thank you, Gigi. Sorry, I saw Fizie pop up. So just real quick, just in a small world category, I was a Brad's DGLE back in the day, but that's not my question.

Tom Barkin:

Wait, wait, you were-

Ronald T. Piervincenzi:

My question-

Tom Barkin:

Whose DGLE?

Ronald T. Piervincenzi:

Brad's DGLE. DGL, sorry.

Tom Barkin:

No, no, you're Brad, which Brad?

Ronald T. Piervincenzi:

Your son Brad.

Tom Barkin:

Oh, no, no, my ... Oh, Brad Barkin, my cousin, sorry.

Ronald T. Piervincenzi:

Your cousin. Oh, sorry, I thought it was your son.

Tom Barkin:

No, no, no, ... Yeah, yeah, no, we're still in close touch. That's hilarious.

Ronald T. Piervincenzi:

Yeah, I know, small world. Just a simple question, you mentioned before about exports, and of course obviously the impact of inflation on exports, but of course, that also depends on what other banks are doing. I just wonder as USP as an exporter for most of our revenue, and of course others in county are, to what degree does it matter what other banks are going to be doing for export businesses from the US, and it's impact of rising rates and a stronger dollar?

Tom Barkin:

It's a great question because a lot of these things that work in theory, don't actually work in practice. You can announce you're raising interest rates and the dollar can go up, and the dollar go down, and that's of course because of a thousand things happening all at the same time, not least of which is flight-to-quality in the context of global tensions. So, we're raising the short end of the curve, but the long end of the curve isn't moving at all, and I think that has a lot to do with flight-to-quality. The dollar is not moving as much as you would think, same thing, I think people are putting money here for all those reasons.

Tom Barkin:

I think this inflation thing is quite global, or at least it's Western Europe, US quite broad, and so you're seeing prints in the UK, in Germany, a place that they haven't inflation since the 20s, and they do not want it, you're seeing prints that are quite inflationary in all those places. The places you're not seeing inflation, which are interesting, is Asia. Japan still is not over zero, China is still quite low, even though its PPI is high, Singapore, Hong Kong ... In our part of the world, you're seeing it everywhere, and so you're seeing central banks embarking on similar paths. So in my talk I controlled for all that, but I think in truth, what you're going to see is you're already seeing rates go up in the UK, and Canada. You'll see it going up in Europe a little bit behind us, but I think not far not behind us. You're not really seeing it in Japan. You're not really seeing it in Japan. It's an interesting dichotomy.

Juliet:

We have Fizie Haleem from Montgomery College.

Gigi Godwin:

I was just going to say, and then after Fizie, hi, Fizie, we have our board member David Nguyen too, so we can acknowledge him. Go ahead, Fizie.

Fizie Haleem:

Would you like David to go first? Okay. I just wanted to ask if you could comment on what's expected, or what we can expect regarding the construction industry? Right now, there are cranes going up, there's approximately 2 to 3 million square feet of biotech lab space, including biomanufacturing that's anticipated to come out of the ground or be developed in the very, very near future, that would put Montgomery County at a tremendous advantage because it's offering opportunities that the other four larger areas in the country may or may not have. So, from an education standpoint, I'm hoping that you could tell us, if all of this does come out of the ground or even a significant part. One, what's the possibility that there may be some lag, there may be some issue that the construction is going to face so that it may not happen in time, and how we can anticipate being able to bring the workforce into, I guess, productivity level at that point so that we can supply the companies that need to fill those spaces with the right workforce?

Tom Barkin:

Well, I'm not surprised, but you're right on the issue. Most of the COVID workforce conversation has been centered around either the lower income service sector workers, whose restaurants shut down, or hotels shut down, and who didn't want to wear a mask, and fear of COVID, and had kids they couldn't take care of, or retired, or those of us who are working from home and have gotten disattached from the workforce, and are going through the Great Resignation, and I think those stories missed, and I wrote an essay on this within the last couple weeks, I think a screaming issue in our economy, which is skilled trades. Now, skilled trades, you talked about construction, but I'd put nurses in there, I'd put manufacturing in there, I'd put truck drivers in there, they were all incredibly tight pre COVID. We did not have enough construction people pre COVID, but then, and by and large they haven't left the workforce, but what's happened is COVID just trunked up the demand.

Tom Barkin:

We talked about the housing market a second ago, but you could add all the warehouses that Amazon's, and others are building in e-commerce. Demand for construction is extremely strong. Demand for manufacturing is extremely strong. Traveling nurses right now are getting paid unbelievable amounts. No one can find a truck driver. So you've still got, by and large, the same number of people, but you don't have any growth in a context where demand is just booming, and so we got a problem there, and I'll call it a manufacturing problem. We have to manufacture more construction people. I don't think demand's going to drop anytime soon, same for manufacturing, same for nursing, same for truck drivers.

Tom Barkin:

Depressingly, and I don't know in your school what the situation is, but nationwide, for two years in a row, community colleges, which generally produce most of these folks, have had their enrollments decline. A little bit, I think, of that at the beginning was COVID, and distance learning, and it's not a really friendly kind of distance learning environment for skilled trades. But I think, it's also that the opportunity cost of going to school has increased, as entry level wages have increased. I've been to community colleges, I've talked to a bunch of individuals who tell me their friends aren't there because the job that used to pay $12 an hour now pays $17 an hour and they go, "Hey, I'm making 35,000 a year, I'll go to school sometime later." So, we do have a manufacturing problem, getting people into these programs, and then getting states, and getting clinical placements, getting certifications, getting licensing worked out so that we can get them employed, I think this is a crying need for the economy. I'm agreeing with you a 1000% without any good answers.

Tom Barkin:

The people who I think are doing the best job on this though, are taking on the pipeline issue with a whole life lens, using some of the stimulus money to not just pay tuition, but also provide childcare, and all the rest of the thing, transportation to get people there. Then I1 think companies outsourced the creation of a workforce to the schools, again, in the world where labor was long, and I am seeing companies adopt schools, and basically ... You know how it is, if you promise somebody a job, your odds of keeping them are much higher, and just working end to end there. I think it's an end to end manufacturing problem, and it is really, I think, the most important talent issue our workforce has right now.

Lowell Yoder:

David, please.

David Nguyen:

Hi, can you hear me?

Tom Barkin:

Yes.

David Nguyen:

Okay, wonderful. So you spoke about having alternatives for supply chain in logistics, but what about an alternative for the financial ecosystem as a whole with cryptocurrency? I think today the total global crypto market cap is about $1.93 trillion, and it looks like more money will continue to flow in it, and it's a very efficient way to move money globally. Do you see cryptocurrency as a threat to the dollar, or has that mindset shifted in some way?

Tom Barkin:

Well, I'll give you my point of view, but there are a lot of investors in cryptocurrency who have a different point of view, so I'll just warn you that in advance, and that would be [inaudible 00:50:28]. So, I think there's crypto as an asset, you talked about market cap, and then there's crypto as a currency. Crypto as an asset, I mean, it's an asset class, and assets are worth what someone else is willing to pay for it, and there are a lot of people who are willing to buy it. People see it as a somewhat diversified asset class versus a bunch of other asset classes, which right now don't look very attractive because of valuation, and a lot of people have made a lot of money in crypto as an asset.

Tom Barkin:

So, you get to make your own asset decisions. I'm not an investment advisor, the only thing I can say is there are lots of assets like that, gold, fine arts, baseball cards. I don't own a lot of fine arts, but if I owned it, and everybody else decided they no longer like the value, then I think I could still put it on the wall. You're highly dependent in a crypto investment, and everyone else thinking it has value because there's no wall to put it on, but that's crypto as an asset class.

Tom Barkin:

Crypto as a currency, your 1.93 trillion doesn't work on the currency, you have to look at transactions, and what the penetration is as a currency right now, which is just a knit on the dot of global currency transactions. We have a digital currency today. I've got $50 in my pocket, and I've got a lot more in my bank account. I use my bank account to pay all my bills, so I'm already in a digital currency of the dollars, so if I need to be in a different digital currency, then I guess I'm still trying to figure out why I would want to do that. Maybe you could convince me that the blockchain security model is a much more secure than my bank account, and that there are fraud issues in other places. People talk about international transactions, which I agree are inefficient, but there are probably other ways to make those efficient.

Tom Barkin:

People talk about accounts for all, everyone having their own account, which would ease stimulus payments, and other things, but of course, that then puts the banking system at risk, so you have to ask yourself how you feel about that. People talk about China having a digital currency, but you have to remember that China doesn't care about privacy in the same way that our country seems to, and crypto enables transaction inspection. I think you can look at all these things. I haven't yet seen the use case for me, other than if people really do end up deciding for whatever set of reasons, including fashion, that they want to use crypto as their medium of exchange, then I think the US government is going to have to say, "Well, we don't need other people creating a medium for exchange for us. We're going to make our own medium of exchange."

Tom Barkin:

If that happens, I'd just refer you back to the Wildcat currencies in the 1870s, where every state had its own currency, and eventually the Federal government said, "We're just going to use our currency." The one thing that didn't have value after the Federal government says, "We're going to use our currency," was the state currencies, so I think that's the issue. We can do it. We've figured out the technology of it. We can't quite figure out, "Do we want to do it?" There's cyber risk too if you do that kind of thing, but we could, but if somebody else is doing it, and it gets a lot of acceptance, then I think you just have to ask how that product competes against the US Federal government guaranteed currency.

David Nguyen:

What would happen if our adversaries, say Russia, China, all the countries that maybe not favor the US so much, decided to create their own blockchain because they don't ... because of our sanctions, and what we've done to them, if they then decide to create their own blockchain, and they move money much more efficiently through that blockchain, what will we do in response to that?

Tom Barkin:

Well, don't say yes. I mean, the dollar is the reserve currency that gives us great benefits, it's not an entitlement, it is the reserve currency because we have a great economy, because we have the rule of law, because we have very liquid market, because people want dollars. What we've done through sanctions, and you mentioned Russia, but I'll just talk about Iran for a second, is we've weaponized the reserve currency in ways that other countries don't like. When I was with my old firm in 2014 or '13, whatever, we had the height of the Iranian sanctions, I can tell you the European companies that I was exposed to, hated the fact that we could somehow put sanctions on Iran that prevented a German company from doing business with Iran. They just didn't ... they thought that was abrogation of their sovereignty.

Tom Barkin:

Mark Carney, who was then the Head of the Central Bank of the UK, gave a Jackson Hole speech in 2018 that basically said, "We hate the fact that you can put sanctions to control our economies and so," he was talking about Libra, "but we're going to come up with other models to do that." So I don't think it's ... I think that we have weaponized our status as the reserve currency, that will be sending countries into alternatives, and that will be sending obviously sanctioned countries, and competitor countries, but also ally countries into other currencies.

Tom Barkin:

I don't think crypto is the point there, I think sanctions are the point. I don't think there's a more efficient digital model that somehow beats our model from an efficiency standpoint, because we can duplicate it, but I do think that people don't like that we have weaponized the status of the reserve currency, and that's going to move people out of our currency. What's kept us alive frankly though, is there's no good alternative, and I'm not sure that third parties are going to buy into the Russia, China, one equivalent for all the reasons that are obvious, but could something else get created? Absolutely.

David Nguyen:

Thank you.

Lowell Yoder:

Tom, another question. I know we're coming up on our time slot that we have for you, but I'm curious, I know your district means a lot to you, so some of it's rural, some of it's urban, I'm just curious if you could just talk a little bit about, maybe some of the challenges that we see ... that you see in the rural parts of your district, and then the urban. I know there's the whole ... it seems like there's even a politically right, there's a pretty correlation between rural and urban. I'm just curious, from your perspective, what are the challenges there?

Tom Barkin:

Well, I think one of the fun things to think about actually is, people think of there being an urban-rural divide as a racial divide, as a political divide, but if you look at my district, South Carolina, North Carolina, Maryland, Virginia, the Eastern part is very rural, very poor, and largely black. The Western part is very rural, very poor and largely white. The difference between the former plantation areas in the ... Appalachia is quite striking. So, one of the reasons that I've gotten intrigued with it, is that economic performance in those areas, the rural areas, massively lags the urban areas.

Tom Barkin:

We have a mandate of full employment, maximum employment, and so you got to ask yourself the question, "What's going on there?" You know what's going on because it's been written about a lot, it's education, it's jobs leaving, it's isolation, and anchor institutions not being there. It's obesity and opioid addiction. All of those things are part of it, but I think it's really interesting to see places that are starting to make things work, particularly because ... Because of all the stimulus that was passed in the last two years, there's now funds available in ways that were never available before.

Tom Barkin:

We're doing a conference next week actually in Greensboro for small towns, try to imagine, and I'm giving a speech on this topic, but why can't we get this money deployed in the right place? Just talk about broadband, for example. Well, that makes sense, everyone today believes broadband is a big deal. If you put broadband everywhere in a small town, then people who wanted to live there and work somewhere else could do that, and you'd move out of this whole issue of the jobs have all left. Well, the deployment of broadband money is brutally difficult. I was talking to someone, I think Maryland's got one person in the state office trying to deploy all this money, which means it's going to take forever. The phone companies, obviously are making the right economic decisions for them by putting in the densest places first.

Tom Barkin:

Those grants that are being sent out require someone who can write a grant. The people who are deploying the money don't want to give it to somebody who's not capable, they're worried about having another [inaudible 00:59:23] public relations issue. The money disproportionately goes to the same few people, it doesn't go into the places where it's needed because they don't have the capacity to do it. So this question of how to create the capacity locally, which Lowell, your brother and I have spent a lot of time talking about that that's a real opportunity and need, and a place where you can go, "Okay. Well, it all makes sense why the money's not getting there." But it doesn't take that many grant writers to write a few good grants, to get some money in the right hands to go do some of the stuff. I think I like it because it's important, it's bipartisan, it's biracial, it's necessary, and I can start to see a little bit of how we could start to move the needle, which is something that gets me excited.

Lowell Yoder:

Very good. I don't know ... I know we're past our time, so I know you're a busy guy, I don't know if there's ... Gigi, if we want to take one last question, or Tom, if you have time for one last question.

Tom Barkin:

Sure.

Lowell Yoder:

Does anybody have one last question for Tom? I'm sure Gigi does. I've got a couple technical ones, but I'll save those banker types of questions, no one else wants to hear those, but please, anybody have a question? or Gigi?

Gigi Godwin:

A million more, but we'd be here all night. I'm looking forward to the next time that we get to see Tom so that we can explore, there are so many industry specific issues, there's just a lot going on in the world right now, and right here in our own community. I consider ourselves fortunate because we've got a lot of great things happening here in our business community, and in Montgomery County, and in Maryland, and the Greater Washington Region, and your entire territory for that matter.

Gigi Godwin:

We have been big proponents from an advocacy point of view on the greater deployment of broadband. We see it as hugely important to address all the issues you just mentioned. We see the advocacy piece there, but so much more to do, and there's so many more questions, but I do think we're at time, and we're grateful that we had so many board members and guests with us. As always, Tom, we love it when you can share your thoughts because the world's ever-changing, and it's good to find out what you're thinking as we're presented with new challenges and opportunities. So with that, I'm going to turn it back to you, Mr. Chairman.

Tom Barkin:

It's been great.

Lowell Yoder:

Thank you, Tom, greatly appreciate it, and we love that you're friends of the chamber because we're going to continue to ask for your involvement, so thank you. Thank you for everyone for attending, and good night.

Gigi Godwin:

Thanks everybody.