Fed Unfiltered, Transcript

9/8/22 – Jerome Powell, Interview: Cato Institute Monetary Conference

Jim Dorn:

I'm Jim Dorn, Vice President for Monetary Studies at the Cato Institute. Welcome to Cato's 40th Annual Monetary Conference. Pleasure to have you with us today. Our first conference, The Search for Stable Money, was held in January 1983. That search continues as we face the highest inflation in 40 years. A short time ago, the Fed was worried about hitting its 2% inflation target. In 2020, the Central Bank implemented a new monetary framework, Flexible Average Inflation Targeting. The idea was to make up for shortfalls by temporarily allowing inflation to exceed 2% while averaging 2% in the longer run. Yet, no specific timeframe was given. This flexibility increases uncertainty about the Fed's commitment to price stability.

Jim Dorn:

Until recently, the Fed's mantra in setting its policy rate was lower for longer, but forward guidance was often misguided. The Fed's macro models were unreliable, and forecasting errors eroded confidence in monetary policy making. The Fed initially saw inflation as transitory and was slow to increase its policy rate. However, the consensus has changed and the Fed has made it clear that rates will rise until inflation falls to a more normal level, even if the US faces a recession. Of course, the underlying problem with our current monetary regime is that too much is expected from policymakers. The limits of monetary policy are often forgotten. Moreover, there is no clear rule for guiding policy.

Jim Dorn:

Karl Brunner, who spoke at Cato's first Monetary Conference, pointed to the importance of rules in the conduct of monetary policy given the complexity of the real economy and the knowledge problem. According to Brunner, "We suffer neither under total ignorance nor do we enjoy full knowledge. A non-activist that is rules-based regime emerges under the circumstances as the safest strategy. It does not assure us that economic fluctuations will be avoided, but it will assure us that monetary policy does not impose additional uncertainties on the marketplace. With this large staff of economists and access to massive amounts of data, the Fed missed forecasting the 2008 financial crisis and missed warning signs of the current inflation." At a forum hosted by the ECB in June, Fed Chairman Jerome Powell stated, "We now understand better how little we understand about inflation."

Jim Dorn:

I hope today's conference will help shed light on the causes of inflation and provide positive lessons for improving monetary policy. Before moving to the... Harold J. Bowen, Jr. and DuVal Bowen Family Foundation for supporting today's event. I'd also like to thank Cato's excellent staff for helping with the conference, especially Nick Anthony and Kiana Graham as well as David Tassey and Jonathan Fields. Finally, thanks to all our speakers and moderators for taking time from your busy schedules to join us. Now, let's begin with Fed Chairman J. Powell and Peter Goettler, President and CEO of the Cato Institute. Thank you.

Peter Goettler:

Thanks, Jim. Good morning, everyone. As Jim said, I'm Peter Goettler. It's my honor and privilege to be President of the Cato Institute. Before proceeding, I want to offer my congratulations to you, Jim. Cato has been an important voice in the monetary realm for over four decades. While there are lots of people who've contributed to this, no one has contributed more to this work than our colleague, Jim Dorn. He's played a role, a large role as anyone. Jim inaugurated our Monetary Conference, and under his leadership, it's become an annual institution. Jim's presided over each of these conferences, including today's, which as he pointed out is our 40th. Following these past 40 years of service to Cato and our mission during which he also created and edited our Cato Journal, Jim will be retiring later this month and will assume the title of Senior Fellow [inaudible 00:04:31] at the institute.

Peter Goettler:

Jim, I just wanted to offer our heartfelt thanks for your many contributions, one of the longest tenured employees in Cato's history, and I offer you best wishes for fruitful and enjoyable retirement. I know you'll continue to make your voice heard in the policy debates and in the policy world, but I also hope you reserve plenty of time to enjoy your wonderful family.

Peter Goettler:

Now, let's turn to our 40th Annual Monetary Conference. My honor and pleasure to welcome Fed Chair Jerome Powell to the conference along with Alan Greenspan and Ben Bernanke who's now the third chair of the Federal Reserve Board of Governors to address the conference. Jerome Powell was first appointed as chair in 2018, and then reappointed this past spring. He's no stranger to the Fed. Prior to his time as chair, he served as a member of the Board of Governors starting just over 10 years ago.

Jim Dorn:

That is okay.

Peter Goettler:

The one certainty that seems to come with the position of Fed Chair is that one will invariably face a time of great challenge. Paul Volcker confronted our last and worst bout of inflation. Alan Greenspan saw the stock market crash a mere two months after his confirmation, and Ben Bernanke led the Federal Reserve amidst the financial crisis of 2007 and 2008. Chairman Powell, as we all know, has served throughout the COVID-19 pandemic and its aftermath, a period in which we've seen inflation reach its highest level in 40 years.

Peter Goettler:

As we've sat in front of Zoom screens over the past two and a half years, I'll just speak for myself, many of us have watched as our hairs turned grayer, but few of us have as good an excuse for this as Chairman Powell. We're delighted to have him with us today and have a conversation about key policy issues, what he's learning, and the challenges now facing the Fed. Chairman Powell, it's good to see you today, sir. Welcome.

Jerome Powell:

Thank you very much, Peter, and thank you to... Go ahead.

Peter Goettler:

I don't think it's a failure of imagination on my part nor do I believe anyone will be surprised if the first topic we turn to is inflation. As Jim mentioned, it seems policymakers were given... including at the Fed, were initially given a bit of a head fake on inflation. We heard policymakers ascribing the increase in price inflation to the pandemic and related supply disruptions. While this has undoubtedly contributed, there seems a much stronger consensus now that it's been in larger part policy bill. Can you discuss for us or give us some insight into how your thinking evolved on this topic over the last year and a half, and how those conclusions may have evolved as well?

Jerome Powell:

So, Peter, thank you. Jim, thank you, and congratulations to both of you and to Cato on 40 years of great monetary policy conferences. So I think a good entry point for that question, Peter, is to start by recalling that before the pandemic, unemployment was at a 50-year low, inflation was low and stable, and the economy was growing stable... sorry, steadily with no obvious imbalances threatening continued expansion. So, of course, in that sense, none of this high inflation that we see around the world now would've happened without the pandemic. The pandemic severely disrupted the economy, gave rise to risks of much more dire economic consequences, then actually transpired, really, and that was thanks in part to the policy response.

Jerome Powell:

So, to start with policy. There's no question that policy certainly supported strong demand, but in my view, you would not have seen anything like the inflation that we have seen without the pandemic effects, and those pandemic effects include both shifts in demand and also playing a role in, not solely causing, but playing a role in the supply side constraints that emerged. So, as for the pandemic, it did lead directly to an extraordinary shift in demand away from in-person services and to goods, and that shift, of course, was a major contributor to inflation in goods' prices, which was really the main inflation story at the very beginning when inflation broke out suddenly in March of 2021. It's worth remembering that inflation actually declined in the early stage of the pandemic, and then suddenly rose up in March of '21.

Jerome Powell:

The pandemic also contributed to constrained supply in a number of important ways, including a large and persistent reduction in the size of labor force, which contributed to extremely tight labor market conditions and upward pressure on wages. Also, the turmoil in global supply chain was probably caused by, to some extent, by pandemic-related shutdowns as well as strong demand and particularly goods demand. I think cars are a good example. So, yes, people had money, and rates were low, and demand for cars was strong, but also, the pandemic shifted demand upward for cars because some people wanted to avoid public transportation. That amped up new demand, demand for new and used cars, and also, the shortage of semiconductors for cars emerged from pandemic-related demand shifts as well. So the bottom line for me is that there's really a role for both here, and the two were tangled up in a way that it's really not easy to disentangle.

Peter Goettler:

Those of us who grew up in the '70s, I think that the danger and cost of inflation can't be exaggerated. In September 1979, his first testimony a month after he was confirmed, Paul Volcker made clear he understood that the damage that was being caused by inflation and the need to bring it down, even if it required great costs in other economic ways. One of the lessons of that episode was the greater the extent to which inflation slips the leash, the higher the cost and greater economic damage necessary to bring it under control.

Peter Goettler:

I worry whether we have the resolve to bring inflation under control today to face the potential economic costs. I took some comfort from your recent remarks in Jackson Hall, which seemed an attempt to signal that kind of resolve, but I do remain concerned that the intense political pressure that might be brought to bear to avoid collateral economic damage before the inflation fight is long, and I just wondered if there's any way you can help me sleep a little bit better on that score.

Jerome Powell:

Sure. So I think it's worth going back and remembering... and I pointed this out in my remarks last two weeks ago at Jackson Hall, 10 days ago, that what Paul Volcker did and the Fed did to finally get inflation under control followed several failed attempts to get inflation under control. What had happened over the course of that long period of the Great Inflation is that the public had really come to think of higher inflation as the norm and to expect it to continue, and that's what made it so hard to get inflation down in that case. So it is very much our view, in my view that we need to act now forthrightly strongly as we have been doing, and we need to keep at it until the job is done to avoid that. We think we can avoid the very high social costs that Paul Volcker and the Fed had to bring into play in order to get inflation back down and set us up then for a long period of price stability.

Jerome Powell:

That speech, the point really there was to deliver a speech that was narrowly focused on inflation more direct and a lot shorter than a typical Jackson Hall speech, and I thought that what was appropriate was a very concise and focused message to your question. The message really was that the Fed has and accepts responsibility for price stability by which we mean 2% inflation over time. Again, to your question, the longer inflation remains well above target, the greater the risk that the public does begin to see higher inflation as the norm, and that has the capacity to really raise the costs of getting inflation down.

Jerome Powell:

So, finally, history cautions strongly against prematurely loosening policy. I can assure you that my colleagues and I are strongly committed to this project, and we will keep at it until the job is done. I can also assure you that we never take into consideration external political considerations. We are accountable to the public through Congress. That's a very fundamental, important aspect of our work, but we focus solely on the goals that Congress has given us, and that's what we're going to do here.

Peter Goettler:

I think that that's really important because it's clear that we could see political pressure coming to avoid economic costs when there could be claims from political players that inflation is back in its box long before it is. Jim mentioned in his opening remarks that two years ago, you moved to a new framework, Flexible Average Inflation Targeting, and I'm bringing this up now because, again, just reiterating the point about trying to sleep better at night. By many accounts, this move has created some more uncertainty in the market, as you mentioned, and coming at a time when inflation now has increased remarkably. It creates concern that despite your stated resolve, the commitment to price stability has become less strong. Should you consider modifications to this framework that weighs these concerns and better manage short-term expectations?

Jerome Powell:

So, the framework. We began the work on the new framework in 2018, and we announced the results in August of 2020, and it really followed 25 years, basically, of global disinflationary forces. The problem was that monetary policy rates were close to the effect of lower bound much too much of the time, much too close, and even during good time. So that meant that central banks were having a hard time all over the world finding ways to support the economy when it was needed, and that's why central banks, including the Fed, resorted to things like forward guidance and asset purchases.

Jerome Powell:

So that's why we did that, but the changes that we made were a very mainstream part of a literature around makeup strategies. But really, the point of our framework changes. The point of all of them was to... and we said this very clearly, was to have inflation expectations well-anchored at 2%. The average inflation targeting idea was meant to support having inflation expectations. That is the goal at 2%, and the reason is that we believe that the public's expectations of future inflation will play an important role in the actual path of inflation. So that is the fundamental basis of our framework.

Jerome Powell:

As I just discussed, it is very important that inflation expectations remain anchored. I think the evidence today is that if you look at longer term expectations by households, businesses, and forecasters, and also markets, you'll see that they are pretty well-anchored around 2%. Of course, short-term expectations are higher because of high current inflation, and also, the clock is ticking. As I mentioned, the longer that inflation remains well above target, the greater the concern that the public will start to just naturally incorporate higher inflation into its economic decision-making. Our job is to make sure that doesn't happen, and we're committed to doing that job.

Peter Goettler:

It seems to me there's a chance that the... There's a real risk that the labor shortages persist. Does that create a risk that takes some of the ability to manage this process out of your hands to the extent that there continue to be labor shortages? Does that then feed into expectations that the public has about inflation as you've mentioned very prominently?

Jerome Powell:

Well, I think you're right that if it does turn out that we are in a world of a persistent labor shortage over time, that will be a challenging world for companies, and it will certainly create upper pressure on wages and that sort of thing. Today, the labor market is... demand is very, very strong still in the labor market. We're still printing new payroll job numbers at a high level. Wages are running at elevated levels. So we think by our policy interventions, what we hope to achieve is a period of growth below trend, which will cause the labor market to get back into better balance, and then that will bring wages back down to levels that are more consistent with 2% inflation over time. That's what we're trying to achieve.

Jerome Powell:

The shock to labor supply that we got from the pandemic was large, and unexpected, and unfortunately, persistent. I will say that just in the very last labor market report that we got last Friday, we did see a welcomed increase in labor force participation. Nonetheless, it's still a full percentage point below where it was before the crisis. I think it's important as a society that we have measures in place to support a strong labor market and high labor force participation, and that goes beyond what we can accomplish with monetary policy.

Peter Goettler:

You've made some contrast to how things are different today, what's different today from the high inflationary period of the late '70s and early '80s. I guess some other distinctions are... I remember as a student in Boston in the early '80s in the days before the internet, I remember seeing people actually line up at the Fidelity office to see the monetary aggregates released on a weekly basis. The way the money travels through the economy has changed dramatically since Milton Friedman first said that inflation is always and everywhere a monetary phenomenon. I'm just wondering. How do you respond when people look to the huge spike in government spending and say... I think you answered this in part in the first question, but when you look at the huge spike in spending and say, "The Fed printed all this money, so of course, we have inflation?"

Jerome Powell:

So, I too graduated from college in 1975, which was close to peak monetarism, and there was quite a focus on monetary aggregates. I recall it just as you do. So to go to this current situation, so as part of our response to the pandemic, we did resort to large asset purchases to address what were pretty severe disruptions in markets, and then also to support the economy, and our balance sheet expanded dramatically. But remember that our purchases of securities don't actually increase the quantity of government obligations held by the public. They really changed the mix because we issue bank reserves to pay for those securities. So we're not changing the quantity of obligations.

Jerome Powell:

That is not to say that that money growth wasn't high. It was, of course, extraordinarily high in 2020, and then slowed down in '21. Now, it's quite sluggish. I guess I would just say it this way. There are different theories on what caused the inflation that so suddenly jumped up out of the ground in March of 2021. Whatever that cause was, the relationship between the money supply and inflation economic output has been much more unstable than it was in Friedman's day for a very long time.

Jerome Powell:

So, literally, changes in monetary aggregates have not had a consistent reliable relationship. They haven't been a good predictor of the economy or of inflation. Now, of course, the economy is ever-changing, and that too could change to where it is important again. But for now and for really many years now, monetary aggregates don't play an important role in our formulation of policy, and we don't think they're generally a good way to think about policy or about inflation. It's more about demand and supply, and things like that. So that's where we would be on that.

Peter Goettler:

That actually cause the mind... At Cato, we do have a strong aversion to a fully discretionary fiat money system, and so we do like to socialize and promote alternative frameworks like good policy and a market direction that eliminates some of this discretion. Jim mentioned that consistent theme over the years with this conference has been potential monetary rules, and that calls into question whether inflation and prices are really the best targets to use for monetary policy. Some folks have advocated for rules-based systems such as... Targeting nominal GDP is something we've heard a lot about in recent years partly because as you say, monetary policy is not suited to address, well-suited to address supply shocks.

Could you share with us some of your thoughts of that type of approach and whether it's something that you would consider?

Jerome Powell:

So more broadly on rules. Of course, Taylor rules have become part of the fabric of economic analysis, particularly monetary policy analysis in ways that must be far greater than John Taylor could have hoped when he wrote his original article in 1993. But we know central bank and the Fed has never explicitly tied our monetary policy decisions to any formula, including Taylor rules, but Taylor rules, nonetheless, are ubiquitous in all of the work that we do. You have to have a variant or a way and a model of explaining how monetary policy will react in some kind of Taylor rule is now... They're very much part of the way we think in terms of nominal income targeting.

Jerome Powell:

By the way, I know that Cato is one of the home courts for nominal income targeting along with Mercatus and some others, and I know that this is a... A lot of well-known experts, many of them at your institution do support nominal income targeting, and I'll just say that we've looked at that. I've looked at that and really come to the view that nominal income targeting is not the right way to go, and I'll try to explain why. By the way, I know that these arguments are well-known to nominal income targeters and will be found to be unpersuasive. But nonetheless, I'll just give you my...

Peter Goettler:

Yeah, yeah. One thing I would interject is that we have debates internally as well, and I think for us, the concept really is more wanting to socialize a number of alternatives and try to move towards alternatives that do have more of a market basis, and again, remove discretion to some...

Jerome Powell:

I think that's a very healthy process, and the whole debate over many, many years about rules and discretion is a fascinating and important one that is far from over. So it's really a mix of the two, I think, but getting to nominal income targeting. We've got a dual mandate, maximum employment and price stability, and it comes down to, "Is nominal income targeting the best way to promote that?" We don't think it is. I don't really think it is, and part of that just is that would be, I think, very difficult to explain to the public the relationship of a nominal income target, nominal GDP target to those goals. It's a level of complexity that even some economists and policymakers struggle with, let alone the general public. So it seems like it would be a reach for us to have that be our fundamental framework.

Jerome Powell:

A couple of examples that would be difficult. One in particular would be what do you do with changes in trend growth? We have highly uncertain estimates of levels of trend growth that we amend down through the years, and many years later, we may have very different view, but it is broadly understood, I think, or believed, thought that that trend growth has declined consistent or considerably rather over the course of the last... well, since the global financial crisis. So how do you incorporate that into a nominal income target? Do you just raise the contribution of inflation, or do you annually re-estimate trend growth?

Jerome Powell:

If you do that, you're incorporating both communications issues, but also, just big chances of policy error because we just don't know these things with that kind of... We don't know any of the starred variables, so to speak, with that level of certainty. So I'll just say it's really interesting, and it works very well in models, but it seems difficult to implement from a practical standpoint, and it's not something that we have chosen to do or that we are currently looking at.

Peter Goettler:

You mentioned the dual mandate. I don't want to ignore the unemployment rate during this conversation. When I said earlier that we obviously have an aversion to a fully discretionary monetary system, many of us also regret the adoption of the dual mandate in lieu of a strict focus on monetary stability. The Fed Zone website acknowledges that maximum employment is driven mainly by non-monetary factors. If we accept that, does it really make sense for employment to be part of the Fed's mandate?

Jerome Powell:

So, Peter, as you know, we're created by Congress in statute, and Congress assigns our goals, and it has assigned maximum employment and price stability. It's my view that the dual mandate has served the public well and is generally workable. In particular, at the moment, I don't see the two goals as in conflict at all because without price stability, we will not be able to achieve the kind of strong labor market that we want for a sustained period that benefits all. So I don't see a case for moving to a single mandate, but that's really a question for Congress, and we will, of course, implement whatever mandate Congress gives us.

Jerome Powell:

To your point about maximum employment, it's true, and we do say that and have for some time that non-monetary factors are really what drives the level of maximum employment, which clearly changes through the business cycle and over time, but we can and do assess that, and we do a transparency, and Congress has said that should be a goal, a co-equal goal with price stability. So that's what we're implementing. Again, I don't think there's a strong case for changing that. I don't think it hampers us in our pursuit, and I think we can achieve both goals in the medium-term.

Peter Goettler:

You stole my follow-up because you blurted it out saying Congress sets the mandate, and so my follow-up was going to be, "Well, should they consider changing the mandate?" I think you've answered that, but I guess a natural follow-up might be then, if the dual mandate weren't enough, there's been talk of adding more elements to the Fed's objectives, including racial equity that steam far from the Fed's ability to address. In addition, the Fed's remit has expanded from the banking system to the broader financial system, and its regulatory responsibilities were widely expanded in the wake of the financial crisis. How does continue expanding the Fed's mandates not undermine focus on that fundamental responsibility of monetary stability beyond things such as that the employment element of the mandate?

Jerome Powell:

So I think our current mandate is appropriate, and I would not want to see it narrowed or broadened for that matter. We've got narrow and we've got well-defined goals that we're supposed to pursue, and what we get with that, what we've gotten with that is a precious grant of independence that lets us pursue those goals without direct political control. For monetary policy, that's maximum employment and price stability, and I think that dual mandate has served the public well. I really don't think it would not be a good idea to broaden it to goals that might be inconsistent with those two mandates, and that would be very difficult for us to achieve with our tools.

Jerome Powell:

More broadly than that though, I think it's really important that we stick to our assigned tasks and resist the temptation to take on issues that are the province of elected representatives or of Congress. If we do that, if we do stray from our core mandates, that will eventually undermine the case for our remaining independent. I think Fed independence is an institutional arrangement that has served the public well, and I think that's pretty well-documented and accepted.

Peter Goettler:

I mentioned a couple of times our concern about a fully discretionary system, and one of the biggest of those concerns is that in the face of large economic dislocations, we've been running what really amount to unprecedented experiments. I would cite the quadrupling of the Fed's balance sheet in the wake of the 2008 financial crisis, and then doubling it again during the pandemic. To your credit, it was right before the pandemic that you were beginning to move towards reducing the balance sheet. Could you shed some light for us on where you hope to take the balance sheet over time, and what's the way that you really, really try to get there? Do you see the Fed ever moving back to a scarce reserve framework like it had before the 2008 crisis?

Jerome Powell:

Sure. So, in the last cycle, after we ended our asset purchases, we froze the size of the balance sheet in 2014, and then allowed it to shrink passively relative to the size of the economy for about three years. So, as the economy grew, the balance sheet didn't grow. Then, in 2017, we began to allow maturing assets to run off, and that process went on till 2019. By the end of that period, we had a balance sheet that was significantly smaller relative to the size of the economy and smaller than it was overall. So then, we resumed asset purchases, as you know, 2020. Once again, now, we are embarked on shrinking the balance sheet, and the test will be back to levels that satisfy the public's demand for our liabilities. That's currency, and reserves, and things like that, but also with reserves maintained at levels that are consistent with our ample reserves regime.

Jerome Powell:

So the balance sheet is substantially larger now, obviously, and consequently, the runoff process is designed to be substantially faster in the last cycle to the tune of... on the order of a trillion dollars of runoff per year. That process began in June... once it's up to full speed. Process began in June, and the pace of the balance sheet increases. Actually, it rises this month. The plans are spelled out in detail on our website around the January and May meetings. Of course, one thing we always say is that we're prepared to adjust the details of the plan based on economic and market developments at any time.

Jerome Powell:

As far as returning to a scarce reserve regime, I guess I would say that I think that our current operating framework is a better one, and I don't see a case for returning to scarce reserves. Now, why is that? So the world has really changed as a result of the global financial crisis and the pandemic. The scarce reserves framework would be challenged to work in a world where there's very high and sometimes volatile demand for safe and liquid assets. Central banks may need to rely on large-scale asset purchases again from time to time in response to severe shocks, and remember that the large financial institutions hold very, very large quantities of safe assets now as a liquidity buffer, and that includes a lot of reserves. So the bottom line is that the quantity of reserves is just so much higher, it would seem to be impractical to try to manage scarcity, and demand will be volatile too. So it doesn't seem practical, and again, we think that the current system works well and provides a lot of liquidity to the system, which is a net gain.

Peter Goettler:

All right. I thought it might be time to shift gears a little bit away from inflation and monetary policy. I remember in the first year I joined Cato, I read an op-ed in The Wall Street Journal advocating for the Fed to implement a digital currency, and I was kind of horrified at the privacy implications of the prospect and said so in a letter to the editor at that time. Since then, the Fed has formally stepped into the digital currency ring, and digital currency has obviously been a very recurring theme in these conferences, but the Fed has stepped into this arena with a discussion paper on a central bank digital currency and several speeches from Fed governors.

Peter Goettler:

Our team has reviewed the more than 2,000 comments that the Fed's central bank digital currency discussion paper received, and we find that about two-thirds of them are concerned or outright opposed to the idea. Commenters raised concerns of financial privacy, financial oppression, and disintermitting the bank system. Some of the same concerns that led me to write that letter to the editor seven years ago. How can these serious concerns about privacy and freedom be reconciled with a digital currency?

Jerome Powell:

Let me start by saying that we haven't made any decisions at all about whether to issue a CBDC, and we continue to evaluate the pros and cons, and look at the technical questions and the policy questions, and we expect that evaluation process is going to take some time appropriately so. Secondly, I'll say that we do not intend to proceed with issuance of a CBDC without clear support from both the executive branch and from Congress, ideally, in the form of a specific authorizing law.

Jerome Powell:

So we did get, it was very gratifying, 2,000 and some comments. I won't tell you that I've read those, but I've read... all of them, but I've read some of them, and I've read the summaries, and it's very... a lot of very thoughtful concerns, including the ones that you raised, and there are things that we're considering very seriously. So, in our own paper, we suggested that a CBDC in our jurisdiction should be privacy protected, intermediated, widely transferable, and identity verified.

Jerome Powell:

So, on privacy protection, let's start with that. Very, very important. We all see what's happening with the digital R&D and the issues with privacy. We would not want a world in which the government sees in real-time every money transfer that anyone makes with a CBDC. That would not be something that would be at all attractive in the American context. So privacy protection is going to be extremely important, and we're attentive to striking a balance, of course, between law enforcement and privacy protection, but that can be managed in the same way that it's currently managed in the banking system or in some similar way.

Jerome Powell:

Another issue, really, is disintermediation, and that really is a question of... Say you had an interest bearing CBDC. It could be attractive. It could compete with deposits. It could draw deposits out of the banking system. That could limit credit availability. That's another issue to be managed. I think one of the things that actually that Cato mentioned in your... was also the run risk issue, and that is the question of, "Are you creating an asset that would be very attractive in a panic or severe stress situation and fostering runs?"

Jerome Powell:

So, look. It's going to be, as I mentioned, it's going to be... We think our role is this. We want to carefully and thoroughly analyze the public policy and technological challenges, public policy trade-offs and technological challenges. That's what we're doing. The idea is that this will lead all of us to a better understanding of those trade-offs and prepare the way for, hopefully, a well-informed decision on whether and when to issue a dollar central bank digital currency. That's what we think our role is, and we think that the Fed is the right institution to do that. We can proceed without... We're a nonpartisan institution, non-political institution that can do these things and I hope present conclusions and analysis that will support an intelligent decision when it's time to make that.

Peter Goettler:

Well, this is something we'll definitely be having a lot to say on in the future as well completely, some perspective of privacy and privacy concerns that's being [inaudible 00:37:29] those issues. It has a very important role for it in Cato. I do want to ask about cryptocurrency, but first, I should probably, in fairness, reveal that the gentleman who photo-bombed Janet Yellen five years ago by holding up a "Buy Bitcoin" sign behind her during her Humphrey-Hawkins testimony earlier this year became my son-in-law.

Peter Goettler:

So that's a little bit of disclaimer I'm going to put out there. But without debating the merits or future of cryptocurrencies generally or one or another crypto products, I'll say that in the monetary arena, Cato stands for nothing if not a desire to see more interest in monetary policy, to see more people concerned about our discretionary fiat system. Also, we want to see private market innovation and experimentation in developing alternatives, and crypto is just such a great example of this. There's a long history of government and regulation thwarting such innovation and experimentation, which we find really disappointing. So I wonder if you could respond to these kinds of concerns, namely that regulators might ultimately stand with crypto to the extent that it really does develop into a viable alternative system.

Jerome Powell:

So I'll talk about it in two pieces. One is unbacked cryptocurrencies as such, and those have not offered and don't appear to offer much in the way of public interest in using them as payments, let's say. It's not a great store of value. What it is, is it's a speculative asset. It's not backed by anything, so...

Peter Goettler:

It could be an argument that's still during the development phase and that it's something that we could see emerge, but be as it may.

Jerome Powell:

Yes, and I also have close in family members who offer that perspective vigorously. So, as you suggest, but stablecoin is a different thing. The question is, are there forms of private money like stablecoin which can play a role in our financial system which would... and the answer is of course, we don't want to stand in the way of appropriate innovation, particularly including digital innovation, but we think that something like that which is purporting to be money would need to be appropriately regulated.

Jerome Powell:

I hear that wide agreement on that, by the way, from a lot of the stablecoin companies now are seeing that as part of getting to a place where they are a legitimate part of the financial system. So I think you need regulation. If people are going to think something is money, then it needs to actually have the qualities of money. If it doesn't, then I don't think you want to take money and make it into just another consumer product where sometimes it fails and sometimes it's good. You want it to be guaranteed to be good. If the public is going to look at it was a dollar, you want to have clarity, transparency. You want to have full reserves of very liquid, high-quality assets, and things like that. That's all.

Jerome Powell:

I think that we need legislation on this. It's typical of technological innovations. There isn't a regulatory framework that really gets after payment stablecoins, and so I think that's what's needed, but I wouldn't think of us as being opposed to that kind of innovation. We're more the people who are saying among others that we need appropriate regulation.

Peter Goettler:

Mm-hmm. Yeah, and it doubles ultimately in the details. While we have these debates, I mean, we would concede we're living in a world where we will see innovation, and we've basically promoted a light touch, market-focused approach because there is a real risk of, again, having an impact on the development of these innovations and really thwarting what could be very promising, promising and useful innovation.

Jerome Powell:

No, and I agree with that. We don't want to be in that place. We want to be in favor of innovation, but also appropriate regulation.

Peter Goettler:

Mm-hmm, and ultimately, some of the people who end up driving the regulation might be, as you mentioned, legislation. The end product may not meet the objectives that you and I both say that we want. Another topic. As long as I can remember, successful [inaudible 00:42:11] have warned of our unsustainable fiscal path. Regrettably known in Congress, the White House, that we should be listening. Particularly during a period of high inflation, I've been continually chagrin that the number of big spending bills that continue to come down the pike and legislation that's passed long after, I think, the crisis of the pandemic has ended.

Peter Goettler:

The lessons of the financial crisis in COVID might be that keeping our fiscal laws in order is essential as preparation to meet the challenges of unexpected, but inevitable economic dislocations. But the opposite lessons seems to have been learned that we can keep spending whatever we wish without worrying about a day of reckoning. I'm very concerned about the day of reckoning and what risks we're laying for the economic wellbeing of future generations, and I just wonder your thoughts on those concerns and the potential timing of that day's arrival and its consequences, and whether you have any ideas about how we can build a real constituency for fiscal responsibility in America.

Jerome Powell:

So I do share those concerns in effect. I was working on those issues before I joined the Fed, but at the Fed, my position needs to be that fiscal policy really is the responsibility of Congress and the administration. It wouldn't be appropriate for me to comment too much on specific policy proposals or laws, more to the point with inflation running so far above 2%. This is probably an especially good time to focus on achieving our own mandate rather than doling out advice to others. But like my predecessors, I'll point out that our federal fiscal policy is not on a sustainable path, and it really hasn't been for some time, and we will need to get back to a sustainable path sooner or later. To your point, sooner is better than later, and I guess I'll just leave it at that.

Peter Goettler:

All right. Thanks. We're getting close to the end of our time, so I'm thinking about a closing question. I wonder, with everything that we've discussed thus far, what are some of the key lessons that you've learned since you became Fed Chair, and what advice might you give to a lot of the young monetary scholars out there that Cato and other places are working to develop?

Jerome Powell:

So I guess I would say that both experience and also studying history are great teachers of what can be hard lessons. I actually mentioned three lessons at Jackson Hall 10 days ago, and those were, first, that the Fed does have and accept responsibility for price stability. Even now, some are questioning that, but that to us is settled. Secondly, that inflation expectations are really important and need to be carefully monitored because if they do move up, they can make the job of getting back to price stability so much harder. Third is that the record is... There's a record of failed attempts to get inflation under control, which only raises the ultimate cost to society of getting under control, hence the need to do this job now and keep at it. So those are three lessons.

Jerome Powell:

I would say more broadly, another really fundamental lesson to me is that the structure of the economy is ever-changing and highly complex. We see that today around the world. Many nations are experiencing the first high inflation in 40 years all around the world. Different countries have different composition and backstories, but it's really quite global. The question really is, is this going to be a temporary thing that's really related to the pandemic in some way, or is there actually something more structural and persistent happening?

Jerome Powell:

For example, if we're moving to a world where we're going to see more frequent, larger, and more persistent supply shocks for whatever reason, that will have critical and difficult implications for the conduct of economic policy and monetary policy in particular. So this is not possible to know right now, but it's certainly a question that looms. I mean, to me, to sum it up, I would just say economics is not physics. There isn't any specific temperature at which the economy boils over. It does boil over from time to time, and when that happens, it often takes many years of analysis, discussion, and debate to reach general agreement on why that has happened.

Jerome Powell:

So the point is that we are always making monetary policy under high uncertainty about the structure of the economy and the path ahead. That makes our work challenging. It also makes it getting it right very important for the people that we serve, and we do think about that every day. So our understanding of the economy has to evolve. As the economy evolves as time passes, we do learn more, and I think it's okay to follow the evidence and change one's mind. I think an advice to scholars, young and old, is that people shouldn't be afraid to say that they've changed their view and explain why. I actually find that refreshing when people say, "My view has evolved in the face of the evidence."

Jerome Powell:

I guess one more word to close for those young researchers you mentioned, and this is a commercial for public service and for the Fed. So the Fed is a very special place where people can combine policy research with policy making. This is a place that has... All of us have a very strong sense of mission in our work, which is very satisfying, and that mission is to serve the public. It really matters. Our work really matters to the public. I would say there's no higher calling when we're satisfying mission. So I hope that young researchers, and economists, and others will consider public service as part of their career. For me, it's been only a part, but in particular, consider working at the Fed where you'd be most welcome.

Peter Goettler:

Thanks for that. I mean, I share those sentiments. You mentioned your work at the Bipartisan Research Center. I'm at Cato because I care about the future of our country and the future, of course, of liberty and freedom in America and for the kind of world future generations are going to grow up in and whether they're going to have the same opportunities that we all have had to live in a free country and to pursue their American dream. Being part of that is a real privilege.

Peter Goettler:

At Cato, we work very hard to raise consciousness of monetary policy and the potential for monetary reform. We think this is a very important topic and that more Americans should pay attention to it, even though it's complicated. We wish there were more policy organizations that would prioritize this policy area and raise their level of resources dedicated to this area.

Peter Goettler:

As you know, Mr. Chairman, Cato is not shy about being critical, and we enjoy intellectually jousting with you and your team, but we also recognize that we share common goals and objectives for our country and the country's best interests by which that jousting and those debates in areas of disagreements. It's within that context that they occur. So I do thank you for your work. You're in a challenging position, and I thank you very much for being part of this conference today. It's been a real pleasure.

Jerome Powell:

Thanks, Peter. The pleasure is mine, too.

Peter Goettler:

Thanks so much. With that, I'm just going to let all the viewers know that we're going to be taking a break now until the top of the hour. So we're going to reconvene with the next panel at 10:00 AM. So we'll see you then. Chairman Powell, thanks very much again. Have a great day.

Jerome Powell:

My pleasure. You, too.