Kyla:

Hey, everybody, my name's Kyla. Welcome to my channel by talking about the stock market and the economy amongst other things. I had the incredible opportunity to interview Mary Daly, the president and CEO of the San Francisco Fed, about the Fed's policy decision making path. And we really talked about the generational impact, the impact that all of this has on wealth disparity, and talked a lot about the world that we're going into.

This is a really unique time. We all know that. I talked extensively about the Federal Reserve and the concept of raising rates, shrinking the balance sheet in order to fight inflation and the consequences that those policy decisions have because people are the economy. The economy is just a bunch of people. People lean around, and it's really important to keep people in mind when making policy decisions.

We discuss all that in more wealth disparity, generational impacts, lessons that the Fed has learned, the concept of data dependency and lagged metrics, as well as the ties between fiscal and monetary policy.

Hi, Mary, it's so great to have you here today to talk about the Fed and lessons from the past and looking forward to the future. I'm really excited to chat with you.

Mary Daly:

I'm delighted to be here, so thanks for having me on.

Kyla:

I wanted to talk about your background to begin with because it is unique from other Fed members. It's a unique background in general. So can you talk about where you've come from and how you think about how that influences how you're making policy today?

Mary Daly:

Sure, and I think about this a lot, largely because we're in a period of time right now when we have high inflation, and that was something happening during some of my formative years. So I grew up in Baldwin, Missouri, and in a family that was in the lower to low moderate income, depending on how you score it. And in my parlance growing up, we just lived very close to the edge, and we were just so many American families be then and today.

We were one lost job, one health event away from falling through. And so we had both of those in my family, my parents had both, and suddenly, we've lost everything. My parents went from figuring out how to pay the bills on a card table because inflation was so high, losing their jobs and I dropped out of school to help out. So I dropped out when I was 15 and I worked.

And at that point, my big aspiration was to, instead of having three part-time jobs and no benefits, was to find a way to get a bus driving job because I saw on the bus that I was taking that you could get benefits with that and you'd be part of a union. So that affected me, I think I didn't really have a sense that I would ever work at the Fed. I frankly didn't know what the Fed was at that point.

But I did know this, that people need both jobs. I needed both a job, and I needed prices to stay stable because I was just on some sort of a treadmill where I was trying to earn enough to put gas in my car and I ended up putting in $2 increments so that I could work, get paid and put more gas in my car. It was this constant battle of trying to earn enough to keep up and then always falling behind.

Kyla:

And I think a lot of people now are in a similar situation where there's concerns about how they're going to pay rent, concerns about how they're going to afford their grocery bills. Can you talk a little bit about how the Fed, and I know this is something you focused extensively on, but how the Fed is thinking about the wealth disparity and the impact that these monetary policy decisions have on that?

Mary Daly:

What I really start from is this, that we always have disparities. We have disparities in wages, in income, in consumption, and of course, in wealth. And what the pandemic did is made them all worse. So the pandemic comes and the people least able to bear it lose their jobs, they lose wages, they lose income, they lose wealth. And the people who could work from home and had jobs that weren't so in person contact, who tend to be over the median wage and above, they're stuck at home, but they're not losing their lives and livelihoods.

And so the pandemic widened the inequalities. So now we find ourselves in a world where we have high inflation. And here's the first thing that I think is really important to recognize is high inflation is what we would call a regressive tax. It is affecting the most, the very people who are the most affected by the pandemic and the very people who suffer from inequality already. So it's hitting those who are at least able to bear it.

Now, the good news about the economy we have right now is that the job growth in those sectors of the world is really good. And if you look at different groups, the people who are usually the most affected are actually doing well. It looks like a strong expansion on the labor market terms. So Fed policy, what I think about is, you know what? We have got to keep our commitment to people to ensure that they have not just that job, but also price stability.

A fact that I'll share with you because I find it stunning, I think about it every day. So if you look at wage growth, you might think, "Oh, it's a great time to be a worker." Nominal wages are rising. People have jobs they can choose from. Average real wages in the United States, average real wages, the ones that are adjusted for inflation are falling 9% over the last two years.

So in other words, you're going to work, you're making a living and you're falling behind every single day. And if you looked at the data disaggregated, you'd find that really tilts to the lower end. So right now, because of inflation, disparities are growing in wages, income, consumption, and wealth.

And so what Fed policy does is raise the interest rate, slow the economy, and we know that a long and durable expansion narrows wage gaps, narrows income gaps, narrows consumption gaps, but of course, raises wealth gaps. And that has little to do with the Fed policy directly and everything to do with when an economy grows, assets rise in value. And we in the United States do not have an equal distribution of asset holdings.

Those at the bottom and the middle of the income distribution just don't hold very many assets. They might have a house, but they don't usually participate in the stock market or other things. And so that is just one of the realities you learn to live with in the central banking is the things you do to improve wages, income, consumption gaps actually hurt wealth gaps.

And I just think of it this way, because I talked to so many people and I realized this basically, I knew it for my own life. You can't actually acquire an asset if you don't have wages, income. And so that's the starting point. So I think of the Fed's policy as foundational to wealth accumulation, and then we have to think about society's ways where we can equalize their wealth distribution through asset holdings.

Kyla:

And that's something that's incredibly hard to fix. I think it's the top 1% owned, 50% in the stocks, in the housing market is also a nightmare to a certain extent. And I think that goes into my next question, which is about the generational impact of all of this.

So a lot of young people just live through a pandemic. They maybe lost their job then, they maybe just got back to their job now, and the Fed maintaining credibility with this younger generation is really important, right?

Mary Daly:

It is.

Kyla:

So how are you thinking about that and thinking about the ... I don't mean to keep on pointing to the impact of policy, but really the impact of policy on the younger generation and maintaining credibility with them?

Mary Daly:

I'm so glad you asked me that question because I talked to a lot of young people and whether they're Gen Z, Gen X, millennials, I have a little chart, a generational chart so I can figure out what all the groups are because I want to know who I'm talking to and how people describe them or they describe themselves. But here's what I know.

You start with millennials and you go down in the generational groups. Individuals coming in who are really suspicious, and I think rightly so, that they're not going to get the kind of opportunities that their parents have. It is our job, frankly, as older individuals and Fed officials as part of that is to try our best to pass along a better future than the one we inherited so that people coming after us can do other things and don't have to worry that they're going to fall behind their parents, not rise above their parents in terms of economic security and other things that are important to people.

So right now, all young people are really priced onto the housing market, and unless you're really at the top of the wage distribution, it's terribly difficult to get a house. But that was true before we started raising interest rates. I was in Boise, Idaho. They have the nine Western states since I'm in Boise, Idaho, and it's thriving, it looks great.

First time home buyers including young people, they have almost no chance to buy a home in that community because it is too expensive, too frothy. Inflation is too high, and they're paying so much more money for their food, gas, and rent that there's not a real great opportunity to save. So when I think about getting inflation down, I think of just that, that the cost to millennials and all other younger generations and everybody of not getting inflation down is there is no starting point. There is no sustainable path for the economy.

And then you're in a place where you're working hard and you can't catch up. You cannot get enough to save and to do the things that you deserve to be able to do if you're a young person, which is, think about buying a home, think about doing other, building your career. But right now, it's just a treadmill of trying to catch up because inflation is eroding the real wage.

Kyla:

I wanted to ask another question on top of that, because a lot of what I do is economic explainers. And when I talk about, well, a lot of what's being done now is so the future is better. Well, it's like, well, I want things to be good now. I don't want the labor market to suffer now. So how do you think the best way to explain that trade-off to people is?

Mary Daly:

So instead of thinking about a trade-off, and so this is how I do it, maybe it'll be helpful. I don't think of it as a trade-off because you know what people don't want? Inflation or jobs, or jobs or inflation. They want low and stable prices and a job. And so I always look through that lens. I think of it as a singular goal, price stability and full employment. And so when I look at the labor market right now, we have a historically strong labor market. Unemployment is 3.5%.

I just met with ... I spent my entire week this week meeting with business leaders, community leaders, worker groups. This is just a lot of what we do across the entire nine Western states. And I heard again and again and again that people have job opportunities. And even when big tech firms, for instance, announce that they're going to stop hiring and then many get laid off, there are firms right there waiting to capture all of those individuals.

So the job market is strong. People have even opportunities to negotiate where they work and what kind of wages they want, et cetera. What's problematic is that you can't keep up with inflation. So I think of that as, it's not like the world is perfect right now. We're in trouble right now. Inflation is eroding the very thing we told people they could have, which is if you work hard and you do all these things and you have a great career and great job, you'll be able to do things like purchase a home, go on vacation, build a savings, and have children, whatever it is you want to do. And those things have all been made harder by the fact that inflation is so high, you're just trying to keep up.

So I don't think of it as pain now for greatness later. I think of it as there is pain now and we need to get it lowered so that we can be on a sustainable path, give people both of what they want, job opportunities and low and stable prices and let everyone, young people, middle people, older people, get back to the business of living and working and building careers.

Kyla:

I think everyone is on board with that for sure. And I am curious, I feel like there's been a lot of lessons learned by everybody the past couple of years. But the Fed especially, just the meme is inflation is transitory. Obviously that didn't end up being the case, and nobody knew that at the time. But I'm curious how the Fed is taking the lessons learned from the past and applying them towards future policy decisions.

Mary Daly:

So the thing you have to know if you're a central banker is you're always learning. It's a daily experience because ... I have the sticker. I actually wanted to find one for you. I left them all up. I've given them all away up to make another run of them. But I made the sticker because when I first started as president, someone asked me, what does it take to be a policymaker? And I was in a big group of young people, college students, and I said, "It really takes three skills, and then you have to continually repeat them every single day."

You have to be voraciously curious, and you have to look at yourself and learn every possible thing you can about the data, looking forward, talking to people. Then we have to take a decision about what we're going to do on policy eight times a year. So you have to be confident that you've done your job and you've looked with great curiosity and you be confident and take that decision. And then immediately upon doing it, you have to be humble, that there's more to learn and that there's more things that will evolve that you have to pay attention to.

So I just am in, I guess one would call it, a rinse and repeat cycle in a positive way. I just do that all the time. And I think that's what the Feds done. So what is the Fed learning? Well, we're learning a lot of things. We're learning about the fact that supply chains have just been very sluggish to recover. You might, in a standard economics model, you think that prices go up and supply responds. That's actually not happening in the way that we're accustomed to because of COVID, because of the war in Ukraine, because of uncertainty in the economy more generally. And so supply chains have been very sluggish.

The other thing we've learned is that demand is incredibly resilient. There's a lot of, and still you see a pent up need to reengage with our lives after being shut away for two years. And I think that hunger to be part of this has kept demand high on top of supply. And when demand is too high and supply is too low, they don't match, we have inflation. And so the big thing that we have to do now, of course, is bring that down with our tools. So we have the tools to do it and just be resolute to get that back down so that we have an economy that's in balance.

But I do think we learn every day, and if people learn nothing else from this, the Fed is sort of a, what is this phrase that sometimes leadership people use? It's growth mindset. If you don't have a growth mindset, you can't be in central banking because it's a humbling experience, but one you have to do because it's an honor and it's a responsibility to serve.

Kyla:

Thank you for doing it. And in terms of thinking about what the Fed is looking at from a data point perspective and using the rather blunt tool of raising rates, a lot of data points are lagged and the Fed is pretty focused on being data dependent. So how do you think about parsing out that lag and the data as well as being focused on data?

Mary Daly:

Well, that's a great question, and I think it maybe requires us to ... I mean, this is how I think of data. The data is not just quantifiable things that look at yesterday's information. We have a lot of published data that is backward looking. We need those data because we need to see what the trends are. We need the historical evidence. We need the models, all the analysis about those. But that's part of it. That would be incomplete if we simply stop there. We have to be forward looking.

Well, we can be forward looking both by looking at quantitative data. There's a lot of leading indicators and forward looking indicators. But here's the best data source you can have about what's happening and what's going to start happening is you talk to people. That's why I said I spent my whole week talking to our boards, our councils, from all different walks of life, from all different parts of the district. I talked to business leaders and small business. I had a CEO round table of small businesses.

That information, those piece of information, those are data. And those data tell me not just what they were doing last month, which is the published data would show me, but what they're planning on doing as we go forward. And they help me understand the lags in monetary policy, the risk of over tightening, where we are, what is likely to slow in the economy, what's likely to keep going, where they're worried, where they see the risks. And you put those things together and then policy becomes more complete and its ability to make it not only for today, but for the future.

Kyla:

Now, we've seen a lot of market fundamentalism, and I think the United Kingdom is a great example of that where a mini budget was proposed from a fiscal policy side and markets were like absolutely not. And so you saw gilt yields soar, you saw the pound sell off. How do you think about the relationship between fiscal and monetary policy?

Obviously the central bank is meant to be independent, but sometimes they have to be interlinked, especially in terms of fighting inflation. So I guess that's sort of a two-part question, the interlinkage between fiscal and monetary policy and where fiscal policy can step in more here, if at all.

Mary Daly:

Sure. So I think the way ... Well, let me just say the way I think about it is they're not interlinked, but we live in the same economy. So the Federal Reserve, like most well-functioning central banks across the globe is an independent entity. And it's separate from the fiscal agents, but we have a very narrow goal. So Congress says you're independent. You don't have to be beholden to any particular political pressure, but you don't have very many tools. You have one tool and you have the goals we gave you, which is sustainable growth using full employment and price stability as your methods of achieving that.

So that's our place. So that means that we react to the economy we're given, whether that's a pandemic economy or a strong economy. We're adjusting our policy to ensure that we get sustainable growth, price stability, full employment under the conditions we have. So what you're seeing in this world is that with inflation really high, everyone is really uncertain, very uncertain about what is the Fed going to do, what are other central banks going to do. The fiscal side of the house tries to figure out their own remedies.

And I will just offer, there's a lot of work for all of us. So about half of the inflation we see in the United States, the excess inflation is related to demand. And there's a lot of research on this, but the San Francisco Fed publishes our outcomes each month, the data are released and shows about 50% of the inflation is related to demand, excess demand, and about 50% is related to limited supply. So that means the Fed's got 50% of the work of the high inflation to solve on its own, and we're not done yet. So we have a lot of work to do.

And in the meantime, the fiscal side of the house, our elected officials are obviously thinking about what they want to do to help ensure that supply can recover more quickly. The final thing I'll say on that though is the other part that you didn't really mention but is true, I think you alluded to it, is we live in a global economy. So even if we solve our supply issues and our demand issues, there are supply issues in the global economy and tremendous amount of uncertainty.

So we're living in the global economy where we have a domestic mandate to achieve one part, full employment and price stability. And that means that be Fed actually is, we look at the economy we have and we build towards the economy we want. And that's just how we do our work.

Kyla:

Well, I have a million more questions around the dollar, everything that you just said, but we are unfortunately out of time. But thank you so much for joining me here today and talking about all the work that the Fed is doing, and thank you for doing the work. This has been a great conversation.

Mary Daly:

Well, I look forward to coming back sometime. There's so much to talk about. So I hope to see you again soon.

Kyla:

Thank you.

So that was Mary Daly, president and CEO of the San Francisco Fed. I think the main thing is that the Fed is really focused on maintaining trust, on maintaining credibility. As I've said a couple times, the Fed's toolkit is rates, the balance sheet, but also talking, being out there in the community, letting people know what's going on and why things are happening the way that they are. And of course, policy decisions are not without consequence, and that's a conversation that could go on and on and on.

I hope that you all are doing well. Thanks so much for listening, and I will talk to you all soon. Bye.