WEBVTT

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00:05:22.860 --> 00:05:33.990
Markus Brunnermeier: Thanks you. Thank you for joining. Welcome back everybody to another, Webinar, organized by Princeton for one worldwide. We are very happy to have a right semester with us from the grief, and that the president of the

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00:05:34.520 --> 00:05:36.830
Loretta Mester: Hi Mark. It's glad to be with you

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00:05:37.160 --> 00:05:43.000
Markus Brunnermeier: to have you and Loretta will talk about a diligent return to Price stability,

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00:05:43.110 --> 00:06:01.970
Markus Brunnermeier: and we will have a little introduction, and then I will announce the pool. On this you gave us so thanks for participating. And then we have a discussion, after all, of this presentation about the various topics and the topics we want to cover. Among other things, about talking about inflation anchor. Is it wobbly or not?

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00:06:02.110 --> 00:06:08.110
Markus Brunnermeier: What about the labor market? We have a very tight labor market, but you know Gdp output cap is less dramatic

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00:06:08.180 --> 00:06:25.780
Markus Brunnermeier: then about monetary policy, of course. Um! And talking about the real interest rate, you know we hiked a lot. The enumerated into it. How much does the real into it go up quantitative tightening and the flexible average inflation targeting framework that we good, turning to the flexible average inflation targeting framework or not.

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00:06:25.840 --> 00:06:34.359
Markus Brunnermeier: Let me talk about the physical and monitoring the action, and also, perhaps at the end. If there's time a little bit about the international impact of the Us. Monetary policy.

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00:06:34.650 --> 00:06:38.490
Markus Brunnermeier: So let me jump directly to the poll questions.

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00:06:38.840 --> 00:07:04.799
Markus Brunnermeier: So the poll questions we asked you, and you answered very nicely. The first question was, If the inflation anchor breaks, will

it predict smoothly or continuously, or will it break discontinuously? So? That means, if once you lose inflation, and it's very hard to putting it back, and actually twenty-seven percent that it's smoothly or continuously, and seventy-five or seventy-three percent that it's discontinuous

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00:07:04.810 --> 00:07:16.860
Markus Brunnermeier: the second topic is on the labor market tightness is, why, say, labor markets will type this it a temporary phenomenon? Because labor productivity is actually went down. Is it a temporary thing That's a

11
00:07:17.380 --> 00:07:18.760
Markus Brunnermeier: what? The

12
00:07:22.420 --> 00:07:30.039
Markus Brunnermeier: what? Thirty, six percent thought was a permanent decline in labor market productivity? That's what seventeen percent thought.

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00:07:30.050 --> 00:07:53.620
Markus Brunnermeier: And was it a change in workers preferences working from home. And you know, workers have a total of different preferences. We have to figure out how they'll be against our production processes. That's what forty-seven percent thought. So the majority actually almost fifty percent said, It's a change in workers preferences and then it has different implications for welfare. You know, even if it's less productive, they get perhaps more pleasure, more welfare out of that.

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00:07:54.100 --> 00:08:11.559
Markus Brunnermeier: Certainly The third question was about monitoring policy. Where will be aimed to go to. Once we go back to a lower inflation environment, we'll be going back to two percent inflation and target. Or do we go back to a flexible average inflation targeting framework as the fed announced in August two thousand and twenty

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00:08:11.690 --> 00:08:16.140
Markus Brunnermeier: and so fifty-seven percent that we're going back to two percent inflation

16
00:08:16.170 --> 00:08:26.949
Markus Brunnermeier: and uh twenty-six percent said, We go to back to flexible average inflation targeting, or we going back to a framework where there's a higher inflation target than two that's what seventeen percent thought.

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00:08:27.110 --> 00:08:57.080
Markus Brunnermeier: And finally, about the fiscal application, What is thriving monetary policy, fiscal and monetary, the interaction, And to what extent will the inflation reduction act really impact inflation and lower inflation. And actually, you know, only twenty-three percent that inflation reduction act might be much more about environmental policies and industrial

18
00:08:57.090 --> 00:09:07.999
Markus Brunnermeier: erez agmoni still policy, then actually about inflation itself. So with this opening remarks, and I reaction how people think in the audience are the audience things I will pause on the

19
00:09:08.580 --> 00:09:21.500
Markus Brunnermeier: uh, this, the floor with the digital floor to Loretta, who will explain to us. It gives on a little bit of an outlook of the economy, and you know what the thinking is at the Fmc. And what the fair is thinking

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00:09:21.510 --> 00:09:33.319
Markus Brunnermeier: how to bring inflation back down. And we saw today's numbers. It's coming down at least a little bit uh, but hopefully it will go down the system, it back to two percent in a very smooth way.

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00:09:33.480 --> 00:09:38.080
Markus Brunnermeier: Thanks a lot to be looking forward to your uh presentation now.

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00:09:38.100 --> 00:10:00.950
Loretta Mester: Well, thanks, Marcus. I I really um. It's real honor to be here. I listen to your webcast. So it's really a treat for me to actually be on the webcast today. So I I really like the invitation. And although you said i'm going to explain the thinking of the Fomc. I just want to let people know that i'm presenting my own views. Not necessarily those the Federal Reserve system, or my colleagues in the Federal Open Market Committee.

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00:10:00.960 --> 00:10:17.799
Loretta Mester: But I will explain some of the what we've done our in our policy decisions um to date. So last week we met um, and we raised the target range of the fed funds rate by another seventy-five basis points and the range now is three and three quarter to four percent

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00:10:17.810 --> 00:10:32.250
Loretta Mester: um, And we also indicated that we anticipate that we're going to have ongoing increases in the target range. Um, in order to

attain a monetary policy stance that's sufficiently restricted to return inflation to two percent.

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00:10:32.260 --> 00:10:39.549
Loretta Mester: And you know, if you look at the level and persistence of inflation, that journey back to two percent inflation is is likely going to take some time.

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00:10:40.050 --> 00:10:58.909
Loretta Mester: Um! The other thing we're doing at the fmc is we're continuing the process of reducing the size of our balance sheet by allowing assets to roll off, and that also helps to firm the stance of monetary policy. So what I thought I do is I share a couple of slides um to walk through um

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00:10:58.920 --> 00:11:02.100
Loretta Mester: kind of the outlook, and perhaps uh

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00:11:02.520 --> 00:11:04.570
this will be helpful for people

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00:11:04.970 --> 00:11:08.230
Loretta Mester: to sort of understand kind of where we're coming from.

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00:11:08.280 --> 00:11:10.280
So let's see if that worked.

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00:11:11.110 --> 00:11:14.530
Markus Brunnermeier: Um, Can people see those

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00:11:14.780 --> 00:11:22.550
Loretta Mester: Okay, So right last week was the fourth seventy-five basis point increase in as many meetings,

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00:11:22.560 --> 00:11:40.449
Loretta Mester: and then the funds rate target is now three hundred and seventy-five basis points higher than it was at the start of the year. So compared to history, that's a pretty rapid pace of increases in our policy rate. But I I also want to sort of put that in concept, because, compared to history, the economy is experiencing really high

34
00:11:40.460 --> 00:11:42.930
Loretta Mester: and really persistent inflation,

35
00:11:42.960 --> 00:11:56.139
Loretta Mester: and the real policy rate is just beginning to move into restrictive territory. Um, of course there's more than just the Fed Funds rate that matters for the economy. If you look at overall financial conditions there

36
00:11:56.150 --> 00:12:07.799
Loretta Mester: tighter than at the start of the year. Treasury yields mortgage rates, credit spreads, they're all higher. The dollars appreciated, and equity prices are lower. So

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00:12:07.960 --> 00:12:18.650
Loretta Mester: you know, if you look at inflation, though it's unacceptably high. Um! And that persistent inflation that high inflation is the key challenge facing our economy,

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00:12:18.930 --> 00:12:38.260
Loretta Mester: inflation rates still at forty year highs. If you look at the pc inflation rate, which is what we, the Fed's goal is set, measured by measured year every year in September, Um Pc. Inflation was still running over six percent core. Pc. Was um over five percent.

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00:12:38.270 --> 00:12:47.669
Loretta Mester: The meeting and trimming measures so that we like to look at those, because our goal was headline inflation, of course. But we like to look at these meeting and trimming measures.

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00:12:47.680 --> 00:13:00.720
Loretta Mester: Um, which exclude components with the most extreme movements each month they they give you a better sense of where inflation is going, that underlying trend and in in inflation they tell a similar story of persistently high inflation.

41
00:13:01.750 --> 00:13:03.020
Loretta Mester: Now

42
00:13:03.130 --> 00:13:20.820
Loretta Mester: there are some positive signs. One of them is that the three month changes in underlying inflation measures. So that's what I'm showing here. Um! They are lower now than they were in June. Um, although, you know, if you have to look at the level, the level is quite above where we we need inflation to be

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00:13:20.830 --> 00:13:30.199

Loretta Mester: There's other positive signs, commodity prices, and moved down goods. Inflation has begun to ease, and then this morning we got the October Cpi report.

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00:13:30.210 --> 00:13:45.639
Loretta Mester: Um, which is another inflation measure that we look at, of course, and that suggests some easing in the overall core inflation measures. You know the Cleveland Fed produces the Median Cpi series um in the trimming series, and they also confirm that

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00:13:45.650 --> 00:13:58.849
Loretta Mester: there's been some easing um in inflation last month, so That's the positive side. On the other hand, services inflation which tends to be sticky has not really shown signs of slowing.

46
00:13:58.860 --> 00:14:12.359
Loretta Mester: Um, and in addition, inflation continues to be broad based. So if you look at the September Pce inflation report, the prices of about half of the items that people buy were at least five percent higher

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00:14:12.370 --> 00:14:32.269
Loretta Mester: than they were a year ago, and that share we haven't seen much improvement in that share. So that's that's an issue. Because if if you think about inflation. It's really hard, um for people in lower income households who tend to spend a larger share of their income on essentials like food, shelter and energy

48
00:14:32.280 --> 00:14:33.440
Loretta Mester: and

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00:14:33.450 --> 00:14:52.979
Loretta Mester: the double whammy there is that those components have also seen some of the largest price increases, So they're spending a larger share of their of their pocketbook on things that have seen very high inflation rates. Now,

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00:14:52.990 --> 00:14:58.729
Markus Brunnermeier: is it because of the energy prizes primarily, or is it generally true that the Pc. Inflation is leading the others.

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00:14:59.190 --> 00:15:13.999
Loretta Mester: Well, we get the date on Cpi first, and then we get Pc. Inflation. But in terms of underlying trends we like the Pc. Inflation at the fed as our. And we use that as our uh inflation target, because it's broader based

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00:15:14.010 --> 00:15:27.809
Loretta Mester: um. It allows for substitutability as people buy different things. And so that's kind of why we want that to be our our target. But we do look at all the other inflation measures, because again they're all it contain important signals

53
00:15:27.820 --> 00:15:35.719
Loretta Mester: about where underlying inflation is going. They do contain noise sometimes right so energy and food prices can be

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00:15:35.730 --> 00:15:54.609
Loretta Mester: tend to be volatile. So that's why core measures we look at, because it takes those out, and those trimming and medium measures that take out the the components that have the biggest and lowest price increases every month. Those are an important information, too. So again, it's a signal extraction problem. You have a bunch of data.

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00:15:54.620 --> 00:16:18.380
Loretta Mester: Um, And you have anecdotal reports from businesses as well that we talk to routinely. That gives us a sense of where inflation is and where it's going. And, as I said right now, the levels are still very high, some positive news in the most recent data. But now we're near uh what we need to see, to really be confident that inflation is moving down back to two percent.

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00:16:18.390 --> 00:16:19.610
Loretta Mester: So

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00:16:19.920 --> 00:16:25.230
Loretta Mester: again, if we really want inflation to fall, and we do in order for that to happen.

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00:16:25.240 --> 00:16:44.139
Loretta Mester: There's gonna be need to be further slowing in both product and labor markets, and that will help bring the demand in those markets into better balance with supply, and that'll help alleviate those price pressures we've been seeing. So we are beginning to see demand and product markets slowing. Um if you look at um,

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00:16:44.150 --> 00:17:01.289
Loretta Mester: the Gdp report um, you know real output contracted in the first half of the year. We saw it grow again in the third quarter. But if you look at final sales to private domestic purchases that was essentially flat, so that gives you a a pretty good idea about domestic demand.

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00:17:01.360 --> 00:17:15.290
Loretta Mester: Consumer spending slowed in the third quarter. Residential investment fell significantly, and of course, that really is reflective of the the sharp increase in mortgage rates. We've seen um this year.

61
00:17:15.300 --> 00:17:32.479
Loretta Mester: Now, equipment spending grew at a pretty healthy pace in the third quarter. Um! But if you look at again, we have to look forward. We only only look backwards. If you look at the new orders indexes from the Ism and Um, the regional fed manufacturing surveys,

62
00:17:32.490 --> 00:17:46.629
Loretta Mester: they indicate that equipment spending is likely to slow in coming months, so that shows that demand is slowing on the supply side. Um! There has been improvement in supplier delivery times and anecdotal reports

63
00:17:46.640 --> 00:18:02.530
Loretta Mester: from business context tell us that you know there's we're seeing some welcome easing and supply bottlenecks. They're still there, and they're still challenging but there has been some easing in those bottlenecks, so on balance, I do expect real Gdp growth to be well below trend

64
00:18:02.550 --> 00:18:04.719
Loretta Mester: this year and next year.

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00:18:05.170 --> 00:18:16.049
Loretta Mester: Now there's also been some uh slight, I would say moderation and labor market conditions, but overall the labor market remains tight.

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00:18:16.410 --> 00:18:34.330
Loretta Mester: If you look at job gains, they've slowed to an average about two hundred and ninety thousand per month over the past three months. Compared to about five hundred and forty thousand per month of the same period a year ago, and if you look at job openings, they are lower than they were in March.

67
00:18:34.980 --> 00:18:46.589
Loretta Mester: But still we have almost two openings for unemployed persons, and if you go back to another period twenty, nineteen, we had very tight labor markets. To. It was a strong labor market

68
00:18:46.600 --> 00:18:59.710
Loretta Mester: that the current openings for unemployed person is a lot higher at almost two compared to one point, two back in two thousand and nineteen. So again another signal that this market is the labor market still tight.

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00:19:00.210 --> 00:19:04.480
Loretta Mester: So even though we've seen slowing and out the growth um

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00:19:04.600 --> 00:19:22.209
Loretta Mester: business contacts or telling us something that is very interesting one. They they can't find workers they need. So, even though growth is slowing, they continue to want to find more workers. Um! And you can see that I think unemploy rate is at three point seven. It's still very low

71
00:19:22.220 --> 00:19:33.779
Loretta Mester: by historical standards, and some of our um businesses are really saying like, even if growth continues to slow. We're going to try to hold on to our workers as long as we can, because it was just so

72
00:19:33.970 --> 00:19:40.949
Loretta Mester: difficult to find, and to retain workers over the past two years, so that that suggests that. Um

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00:19:41.280 --> 00:19:49.020
Loretta Mester: I the kind of so call that labor boarding. We might see firms keep more people on their payrolls. Um! As the economy slows.

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00:19:49.030 --> 00:20:02.820
Loretta Mester: Now, another sign that labor demand is outpacing labor supply is the strong wage growth we're seeing. So if you look at the year over your growth rate of the employment cost index um, that's five percent

75
00:20:02.830 --> 00:20:16.320
Loretta Mester: um, and that's well above the level consistent with um price stability based on estimates of trend productivity growth. So, Marcus, your question at the beginning and the call is interesting to find out why you know. Why is it seem that? Uh,

76
00:20:16.330 --> 00:20:38.720
Loretta Mester: what's going on in the labor market? Perhaps it's a permanent shock to productivity growth, perhaps just a temporary one? I mean people like I. I like to look at. The three month changes um,

because year every year it's a good smooth series. But if you want to see turning points. You can look at that. I know there is um something made of the fact that the last data point last quarter moved down,

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00:20:38.730 --> 00:20:43.639
Loretta Mester: but I don't see that this is really saying that we're seeing much using it in wages yet.

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00:20:44.150 --> 00:21:00.800
Loretta Mester: So you know, My own view is that you know, even though growth is slowing. Um! And there's some, perhaps moderation in in the strong labor market conditions. Um! There continues to be upside risk to the inflation forecast that we're facing

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00:21:00.810 --> 00:21:10.839
Loretta Mester: um the war. Russia's war against Ukraine um is continuing that I mean gas and energy prices move higher again this winter next winter,

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00:21:10.850 --> 00:21:26.269
Loretta Mester: um, and I have to say I you know it's hard to forget. I remain very aware of the fact that Iconos forecast. The private sector forecast. The Fmc's forecast is revealed in the scp. The summary of economic projections in my own forecast

81
00:21:26.280 --> 00:21:39.779
Loretta Mester: have been underestimating uh the level of inflation, and it's persistent for almost two years. So again, you know, if I look at sort of where the balance or risks are, I think there's upside risks to the inflation forecast

82
00:21:40.190 --> 00:21:54.209
Markus Brunnermeier: you. Did you also look at the within the labor sectors? You know the blue colors was white color, this session coming up, and you see for a long time, our first time a wage compression to some extent that actually

83
00:21:54.220 --> 00:22:11.219
Loretta Mester: low-income workers, we just go up more than he in can we uh what? This? Yeah, that's exactly right. Yeah, We did see that. Um: Partly It's the nature of the pandemic shock. Right? So the type of shock impacted different sectors. And then, when the economy reopened

84
00:22:11.230 --> 00:22:15.379
Loretta Mester: right, those sectors that were hard hit, like if you think about um

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00:22:15.390 --> 00:22:32.589
Loretta Mester: hospitality workers right? When that demand came back it was pinned up demand, and there was a a real strong desire to get people back to work in those sectors that had lost a lot of workers. And So you saw the wages adjust. So you're right. We, you know we when we are doing the analysis we do dealt down.

86
00:22:32.600 --> 00:22:40.690
Loretta Mester: Um I to look at those components but overall, I would say that these wage data Don't suggest to me that we're gonna that we're seeing

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00:22:40.710 --> 00:22:49.119
Loretta Mester: anything on the wage side that suggests that the labor market isn't tight, i'd say this is confirming evidence that it's tight. So

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00:22:49.130 --> 00:23:05.939
Loretta Mester: So again I think there's upside risk to the inflation forecast. But despite the upside risks. I do think we're going to see. Inflation began to slow, meaningful next year um in the following year, and then reach. Come Come back to our two percent goal in two thousand and twenty-five. And that's because

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00:23:05.950 --> 00:23:22.979
Loretta Mester: the Fmc. Really is strongly committed to returning the economy to price to building. So, you know I titled the talk diligent. We're going to be diligent and making that happen, and that means we're going to proceed with care. But also be conscientious in doing that. Um. So one of the things that's helpful

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00:23:22.990 --> 00:23:39.019
Loretta Mester: is um. The behavior of long longer term inflation expectations. So the fact that those near term expectations have risen significantly with actual inflation. That's typically what you see. They have gone in recent months. Um,

91
00:23:39.210 --> 00:23:53.909
Loretta Mester: because what also, you see is that they move around a lot with sailing prices like gasoline prices. Gasoline prices have come down so near term inflation expectations to come down, but they're quite a bit above our target. I mean, with all these measures,

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00:23:54.100 --> 00:24:02.549

Loretta Mester: what you when you look at inflation expectations over the longer term, they've risen less right? So they've been rest less responsive to data.

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00:24:02.700 --> 00:24:16.769
Loretta Mester: Um, And that, I think, reflects the Fmc's commitment right? They they the credibility of our commitment to bringing inflation back down. So if you look at these measures, you know there's you know some of the measures didn't go up

94
00:24:16.780 --> 00:24:30.759
Loretta Mester: right from lower level, seen, you know, pre pandemic. So that is a concern, but they're reasonably well anchored at levels consistent with our goal. Um and the and the why that's important is that that should hope to lower inflation

95
00:24:30.770 --> 00:24:36.860
Loretta Mester: right if we can keep those anchor right. That helps lower inflation without as large. It was slow down in activity.

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00:24:37.190 --> 00:24:38.350
Loretta Mester: So

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00:24:38.400 --> 00:24:48.490
Loretta Mester: you know, in despite this sort of reasonably well anchored, I don't think we should take anchoring for granted, because the longer actual inflation

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00:24:48.630 --> 00:24:52.399
Loretta Mester: and near term inflation expectations remain elevated,

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00:24:52.420 --> 00:25:10.940
Loretta Mester: the greater the risk that longer term inflation, expectations become an anchored, and that would mean that high inflation would really permeate wage and price setting behavior and investment decisions, and then in turn, that would make it much more costly to return to inflation to our goals. So it's really critical that

100
00:25:10.950 --> 00:25:19.390
Loretta Mester: we set our policy to maintain that that anchoring of those inflation expectations. So you know,

101
00:25:19.520 --> 00:25:35.180
Loretta Mester: we at the Fed started um moving rates up expeditiously this year. Um! We started from a very accommodated sense of policy. Um.

And now we're basically at the start of a stand that's becoming restrictive. So

102
00:25:35.190 --> 00:25:53.929
Loretta Mester: the focus when we were well below um. A neutral policy, you know. The focus has been on. How quickly can we get to that neutral restrictive stance? Now the focus can shift to the appropriate level of restrictedness. That's going to return the economy to price stability in a timely way.

103
00:25:53.940 --> 00:26:13.630
Loretta Mester: And so, you know, given the current level of inflation and the fact that it's broad based, and it's been persistent. I think we're going to need monetary policy is going to need to become more restrictive and remain restricted for a while in order to put inflation on a sustainable downward path to two. So

104
00:26:13.640 --> 00:26:21.200
Loretta Mester: if you look at the Fmc statement last week, right. We say that in determining that pace of future increases

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00:26:21.210 --> 00:26:39.479
Loretta Mester: we're going to be taking into account the cumulative tightening a monetary policy, You know we recognize we've brought the funds rate up. Um, we're going to a course Monetary Policy Act on the broader economy with lag effects um both on activity and inflation,

106
00:26:39.490 --> 00:26:46.969
Loretta Mester: and also to me very important. Right. Economic and financial developments are important

107
00:26:47.070 --> 00:26:56.770
Loretta Mester: in our policy decisions, because those factors figure into the economic outlook and the risk around the outlook which inform our policy decisions. So

108
00:26:56.820 --> 00:27:16.649
Loretta Mester: you know precisely how much higher the fed Funds rate will need to go, and for how long policy will need to remain restricted, are really going to depend on how much inflation and inflation expectations are moving down, which then depends on how much demand is slowing. Um! How much supply challenges are being resolved

109
00:27:16.660 --> 00:27:19.549
Loretta Mester: and price pressures are. So

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00:27:19.560 --> 00:27:38.570
Loretta Mester: you know i'm gonna be making that assessment assessment of how long and how high. I'm gonna be looking at a variety of incoming information. I think sometimes people when the Fed says and I've been, I've used this. We're data dependent. Some people think that we only look at the official statistics, and they, of course, lag

111
00:27:38.580 --> 00:27:51.790
Loretta Mester: um the economy. And and it seems like you'd always be sort of running behind. But when I say data dependent, I really look at a variety of information. So it's information and data. So there's the official statistics.

112
00:27:51.800 --> 00:28:02.189
Loretta Mester: There's a lot of survey evidence. The Cleveland fed runs our own um inflation, expectation surveys, which is very helpful There, you know it's a weekly survey of indirect consumer

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00:28:02.200 --> 00:28:21.490
Loretta Mester: um inflation expectations which has been helpful over this period. Um! And then we have a lot of business labor, market and community contacts. They provide us with a lot of forward looking information, and that, of course, um is helpful and sort of assessing conditions and and setting appropriate policy

114
00:28:21.500 --> 00:28:50.609
Markus Brunnermeier: somehow weighted. Somehow. Is it like the expectations, the service from households. Or is it more the bond traders, you know, financial markets for cost of inflation? Okay, So that's a really good question, Marcus. It's an open question, you know. Some people have their favorite. Some people have other ones, I mean. I like to look at a lot of different indicators. Because, again, the theory doesn't even suggest necessarily, which inflation, expectations, matter,

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00:28:50.710 --> 00:29:09.149
Loretta Mester: um, and the measurement issues involved in some of these right? Suggest that you, You're better off at looking at a variety of measures and trying to extract the signal from those measures. Understanding caveatting that, like, for example, in your fed Survey right. This is a three year head um

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00:29:09.350 --> 00:29:23.780
Loretta Mester: inflation series. This is a relatively new survey. So you have to take that into account, too. The market expectation. So that's the blue line here. Um! This is five year fire forward. Sometimes they're affected by things that are independent of

117
00:29:23.790 --> 00:29:41.429
Loretta Mester: um inflation. Real rates can be affected by, you know, liquidity, premium, and other premiums. So you have to be. If there's, you know, a lot of molecules in the markets. Again, the signal extraction problem. So my own approach is, I want to look at a variety of measures. Um to inform my view.

118
00:29:41.440 --> 00:29:46.249
Loretta Mester: Um! And of course you know you can try to put these together. The the uh

119
00:29:46.260 --> 00:30:02.340
Loretta Mester: um Bora governors has this common inflation, expectations, index um, and that does exactly what we're talking about it tries to extract the signal um, And so that's going to be a smoother series. So there's a lot of variety of techniques that you can use.

120
00:30:02.350 --> 00:30:09.720
Loretta Mester: But again, you know I this moving up um when we saw inflation moving up is was problematic, because

121
00:30:09.870 --> 00:30:25.790
Loretta Mester: it moved up when inflation moved up, and Then it started moving back down when gasoline prices started falling. And so, to my mind, you know, if it's truly anchored, you would see less correlation with the data. Um, but the level certainly isn't,

122
00:30:25.800 --> 00:30:43.750
Loretta Mester: you know, I would say reasonably. Well anchored at our goal. But we gotta not take that for granted, and we gotta do. What we can do is a business inflation expectation. So it's about the from setting the devices, I guess exactly, and that down in the last um quarter right, but again

123
00:30:43.860 --> 00:31:03.560
Loretta Mester: one quarter doesn't make it trend, or whatever they say right, so we have to again. It's positive that that moved down. But still, you know, we got to take that into the consideration that you don't want to be to given the the cost of getting this wrong. You you really need to to look carefully at that. So

124
00:31:03.960 --> 00:31:13.940
Loretta Mester: seventies one of the mystics was made that you know there was a lot of interest that hikes in the S. Too. But then, you know, when the economy cooled down immediately was withdrawn.

125
00:31:13.960 --> 00:31:38.690
Loretta Mester: Did you fit to learn some lessons from from the one thousand nine hundred and seventys, and this we call this Okay, good to see it. He has to be more persistent in a sense.

126
00:31:38.700 --> 00:31:52.980
Loretta Mester: Labor market numbers move down. Oh, we're done, I mean I to my mind, right. The big lesson is, you don't want to stop and go. Policy that gets you into a position where inflation expectations become on anchored, and

127
00:31:52.990 --> 00:32:00.550
Loretta Mester: I think we'll talk about later, the flexible inflation targeting and the new. You know the strategy document that was put out um

128
00:32:00.680 --> 00:32:14.970
Loretta Mester: before the pandemic. We really um underscores that anchoring of inflation expectations, and I think that's very much in everyone's mind. Um at the fmc to be very um attentive to that.

129
00:32:14.980 --> 00:32:32.549
Loretta Mester: Um, because that just raises the cost to getting back to price stability. So in December we're going to be putting out Um, the Fmc: we'll put out new um summary of economic projections. And basically that's going to incorporate every participants thinking about the appropriate path of policy. So

130
00:32:32.560 --> 00:32:51.829
Loretta Mester: you know this transaction transact transition back to price ability. It's going to take some time. Um, and it's not going to be without some pain along the way. Um, you know It's likely that we're going to continue to see higher than normal levels of financial market volatility, and that can be difficult to navigate

131
00:32:51.850 --> 00:33:04.710
Loretta Mester: um growth, I think, is likely to be well below trend. I think it could easily turn negative for a time if they're depending on a shock hitting Um, As I said earlier, business products are telling us that they,

132
00:33:04.720 --> 00:33:21.859
Loretta Mester: you know, plan to to keep workers, even as the economy slows, because it was just so difficult to attract and retain them over the last few years. But, um! And that would be a good thing in the sense that on it the unemployment rate right would not have to go up as much.

133
00:33:21.870 --> 00:33:29.209
Loretta Mester: But it's also possible that we will see unemployment Um. The unemployment rate go up more than anticipate, and then that would impose

134
00:33:29.390 --> 00:33:39.020
Loretta Mester: um hardships on households and businesses. So there, there, there, you know, People focus on those potential costs of this, you know,

135
00:33:39.080 --> 00:33:47.220
Loretta Mester: and it's difficult. It's in journey. But I think it's also really important to remember that the current very high inflation is painful as well.

136
00:33:47.320 --> 00:34:02.219
Loretta Mester: Um, you know west. Well well off people and and um businesses. They have to struggle to make ends meet. Um, and that's very um painful, you know. We hear that as a top concern of everyone we're talking to.

137
00:34:02.230 --> 00:34:14.060
Loretta Mester: Um. It used to be that, you know you could be rationally in a tenant to inflation. No one's rationally an intent of now everyone's following it. Um! And I also think it's really important not to underestimate the consequences of

138
00:34:14.070 --> 00:34:31.239
Loretta Mester: continued elevating inflation on the long run health of the economy right? It's. You know, that some of the trade off between, you know. Are we going to go into a slowdown? Versus how long Do you want inflation to stay up? I think there's also long run implications of very high inflation. If you don't have price stability

139
00:34:31.460 --> 00:34:35.360
Loretta Mester: basically businesses, and households have to divert their attention,

140
00:34:35.370 --> 00:34:54.559
Loretta Mester: to try to preserve their purchasing power of their money. That makes it difficult for them to plan for the future makes it very hard to make long term commitments, and I think that it really distorts the decisions people, and businesses made regarding investment in physical and human capital. Right. And then

141

00:34:54.570 --> 00:35:07.889
Loretta Mester: again, without price of building. We're not going to be able to sustain healthy labor market conditions over the medium and longer run. And that really is inconsistent with the maximum employment part of the fed stool mandate. So you know.

142
00:35:17.220 --> 00:35:31.200
Loretta Mester: Hence the decisions are much more short to them.

143
00:35:31.210 --> 00:35:52.979
Loretta Mester: You know that, and that's because on those sides businesses, thought Well, I. There's a lot of demand for higher wages at this moment. I think it'll cool, or i'm hoping it'll pull. So I have an incentive to have shorten the horizon, and the workers are like Wow! I think inflation is going to go up a lot more in the next couple of years, perhaps, and I don't want to lock into a three year contract. So we've seen that.

144
00:35:52.990 --> 00:36:04.949
Loretta Mester: And again, those kind of distortionary effects have an impact on the you know the longer run economy I've had. Ceos tell me um that

145
00:36:04.960 --> 00:36:24.920
Loretta Mester: you know they've spent over the last two years. It's been so hired a hard to hire people that they have had to focus their attention on the labor force in their company, and not on innovating and not thinking of new products and new ways of doing business. That's a productivity head, right? And that could have long run implications. So

146
00:36:24.930 --> 00:36:41.060
Loretta Mester: you know, I I think those kind of things are hard to quantify. Necessarily. Um, but I it does, you know, give me a sense of the the fact that we have to prioritize getting the economy back to price stability. So

147
00:36:41.100 --> 00:36:51.360
Loretta Mester: while we're doing that, of course we have to balance right whenever there's a transition in monetary policy we need to balance. We need to weigh the risk of tightening too much

148
00:36:52.040 --> 00:37:04.640
Loretta Mester: against the risk of tightening too little. So, of course, if we tighten too much. Um, we would slow the economy more than necessary, and that would it basically impose more costs than needed.

149

00:37:04.660 --> 00:37:25.970
Loretta Mester: But if we were to time too little, and you alluded to this earlier, Marcus. You know we'd be allowing high inflation to persist again, and that has short and long run consequences. It would necessitate a much more costly journey back to price stability. So we're going to need to be very diligent in setting monetary policy um to get back to price stability, and

150
00:37:25.980 --> 00:37:33.080
Loretta Mester: we have to be judicious and balancing these risks so as to minimize the pain of the journey. So

151
00:37:33.400 --> 00:37:46.780
Markus Brunnermeier: you can ask about this average inflation targeting. Perhaps, you know, if you take it seriously. Now, we have this high inflation. We should actually have some. The low two percent inflation in what we get an average two percent,

152
00:37:46.790 --> 00:37:54.130
Markus Brunnermeier: or is this ha average inflation target an asymptotic rule? Whenever we undershoot, we make up for it. Whenever we overshoot, we ignore it.

153
00:37:54.200 --> 00:38:12.390
Loretta Mester: How should I? I should I read this average so flexible average inflation Targeting Well, flexible is a good word in there. Um. Sometimes it applies to a dual mandate as as a When When Chairpow gave his speech where he rolled it out the new framework,

154
00:38:12.400 --> 00:38:22.230
Loretta Mester: he was very careful to say that we don't view this as a numerical averaging exercise, right? It was an exercise of,

155
00:38:22.240 --> 00:38:32.399
Loretta Mester: you know. We want to get back so that we it, it was basically saying, Look, we're not going to take one reading. It's sort of being. We're right. We're going to try to keep inflation

156
00:38:32.410 --> 00:38:54.460
Loretta Mester: right near two percent right, and not allow it to go too much above it too much below. But we do have a dual mandate, so there are going to be periods where perhaps it's the labor market that gets more intention than than price really. But price of only has to come first in the sense that if we really don't have price to believe. We cannot have a strong labor market, I mean they all go together.

157

00:38:54.470 --> 00:39:01.890
Loretta Mester: So again, the current environment is one in which, you know, we really have to be focused on this inflation.

158
00:39:01.940 --> 00:39:24.929
Loretta Mester: Um part of our mandate, because it is a precursor to having sustainably good, healthy labor market conditions. So that's how I see the two pieces fitting together. But is it like if you were to undershoot below two percent accidentally, because it was happen to be too tight. Is it a problem? Or it's saying, Oh, that would fit in the average inflation time.

159
00:39:25.100 --> 00:39:34.970
Loretta Mester: We wouldn't want inflation to run persistently below two percent. We saw that right in the period before the pandemic right inflation was actually too low.

160
00:39:34.980 --> 00:40:01.100
Loretta Mester: Um! And you know, if you think about the the financial crisis. I mean one of the puzzles back. Then, when you know we were in that deep um recession, and the great recession was Wow! Inflation didn't fall as much as people thought it would, and that pointed out the very important role that these longer term inflation expectations remaining well on care helped us right, because it basically kept inflation. You know, the public businesses believe that we would get back

161
00:40:01.150 --> 00:40:19.410
Loretta Mester: um to two percent because they knew we were going to add, You know, now we have the opposite situation. We have a potential that high inflation and high near term inflation, expectations, right could be detrimental to that anchoring, and so that that's why we have to take this very seriously. But I don't think you should view this as

162
00:40:19.420 --> 00:40:35.029
Loretta Mester: a numerical um that we have to offset every you know time we go a little, but above, by a time we go a little below I that isn't kind of the way I view it. I think it's more giving us the ability over time

163
00:40:35.040 --> 00:40:45.279
Loretta Mester: to bring inflation down and keep it at two percent reasonably measured in terms of our Pc. Target. You know the other thing I I have to say in your poll.

164
00:40:45.290 --> 00:40:59.310
Loretta Mester: I guess I would have phrased the question a little bit differently, because we almost made it sound like our goal was change

with the flexible and like average inflation target. And I didn't I never viewed it that way. We took two percent as our long term inflation goal

165
00:40:59.320 --> 00:41:15.950
Loretta Mester: before I even started, you know, looking at the strategy for getting there, and in that strategy this the The consensus view was that if we do an average inflation targeting, you know methodology that'll get us Um,

166
00:41:16.440 --> 00:41:45.360
Loretta Mester: That's a more effective way of getting to price stability. But of course there's going to be a lot of, I think discussion about that. I mean, there's probably Phd. Dissertations being written at Princeton right now that are gonna ask the question about what role did the new strategy have? Um in the current episode? But so far I think that strategy is is still serving as well. Um! And I certainly think that we're very committed to two percent as our goal for longer term inflation. So

167
00:41:45.760 --> 00:41:49.889
Loretta Mester: you know, getting back to sort of like this risk management, um,

168
00:41:49.940 --> 00:42:09.169
Loretta Mester: you know, tightening too little, weighing that against tightening too much. My own view. Um! Is that, despite the fact that we've moved the fundra up um this year just based on the consistent, you know. Um, the consistency, the that are

169
00:42:09.180 --> 00:42:25.950
Loretta Mester: our forecasts have been um really underestimating, the the the both the persistence and the level of inflation. Um. And then added on to that, the fact that there are significant costs of high inflation continuing, I I currently do that. The larger risk

170
00:42:25.960 --> 00:42:38.589
Loretta Mester: come from tightening too little. Um at this point. Um! But you know, as policy moves further into restrictive territory. Um, and stays there for some time.

171
00:42:38.600 --> 00:42:52.309
Loretta Mester: The effects of that cumulative tightening are going to work through the broader economy, and I I do anticipate that I we're going to see inflation pressures ease, And at that point I expect, in my view of the balance of the risk will shift to

172

00:42:52.320 --> 00:43:03.679
Loretta Mester: um, and I actually will welcome that, because when that happens that means that we've seen inflation moving down in a meaningful way. So that kind of is where I am on the prepared remarks, Um,

173
00:43:03.790 --> 00:43:25.939
Markus Brunnermeier: Marcus, So I i'm going to stop sharing the slides, and then we can talk a little bit more about this lag of monetary policy. You know it, you know. Milton Friedman was talking a lot about this, but more recent voices out of the Fed said the legs got short because we have not better information. Do you have a take on on? You know how variable these legs are and how long they are, what

174
00:43:26.050 --> 00:43:35.470
Loretta Mester: it's a really yeah, it's a really good question, Mark. I think the other thing in that question, though. And why there is this sort of um

175
00:43:35.980 --> 00:43:53.389
Loretta Mester: sort of view that Wow! Things move passing, I think, where you measure the start of the tightening matters so. Yes, what the Fmc. Raised It was until March of this year that we raised the target range of the fundra. But you know, perhaps the way to think about

176
00:43:53.400 --> 00:43:58.239
Loretta Mester: um. The start was when we sort of pivoted our communications,

177
00:43:58.250 --> 00:44:20.939
Loretta Mester: and we pivoted the communications back, you know, starting probably in September uh definitely December right? When we really started talking about the fact that, you know we're getting to a point where we're gonna have to, you know. Move off, remove accommodation. So again, partly, I think it is that we do communicate very differently now than we used to

178
00:44:20.950 --> 00:44:37.799
Loretta Mester: right, and that could contribute to to some of it partly is because the financial markets did react strongly like the mortgage rates, went up very significantly right there above seven. Um! Once we started tightening, but also some of the action happen before we even raise the funds rate

179
00:44:37.840 --> 00:44:41.139
Loretta Mester: and mark. So again, Um,

180

00:44:41.440 --> 00:44:47.179
Loretta Mester: you know, we started to see some of the impact I The way I read is we've done, you know.

181
00:44:47.810 --> 00:44:51.760
Loretta Mester: You know we're based on that, I think right at the beginning of restrictive,

182
00:44:51.780 --> 00:44:58.020
Loretta Mester: and we still have inflation running well well above our goal. So that just to me, says we it

183
00:44:58.140 --> 00:45:06.859
Loretta Mester: we need to do more, and and we will. You know we indicated that, you know we think ongoing increases are necessary,

184
00:45:06.870 --> 00:45:24.140
Loretta Mester: and you know. Now, it's a question of Okay, let's look at incoming information right forward looking information. Um, as well as the statistical information we get from the official reports. Um! And then sort of gauge that right? But my own view is that

185
00:45:24.150 --> 00:45:35.369
Loretta Mester: you want to be very convinced that inflation is on a sustainable downward path to two percent, because the cost of not being, you know, the cost of of of um.

186
00:45:36.030 --> 00:45:49.949
Loretta Mester: You know we're treating too quickly, I think, are much are greater right, and it's because of the short one cost it's great. But also these long run costs, because once, you know, if if inflation expectations get on anchor if inflation moves down,

187
00:45:49.960 --> 00:46:00.169
Loretta Mester: you know, for a month, and you stop. But then it moves back up. You're in a worse position, and it's a more costly journey then, and no one wants to post more costs.

188
00:46:00.390 --> 00:46:06.350
Loretta Mester: Um then necessary to do this. Um! So we recognize, or I recognize their costs

189
00:46:06.430 --> 00:46:14.119
Loretta Mester: to doing what we're doing, but I think there's cost much greater cost. I'm not doing what we're gonna do if that makes sense.

190
00:46:14.450 --> 00:46:32.369
Markus Brunnermeier: So I see that the risk management approach really says you should actually do more now. Otherwise there might be. If you happen to have done little subsequently, the costs will be much more dramatic. But I have another another question, you know. According to the Taylor principle, you should raise the normal interest rate more than the

191
00:46:32.380 --> 00:46:34.689
Markus Brunnermeier: inflation increases,

192
00:46:34.710 --> 00:47:04.669
Markus Brunnermeier: and that the real debate has to go up. The question Is that what maturity to look at? You know I can look at the short end, or i'm a little bit out in the yield curve, and then it depends very much what inflation expectations you look at. Is there any favorite number? And this always say anything. The Fermi, he said. Okay, we look at, you know, two years out, and that's what we do. What? Three years out, or how do you apply this Taylor principle? At what rate do you apply it

193
00:47:04.680 --> 00:47:18.659
Loretta Mester: overnight rate? But that's sort of the policy rate that we need to use as sort of the anger. And we The reason I think we're basically just beginning to be restrictive is because if you take that rate and you use like one year ahead. Inflation expectations.

194
00:47:18.670 --> 00:47:30.669
Loretta Mester: We're about, maybe, where, you know. If you I was looking at sort of like Sc. Take the Median sc inflation prediction for the next year, three and a half percent or mine was three and a half percent. I was a little bit

195
00:47:30.680 --> 00:47:49.300
Loretta Mester: above theirs. You basically meet right now, starting to be restrictive. But you do want to look at more than just an overnight interest rate because of these other interest rates affect economic activity. Right? So you know, a short run, short interest rates. You want to look at those, and if you look at sort of the you'll occur

196
00:47:49.310 --> 00:47:55.289
Loretta Mester: right. Real rates are, you know, in positive territory, you know, for the first time. But again

197
00:47:55.400 --> 00:48:05.619

Loretta Mester: just the fact that we have been, you know, moving off of a a very, very, very accommodated stance. We just have to keep going to make sure that we're doing enough.

198
00:48:05.680 --> 00:48:15.329
Loretta Mester: Get inflation back down and inflation hasn't, I mean. Yes, there was some positive news today, and there's some positive in some of the readings of inflation. So that's

199
00:48:15.340 --> 00:48:26.000
Loretta Mester: very good. Um! But again, we're gonna have to just bring the funds rate up some more to make sure that we get that sustainably.

200
00:48:34.760 --> 00:48:42.559
Markus Brunnermeier: The emphasis very much on the Interstate policy. I guess you just just run off the balance sheet rather than actively selling off. Uh,

201
00:48:42.640 --> 00:48:57.990
Loretta Mester: all right, I mean we have more experience, of course, with the policy rate right. We we as as much as we've just been talking about the uncertainties around monetary policy. There's lags. And where do you count when you start policy? Because the communications

202
00:48:58.000 --> 00:49:09.810
Loretta Mester: There's even much more uncertainty about sort of the taking a balance sheet shrinkage. How much does that impact the real economy? How much does that in inflation? So this strategy was

203
00:49:09.820 --> 00:49:24.110
Loretta Mester: right. Let's pick something that seems like a reasonable pace to run off, and it is much quicker than the last time we did it, but we learned some things the last time right, and allow it to to sort of run. I would call it passively.

204
00:49:24.120 --> 00:49:35.169
Loretta Mester: It does have an in fact on the economy it is, it is affecting. It is another way of tightening policy, but the main action is with the policy rate, because we understand it

205
00:49:35.180 --> 00:49:51.650
Loretta Mester: more than we do, that the we are in it to the balance sheet run off right, and if that you know, but then we use our policy rate right as our as as the rain the active one. So with balance sheet runoff is having a a uh,

206
00:49:51.920 --> 00:50:10.919
Loretta Mester: you know, a good effect on helping inflation to come down right. That means we might have to do less work with the interest rate tool right? But we can allow that to happen, and then use our interest rate tool right, depending on what we see in the It depends a little bit whether you want to affect the short end of the or the intermediate or long end of the

207
00:50:11.110 --> 00:50:21.060
Markus Brunnermeier: with the balance sheet movements. You can affect the long end of yield curve more, but you can also affect it through communication about future.

208
00:50:21.190 --> 00:50:22.479
Loretta Mester: Um

209
00:50:22.550 --> 00:50:29.840
Loretta Mester: think back to the financial crisis when we use quantitative easing right that we were on. We were operating in the long end

210
00:50:30.040 --> 00:50:45.939
Loretta Mester: right. It brought the funds read down. We wanted to bring long rates down this time when we went in and started buying treasuries and Mbs. Remember, it was in March two thousand and twenty that wasn't about monetary policy that was about financial stability and the functioning

211
00:50:45.950 --> 00:50:52.730
Loretta Mester: right uh the Treasury Market right. So we bought across, you know, the curve. So again,

212
00:50:53.280 --> 00:51:03.210
Loretta Mester: you know one of the things I think is not as well understood, and I I think our communications weren't as clear as you know, we bought in the beginning

213
00:51:03.250 --> 00:51:19.689
Loretta Mester: those assets, not as a monetary policy, but really as we had to restore market functioning. And then, later on, once the funds rated hit zero, and the pandemic was in full fledge, and there was a lot of uncertainty about how deep it would be. And if you remember, back

214
00:51:19.910 --> 00:51:34.859

Loretta Mester: there was a lot of thought really dire scenarios Right then we would started using that as a tool of of monetary policy. But we weren't as clear about that as in my opinion, as maybe we should have been.

215
00:51:35.320 --> 00:51:53.419
Markus Brunnermeier: I come back to the inflation anchor, because you know. I also i'm worried about the inflation anchor, so it's very important to to make sure that it holds. But there's a tension there. So, first of all, there's a tension that if I look at core inflation, it's typically considered as a better predict of future inflation.

216
00:51:53.430 --> 00:52:00.250
Markus Brunnermeier: But if I look at what anchors at least households. Expectations are the non-core products like energy and food.

217
00:52:00.510 --> 00:52:29.480
Markus Brunnermeier: So it's a little bit of attention. It seems like if I do, inflation prediction, the usual way in the usual business way. I should look at. You know all the inflation numbers except for energy and food. But if you're worry about people be getting scared, and Don't, believing the inflation numbers and getting the in, that I should actually look at the energy and food aspects. So how do you deal with this tension, in a sense, or you don't have to be able to say, We focus more on the point that it doesn't the

218
00:52:29.510 --> 00:52:45.639
Loretta Mester: I mean? That's these are really important research question, Mark, because I mean, we have an inflation research center here at the Cleveland fed, and that's one of the things that they look at. It's like which whose inflation expectations matter right for the health of the economy.

219
00:52:45.650 --> 00:52:50.959
Loretta Mester: And you know, if you think about it, is it wage bargaining

220
00:52:51.160 --> 00:52:53.199
Loretta Mester: with firms, and maybe it's

221
00:52:53.210 --> 00:53:12.809
Loretta Mester: the bet. Business inflation, expectations, right, or the or the salient thing, if it's, maybe it's financial markets as you saw right that that measures so again, And maybe it's, you know, professional forecasts, because in some models they actually do better in terms of sort of the prediction of where we're a long run, and I think the important thing is that it's

222
00:53:12.820 --> 00:53:18.799
Loretta Mester: probably a longer run medium long run. That gives you some information about how credible

223
00:53:18.880 --> 00:53:19.970
Loretta Mester: right

224
00:53:20.050 --> 00:53:50.040
Loretta Mester: the public thinks the fits commitment to price. Stability is right. So it's important to look at those because that gives you some separate information right? The short-run measures You're exactly right. There are these sailing and prices food right? We used to be milk prices for the key ones, although maybe it's aluminum. Now, everyone's buying different kinds of milk. But anyway, there's too many different kinds of milks now. Um and gasoline prices, for sure. Just seem to figure into people's expectations. But then the question is well,

225
00:53:50.050 --> 00:54:08.389
Loretta Mester: so how much does that matter for the economy? And where the inflation readings are going to go? And I think there's a good reason to think that we should be looking at those for sure, but because they might lead to long or run inflation expectations moving up, and that it would be a very

226
00:54:08.400 --> 00:54:10.630
Loretta Mester: um bad situation to be in.

227
00:54:10.860 --> 00:54:29.879
Markus Brunnermeier: You also. Look at the like the tail events like, you know, and if you look at option like inflation, sw options and options, you can actually figure out how likely it is that you know the reach or tail event of an inflation increase

228
00:54:29.890 --> 00:54:38.790
Loretta Mester: right in the survey responses, which I think is again reflective of how anchored are things right? So if you think about like

229
00:54:39.040 --> 00:54:40.279
Loretta Mester: um

230
00:54:40.450 --> 00:54:54.380
Loretta Mester: the mean as opposed to the medium in those surveys right that can move around quite a bit, depending on what happens in those

tails. Um! And so those those indicate I mean. One thing was very interesting is that

231
00:54:54.390 --> 00:55:00.709
Loretta Mester: we saw sort of this in the beginning, you know, when inflation started moving up. It was

232
00:55:01.320 --> 00:55:13.579
Loretta Mester: the meeting, The The inflation expectations moved up, but it was mainly on the. There was a lot of weight on the tail, the positive tail. Now you're seeing some weight in the negative tail. Um,

233
00:55:13.590 --> 00:55:34.160
Loretta Mester: And I think the New York fed is on research. That's just. You know. One theory was Well, That's because people think the economy is really going to tank the New York fence. Recent research is no, they're actually thinking that things are pretty positive, and place is going to come down. It's just that. Maybe they don't understand. The fed has a two percent target, and so they're just putting a low number in there. So again, these are really

234
00:55:34.210 --> 00:55:44.950
Loretta Mester: hard research questions, markets. There's not a lot of work, but we're We're doing a lot of work here in Cleveland to get a better handle on. Sort of that. Those questions that you're asking

235
00:55:46.170 --> 00:55:59.450
Markus Brunnermeier: and coming back to the labor market. So one one thing which is striking. You have shown that how tied to labor market is on. And, on the other hand, you know Gdp is not growing so well, so it's. It's more the labor market than they are all economy.

236
00:56:00.280 --> 00:56:16.009
Markus Brunnermeier: So how what do you make out of this? Do you think it's a long term shocking workers preferences? So you know It's like we have just want to work from home, and they want to work essentially in a different way, might be less productive, or by even more productive. We Haven't figured it out yet.

237
00:56:16.040 --> 00:56:23.980
Markus Brunnermeier: And how would you? How does this affect the monetary policy? Do you see? Okay, That's you know we have a different way. It might be the case that

238
00:56:24.330 --> 00:56:30.780

Markus Brunnermeier: productivity is lower for now, but that would take into account in your if i'm see meetings as Well,

239
00:56:31.090 --> 00:56:46.250
Loretta Mester: so yeah, I mean, I guess I separate out some of this into their like short run things happening cyclical, perhaps things, and then structural. So I think the shift in preferences. I think that's going to be a longer run.

240
00:56:46.260 --> 00:57:14.120
Loretta Mester: You know I I don't see everyone waking up tomorrow and saying, Okay, Now Let's go back into the office. We certainly don't see there's like and different people have different preferences, you know. When we all started coming back in the office. We had some some of us who love being here. He wanted to be in the office, and other workers who said, You know i'd rather, you know, spend more time at home working there. So I think each individual has their own preferences. Of course you got to aggregate up when you're thinking about What's the implications for

241
00:57:14.130 --> 00:57:33.329
Loretta Mester: um the Us. Economy? So I think that you know that's a long run issue, and that all have implications for the level of interest rates, for example. Um, our star. You know that that. But they're also short run issues about. Okay, are we? Do we really think so? If you look at labor force participation now.

242
00:57:33.340 --> 00:57:51.929
Loretta Mester: Um, It's Still, if total, you know for the total right, it's still below three pandemic levels. Okay, if you look at Well, no, if you look at prime age, right? That one is basically on trend, right? So the question is, Well, are you gonna see? And what happened was a lot of people retired

243
00:57:51.940 --> 00:58:02.019
Loretta Mester: right during the pandemic. So one question was, or are they going to come back into the labor market? So one school of thought is, we will see them because of the stock market.

244
00:58:02.030 --> 00:58:13.640
Loretta Mester: You know. They were re relying on stock market earnings right their income. It's taken a hit, and they'll come back. But the other school of thought is, and I think the evidence suggests this is true is once you start taking social security.

245
00:58:13.850 --> 00:58:31.089

Loretta Mester: You, Don't, typically come back in a layer, for so, for on a short run where we are now in terms of, do you expect the balancing in the labor market to come from the demand side or the supply side. I think the work has to be done on the demand side, and so you know

246
00:58:31.100 --> 00:58:43.179
Loretta Mester: whether that's And we've started to see Job. Openings are coming down. So firms have already recalibrated. Oh, okay, I don't. I I thought I was gonna have this much activity.

247
00:58:43.190 --> 00:59:02.850
Loretta Mester: Economy may be slowing. I don't need as many workers that's already starting to happening. You do see that. But nonetheless it still looks like demand, and the labor market is out casing supply, which again feeds into. Okay, we're gonna have to bring the funds right up a bit more, you know, move further into restricted territory. Um! Again, to try to ease

248
00:59:02.860 --> 00:59:11.069
Loretta Mester: right. That disparity between demand or the in balance between demand and supply, both in the product side and the markets and in the labor market.

249
00:59:12.060 --> 00:59:31.929
Markus Brunnermeier: So I would like to go to another topic beyond the labor market, which is like a fiscal monitor interaction also financial interaction. So one has the impression, you know, before the increase in the inflation among policymakers there was a sense we can do modern monetary theory. We can just spend whatever we want without impact inflation

250
00:59:32.490 --> 00:59:42.960
Markus Brunnermeier: erez agmoni. And do you think, uh this mentality has changed among the policymakers? And does the central banks. Do they have to do something for going back to a different mentality? One hundred and fifty?

251
00:59:42.980 --> 00:59:57.020
Markus Brunnermeier: Do you also think that the Inflation reduction act had some impact. Does it impact what? The how? The fed is reacting because it all the inflation and the reduction act will do the job for you? Or is it something which you think has not really an impact on the inflation?

252
00:59:57.730 --> 01:00:22.689
Markus Brunnermeier: And then there's an issue about fiscal monetary. You saw the fiscal monetary dominance and financial dominance. Playing out in

the United Kingdom recently was actually there was a battle going on between the Uk Treasury and and the Bank of England, and also the the pension funds. Uh, how well how to deal with this circumstances! And you saw the the interest rate exploding on the guilt on the long term Gilton's financial stability issues popping up.

253
01:00:23.030 --> 01:00:25.380
Markus Brunnermeier: Did this. You know

254
01:00:25.670 --> 01:00:41.060
Markus Brunnermeier: this episode in the United Kingdom? Does it also raise some issues for the United States and has it to walk it up certain policymakers, or even the fad, saying, Okay, we have to be more careful about such episodes, and this will actually make people more

255
01:00:41.620 --> 01:00:55.509
Loretta Mester: uh reluctant to expand and and spend in on the fiscal side of be more prudent on the fiscal side as well. Do you see any interaction on this dimensions?

256
01:00:55.520 --> 01:01:03.269
Loretta Mester: I don't think many policymakers that I talked to had bought into the Mmt. Um

257
01:01:04.770 --> 01:01:24.640
Loretta Mester: thinking as you put on the slide so so again. Yes, there are some policymakers who obviously did, because that's why it became part of the news story, but I don't think we I certainly didn't. And I don't think many of my fit colleagues. Um, that I talked to quite a bit, really.

258
01:01:24.650 --> 01:01:44.449
Loretta Mester: Yeah on the fiscal side. Yeah, so that Yeah, there may have been in the fiscal side. But I We've always been focused on making sure that we're going to be at two percent long run inflation goal and calibrating our monetary policy to get there. So I I don't, and the way you kind of approach have to approach It is, of course,

259
01:01:44.460 --> 01:01:46.439
Loretta Mester: fiscal policy

260
01:01:46.580 --> 01:02:01.650
Loretta Mester: has implications for the economic outlook right? It has implications for Gdp growth. It has implications for perhaps the labor market depending on what the form that the fiscal policy takes. So you have to take it into account

261
01:02:01.760 --> 01:02:27.959
Loretta Mester: right when you're setting monetary policy because it has an implication for the E current and future economic conditions. And of course, that then implies that. Okay, Once, you know, kinda the outlook and the risk around the outlook, then you calibrate your monetary policy for it. So that's kind of how I think about it. You have to take into account what's going on on the fiscal side in order to run monetary policy, because

262
01:02:27.970 --> 01:02:36.910
Loretta Mester: you know that influences um the economy and your outlook for the economy and the risk around that outlook. So in that sense, you know,

263
01:02:37.120 --> 01:02:56.180
Loretta Mester: There we we we take that as sort of part of the economic environment. Similarly, the way we take some of the things going on in other countries right. We don't ignore them right, because they do influence the outlook for the Us. Economy. And then we set our policy to achieve the goals

264
01:02:56.190 --> 01:03:00.659
Loretta Mester: right that are domestic goals, right? Price, stability, maximum employment

265
01:03:00.760 --> 01:03:09.620
Loretta Mester: in terms of what happened in the Uk. I mean, I take that as a cautionary tale in the sense that um

266
01:03:10.270 --> 01:03:12.709
Loretta Mester: markets have been extremely volatile.

267
01:03:12.800 --> 01:03:17.269
Loretta Mester: Right? I thought that I have to give credit um

268
01:03:18.080 --> 01:03:31.959
Loretta Mester: to to that, to the central bank, in the sense that I thought they did a very good job of explaining that they were doing their action for fiscal, but for sorry for financial stability, reasons

269
01:03:31.970 --> 01:03:46.180
Loretta Mester: not for monetary policy Meaning and the Andrew Bailey, you know, explain that as as well as from the others, that this was a

financial stability action, and on it monetary policy action. So I think that was a very um

270
01:03:46.190 --> 01:04:00.270
Loretta Mester: difficult challenge, and they I think they pull that off very well in terms of being able to explain why they had to do what they did. But it does give you sort of one of the things that the Financial Stability report that the Board of Governors put out

271
01:04:00.300 --> 01:04:18.709
Loretta Mester: um earlier this week, I think. Came out Um, maybe Monday or Tuesday was um. You know there are some structural issues right that we've known about for a while, and like the Treasury Market and other markets. Um! And so we should really address those, because,

272
01:04:18.720 --> 01:04:26.669
Loretta Mester: you know, if there's a shock, and you know you could say like the shock in the Uk was that very, very sharp? Um!

273
01:04:26.680 --> 01:04:53.179
Loretta Mester: Quick increase in the guilt rate deal right that can precipitate right things that could be calm, right? Market dysfunction that become could become a financial slowly issue. So I take those very um seriously, and you know, I think a number of us are, you know, really trying to make sure that we're monitoring those situations? I mean the other thing. That was also a cautionary tale. There is that

274
01:04:53.470 --> 01:05:01.439
Loretta Mester: you know it like hidden leverage. I mean, Marcus. This is, you know this better than anyone right

275
01:05:01.450 --> 01:05:21.459
Loretta Mester: is really the source of a lot of these instabilities, right? And you know the fact that we there are parts of our financial system where we don't have as much insight as we do into as we do, to like the regulated banking, traditional personal main concerns, and that you know we're doing the best we can do to monitor those situations.

276
01:05:22.030 --> 01:05:29.819
Perhaps we can spend another two minutes on another topic which you touched upon already the the international impact of us monetary policy,

277
01:05:30.090 --> 01:05:47.200
Markus Brunnermeier: you know, Do you have any? Is Are there any models at the Fed or any where we say? Okay, what are they? Spillo was of us monetary policy on other countries, and then the spill backs I mean by

your mandate. I guess you can only take into account the spillbacks. But can we quantify somehow how big the spillbacks are,

278
01:05:53.260 --> 01:06:11.329
Markus Brunnermeier: What are the implications of that? And uh, to what extent it also feeds in and monetary policy. And of course there is, of course, there we touched on the okay already. But there's also in back of Japan is, you know, it's a of control. It might be at some point, if they want to get out of it, to exit from the zeal of control where you control the ten year

279
01:06:11.340 --> 01:06:29.070
Markus Brunnermeier: interest rate. Uh, if you want to exit from that, it might also lead to some discontinuous adjustments. What are the implications then coming back to the United States? And are you, you know. How would you react to that? Or is a contingency plans uh for that? And so that's I think, another

280
01:06:29.080 --> 01:06:34.220
Markus Brunnermeier: uh open. Perhaps you can spend just one or two minutes on this. I know that you have to leave soon.

281
01:06:34.260 --> 01:06:49.819
Loretta Mester: I mean, there's It's definitely the case that when we're doing our own modeling and the fed right, and which is one of the foundational things that we do to help us set monetary policy. The models have right, an international

282
01:06:49.840 --> 01:07:06.440
Loretta Mester: right section right? The models have sort of foreign economies in them, and I would would suggest anyone who's very interested is we? We uh post all teal books right. The The policy document that really goes through the staff

283
01:07:06.450 --> 01:07:14.999
Loretta Mester: forecast. Um! They're on the board of Governors website, right? If you look in those documents, you'll see that there's a large section

284
01:07:15.060 --> 01:07:22.939
Loretta Mester: that just covers the international um environment, because it is very important when we're setting us monetary policy to understand

285
01:07:23.140 --> 01:07:42.789

Loretta Mester: what's happening in um other countries with their monetary policy, as you suggest. Um, but also you know what are the economic conditions there, right? So there's channels through our financial markets. But there's also a trade channel. Um, not as big as other countries, perhaps because you know

286
01:07:42.810 --> 01:07:51.799
Loretta Mester: um, it's a smaller part of our economy. Other, you know, economies. It's a much bigger sector, but there's certainly we certainly don't think of ourselves as an island

287
01:07:51.880 --> 01:08:03.930
Loretta Mester: um separate from other countries. We're in a global economy, and we have to take into account right not only how our our monetary policy is going to affect their economy,

288
01:08:03.940 --> 01:08:18.759
Loretta Mester: which then comes back. It affects our economy. So again, it's general equilibrium. What! You right that you have to sort of use that lens. Um! How well we do that in terms of the empirics. Um, I think those are hard models

289
01:08:18.770 --> 01:08:29.420
Loretta Mester: um to get precisely right, but it's true that you know we do look at those things and consider um them, but through the lens up. What are those developments abroad

290
01:08:29.450 --> 01:08:31.559
Loretta Mester: mean for the Us. Economy?

291
01:08:33.170 --> 01:08:54.160
Markus Brunnermeier: Okay, I think. Uh, that's all the time we have. We are very grateful to you for all the enlightenment you give us, and make clear clear that give us a keep, a picture. How monitor the policy will or ease, and what the object is of go and wanted policies. I'm. Also very grateful for all the questions you asked in the Q. And A. Box. So thanks a lot for the audience.

292
01:08:54.220 --> 01:08:58.400
Markus Brunnermeier: I hope to see you soon, for our next Webinar with the

293
01:08:58.430 --> 01:09:13.850
Markus Brunnermeier: Martin will. From financial times he talks, we will talk more about the United Kingdom and a great button. Thanks again. No it, and hope to see you soon, and.