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JARED BERNSTEIN ON THE US ECONOMY:

WHERE IT'S BEEN AND WHERE IT'S GOING

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WELCOMING REMARKS:

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REMARKS:

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DISCUSSION:

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David Wessel: Welcome, I'm David Wessel, I'm director of the Hutchins Center on Fiscal and Monetary Policy here at Brookings. The past couple of years have been rather unusual ones for the American economy. We put the economy into a medically induced COVID. We had an enormous, we had an enormous amount of fiscal and monetary response. We had a much quicker recovery than I think many of us anticipated, and perhaps in part because of all those things, we got more inflation than we had hoped for or expected. There are a lot of things in the economy that are quite puzzling now. Like, how is it that unemployment is still very low, but the inflation rate is falling? And so we invited Jared Bernstein of the Council of Economic Advisers here to explain all those questions, particularly the hard to answer ones.

Jared is going to talk about where the economy's been, where it's going, and his remarks are going to be followed by a panel moderated by my colleague, Louise Sheiner, with Greg Mankiw, who is the Robert Beren professor of economics at Harvard University and was chairman of the Council of Economic Advisors in the George W. Bush administration. The other panelists will be Seth Carpenter, who did time at the Treasury and the Fed but is now global chief economist at Morgan Stanley. And for full disclosure, Morgan Stanley is a supporter of Economic Studies at Brookings. And our third speaker will be Heidi Shierholz, who's president of the Economic Policy Institute. Assuming she shows up, in which case, if she doesn't show up, she won't be on the panel. And I want I want to sit—and here she is, dramatic entry. Yeah, yeah, I know you were just waiting out there for me.

I want to say a quick word about the Council of Economic Advisers, three-member council created by Congress in 1946. In my experience as a reporter, the CEA has absolutely no power, it only has influence. And its influence is directly related to the relationship between the members of the CEA and the president. And I think Jared is in very good position to do that. He was, after all, an economic advisor to Vice President Biden in the early years of the Obama administration. Jarrett began his career as a musician, he played the double bass. He got a master's in social work, and he played jazz bands and did bar mitzvahs and weddings for years while counseling New York City's troubled souls. He then got a Ph.D. in social welfare with an emphasis in economics at Columbia and came to Washington in the early nineties. And he's been involved in policy ever since, some in the government, some outside the government at the Center on Budget and Policy Priorities and the Economic Policy Institute.

I think it's safe to say— I didn't check this with you, Jared— that you consider yourself a progressive economist. I've always found you to be very good at asking hard questions, often challenging the conventional wisdom, an excellent advocate and very good at speaking about the economy and economic policy to a general audience, which I hope you'll do today. So with that, Jared Bernstein.

Jared Bernstein: Thank you for that and thank you for that really nice introduction. And thank you to David, Louise, the Hutchins Center for the invitation. The work of the center has been important to our White House economics team over this challenging period. And just the other day we were on a Zoom meeting and the question of fiscal impulse came up and somebody quickly shared on the screen the Hutchins tracker, and they solved that, answered that question for us. Your recent cautionary work on the debt ceiling has been especially welcomed. I knew David when he was a cub reporter at the Journal about 150 years ago. And of course, I've learned a ton from Ben, Louise, Wendy, Don, Bill, Ron and the rest of the team.

What I hope to do today is to look at U.S. macro from the perspective of our team at the White House, reflecting on where we were, where we are and where we might be headed. I'll pause along the way to try to engage the panel and audience and some of the questions David alluded to, questions we view as consequential in, in current macro. Actually, let me go here to the summary and you see those right there in bullet four. What's the sacrifice ratio right now? How much activity do we need to give up for inflation reduction and other, other points you see there. I should also underscore from the outset that my talk comes to you in the spirit of humility in a period of uncertainty. And that's a, that's a spirit we're in as many questions are generated as answers.

Okay, so just getting organized here. Let's start by briefly collecting macroeconomic lessons many of us took from the last few cycles, not just for collection purposes, but to understand the framework many were working from in the, in in early 2020 when the pandemic hit. Now, one theme of my work has long been that estimates of u*, the lowest unemployment rate consistent with stable prices, was A, difficult to estimate within confidence intervals narrow enough to make the concept particularly useful for policy work and B, too high. So the fact that recent expansions saw u fall below conventional estimates of u* with inflation missing more from the downside of the Fed's target than the upside was an important lesson, one that led many of us to trust data-driven policy more than star-driven policy.

A related observation— one that was especially important for economically vulnerable workers who are hurt most by labor market slack— was that their labor force participation was lifted at both the extensive and the intensive margins by tight labor markets. In this way, many of the attributes of running a tight labor market, including stronger wage growth for middle and lower paid workers, we can include a higher y* as another question in the sense of a tricky policy variable to estimate within an interval that makes it useful for, for our analysis. Others have pushed this sort of thinking further and made connections between chock full employment and productivity gains. To me, this makes some sense in theory. If tight labor markets raise labor costs, then discovering productivity gains can stabilize unit labor costs and preserve margins. Empirically, I wouldn't push that connection too far, but suffice it to say that u* is also I'm sorry, y* potential GDP growth, I mean, the potential level of real GDP is also a moving target, one that's tough to estimate and therefore, as I mentioned, another tricky policy guidepost.

Anyway, by early 2020, many of us believe that the price Phillips curve was pretty flat, that very full employment was an essential and reachable policy goal that advanced economies even through periods of pro-cyclical stimulus, tends to be far more demand than supply constrained. Note that these observations map in important ways onto the Bidenomics goal of bottom up, middle outgrowth that you heard about last night. The idea that if you're helping to bake the pie, you ought to get a fair slice. The president is acutely aware of the linkages between tight labor markets and workers bargaining clout. I will add from the perspective of countercyclical policy that loom large when the pandemic hit the economy, that there was evidence that we'd pulled our punches in past fiscal responses with the result that initial expansions were quite weak.

The last few decades, the last few, the last few decades saw quite slow recoveries out of trough that were initially labeled jobless, wageless or both. This certainly isn't the case with the current expansion. In the first conversation I had with President Biden when he asked me to help on the campaign, he emphasized the joint health and economic shocks caused by the pandemic and early conversations of the team that led to the American Rescue Plan were founded on this insight. The implication for countercyclical, countercyclical policy was that there was, was that there needed to be a dual vaccination and fiscal relief strategy or what became the talking point shots in arms and checks in pockets. And that's what we did; we understood that executing simultaneously on both vaccine and, and fiscal support were essential to avoid scarring. Hard hitting, quick acting policies

were needed to help families and businesses get to the other side of the crisis. And that sure could be brought closer with effective distribution of both the vaccine and transfers.

As you see on the figure on the left, the black line is, on the right axis is cumulative vaccine doses administered, which really takes off in early '21. We needed to push back on the sudden loss of labor earnings, potential waves of evictions, nutritional shortfalls of vulnerable families, sharp increases in child poverty, loan defaults and the needs of the health system. Note also, in the movement between the last two bars in the figure, the last two blue bars, the negative fiscal impulse in 2022 is the transfers diminished fiscal complement to the Fed's tightening and pushing back on inflationary pressures. Now, strong demand plus constrained supply helped unleash these price pressures in 2021, exacerbated in February of '22 by Russia's invasion of Ukraine.

The combination of pent-up savings and snarled supply chains also contributed to inflation's rise. One way this played out was through shifting consumer preferences from in-person services to goods where demand for goods grew quickly and sharply while their supply response was near-term, relatively inelastic. In fact, as you see in red, that's the goods services ratio line, that shift is still in the process of normalizing. I'll have more to say about inflation in a moment. But in the spirit of sharing lessons, let me say a word about the T-word. Transitory. I'm not defending its use, and it's clear that its temporal ambiguity was problematic from a communications perspective. Did it mean two weeks, two quarters, two years? But speaking for myself and I suspect many others, the idea was that there were things behind the 2021 inflation that were clearly temporary.

The disruption in computer chips and their impact on vehicle prices provides a clear example. This figure shows the contribution, not the growth rate, the contribution of used cars and trucks to the year over year change in the CPI over the past few decades. The average contribution of this component over the full period is zero. And most recently this component has been a negative contributor. But those remarkable outliers you see there are, to my eyes, a classic example of a temporary shock. Though again, I say that while recognizing the temporal ambiguity of the term.

Turning to where we are now, current macro is raising a number of rich, pressing and consequential questions. After playing my bit part in the political economy of the past few years, I'm quite sympathetic to the old proverb, may you live in uninteresting times. On the other hand, one of the reasons I'm pleased to be here with you today is to discuss these questions with Louise and the panel. I find this figure to be useful in motivating the conversation: on the x-axis is real activity with

higher numbers, meaning less activity, so think unemployment or whatever slack variable you prefer. On the y axis, think trend, core or underlying inflation. So this is the price Phillips curve space though we could, and some are having this debate in Beveridge curve space. The two lines reflect different sacrifice ratios, that is, different trade off magnitudes between less activity and lower inflation. The higher line represents a more painful tradeoff.

Another way to frame the question posed here is how much inflation reduction can we achieve on the vertical part of the curve and how much on the flat part. Because it's both theoretically interesting and empirically consequential, it's worth pausing a beat on the question of non-linearities. While some researchers noted in this slide, as you see in the last bullet, have long argued this point, I believe that pandemic economics, specifically joint shocks to the economy, supply and demand sides where strong demand in a particular sector, in this case goods, occurs before supply can adjust, can lead to sharp and fairly sudden capacity constraints. And this in turns leads to convexities like that in the figure from Cerrato and Gitti showing a city's derived price Phillips curve that became quite steep in recent years, you see the slope there of -0.85.

As I note in this slide, thinking about these constraints on the economy supply side, I don't think I ever said the words dwell time, which is how long shipping containers stay in ports until 2021. And then I woke up every day and checked dwell time and my colleagues and I were, were checking the metric daily. Yet another way to think about the question implied by the figure is how much inflation can we get from supply chain unsnarling, burning off of excess savings and greater labor supply, all of which I put in the less painful bin versus how much will require demand destruction, which I'd put in the more painful bin. And to underscore a point that should never get lost in this context, the pain of demand destruction is not equally shared. It inevitably hits the most vulnerable, a fact, I promise you, is not lost on our president.

Thus far, we've seen significant inflation reduction without giving much up at all on unemployment. Many have pointed out, and I agree, that year over year inflation measures are less informative when higher frequency movements are occurring. So along with the usual time series figures that you see in the first slide, that's just PCE core, headline and core inflation three-month changes annualized, and you can see somewhat of a rise and fall there, I find the approach in these bar charts here to be a useful way of tracking inflation's motion. Now, let me explain what these bars are showing. Each set of bars takes the annualized change in inflation over one-, three-, six- and 12-

month intervals. So when the bars are sloping up, that typically means that inflation is accelerating and vice versa. And by running these annualized rates in different months, we can capture inflation's dynamic profile at that time.

So, for example, consider the first slide on the right there, which is headline CPI inflation. In March 2021, which is that first set of bars, I can't tell what color it is because I'm colorblind, but you'll see in March 21, the bars slope up pretty sharply, 12-month inflation around 2%, but one month inflation annualized all the way up to eight. So what you see there is the bar showing a sloping up sharply, showing that inflation was taking off. At the end of the year in December 21, that's the middle set of bars of each set, inflation was a lot more elevated and still accelerating. But the most recent reading, which is the reddish bars, they, they show a clear deceleration. The PCE core, which is on the bottom, shows a roughly similar pattern, though the recent deceleration has been more muted.

Now, chair Powell's inflation decomposition, which I think he may have broken out on this very stage, breaking inflation, core inflation down to core goods, housing services and non-housing services, which I'm going to call NHS, so I don't have to keep saying non housing services provides a useful, useful perspective. Here on the left you see a picture of CPI core goods against the New York Fed's supply chain disruption index, with both coming down sharply in recent months. That's an important part of, of the disinflation we're currently seeing. We expect the current softening of home prices, including some actual reductions in new rentals to start showing up in inflation prints in the back half of this year. But non-housing services inflation, as the bar chart shows, has on the other hand, been moving sideways.

And again, I, you probably shouldn't get someone so enamored of your own slides, but you know, I think when you set it up this way it shows you that that those orange bars or reddish bars, they're kind of flat. And that's the most recent, that's the December 22 PCE non-housing services inflation. So that's proving to be more sticky than the other components of this decomposition. Chair, so we've developed, at CEA, so this is something you haven't seen before unless you read Greg Ip's column this morning, we've developed an index of non-housing services wage growth. So thus far I've showed you non-housing services price growth, but part of the argument around non-housing services is that that part of the economy is more sensitive to labor markets and wage growth because it's a labor-intensive sector.

So we developed an index of non-housing services or NHS wage growth using detailed industry average hourly wages weighted by each sector share of 2019 labor costs in final consumption of services, excluding food, energy and housing. And here you see that the year over year growth rate in this series remains elevated, though it is clearly slowed quite sharply. The table to the right there examines the, examines the correlation of this series with NHS inflation showing that in a simple price Phillips curve model, with wage growth taking the price of slack, taking the place of slack, this wage series has a smaller out of sample error than the others. So, you know kind of a, a better correlation with non-housing services can be found in this, in this NHS wage series. So we think the fact that it has decelerated is instructive and hopefully kind of hopeful in that regard.

Now, the wage dynamics in the prior figure, raise the next pressing question for current macro. If u is less than u* if job markets are really that tight, why are we seeing wage deceleration? David posed the same question. The slide offers a number of hypotheses. Perhaps u isn't below u*. Well, as I've noted, it's awfully hard to pin down u*. But many analysts have come to prefer the vacancies unemployment ratio as a slack measure, and that seems to be well above any aversion of v/u*, that is it's, it's, it's it really is quite elevated. So while I can make an argument that there's been some softening of labor demand, I don't think there's been much. I'll come back to that slide in the second.

At least before the latest ECI release, some argued, well, maybe nominal wage growth isn't slowing. That's getting hard to maintain. And we've developed a composite measure compositionally adjusted, which I think is important these days, that shows clear slowing in the growth of nominal pay. So with the caveat that wage data are particularly noisy and that the level of wage growth is still elevated, I'd call this a legitimate head scratcher. EPI's Josh Bivens, a close watcher of Factor shares, suggest that labor share of corporate income is still quite low, despite the persistent strength in the job market, and this could help explain slower nominal wage growth. This has led Bivens to remind us that lower profit margins are a source of non-inflationary wage gains, a point Vice Chair Brainard underscored in a, underscored in a recent speech. I note that this channel is highly consistent with President Biden's emphasis on tight labor markets as equalizing. I'm also sympathetic to a view from a recent Jorda et al paper which found that the pass through from inflationary expectations to wages has been highly elevated in this expansion out of the pandemic, which is another non-linearity.

Now measuring expectations is a challenge and we haven't seen a great deal of movement in longer term expectations. Near-term expectations have, however, come in quite a bit, especially in the U Mich survey, and perhaps that's putting downward pressure on nominal wage growth, even at very low unemployment. I tend to think of one year inflation expectations as moved around by retail gas prices, but that doesn't mean they're not impactful. And I think that that study is, is but one study, but I found it kind of convincing of this point.

Before I close with a round of tailwinds and headwinds to the forecast, let's briefly look at where we are from the perspective of job gains and household finances, echoing some of the president's points last night, the, and the rescue plan with its dual focus on hitting back hard on both health and cyclical shocks, how that sets us up for one of the strongest and fastest labor markets on record. Sorry, this this slide just shows how quickly the 2020 payrolls climb back to their pre, climb back and exceeded their pre-pandemic peak, not just a bounce back— I mean definitely there's a strong bounce back— but you also see just a very different shape of this jobs recovery out of the trough where the others were, as I mentioned earlier, often labeled as initially jobless.

The strength of fiscal and monetary support must also be credited with preventing deep, damaging and lasting economic scarring. Claims supported by evidence regarding the wide variety of household finances shown in this figure. Thinking back on my days in the Obama administration, when household balance sheets were in a very different place, today's balance sheet conditions have been an important complement to the durability of the ongoing expansion.

Now, in thinking about where we're headed, I find the sequencing model from researchers Goldman Sachs, at Goldman Sachs to be instructive. Slower GDP growth drives slower payroll growth, which leads to slower wage growth, nominal wage growth and finally slower price growth. So this is a very sequencing flow chart, very much in Phillips Curve space, where you look at the starting point, where you are now, where you have to get to in each sequence in the flow to get from below-trend GDP growth to finally core inflation closer to target. By some core-like measures, real GDP has decelerated from above trend to below trend, so step one has kind of a check, but closing the gap between demand and supply in the labor market remains a work in progress. As I've shown, on the other hand, as I've shown, we're seeing some slowing, non-trivial slowing in wage and price growth.

In this regard, one conclusion that you can draw from this moment is that the Phillips curve space in which many of us reside to one degree or another with its well-established hydraulics, as in

this flow chart, may not quite apply, or at least not fully apply to the current moment. Steps three and four in this slide, slower wage growth and slower price growth, are arguably coming in more so than steps one and two. So where does that leave us? Perhaps closer to post-shock or post-war economics, wherein recovering from a shock while rebuilding and in the case of the Biden agenda, significantly expanding the economy supply side must be factored into the analysis.

Now, here's a list of some of the tail and headwinds that our team thinks about, all of which are familiar to you, and most of which I've discussed already. On the new shocks, the political own goal I have in mind is around the debt ceiling. It's never anything but the height of irresponsible government's, governance to try to politicize or weaponize what should be a pro-forma action. It is in fact, an unequivocally clear constitutional obligation to defend our sovereign debt and pay for existing, existing spending obligations. But to play these games when they're in the, we're in the midst of transitioning to more steady, stable growth with the Fed in the midst of a hiking cycle as the rate of inflation is coming down is especially reckless.

We're watching energy closely as well. The retail gas price remains about a $1.55 below its peak from last summer. But we're closely watching refinery capacity, which has been tight over this expansion. China's reopening is a pressure point, though it's worth remembering that China is both a consumer of energy and a global distributor of refined product. Bottom line, with the war ongoing, the energy price remains a potential impactful uncertainty. I've already gone through most of these, most of the tailwinds I just listed in that list, including generally solid balance sheet conditions, though we haven't looked at excess savings. Here we use a similar approach to some Hutchins Center's work on this impactful variable, and while we see some burn off of the excess aggregate at the end of the figure, the part under the average savings line remains smaller than the cumulative part above it, so I think there's still some juice there when it comes to excess savings.

These potential shocks all bear close watching, but we on the Biden economics team, along with many of you who've advised us and along with our counterparts in economies across the globe, we've all faced down shocks and tailwinds, expected and otherwise. It's been a challenging few years, and I suspect we'd all welcome a period of less interesting times. Among the lessons we've learned, more accurately relearned in this case is the need to fix your countercyclical infrastructure. I'm thinking about unemployment insurance software, for example, when the sun is shining as you'll need it in the next storm. The Internal Revenue Service was highly efficient in check and child tax credit

distribution, no question. But the investments in the agency from the Inflation Reduction Act are critical not only for getting tax evaders to pay their fair share, but for the continued improvements in the agency's functionality in the next downturn.

But let us pause one last time and appreciate that at a time of massive uncertainty, wherein the world was dealing with a pandemic the likes of which we hadn't seen for a century, macro policymakers amply and quickly met the challenge. Given the magnitude of the shocks which have been further exacerbated by the war in Ukraine, the fact that the U.S. has been at or near full employment since President Biden took office, that we face an increasingly credible and plausible path and transition, in transitioning to sustainable growth, that even the EU, with its greater exposure to commodity pressures from the war, is seeing a somewhat improved outlook, all of these should be taken as testaments to the power of macro policy interventions in the face of shocks.

To be clear, there are no victory laps. Inflation remains too high, and we should of course always learn how we can do better next time. But if we can get away from the fevered pulse of social media, hyper-partisan critiques and it only leads if it bleeds media takes, we can recognize, appreciate, learn from and build on this success story for fiscal and monetary macro policy in offsetting some of the greatest economic shocks of our lifetimes. Thank you.

Louise Sheiner: That's right. Great. Thank you, Jared, for really interesting slides. Now we're going to give a chance to people to comment then and we're going to come back to you. I'm going to sort of talk about three, three buckets. I'm going to talk about fiscal policy, I'm going to talk about what's going on in the labor market and I'm going to talk about the outlook for inflation and monetary policy. And so we're going to start with Greg to give us your take on, so Jared gave a pretty good grade to fiscal policy during the pandemic. How do you, how do you judge it?

Seth Carpenter: Completely unbiased.

Louise Sheiner: Well, yeah.

N. Gregory Mankiw: Well, thank you. Thank you, Jared, for a great presentation. That was really, really terrific. I want to make sort of three, three points. I want to talk first about the unusual nature of this recession, and then we'll talk about fiscal policy and that we've had a recently and then think about fiscal policy going forward. So first of all, you have to realize this is a very unusual recession. The standard recession is some sort of mistake, some sort of shock happens, output and employment decline, we're unhappy with the decline in employment, we're trying to get employment

back to normal as quickly as possible. That's usually takes a long time, the recovery tends to be very slow. In fact, there's a literature almost 40 years ago that I participated in called the unit root literature, I won't tell you why it's called that. But anyway, it's about the permanent and the persistence of economic fluctuations and the basic, the bottom line from that literature is that fluctuations in GDP are so persistent, they're almost impossible to distinguish from permanent. That's when output declines, it never gets back to previous trend.

This was a very different recession. This really was a recession by design. Policymakers saw the pandemic and they said, don't go out and spend, don't go to work unless you're an essential worker. And we basically, we purposefully put the economy into a recession. If people were to let people to come back once this situation changed, and that's, what's, once we got the pandemic under control, once we got vaccines and so on. So if you want, if I can draw an analogy. So if we had daily data on GDP, what we'd find is that we have a downturn of this sort every Saturday, and then, then we quickly recover on Monday. So what we, what we had was a very, very long weekend at home, just like weekends. We recover from weekends quite quickly. We can recover from, from this kind of because it's a very different kind of recession. And it's not surprising that the dynamics look very different in the data than in previous ones, I thought Jared's picture about comparing the different recessions really showed how very different the dynamics here were.

The second thing to say about it is because this was a recession by design, this fiscal policy was not a standard stimulus. If you think of sort of standard fiscal stimulus, whether you're talking about the Bush tax cuts or the Obama Recovery Act, the goal is to put people back to work. We want to expand aggregate demand. Here we weren't trying to put people back to work and wanted them to stay at home. We told them to stay at home and that's why they were staying at home, we told them to. So the fiscal policy was not really stimulus in the normal sense, but it had some stimulus effect. But that was not the motive for it. It was really disaster relief because we realized that people were suffering. This was going to be a very long weekend. They didn't have what they didn't have the financial resources to stay in, stay at home for that long a weekend, so we had to provide them this kind of disaster relief. Having said that, so I think it made sense as a form of disaster relief. But I think there's two problems with it in my mind.

The first problem was it is very poorly targeted. A lot of, a lot of money went out that probably didn't need to go out in exactly the form it did. So let me give you just a couple examples. The

Paycheck Protection program, which I think was very well intentioned, I think looking back, we sort of see that it was not very well targeted. First of all, we've seen a lot of fraud for sure. But even people who are not being fraudulent, people are getting it legitimately, a lot of people we probably don't think really should have gotten it. So to give you an example, I remember Secretary, Secretary Mnuchin found out at some point that the hoity toity prep school that his kids went to were getting millions of dollars from the Paycheck Protection program. And he said, oh, no, no, this is not the target for this, this is, they should not be getting this money. Well, as it turns out, I happened to be on the board of another hoity toity prep school. And, and they also got paycheck protection money. And we talked to lawyers and absolutely, these lawyers, we did everything legally. And so you may have thought it's politically expedient to say this, that it shouldn't go to the, his kids prep schools, but it was a completely legitimate that it went there. Arguably, it's not what Congress intended, but that's the way the law was written.

To give you another example, the act expanded unemployment insurance. The extra $600 checks that people got was very indiscriminate. I remember talking to a president of university, not, not, not Harvard, another sort of major deep pocketed university. And she was saying that, you know, she sent all the kids home. We don't, I don't need as much janitors, but we have really deep pockets, so my, my inclination was to keep our janitors on staff. But my janitors told me that if they went home, they got laid off, they'd get more in unemployment insurance, I'm not doing them a favor by keeping them employed. I don't know. I don't know what she did in the end with that. But, but that sort of shows how sort of poorly targeted, you know, this was.

The second basic problem with the fiscal policy, I think, was it was basically too large in aggregate. We spent too much money out there. So these, Jared showed you the excess saving. As we said, we sent lots and lots of money to people. I think in particular the American Rescue Plan, which is the one of the first acts of the Biden administration, I voted for it, for Joe Biden, by the way. So I'm not here as a partisan, I voted for Joe Biden, but the American Rescue Plan was too big. And I wrote a column in The New York Times saying that about two years ago, saying this was risking inflation and I wasn't the only person saying this. Olivier Blanchard was saying it and I think Larry Summers was by saying it more frequently than anyone else I know. Having, having said that, I don't think anybody predicted 8% inflation. So I was thinking inflation would creep up, but I wasn't thinking of, get to eight. The only person I know, by the way, who said it would get to eight was Jeremy Siegel

of Wharton. And he did that by looking at M2, which is something that's not very fashionable these days, and I kind of wonder whether it's gone too far out of fashion.

Basically what happened, we sent people checks, people were told people can't go out and spend it, you're stuck at home. So they stuck in their checking account and instead it sat there waiting until they said, we'd let them off. Now, I don't think aggregate demand was a full part of the inflation surge. I think Jared's actually right, there were a lot of supply chain issues, shifts in composition of demand that are important. But I think fiscal policy does deserve some of the blame for the inflation surge.

Okay. What's, what about fiscal policy going forward? First, Jared did not show us a path of the debt to GDP ratio up to now and going forward. But if he did it, we'd basically realize that we're pretty much close to the peak debt to GDP ratio reached at the end of World War II. And CBO says under current policy, it's going to continue going up forever. And at some point, we got to deal with that. I think, and no, four years is a short period of time. So are there any President, for four years, you can say, that's, that's, a future problem. But at some point, that future comes, and we need to worry about that. I think there's no possible way that if you stick to all of President Biden's promises, which is no cuts in entitlements, no taxes, extra taxes for people making under 400,000 a year, there's no way to fix this long run sustainability problem under, with those set of commitments.

Regarding future countercyclical fiscal policy, I don't think it's going be anything like we've seen in the past three years. So I don't think we've learned very much about normal recessions. I suspect the next recessions will be normal recessions, I certainly hope so. I think that this pandemic, I think, was very unusual, I don't expect to see something exactly like this. If we did see something like this, I guess I'd want something that's more, that's more targeted. My guess is going forward, fiscal policy will be more the traditional stimulate aggregate demand to get people back to work, that future recessions will probably be more normal recessions, unlike the one we just, just experienced. I'll stop there.

Louise Sheiner: Great. Thanks so much. So we're going to stay on fiscal policy a little bit if Seth or Heidi want to weigh in. Heidi, is there something that you saw from fiscal policy that you like that we should repeat in the next recession or just.

Heidi Shierholz: Yeah, I mean, one of the key things I want the lesson to be learned is that fiscal policy actually can generate really strong jobs recovery. Like if you look at, I'm going to talk

about this when I when I do my comments, but if you're sitting in December 2020, you know, we had already had the big, big surge of, you know, millions of jobs coming back as businesses that had locked down came online and brought back their workers that they had temporarily laid off, the recession was, or the recovery was faltering. We actually lost jobs in December 2020. At a very similar point in the recession following, in the recovery following the Great Recession, policymakers sort of mind bogglingly turned towards austerity, and that directly led to our very, very weak and slow recovery from the Great Recession.

And they didn't do that this time, right. Like we had the, the package of December 2020 and then the American Rescue Plan in March of 2021. And those things led to this unbelievably strong jobs recovery that we have had. I mean, over the last two years, we added more than 12 million jobs. It's just a total game changer. So I do hope that's a lesson that policymakers really learn, like the pace of our recovery is a fricking policy choice. Right? And we can choose to do something different. And we really showed how that's possible in this recovery.

Louise Sheiner: Great. Thanks. Seth, do you have anything?

Seth Carpenter: Yeah, just make two, two comments on the fiscal side of things and I thank Greg for opening up by saying just how different or how unusual this recession is. Very often in my profession, if you start off a pitch saying, well, this time is different, people laugh at you. But I think Greg very convincingly made the case, I don't know why it should be hard to make that case this time around, anyone who's been living through the past two or three years, I think, hadn't lived through it before. Nevertheless, thank you for that initial point.

I want to, you know, Greg's commentary on, or critique of some of the fiscal policy, I guess I'd want to agree with some cautiously and then push back cautiously all through the lens of humility, having spent a bunch of my life at the Fed and then in the Treasury Department, designing policy in real time with incomplete information is extraordinarily difficult. And so where I think I think the fiscal policy response was at its greatest was in the income replacement side of things. So as Greg said, a bunch of people lost their jobs or stayed home or didn't work in part because they were asked not to or because of the public health situation. And so in that sense, replacing those people's income through government transfers seems like a reasonably targeted approach. Could it be perfect? No. The, the university where janitors perhaps could have made more if they hadn't been kept on, I can

believe those stories happened, I don't know for sure how widespread that was. And I think ultimately the question becomes, are we letting the perfect be the enemy of the good in those sorts of things.

I think where I, so in general, I think the first several rounds of fiscal worked the way we we probably wanted to. Greg said we probably had too much and there I think I want to cautiously agree with Greg in particular the last tranche, the direct transfers of cash, not particularly means tested. Again, always very difficult to calibrate these sorts of things and get the systems to work right in real time. But one does sort of, that last sort of round of stimulus one could sort of I think there start to quibble a little bit. The challenge, though, in directly translating that fiscal policy to the inflation that we saw is a little challenging because we have a very, another part that's very different here is the pattern of the increase of inflation.

Usually what happens when, in cycles when inflation goes up is lots of things are heavily correlated here. Clearly, very initially a surge in goods prices, especially automobiles, and then only subsequently the, the other components. And so to me that says the standard analysis any of us may have either learned or taught in university classes on economics about cyclically defined inflation probably isn't right here. And I think the interaction between doing a bottoms-up approach for inflation is really important, and doing so might make you sort of pull your punch a little bit more if you're going to be criticizing the fiscal stimulus.

Louise Sheiner: Right. Do you want to respond, Jared.

Jared Bernstein: A little bit. I mean.

Louise Sheiner: Let me ask you a question, too. One of the things before you were going to answer this, you one of the things I worry about is that we will have learned Heidi's lesson is one lesson, which is that you choose your response, and so fiscal policy can actually be effective. But I worry that the, that the lesson will also be don't do that because you're going to get inflation. And what Greg says, this was a different kind of recession, and what Seth said is also that inflation response is going to be different, too. Like, should we learn the fact that if you if you go and sort of get fast recovery, you're necessarily going to get inflation?

Jared Bernstein: I think that's maybe the most important point from this conversation, because I agree with you, and I worry about this also that I talked about lessons I think we should learn. I didn't talk about learning the wrong lessons. And I think you expressed it exactly right. And I think when someone is sensible as Greg points out, the, the sui generis characteristics of what we

just went through and their impact on inflation, again, with the points that Seth made, if you kind of take the combination of the three things you just heard, that would make a really important argument that I urge the three of you to work on together, maybe, or separately, however you'd like to do it. And that's a really, really important argument that we should be leaning into so that we don't come out of this with the wrong lessons learned.

A couple of tiny points. You know, the checks were, were means tested, but they, they may not have been as means tested as you wanted them to be. I think in terms of, look, I think the, the discussion about fiscal sustainability is near and dear to my heart. It invokes conversations about where growth is going, where interest rates are going. But I will encourage Greg and others to look at the budget that we're putting out on March 9th because we think we achieve sustainability in precisely the kinds of ways you would like us to, given where trajectories of, of, of, of deficits and GDP go. But of course, you know, the President's budget is a, doesn't exactly pass go immediately. So, so we think you know, we're sensitive to, to, to that trajectory that you described. And, you know, the President would very much like to build on the 1.7 trillion record deficit reduction we've achieved thus far, which for the record is not just spending cuts rolling off of, of the COVID support, but in fact, a much larger effect comes from receipts, receipts which have come in stronger than expected in no small part due to the dynamics Heidi described about the strength of the, of the recovery.

Louise Sheiner: Great. Okay. Let's move on to your, I love this slide, riddle me this question, which is what's going on in the labor market? How do we explain the fact that we see this slowing in nominal wages, even as real wages and labor share are still depressed? Heidi, I'll start with you.

Heidi Shierholz: Okay. I can go for that. Okay. So I do want to back up to this period at the end of 2020, when we got that big, we'd already gotten that big dump in of jobs where people were just being brought back online. We still had a jobs gap of 10 million jobs. And as we know sitting there, that inflation was just about ready to really take off because of extreme pandemic sectoral shocks. So that's our situation. And if that at that time, if you had asked me if I thought typical workers would be able to weather a huge inflationary spike caused by a pandemic a year later, also war, without basically a one for one drop in real wages, I would have said no way. There's no way that's not happening, because had just come off of four decades of rising inequality and wage stagnation for most people, for most workers, for most of that period. And what that means is that employers held the cards, right the, that working people had very little bargaining power. So the idea that that was

going to turn around even an iota when we're in a global pandemic and we're in a 10 million jobs gap, it's just, that is just not what I would have predicted.

But it is exactly what happened. Workers saw an acceleration of nominal wage growth that offset a huge chunk of the acceleration of inflation. It didn't offset all of it. So, for example, over the last two years, inflation measured by the CPIU increased 14% in total and average nominal hourly wages for private sector workers increased 10.1% over that period. So wage growth didn't, nominal wage growth didn't fully offset the increase in prices, real wages declined, but they declined a lot less than I would have thought. And before I go on, I just want to say I should note that I'm taking it as given here that inflation was basically not driven by wage growth itself. Falling real wages, enormous pandemic shocks, the historically large contribution of rising profit margins to, to price growth, the global nature of inflation in this, in this era, they all make that actually pretty clear.

And so given that, the question became how much is the spike in inflation really going to hurt workers' wages and rising nominal wage growth on a completely unexpectedly to me, others might have foreseen this, actually blunted some of that pain. And even within that, there were very unusual dynamics. So workers in low wage industries that were hit the hardest by COVID like leisure and hospitality, saw the strongest wage growth over this period. Racial wage gaps that have been growing steadily for the last 40 years actually narrowed during this period. Again, given the trends over the last four decades of who holds the cards, right, those things are just very, very much not what I would have expected.

So why did they happen? I think there's a number of things that contributed to contributed to it. I'm going to focus on just a couple things that I think also give us an idea of maybe where things are headed. So one reason, my colleague Josh Bivens, who Jared mentioned a different paper of his, he has coined a term that I really like called "severed monopsony." To explain, so one of the things that drove our wage stagnation for working people for most of the four decades leading up to the COVID recession was the decline, due to relentless attacks, of labor standards and institutions like unions that provided a broad swath of the labor market and actual counterbalance of power, counterbalancing like inherent employer power. That unequal balance of power that remained, that sorry, that unequal balance of power that happened as a result of that decline in things like labor standards and unions meant that workers often remained in jobs, even at suppressed wages.

But then the massive layoffs and business closures of the pandemic meant that employers' usual degree of monopsony power over their workers' wages was sort of abruptly diminished. So that's one thing. And then another thing, it was our relief and recovery packages, and we sort of talked about that, they were game changers. I just, the unbelievable job growth they created was, it was just, it was we just have seen this unbelievably fast jobs recovery. And then the other thing is, as employers staffed up, they actually had to compete for workers, which, you know, is good for workers' wages. And then they had to do it in this context of workers having far fewer ties actually binding them to current employers, ties, which, had they been in place, would have subverted a big chunk of that, the need for employers to compete for workers. So I think all of this led to workers and some unlikely workers actually being able to weather the inflationary spike caused by the pandemic and war with substantially less than a one for one drop in wages.

And so I feel like I've been going on for a, do you want me to do the, where I expect things to go? Okay. So, so there is this the where do I expect things to go from here? And I really like Jared's comment that, you know, and also, we were speaking in the spirit of humility in the face of total uncertainty, I've been wrong about a lot over the last three years. But what do I expect going forward? Okay. So for one, the extremely strong job recovery that we've seen over the last two years, the extremely strong job growth, that's unlikely to last. So that means that I don't think well, anyway, that we're unlikely to see the same pace. So that means that the boost in leverage that workers got from having employers scrambling to staff up, that's not going to last either. And the severed monopsony boost to workers' bargaining power is also, I think, unfortunately, going to fade out. And that will happen as the new employer-employee matches become cemented. Like it's essentially that the same frictions that hinders, that hindered workers search for better jobs pre-COVID, they are very likely to reassert themselves as job openings rates get back to normal.

And then there's, I will just end with one, there's one other factor that I have not talked about that I think is worth ending with, because it's a little bit of hope that maybe we'll see some of the increase in worker power and the better balance that that created actually continue even as the labor market softens. So very broadly, we know that individual workers have two basic sources of power. One, the implicit threat that they could quit their job and take another job. And that's what I've totally focused on. But there is another source: joining together with your coworkers to make collective demands. Being in a union. And it is worth noting that we also saw over this period a big increase in

interest in unions. Public support for unions is at a more than 50 year high. NLRB election petitions have increased dramatically. Unions made high profile advances, honestly against all odds at places like Starbucks and Amazon.

And those things do not have to dry up as the labor market slows. I do want to say that I think they will likely take a bit of a hit, and that's due to our unbelievably weak labor law that makes it really risky for workers to engage in union organizing. It's technically illegal in this country for employers to retaliate against workers for organizing, but the penalties are basically nothing. And so it happens all the time. And so that means a labor market where there's just a ton of job openings, like the ones we saw over the last two years. That was great for workers' ability to take risks and organize. And as job openings come down to more normal levels, that will, that will then re-increase the risk of organizing, because it means that if a worker is retaliated against, they're going to be less likely to be able to find another job in a reasonable timeframe.

So coming down from record job openings will likely put a damper on the growing interest in union organizing. But I don't think it's going to dry up completely. It totally remains to be seen, but I think there could be something of a structural shift underway with more workers recognizing the importance to their wages of collective action. And if that were to happen, if that happens, it will have a really positive impact on workers' wages going forward. And there I really will end.

Louise Sheiner: Okay, so rather than let everybody else chance respond to that, I'm going to move on to this question about inflation that we're going to bring back into the labor market, which is like, how does that, how do we think about that confluence of what's going on with wages, what will go on with wages and inflation? So when we say, so we've talked about the fiscal policy response and what happened with the labor markets, so now we're stuck with, now the problem is that we're all worried about inflation and the prospect of a recession or a soft landing. Seth, what is how do you think about the monetary response and what's going to go on from here?

Seth Carpenter: Absolutely. So it has been said that inflation is always an everywhere, a monetary phenomenon and so leave it to central banks. This may be one of those cases. We're in a slightly quirky position where it's mostly or partly a monetary phenomenon. So what has happened? So the inflation took off, initially it was very much through consumer goods. Then it started to spread, especially for rent. And now, as Chair Powell has emphasized, the core services outside of, of housing is part of the story as well. And so the Federal Reserve started reacting to it and started

raising interest rates initially somewhat slowly, and then in leaps and bounds, 75 basis points at a clip. And so here we are now closing in on a Federal Funds Rate close to 5%. The Fed's last projections have them getting to just over 5% and then staying there for the rest of this year with the idea that they would be tightening financial conditions enough to slow the economy, not just slow it down from the rapid pace we saw a year and a half ago or more, but to where it's slowing and it's growing below the potential growth rate of the economy for sufficient amounts of time that in level terms slack opens up and inflationary pressures go away.

So I think that version of the story is, is feels very standard cyclical macroeconomics. And I think it's the story that the Fed's telling. And I don't, I don't see a particular reason now to criticize them for that. We can quibble about did they start soon enough; did they keep QE going on long enough, none of which matters at this point because I think it's largely in the rearview mirror. So what is going on with inflation? How does it interact with labor markets and what does it mean for, for monetary policy? I think here again, Greg's framing of just how different this, this recession was, is important. I think the discussions we just heard about the fight in labor markets and perhaps the severed monopsony or at least a temporary change in power, negotiating power, I think is very important.

And so then to answer the question that Jared put up on the screen, what have we learned and puzzle me this, how are we seeing wage inflation coming down at a time when other things still seem tight? I think they all actually fit together. My personal take on this— and I'd be curious your views as well— is that part of what we saw in wages was a level shift higher. So we remember the slogans for more unionization Fight for 15, it was particularly acute at the lower end of the income distribution. And so if we think there was not literally from one day to the next, but over six months or so, a level shift higher in wages, that means that the normal cyclical patterns of more slack mean slower wage growth, less slack means faster wage growth, was temporarily overwhelmed by this level shift higher that gave us for several months in a row measured wage gains that were particularly outsized. And now we're going back to the normal cyclical patterns there. And so it looks like we're getting this deceleration even with the tight labor market. And my personally fairly strongly held view is what we're seeing is the back end of that level shift. And I think that that matters for lots of reasons, and it'll come to you in a second.

So where is inflation going? Goods inflation is now negative. Jared put the chart up on the screen. I think if you took the same chart Jared had and instead of doing it in growth rate terms, he did it in levels, you would see that there's still a far distance to go for the level of, in that case, auto prices to come back to the long run trend, which means that this negative month on month change for the level could go on for quite some time and help pull measured inflation down a lot more. Similarly, rent inflation has gone up, spot rents have stopped rising. And so over the rest of this year, rent inflation should come down a lot, which will leave us with those other services.

So why does all of that matter? All of that matters because if we take the fact that Jared appealed to one of my competitors to have that model of how inflation might work in the economy, wage inflation really shouldn't matter that much for goods inflation. And in fact, they're coming down even though wage inflation is high because a lot of the majority of consumer goods are imported. U.S. wage inflation isn't a direct input to imported goods, and so that those two are working at odds with each other shouldn't be surprising. Similarly, at least in core CPI, rent inflation is 40% of core CPI, and there's not that same production function of labor as an input to rent and, you know, to shift over to get a new apartment. And so, again, that we're having those inflation dynamics move in a different direction from wage inflation again, shouldn't be that surprising.

So then we're left with this other core services outside of, outside of housing. And there I would just like to note that if you take something like the employment xost index and go back through until the 1970s, so leave out the 1970s, the super high inflation that was clearly eye popping, we have seen other periods where employment cost index has gone up pretty dramatically, with no subsequent rise in consumer price inflation. And if you do a bunch of egg headed, wonky statistical analysis in the data, what you will find is that statistically, consumer price inflation leads wages the opposite direction, the feed through from wage inflation to consumer final consumer prices is actually extraordinarily weak. Even if you focus just on the other services component. It's not zero, it matters, but it's not as strong as I think people would like it to be.

So what does that mean? I think we're going to get a lot of fall in inflation over the course of this year as goods inflation is negative, as shelter inflation falls. And so the, the, the anomalous, the non-cyclical part of inflation is now starting to go away on its own. And I agree with Jared, we need a good word that doesn't that's not transitory which sounds really really ephemeral, like boy it's the non-

cyclical component, it's the non-textbook macro component of inflation and that is going away on its own.

So what does the Fed want to do? The Fed wants to say, okay, suppose that's right. What about the rest of it? The part that really is that cyclical inflation. How much is it? Hard to know for sure, you can look at that other services component. But what they're trying to do then is to slow the economy down, to keep aggregate demand below the productive capacity of the economy for long enough such that once the dust settles, and that non-cyclical component of inflation has gone by the wayside and it is in the rearview mirror, the rest of it, the rest of the cyclically driven inflation is brought back down to target.

So how are they going to do it? They're going to, they're, they're driving along by feel. It's really hard to know. Jared pointed out very appropriately that we shifted from star-based policy setting, having a strong view on where r* is or where u* is. It's hard to know. And so they're waiting to see slowing in the economy. They're going to stay restrictive in their estimation, until there's enough slowing for long enough that inflation is clearly on track. And then they're going to be data dependent, which, you know, is sort of fly by the seat of your pants, because what else can you do? Models are great, but there's only so much precision that any model is ever going to give you. It's a very difficult job, but that's how I see them going about doing.

Louise Sheiner: Great. Greg, do you want to hop—.

N. Gregory Mankiw: Sure, just to say a couple comments? First, the one thing we all agree on this panel is the need for humility. That's an incredibly important, I don't think there's any profession beyond macro economists that requires more humility than what we do. We wouldn't always know that from watching CNBC. But we, macroeconomists have a good reason to be humble. In particular, I think Jared made a very good point in his original comments, which is as about u*, which is the confidence intervals that u*, the first person to make, that I saw make this point was actually in a paper by Staiger, Stock and Watson many years ago, which is the first paper I've seen that not only estimated u*, they actually econometrically generated a 95% confidence interval and that shocking thing was how wide that confidence interval was, which basically said we had no clue really what u* is, more or less. And so with the question, what does that mean? I mean, some people say, oh, therefore there's no Phillips curve, so throw that apparatus out the window. I don't believe that. But I do believe the Phillips curve is much more useful as a concept in economics textbooks than it is

as a practical monetary or fiscal policymaker. So I think it's much, much, much less useful than we, that we think. And I'll stop there as I know we're running out of time, and I'm sure other people have comments.

Louise Sheiner: Yes, Heidi, do you have any words? You don't have to.

Heidi Shierholz: I could just talk really briefly about the like, this question of how hard can wages go without like putting upward pressure on inflation. This like, the, if you in normal times, in the very long run, you take, you know, if we have inflation running at 2% and productivity running at 1.5%, then essentially at 3.5%, annual wage growth is in the long run sustainable. But we have seen this total smashing down of the labor share over the last three years. That means we actually have a lot of running room to stay at our higher levels of wages right now without putting upward pressure on inflation.

And Josh Bevins, I keep, we keep referring to him, but I will just say if we, just, just to give you an idea of the numbers that we're talking about, if we use 20, or sorry, 2000 labor share, the labor share that we had in the year 2000 as our benchmark, wage growth at its current pace is possible without seeing inflation above 2% all the way through the end of 2036. Like that's the kind of wiggle room we have to have higher wages and have, have labor sort of claw back what they've lost over these recent decades.

Louise Sheiner: I'm going to give you a few minutes if you want to, and then I'm going to go into a few questions from the audience.

Jared Bernstein: Just two points. I think this has been a great conversation and a lot of food for thought. Some of this stuff, like my riddle me this slide feels a little overdetermined, like we have more reasons why we know more explanations for this than we can quite balance out. But I'd like to make two comments. One is sort of a, a question or a little bit of a challenge to Heidi, because I think the last point you made is really important. And as I said, you know, the idea that, that a rising labor share or tempered profit margins, again, I cited Vice Chair Brainard's comments in this regard in my talk can pay for non-inflationary wage gains, you know, that, that's the kind of that's the kind of dynamic that I think President Biden walks around thinking about in terms of worker bargaining power and the equalizing impact, as Heidi and, you know, really your life work has underscored. And in fact, I was doing that work with you before you got there. I had, I hired her, at the Economic Policy Institute, gazillion years ago.

But, you know, so, so you see— and this is sort of an Econ Twitter thing— but it's a real thing, too. You see you see people like, well, the Fed should just, you know, cut it out and, you know, sort of kick back and, and not, you know, take jobs away. And we have, and the, you know, the kinds of dynamics that you and Josh Bivens write about. I think one of the challenges and maybe we haven't on the progressive I've done enough to talk about this is, you know, what mechanisms do we have to boost labor share, what mechanisms do we have to restrain profit share? Now, you mentioned unions, which, of course, you know, are key. But we need some, you know, we need more than that. And, and so I do think that, you know, I know Jason Furman talks about this in the spirit of like, talk about, you know, yes, that's certainly algebraically correct, but like we want to think about the kind of hydraulics, the mechanisms that get us there. And, you know, the Fed has a, a very strong and powerful and tried and true tool. So, you know, I don't know that we have a tool like that on the other side. I like to think more about that.

Last point, which I hope Greg in particular, and I know you've worked you know, you've led the council, so, you know, I hope this resonates with, with you as well as with the other panelists and with the audience. So the humility point is a really strong one and a good one. And we all, we all admit we're very humble.

Jared Bernstein: I have a very good joke about that which I don't have time to tell right now. See me later. But there's another level of humility that I'd like to suggest, and that's kind of political economy humility. There are a lot of things that economists and sort of more mainstream economists— that's not a critique— see in politics these days or politics forever that you know, they don't like. And that's aesthetically displeasing to them, this was to, you know, this stimulus was too large and this, you know, buy America thing is, you know, against what we've learned and all that. And, you know, I'm, I'm trained in these economics, and I understand where all that is coming from, I really do. And, you know, in many cases, I share the critique and I understand the rent seek and all of that.

But there's a level of humility that I encourage us all to think about which says we're trying to do you know, what we believe, what the president believes, what, Heidi, and I think what other people here believe is really great, important policy on behalf of strengthening workers. And sometimes that's not necessarily all kosher economics, sometimes it's political economics. And sometimes you have to do things that may not be as esthetically appealing in a neoclassical model to get to the policies that

do a lot more good than harm. So, you know, I think that's another level of humility that I would ask us all to embrace.

Louise Sheiner: Great. Thank you. Okay, we're going to open up. We just have a few audience questions right here. Wait, please wait for the mic. Stand up and tell us who you are, where you're from.

Audience Member: Hi. I'm Alexander Rifaat with Tax Notes. We talked a lot about sort of the demand sort of wage side, but it wasn't much discussion in terms of the supply side, structural issues of inflation, particularly on the sort of supply bottleneck issues that sort of led to, you know, sort of with sort of higher demand and few goods and services. You know, with, you know, the Biden administration's proposals for corporations, in particular the 15% minimum corporate tax, and then now also with high-net-worth individuals and minimum tax as well, do you have any concerns that this could deter investment in those critical infrastructure supply chain issues that sort of led to part of the inflation?

Louise Sheiner: I mean, you know, I'm going to take like two or three questions and then we'll answer the questions. Yeah, go ahead. In the back there.

Audience Member: All right. Thank you very much. That was a great panel. Thank you all very much. This would be a Jared Bernstein, please. Just a very maybe a simple question. You had that sort of Goldman Sachs, you know, that the inflation rate came down and wage, wage growth came down a lot more faster than we would have expected when we're looking at the unemployment and the GDP pain. But when I was looking at that NHS thing that you have, you have wage growth of that coming down a lot, but you don't really have, as you said, the inflation rate is sort of stable through that whole period. So I'm just trying to get my head around that.

Jared Bernstein: I can quickly sort of answer both of those. So on the last question, long and variable lags. So I'm being glib. You know, this is something that economists have dug into non-housing services will know it is a dog's breakfast of a category. It includes financial services, transportation, leisure hospitality. So it does correlate with non-housing service wages in the way that I, you know, kind of probably blew by too quickly in my presentation, myself, Ernie, Ernie Tedeschi and I, my colleague at the, at the council did look at the correlation between various, all the different wage measures and non-housing services inflation and the non-housing services wage measure was the best. It led, you know it it it it had the smallest error in predicting where non-housing services

inflation was going. But the r, but the correlation wasn't that high. So I think that those are related in the way that I argued they were. And if you look at Greg Ip's piece today, and I think he gets into that a little bit. But I don't think the correlation is gangbusters by a long shot because it's such a dog's breakfast of a category.

On the other point that you asked about, I think that the, I think that there's separable issues here. I think the taxation that you've talked about is really the least we can do to achieve the president's goal of achieving more fairness in the tax code and trying to ensure that those who are at the very top, the most profitable, stop paying effective tax rates that are lower than firefighters, nurses and teachers. And I think that's what that's all about. I think if you're looking to the economy, our work on the economy supply side in terms of both public and crowding and private investments, you need to look at the Inflation Reduction Act, the CHIPS Act and the Bipartisan Infrastructure Law, all of which we think have the potential to transform the economy supply side in terms of domestic production of chips, clean energy, and of course, reversing decades of disinvestment in public goods. So we feel pretty strong about where we are there.

Louise Sheiner: Great. I think we have room for one more question, up front here, I will take two actually, the first two people right up front.

Audience Member: I'm Annie Linskey at the Wall Street Journal. You didn't talk very much— thank you so much for doing this, I really appreciate it and for taking my question— you didn't talk about very much about the sort of looming crisis ahead of the administration, which is a possibility of a default on the, with the debt ceiling is not lifted to sort of given all of the sort of nuanced discussion that there's been about coming out of this last crisis, could you talk a little bit about what the impact of a debt ceiling, passing the debt ceiling would be, the kinds of things that the administration is looking at to mitigate that impact or to prevent it from happening in the first place.

Louise Sheiner: Just pass it to her and then we'll.

Audience Member: Yeah. Andrea Shalal with Reuters, thanks for taking the question. I wanted to ask about this kind of discussion that's starting now about whether the Fed needs to think differently about its inflation target. You know, is it time to sort of think about a slightly higher target or how long or how, how long they want to give themselves to get to the current target? I'm just really curious about that, given what you've said about this being, you know, these are unprecedented times, and the situation has really changed and particularly intrigued about the sort of step change in

terms of wage growth, like whether, you know, that necessarily requires that inflation would be at a slightly higher level, thanks.

Louise Sheiner: Great. Thanks. Do you want to talk about the debt ceiling, then?

Jared Bernstein: Yeah. Why don't you go, or somebody go first on the Fed and.

Louise Sheiner: The Fed up here. You want to answer that one? So, Seth, you want to, you want to take that or Greg?

Seth Carpenter: So I think the first thing is Chair Powell has been asked repeatedly about the 2% inflation target and has been very clear that under his watch it's not going to change. 2% has a long historical lag to it. Partly it would, with Ben Bernanke contributing to the literature on it first and then the formal adoption of it at the Fed, I think what's important from my perspective is that Congress sets a law for what the objectives of the Fed are. The Fed, the FOMC interprets that law and then comes up with a way to make it— to use an overly Washington word— to make it actionable. Flexibility there, I think, is necessary because this discussion by itself just shows how different one cycle can be from another.

So my personal view is any particularly rigid rule in legislation has a large probability of coming back to bite you in terms of not giving the policymakers enough discretion. I think the discussions we had about where the labor share of income is now relative to where it was in 2000, I mean, it fell pretty steadily from 2000 to 2015. We've got a really tight labor market, it started to eke out some gains back up, but I think the research cited is helpful. I don't think the current rate of wage inflation in any way is, is telling you that you have to have a different target other than 2%.

N. Gregory Mankiw: Can I add something quickly to that? Yes, 2% has a long history. I agree with Seth on that. But it's also if you look back at that history, it's kind of arbitrary. So, so, you know, I don't know any economists who'd really go down to the mat about two versus three. So if inflation gets down to three, I wouldn't be surprised that they say three is kind of close to two. So I wouldn't be shocked if they're, they're a little, they show some flexibility on that.

Louise Sheiner: Okay. I'm going to go to the debt ceiling. I just want to, I'm going a little plug, so Wendy Edelberg and I have something up on our website that talks about the debt ceiling and and not just like the sort of what would happen, but the huge risks, the huge uncertainty, how would it unfold? What would the markets do? Would that, would at the minute we reach the debt ceiling would,

all hell break loose, or would it be this slow dribble thing that would get so I think that I'm just, you pointing to that and talk about think about really what would it look like if we actually got there.

Jared Bernstein: You know, Annie, I hope you've heard some really thoughtful policy today from, from this panel, myself excluded. And I think one of the things we, one of the themes we've heard is that with a variety of critiques, you know, I don't think anyone, I don't think anyone contradicted my overarching point that monetary and fiscal policy have put us in a uniquely strong place right now, particularly referencing Heidi's comments from the perspective of working people, a 3.4% unemployment rate, over 12 million jobs, 800,000 in manufacturing, I think, you know the numbers, the Black unemployment rate at 5.4%, Hispanic at 4.5%, those are near historical lows. Those are the kinds of gains, achievements that are at risk when we start thinking about breaching the debt ceiling.

I tried to in my last, in my last slide, I talked about potential risks or shocks to the forecast. And I'm just going to repeat what I said because I thought a lot about it. The political own goal I have in mind is around the debt ceiling. It's never anything but the height of irresponsible governance to try to politicize or weaponize what should be a pro forma action. It is, in fact, an unequivocally clear constitutional obligation to defend our sovereign debt and pay for existing spending obligations. But to play these games when they're, when we're in the midst of a transition to more steady, stable growth with the Fed in the midst of a hiking cycle and the rate of inflation coming down is especially and to my view, just unbelievably reckless. It's, it's, it's political malpractice of the highest type.

David Wessel: So do any of the other panelists want to take the other side—.

Louise Sheiner: Disagree?

Heidi Shierholz: Can I make one really, really fast point about this? It also is a deal is also a big threat. So it's like we don't want to say, yes to everything Jared said I totally agree with. But we can't just say, oh, let's do a deal, the threat that it poses is huge. So to give an example from the Great Recession, the, we had a debt limit deal in 2011 that did anti-austerity to the economy that was twice as big as the 2009 stimulus package. Like it just obliterated it and was a key thing that caused our weak and slow recovery. So we have to also be careful about a deal.

David Wessel: No dumb policy.

Heidi Shierholz: No dumb policy.

David Wessel: So I want to thank Louise, Jared especially, Seth, Heidi and Greg for a lively conversation. I definitely want to call out Greg because I kind of collect good one-liners and we all admit to being humble is one of the best lines I've heard at Brookings in a long time. We might make T-shirts about that. I can think of a number of people who might need two or three T-shirts. Anyways. So thank you all for coming. We're going to post Jared's slides on our website where you can also find the fiscal impact measure that he kindly referred to at the beginning. And the video will be on the website so you can watch it over and over and over again. Thank you all for coming.