THE BROOKINGS INSTITUTION
WEBINAR

TRACKING THE RECOVERY FROM THE COVID-19 RECESSION

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PARTICIPANTS:

Welcome:

WENDY EDELBERG
Director
The Hamilton Project
Senior Fellow
Economic Studies
The Brookings Institution

Fireside Chat:

MARY C. DALY
President and Chief Executive Officer
Federal Reserve Bank of San Francisco

PETER ORSZAG
Chief Executive Officer of Financial Advisory
Lazard Freres & Co LLC

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P R O C E E D I N G S

MS. EDELBERG: Hello. I am Wendy Edelberg, Director of The Hamilton Project at Brookings. Thank you for joining us for our talk today on the economic recovery from the COVID-19 recession. The economic downturn induced by the pandemic threatened families' financial stability.

Today, The Hamilton Project releases a new economic analysis finding that in aggregate despite the many hardships families have endured household finances at the start of 2022 are in a better financial position than in 2019. That's thanks to robust federal benefits, the improvements in labor market income, increases in asset prices and reductions in consumer spending that boosted savings.

I'll start our event today by giving an overview of those findings. Then I'll turn the conversation over to Mary Daly, President and CEO of the Federal Reserve Bank of San Francisco and Peter Orszag, CEO of Financial Advisory at Lazard and Former Director at the Office of Management and Budget under President Obama and before that the first director of the Hamilton Project.

Mary started in 1996 at the Federal Reserve Bank of Chicago, the largest and most diverse district within the federal reserve system. She has built a distinguished career working towards an inclusive and sustainable economy. I am honored to have both Mary and Peter with us.

After I describe our economic analysis on the current state of household finances, Peter will pose questions to Mary on how the pandemic is continuing to affect the economy and in particularly the labor market. And what we can expect in the coming months. I know their conversation will tell us a lot about the intersection between the ongoing health challenges and the economic challenges that we are all seeing on a day-to-day basis.

We will be live Tweeting the event from @HamiltonProj using the hashtag #COVIDEconomy. You can submit questions for speakers by Tweeting with that hashtag the #COVIDEconomy or email info@hamiltonproject.org.

To show some of the insights we found in looking at household balance sheets since 2019, I'm going to share a few slides if I can click the right button. Here we go.

All right. I did this analysis with Mitchell Barnes, Sara Estep and Mariah Macland (phonetic) at the Hamilton Project. We looked at household finances from 2019 to 2022 focusing on changes to wealth, income, debt and financial distress.

We'll start with wealth. The real wealth of U.S. households has increased by more than $24 trillion over the course of the pandemic. This increase was driven primarily by rising stock market prices and rising house prices. That increase in wealth from real returns on assets is shown in teal. And only secondarily, the increase in wealth reflects an increase in household savings as you can see purple. These numbers control the rising prices. And so, were shown in 2020 dollars.

In the report, we breakout changes in wealth by income, race, ethnicity, education and age. So here you can see the percent changes in real wealth by income levels. All income groups have gained wealth since the beginning of the pandemic but particularly those at the top. People with lower incomes, and as we show in the report, lower levels of formal education took the longest to recover and saw smaller gains.

When viewed in dollar amounts, the top one percent's real cumulative increase in net worth excluding deposits was 19 times that of the bottom 20 percent.

For this slide, we have to set aside the distribution of the increase in household savings likely held in deposits because there is so much uncertainty about which households are holding that savings, but a rough calculation suggests that adding back that increase in savings would mean that the lowest income groups saw wealth increases more in the order of 20 percent. That's notably more than the increases shown in the figure of between 10 and 15 percent.

Borrower stress and borrower distress have also decreased over the pandemic. Even though debt has risen largely because of an increase in mortgage debt, the overall level of debt and the burden of servicing that debt do not appear to be significant headwinds for consumer spending. The chart on the left shows the ratio of household debt to disposable income.

Household debt to DPI steadily declined in the decade before the pandemic, but early in pandemic the substantial income support and only modest movements in consumer debt resulted in the decline in the ratio to the lowest level in years.

On the right, you can see the measure of the burden of making payments on that debt. Given the dramatic decline in interest rates on household debt, the significant increase in income and the relatively modest increases in debt balances that measure has remained in a serious low since early 2021.

Policy support so far has avoided the potential wave of delinquencies and bankruptcies. Here, you can see how different types of balances over 30 days delinquency reached lows during the pandemic. Delinquencies were heavily affected by forbearance policies under the relief bills in 2020 and 2021. Forbearance along with income support, a rebounded compensation, those low interest rates and continued access to credit resulted in extraordinary declines in delinquencies.

Many of those changes stand in stark contrast to the years following the Great Recession. Here's one example. In 2008 and 2009, credit card borrowing rose. In contrast, credit card balances fell $73 billion in the second quarter of 2020. The largest real quarterly decline in record. In addition, because access to credit card loans didn't decline, this paydown and credit card debt meant households have had greater farming capacity on the credit cards since before the pandemic.

And we've seen declines in credit card balances across income groups. This is likely the reflection of a few factors. Households used some of the fiscal support to pay down debt. Household have pulled back their spending on services during the pandemic. Automatic forbearance for other categories of debt like student loans freed up money that could be used to pay down credit card balances.

All right. So that was a lot of good news. Some of which may have surprised you. And you can read more or dig into the data on our website, HamiltonProject.org. If you're watching this on our website, you can scroll down for the link. But of course, it's not all good news.

Some households entered the pandemic in precarious financial situations and they will leave the pandemic in precarious financial situations. Many households were not helped by the increase in asset prices. And not all households were reached by fiscal support. Or so far by the labor market recovery.

The pandemic is ongoing, but most federal pandemic related programs have wound down putting household finances at risk as people face new health, employment and financial problems. Add rising inflation and many households are watching their household finances worsen with each passing month.

We need to be watchful of the ongoing headwinds from the pandemic and higher inflation, ensure that the labor market recovery reaches the most vulnerable households and prioritize policies that will make household finances more resilient in the long term. There's more to do and we are not out of the woods yet.

In that I think is a good time to turn things over to the next portion of our event. And I would like to welcome Peter Orszag and Mary Daly. I'll remind the audience that you can submit questions by Tweeting with the hashtage COVIDEconomy or by emailing info@hamiltonproject.org. And with that, Peter, I will happily turn things over to you.

MR. ORSZAG: Thank you so much, Wendy. And, Mary, delighted to have you with us. Why don't we jump right in? First question, the economy is being hit with two major shocks. One, the war in Ukraine and its impact on oil prices, on food prices and on supply chain logistics along with general uncertainty.

And the second, a potential, you know, the ongoing pandemic and a potential additional wave which we're seeing not only in the U.K. and parts of Europe but especially in China where the zero COVID policy, even though it's being loosened slightly is still causing significant disruption.

So how do you assess where we are in the face of those two significant shocks?

MS. DALY: Well, thanks, Peter, for the question. And thank you so much for having me here.

So you're absolutely right. Those are the two significant risks that are out there. And let me start with the context which won't surprise anyone. I think we're all living this. Every American is living this. We have inflation that's already too high.

So you add to it two major shocks to supply chains that only push up inflation and you get more pressure on inflation. More upward pressure on inflation at a point where inflation is already too high. So let me take each of the risks and I'll start with the war in Ukraine.

And the very first thing to say about that is that, you know, our hearts go out to the Ukrainian people who are suffering through this invasion and this subsequent war. The impact on supply chains is real. These are commodity producing countries, Russia and the Ukraine.

We get very many imports from Ukraine and from Russia. And both the sanctions and the lack of availability to produce in Ukraine right now is going to injure and disrupt commodity prices in supply chains even more than it already had been being done by the pandemic. So there's upward pressure inflation.

Now, for many Americans, they think, well, this is, you know, potentially a stagflationary shock because oil price shocks or oil supply shocks can also limit growth. But we're in a very different situation there than we were in the 1970s because we're in that petroleum exporter and that actually means that people who produce petroleum in our country get proceeds from it. So it washes out some of the effects on growth. But certainly, uncertainty is an issue. And we're all, you know, thinking about what will happen in Europe as this war proceeds.

And then, of course, while in the United States, you might walk around and think that we're moving from the pandemic to the end demic stage. In China, that's not the case. It's still definitely a pandemic and supply chains which have, you know, in every -- I think every two months, we say, well, they're going to get better two months from now or three months from now.

And we just keep kicking that can down the road because COVID has stayed with us longer than I think anyone thought. So those are both salient risks to the economy. The main risk I see is on the inflation pressures being more than we want, more than we need and certainly more than we thought just three months ago.

MR. ORSZAG: Okay. So there's a lot to talk about packed in there. But let's just start with the inflationary dynamic itself.

And there is a debate about how much is due to the pandemic and supply chain issues and what have you. And how much is due to U.S. fiscal policy to put it that way. When you look at inflation in the U.S. which is running much higher than previously, but also in Europe which is also up significantly. Not quite as much as in the United States, but still a material increase.

How do you sort through or how do you think about the causes of inflation and how much has been due to fiscal policy here in the United States and how much is not?

MS. DALY: So that's a question that many people spend a lot of time thinking about. And we just published some research today from the San Francisco research team that talks about this directly.

But I want to back up from trying to quantify those things and just start from the foundation, which is the pandemic in many ways is the culprit of this. It's the foundation. So why do I say that? Well, because we had fiscal response and monetary policy response that were meant to support people through the duration of the pandemic. Basically, build a bridge long enough to get as many people across the pandemic as possible. They could restart their lives and not be, you know, destitute because of something from no fault of their own.

So the fiscal response is really a part related to that. There's been infrastructure bills as well, but the bulk of the fiscal that people worry about being inflationary is really a response to the pandemic. And, you know, I think history will be the right judge of this, not me. But here you can look back and you can say, well, we actually weathered the pandemic as an economy better than I think many thought.

And so, if anything the bridge might have been a little longer. Both the monetary policy and the fiscal bridge a little longer than was absolutely needed. But you'd rather be on the side of history that builds it a little too long than the side that built it a little too short.

So now, we find ourselves with policy supported demand, which has remained robust stacked up against a pretty fragile supply chains and production. Even the economy where people had lots of money to spend and they rotated all that spending to goods rather than services. So this is a recipe for inflation. And whether you're looking at, you know, used car prices or just the reopening of the economy. And now, we're starting to see some services inflation. This is really a factor of the pandemic induced supply demand and balances. It's policy assisted the demand. There was no doubt about that. And now, we have an imbalance.

Going forward, I expect some of this to roll off. The fiscal isn't going to last forever. I think it has actually ended, but people still have this excess savings relative to history. So that will roll off over some period of time. That's going to be helping get demand and supply back in balance. I suspect, I know I'm doing it, that as I can come out of my house and not have to buy only things. I start taking in services. So I get my own spending back in balance. I expect Americans to do that as well.

That will be a release on some of the inflation pressures. And then, of course, the supply chains will hopefully repair at some point. Although, as you pointed out in your first question, the risks are still salient. So in the end, you know, I think it's less about scoring how much was fiscal, how much was the pandemic because ultimately a lot of the fiscal, the lion's share that's, you know, creating some of the pressure on inflation was related to the pandemic.

Had we not had a pandemic, we probably wouldn't have had those kinds of supports being offered.

MR. ORSZAG: So let's talk for a second about some of the other effects for this year. You mentioned that a lot of the fiscal impulse, if not all of it, actually has reversed. And so, that is a constraint on growth.

The demand destruction from higher energy and food prices is another. There are some forecasters now suggesting the U.S. is only going to grow basically at trend for 2022. How do you see the growth prospects as apart from the inflationary dynamic for the economy as you look out today?

MS. DALY: Sure. And I did shave a little bit off my own growth forecast. You know, I thought it would be above trend. I still think it's going to be, you know, a little bit over trend or at trend. And that's very healthy by the way, when we have already inflation.

So getting this economy back in balance where we grow it about trend would be a very good economy. It would be an economy that continues to support a strong labor market and one that wasn't over its sustainable level in a way that would even put more pressure on inflation.

So I think an at trend growth against all the headwinds that the U.S. economy faces is actually quite remarkable and really something we've seen throughout the pandemic. That there's been this basic resiliency of the economy to shock of the pandemic and all the ensuing constraints. And now, forecasters at trend growth basically around two percent growth for the U.S. economy. And some are a little higher. Very few that I've seen are lower than that.

That is actually remarkable when you've got the pandemic headwinds from China and other parts of Asia. You've got the war. You've got all the constraints on supply chains. You've got inflation and to still think that we're going to have that kind of a growth rate, to me is a good sign.

On the inflation side, you know, I expect the policy adjustments, the federal reserve is making along with all the things we just talked about, the normalization of supply and the rolling off the fiscal impulses you say. Turning from positive to at least neutral if not negative this year. Those are all going to be factors that bring inflation down.

But I don't think we're going to get to two percent by the end of the year. I just think we're going to hopefully see -- this is what I'm expecting to see and what we would need to see -- monthly inflation numbers marching down as policy adjust and these other factors take hold.

MR. ORSZAG: Let me ask you a little bit about that. I mean even over the past week, the fed seems to -- and again, there's a little bit too much, you know, tealeaf reading -- but the feds seems to have shift towards more concern about the risk that inflationary expectations could become anchored at a higher level.

And so, to act more aggressively or expeditiously to avoid that outcome. But if you look at the forwarded inflationary expectations, the five year or so. The expectations of five-year inflation starting five years from now. It's sort of basically exactly where it was. It's been flat over the past few months. It doesn't seem to have moved very much. Ten-year inflationary expectations are up at bit, but they're still at basically two percent.

So if there is sort of a newfound concern is it because of the war? Or are people over interpreting? Or is there something in the data that the market is not seeing?

MS. DALY: So let me speak for myself here and not the members of the community. But I will say that I don't have a newfound fear that we've lost our inflation anchor. When I look at the data you just cited, I see well anchored inflation expectations.

But what I do hear and what I do see is a concern that when something persists for long enough, inflation, high readings on inflation, that that tugs at the anchor. That that tugs at people's sense about is the bad really going to control inflation? And what I've seen repeatedly is inflation that we can link back and we can tie to pandemic related disruptions.

But I'm starting to see that broaden across into services. I'm starting to see it in wage setting practices with a tight labor market that, you know, when firms are having to pay larger and larger wage increases. And workers are demanding higher and higher wage increases to offset rising prices that they see at the grocery stores or other places, at the gas pump.

And so, these inflation shocks that you get from the Ukraine war, but also the COVID disruptions in China that just come around again. These are things that put additional pressure on there. So I would say that my own policy views, I would put it this way. My policy views are we got an economy that has clearly demonstrated it can fundamentally work on its own without the extraordinary support we offer.

So it’s time to remove the accommodation we’ve been providing which is again extraordinary support. So that means marching up to neutral and looking at whether we need to go over neutral. So tighten a little bit, restrict the economy to ensure that inflation comes back down. But ultimately, we're in charge of price stability and full employment.

And right now, the full employment mandate seems to be met. The labor market is extraordinarily tight and it’s tight for a variety of different groups that have traditionally been underserved. And we find that inflation is far too high. People are thinking about inflation when they get up in the morning. And they're thinking about it when they go to bed at night. And that’s actually not price stability.

So that’s why I’ve adjusted my policy stance between say December and March, the last meeting just was -- which was last week. And it will absolutely help solidify the inflation anchor, but it wasn’t because I thought we had lost the inflation anchor.

MR. ORSZAG: Okay. And we're going to turn to the labor market in a bit. And I know that’s something that the San Francisco fed has focused a lot on.

But let’s just for a moment talk a bit about what, you know, just a little bit of retrospective on what might have gone wrong in terms of the belief that inflation would fade more rapidly than it has. Is it just because the pandemic has gone on for longer than expected? Or what's the cause of that?

And I will immediately admit and I'll do this now publicly that I had a bet with Jason Furman about the core PC number for 2022, which I have now prematurely ended because I will be wrong and he will be right. So I'm in the camp also of thinking or hoping that it would have faded sooner than it has. But what's your analysis of why a lot of the predictions from 2021 about 2022 look like they were too optimistic?

MS. DALY: Sure. And I think that's a fantastic question. So, you know, I was one of those individuals who thought that we would find ourselves with lower inflation in '22. That we're going to ultimately end up having.

And so, I've asked myself, where did I get this wrong? What was it that I expected that didn't occur? And there's several things. And so, let me go through them.

So the very first one at the foundation is that I actually thought with vaccinations being as effective as they were and as safe as they have been proven to be that more people would get the vaccine and that we would beat back COVID because we would use the vaccine to really, you know, kill it off. And at least domestically, where we had very effective vaccines and access to them. And that just didn't happen.

And so, we ended up with additional variants that caught hold, Delta, being one of them. That really, you know, put us back into these semi-lockdowns again. Nothing like the first one, but still we limped along in terms of shaking this from us. And then we had Omicron too. And you know, this put people back in their homes again.

And so, it just -- you think about that globally where the vaccines haven't been as effective or the take up has even been lower. And COVID has just lasted for much longer than I anticipated it would given that we had remedies to help, you know, move it away from us. So that didn't happen.

So the second thing that didn't happen is that I expected that as we were able to go back to school. And our kids could go back to school and they could stay in school. That we would find that those disruptions would relax and that moms and dads who were providing kids and also other kinds of, you know, elderly parents, community members. You know, they would find themselves ready to return the labor market. And labor supply would come back up which would ease some of the pressure in the labor market that we still see.

So I expected us to have this labor supply recovery and we just haven't seen that. So that's another place where I didn't anticipate that so many people would stay persistently out of the labor market even as conditions improved. And I didn't expect that the supply chains would take so long to recovery because COVID would still be with us.

And then the finally thing that I didn't expect is I didn't expect people to continue spending so much on goods and that over rotation. I mean, the American consumer has been incredibly resilient and incredibly interested in purchasing things when they couldn't purchase services.

And I've been one of those people. So but, you know, I thought at some point we've all got -- as many pelotons as we can possibly use. And yet, we still see things, this goods rotation for our purchases, you know, dominating what we're talking about. And all of those things contribute to the duration of the inflation ratings we're seeing. And the labor market, the wage growth, et cetera, the tight labor market puts the pressure on wages.

So these things are just here for longer than I expected. And while I continue to think that they will ease up at some point, what's true now is inflation is persisted for long enough that people are starting to wonder how long it will persist? And we know, you know, I'm a student of history. If you read about the 1970s, it took a decade really to get inflation expectations anchored at a really high level. The cost of painful correction. It took many, many years.

But we’ve had it for one year and I’m already focused on, let’s make sure this doesn’t get embedded and we see those longer running inflation expectations start to drift up. So I’m reassured that they haven’t yet, but I’m mindful that if that happens then we get ourselves in a cycle that makes it harder to correct.

MR. ORSZAG: Okay. And I want to turn to the labor market in a second, but just one more question about how to think about the current state of financial markets and growth prospects which has received a bunch of attention which is the yield curve. And in particular, the fact that the 10-year yield relative to the two-year yield is hovering around zero. It's still positive, but it’s down significantly.

Yesterday, Chair Powell said, don’t focus on that. Focus on kind of the nearer terms, 18 months. The yield curve out over a much shorter duration. What’s your view of whether it’s useful or not to be looking at the yield curve in terms of whether we're on the precipice of a recession?

MS. DALY: So either the correlation research and I will distinguish correlation from causation. The correlation of yield curve inversion and recessions is, you know, I think missed one over the course of its history of being correlated.

But that’s not causal as all of us know. And the causal research finds very little evidence that one creates the other. That an inverted yield curve causes a recession. There’s just factors that occur that would make that correlation a positive.

So when I look at the yield curve, I actually ask a different question. I ask why are the 10 years low? You know, why is the yield on 10 years low? And there, you could look for factors and you can -- they're understandable factors. So one is that we have a flight to safety. You know, we are still the reserve currency. And so, we're a safe place, a safe haven when we have geopolitical disruptions. We have pressure on our longer-term yield.

The second is, and I think this is something that's important, is that, you know, markets don't expect us to have an unanchored inflation expectation that will create this longer running inflationary cycle. They don't expect -- and if you look at the yield curve and you read anything from that tenure, there's not a sense that we're going to have a runaway inflation that persists forever.

I think there's a little part of that. And I don't want to be too -- I don't want to put too much in there. That would be hubris. But I do think that that signal is not there. That these are the signals that financial markets, at least expect inflation to get under control in the longer period of time.

And so, with Chair Powell is referencing is the literature on the inverted yield curve in saying that what's really more material is the two year and a shorter duration, not 10. You know, the shorter part of the yield curve, the shorter durations. But I guess the main thing for me is I want all the things that go into the yield curve.

The yield curve is a piece of information but it's not an infinitive piece of information. And what I see out there is that markets seem to understand. As do businesses and households who I talk to on my regular work. They seem to understand that it's time for policy to adjust. That the fed is on track to make these adjustments. To get the economy and the policy right sized again. And that that's going to happen even though we have these uncertainties around the Ukraine. And we have the uncertainties around the pandemic. It's still time to tighten policy in the United States.

MR. ORSZAG: Let me ask you about the first factor that you listed there which is the dollar as the world's reserve currency and kind of the flight to safety.

There are some people who are worried that the impact of the surprisingly strong sanctions against Russia during the war in Ukraine may cause other countries, China, India and others, to seek more of a replacement to the dollar. Sebastian Mallaby and the

Washington Post this morning or yesterday argued that's pretty much an idle concern because there's no other place to go really other than the dollar or the Euro which are both participating in the sanctions.

So how do you evaluate the prospects for the dollar as playing this key role in the global economy? And is there a risk that central bank reserves and basically the role of the dollar in the world economy will change over time?

MS. DALY: So this is a good time for me to remind everybody that we don't make dollar policy. There's no dollar policy at the fed. We don't talk about the dollar. We don't talk about the movements of the dollar at the Federal Reserve.

But I can as an economist back up and say, you know, how do I think about being a safe haven? And it ultimately always comes back to property rights. Do countries think that they can get their liquidity? Get hold of their assets when they invest in a country? Even in conditions of stress?

And that's ultimately what creates a safe haven currency or safe haven asset. And so, that hasn't changed in all of this. Is if you invested in the United States, you buy bonds, you can get them. You can get your money back and return those things. And so, that's ultimately what I think is the driving force. And I will leave it to others to figure out, you know, what kinds of additional pressure we might face because of different political decisions that we've made, important ones, of course.

But that's ultimately what it comes back to. And I would say give the same answer if we were talking about alternative digital currencies and other things. Ultimately, this is about property rights and do you expect to get your money back when you invest it in a country? And in the U.S. we have a long history of doing just that.

MR. ORSZAG: I would note the exception would be if you're Russian and not in the sanctions list right now, but point taken.

Question for you. Let's turn to the labor market because that's been an area of a lot of your focus at the San Francisco fed included before you became president and CEO. So there currently are 11 million job openings in the U.S. Talk to us a little bit about how you see the dynamism in the labor market. And what would you be hoping for in terms of the number of job openings to be in a more sustainable place?

MS. DALY: Well, that's a terrific question. I mean, you know, I get asked a lot by -- so one of the things I do as a federal bank president is I spent a lot of time talking to businesses and labor unions and community members.

And you hear an interesting thing right now which is if you're in labor, you're saying, well, what's wrong with this job market? This is pretty good. Yeah, this is the first time we've seen rapid wage growth in our area. It's the first time we have a pick of jobs. And so, why is this not a good outcome?

And my answer is because it's ultimately hard to sustain, right? It's really hard to sustain the economy when we find ourselves with, you know, firms. It's a regular occurrence now that firms will make an offer. And before the person even starts, they go and work somewhere else. And so, they're just -- you know, this is so much turn and so much, I guess something that used to be only incurred in dating is now occurring in hiring, which is ghosting.

Where you hire a worker. They don't even show up for the first day. And so, these are things that ultimately are inefficient in the economy. They make -- you know, firms are spending a lot of time on trying to figure out how to get workers and retain them. And there's so much turning. There's really no chance to gain productivity and productive output. You know, inputs to get output.

And then on the labor side, I'm seeing, you know, people leave jobs very quickly. And it's actually something fascinating. So I think the dynamism is good. But I was meeting with some young people and they're changing jobs every three weeks. And I said, well, what are you going to put on your resume when you go to find another kind of job? Well, they hadn't really thought of that.

And it was sort of like an outcome of these job market searchers just like auctions. And you can auction every day. It's a spot market in labor almost. They are not ultimately what's good for the long run. Sustainability of the economy. In addition to pushing up wage inflation, which could ultimately shove price inflation. Putting us in sort of a vicious cycle. It's just not a very sustainable way to manage the economy.

So I see dynamism out there as good. I see the labor market as very strong. I also see us in a reallocation period where we're trying to figure out what's the long-run demand that people have for goods and services. And how do we get workers positioned for that?

These are all things that will hopefully work themselves out over the next year or two as we transition out of the pandemic. But the American labor market has been remarkably resilient. And I hope that it remains that way as we go through this. I think it will. That's my goal is to create smooth landing with policies so we can have it be that way. So that all those individuals who have not yet come back from the pandemic will have places when they rejoin the labor force and they are looking for jobs.

MR. ORSZAG: Okay. So a bunch of more questions on the labor market. I would just note for everybody tuning in that you can send in your questions in about 10 minutes or so. I'm going to turn to your questions. We have a bunch that are coming in and that were sent in ahead of time.

But, Mary, let me ask you a little bit more about the labor market because one of the other puzzles has been that over the past, you know, two decades there's been the declaration of the death of distance and you can work from anywhere. And yet, even in the places -- and you know it well because it's in your region. Where there are hubs of innovation. Silicon Valley being perhaps the most famous.

It has still been a very localized labor market where the in-person coffee chats kind of matter. Do you think that's going fundamentally change going forward post-COVID?

Or are we still going to be, you know, in an era where despite all the hoopla about people moving all over the place and working from anywhere, geographic mobility has been declining for several decades. And the in-person experience in a localized labor market still seem to matter? Do you have a view on how that might evolve?

MS. DALY: Yeah. The first thing I'll say is that, you know, I feel like we've lived four lives through the last two years of the pandemic with this.

So in the beginning, I heard from all of our business contacts that we'll never go back to the office. Then I heard, we're going to bring everybody back to the office. Then I heard we're going to bring only a few people back to the office. And now, we're seeing waves of people coming back to the office.

And we just brought everyone back in a hybrid style two weeks ago here at the Federal Reserve Bank of San Francisco. And so, here's what I have learned in the two weeks we've been back in hybrid. People like the flexibility of being able to be home on certain days or live other places or go and see a family member and be able to work remotely for a while. And they also like the in-person contact.

And labor markets are fairly local despite the fact that some people want to live in a rural area and work in a city. But all of these things I think we will have another year or two to figure them out fully and across the economy. But I think what will come through is that we'll want a little of all of those things. There won't be a right model that emerges tomorrow and that's the one we'll all adopt.

What will happen, I think, is that we'll find that the flexibility is actually a much more inclusive way to run a labor market. That divisible labor is a little more inclusive as well. That, you know, we might want -- we've got people wanting to do part time because they found that in the pandemic, they went part time and they like part time.

And so, a divisible hour. So we're not so rigidly attached to 40 hours, Monday through Friday. Having -- some people like working in the morning and the evening and taking the afternoon to do things for their family. That's completely reasonable. Having people live in different locations and only come, you know, two days a week to the office or one day a week or three days a week. Whatever suits them. But having really, we call it here purposeful presence.

When we're here together, let's be purposeful about it. The worst thing you can do to people is make them get in the car or on a train, public transportation or even on an airplane, commute and then sit in an office by themselves zooming with people. That's a terrible outcome.

So what I see is we're all going to experiment. We're going to try things out and we're going to find models that fit people's lives. And my hope there, frankly, and I'm an optimist by nature, but my hope is that we'll find ways actually increase the labor supply in our country because we're not making people fit a specific mold in order to work. We're allowing them to have a mold that works for them but still recognizing they have productive labor to offer.

MR. ORSZAG: By the way, just as an aside. I think I saw that FLMC met in person for the first time recently. If that's correct, I think --

MS. DALY: It's true.

MR. ORSZAG: Yeah. So just talk to us a little bit about how the Fed itself whether that changes the dynamic in the room? How the Fed itself functions virtually versus in person?

MS. DALY: You know, it's really fascinating. And I'll speak more broadly then just about the FLMC. So we were able to do all of our work. We'd go out. You know, we were one of the first banks to go out because we had, you know, cases in the Bay area. So we went out really early in March of 2020.

And the FLMC stopped meeting in person in that same month. The last FLMC I had done was January 2020. And now, this last meeting was the first one I had done again, March of 2022. And in all of those times, we continued to have conversations. We continued to do what everyone is doing. All the centers here are doing. Zooming, using, you know, every program you can imagine to do -- and learning new skills so that we can have all the important conversations we need to have and do all of our important work for the American people while we're at our homes.

I mean so many of the news interviews I did were from my dining room table. And I had a broken wrist at the time trying to prop up my iPad. So we would learned to do all of that. And so, the work hasn't really changed. But what's changed, and I think you notice when you said we're back in person, you saw a smile on my face. What I miss is just the coffee time conversations, right?

The you break from any meeting. You can imagine any meeting you go to, you break and you have a minute to say, hey, what are you working on? And how are you thinking about this? And so, it's that spontaneity that creates innovation. I think creates thinking. We were lucky at the FMLC because we had -- we knew each other already. We had time with each other under our belts. And so, we're using that capital, that relationship capital. We're living off that.

But think about the new people you introduced to, you know, teams or processes. They don't have that relationship capital so well built up. And I think that is another aspect of being together. So I loved being in person. I was smiling from the time I got there until the time I left for having that in-person experience. And it's something that I think is really valuable. It's why we are doing hybrid in I think every bank and board of governors is going to a hybrid model. So we get the best of both worlds.

MR. ORSZAG: Okay. Before we turn to audience questions. Just one more on female labor force participation and the research that the San Francisco Fed has done on the link between school closures and school re-openings and female labor force participation.

First, could you just characterize that for the audience? And also, to the extent that schools have re-opened and you may not have seen the full impact of the labor force uptick that was hoped for. What might explain that?

MS. DALY: Yeah. So the thing that we find and, you know, many researchers have found is that these disruptions to school are really critical because it's childcare, right? It's a form of your children are cared for while you can go to work. And if you have to do the childcare and Zoom schooling is -- you still have to provide the childcare.

Very few children I know, and I know a lot of them, are good at Zoom schooling all by themselves. Especially when they're younger, but even as they get older. So you need, you know, parental help whether that's mom or dads. But moms still in our country take on a large fraction of those responsibilities. So these are disruptions.

And those things matter for labor supply. And I can just also reflect on my own experience in my organization, running the organization. Moms are stressed. Dads are stressed too. But moms are really stressed because they're thinking do I have to pick -- I mean, I had a situation where one mom had three kids. One was on a COVID watch, one was home quarantined, the other had to get to school.

So you've got all these -- one is in a special classroom for the COVID watch, the other one is home and the other one has to get to school and go for a regular day. This is a lot of stress. And it matters for labor supply. And now, we see schools re-opening definitely. But we're just now -- I mean we just came out of our masks a couple of weeks ago here in San Francisco.

And in other parts of the country, you're easily sent home if you've got an exposure or you've got the same thing as here. Your kid gets quarantined. You've got to take care of this. So I don't think we're past COVID yet.

And I think that's why moms and dads everywhere say, well, we don't want to change anything yet because the worst thing you can do is really say, well, I'm starting a new job. I'm all in or going back to full time. I'm all in. Oh, and now I have to miss the next three days because I've got to go take care of my child or my parent or whatever it is.

So that is material. And I do respect women to come back to the labor force when there is some breathing space so that the tradeoffs aren't so severe. Right now, I just say the tradeoffs are too high.

MR. ORSZAG: So we have a question partly in response to the Hamilton Project research that was released earlier today on the increase in household savings, but also partly related to your depiction of the economy still growing at least at trend. Which is fundamentally why don't people feel better about this economy?

It seems like performance despite the inflation is very solid at the least. And yet, the mood is perhaps not fully reflective of that. Do you have any views on what might explain the disjuncture?

MS. DALY: Sure. I will offer a few views. You can come back and see if I'm right down the road.

But here's -- I mean sentiment is an interesting thing. Sentiment's guide to things that are really on people's mind. And so, we aren't fully through the pandemic. You know, the new variance. I mean you're open the paper every day and you see concerns that maybe those will come here. So we're not completely through that. We haven't fully been able to go back to our lives.

We have a lot of inflation. That is a hard thing for sentiment, right? When you go to the gas pump. These are, you know, what I would refer to as pocketbook prices. Food, gas, housing. These are things that hit people directly. And what they're seeing is, you know, in Bay area gas prices are over $6 a gallon. And the down average in the nation, they're up $4 a gallon. These are pretty hard things for people. And then they see their price of food go up. Those are kind of decrease sentiment, of course.

And then the war. I mean the war is a lot of uncertainty. While it hasn't had a direct effect on our shores, you know, many of us known Europeans. Many of us know Ukrainians and it's a lot of stress that environment. And just we had something that we had to think about for a long time.

So you put all of those things together and I think how could it be otherwise that sentiment would be a little weak. But the economy is fundamentally strong. And when we find ourselves with inflation coming down, I think you will see sentiment go up. But for now, it doesn't surprise me. Sentiment is shaky, but it is remarkable how resilient the economy has been.

MR. ORSZAG: You know, one more question on the economy which is about Northern California in particular. I've been to San Francisco and to Palo Alto several times over the past few months. And frankly, Embarcadero feels a little bit like a ghost town and Palo Alto feels like it's sort of back fully. That might be a misleading antidote.

But talk to us a little bit about how Northern California is doing relative to the rest of the country. And how much variation there is within Northern California.

MS. DALY: So the thing that Northern California is it's got a lot of tech. It's got a lot of other things too. Travel and tourism, but tech is important. And tech was a growing sector in the pandemic. It has been for the duration of the pandemic.

As all of us had to buy a lot of things and learn how to do new things under new technologies. It's been just a booming and thriving sector. So Palo Alto has been, you know, it's been thriving since the beginning of the pandemic. It's continued to thrive. And now, you can just see people outside more and thriving because they used to be at home thriving. Now, restaurants are full. People are able to go places. I see the same exact things you do.

Down here where I am. I'm at the Embarcadero. It is really a ghost town still, but it is much more lively than it was during the pandemic. So I see green shoots. I see businesses reopening. I see, you know, we're coming back. I see small shops reopening. New shops opening. Ones that maybe got displaced during the pandemic. I see things coming into their place, but it's going to take a while. Because, you know, think of downtown San Francisco, not Palo Alto.

It's a lot of businesses that are still trying to decide. Are they going to come back? Or are they going to let their footprint go in commercial real estate and just have a remote workforce? Are they going to move to a less expensive area? These are all things that San Francisco and other big cities, the financial districts in particular, will have to sort out.

But I think it is -- this is one thing I will say. I think it's a mistake to judge -- not that you have done that, but, you know, just for anybody looking. It's a mistake to judge the strength of our economy based on looking at just what's happening in this downtown perimeter because there's lots of momentum here. It's just taking place in the suburbs or around the areas from people's homes as opposed to in downtown San Francisco.

So Palo Alto is kind of a good marker for how the economy is doing.

MR. ORSZAG: Question from a viewer about state and local governments. And the declining employment there, but maybe more broadly. They did receive a significant amount of federal assistance. How would you characterize both the employment trajectory of state and local government? And also, their financial prospects?

MS. DALY: Well, state and local governments are in good -- I mean this is not something that you can say universally because some states and localities are differently managed and have different issues.

But in general, they're in good situations. I mean they were not as hard hit. The revenues for state and local governments were not as hard hit as many people thought they would be. And they did get some fiscal assistance from the federal government that shored up those resources. So they are in good financial shape.

In terms of their employment, it depends really on where you are and what they are providing. But I think there's a combination of things going on there. And it varies by state.

But some of it is just they employ a lot of or they are helping with a lot of things that went digital. And so, now you need fewer workers, right? Because you've moved everybody home. You didn't need to provide those workers. And now, you're never going to come back. And so, this is a transition period for state and local governments. And where the steady state level of employment will end, I'm not quite sure. But I do think this is just part of the transformation that all -- the whole business sector is going through and state and local governments are just part of that.

The good news, though, is that the budgets of state and local governments are in good shape especially when you put it relative to where you might have thought they would be after a global pandemic and two years of a lot of economic distress.

MR. ORSZAG: Okay. Another viewer question. How can colleges serve as economic engines going forward? So what's the role of community colleges? And what's their impact on the labor market and on educational attainment?

MS. DALY: So, you know, I'm going to put that question, if you don't mind, in the context of something that we've been working on. We're thinking a lot about.

I think employers across the nation are thinking a lot about it and should think a lot about it. Is that, you know, we have a lot of people who may not want to get a four-year degree. And the question is do we need a four-year degree for everything that people want to do?

But we have a system we asked for that credential. And there have been many researchers who argue we're over credentialed, right? We just use that as a signaling device, but if you trace back the skills and abilities, you don't need all of that type of formal education. You could use other types of things.

And so, in that picture, community college fits as do other certification programs and other things. And I think one of the other things that I learned in the pandemic is that people want more divisible ways to learn, to work, to parse through their careers. And community college offers that type of thing.

So I think community college, four-year colleges, certification programs, on-the-job training. These are all part of what we need to think hard about as employers and as an economy, as a society about how do we ensure that everybody gets an opportunity in the economy? And we recognize that we might not complete every single piece of education you want to do at the age of 22.

Maybe you'll have snippets here and there to help yourself be more nimble as the world changes. So I see community colleges playing a valuable role. They're not the only answer, but neither is a four-year college the only answer. We need an array of possibilities.

And I hope out of the pandemic grows that sense in a tight labor market. Grows that sense that, you know, there's a lot of people out there who could work in the jobs that we have available.

MR. ORSZAG: Okay. One more question from viewers. And I'll just phrase it as, what in your mind is the most important -- and you've touched upon this a little bit so you might just refer back to your previous comments. But what's the most important lesson that we should have learned from the economic response to the pandemic?

MS. DALY: Well, I will refer back to my comments, but I'll try to succinctly restate them. And, you know, one of the most valuable lessons -- well, history will be the judge, right?

I mean researchers, countless new Ph.D.'s and other people will be generated that will study the response to the pandemic and decide whether it was just right, too little, too much, whatever. But what I will say is that when you're in those situations in real time and you're facing something you have not lived through.

We didn't have a lived experience of a pandemic. That you have two choices. You can do the minimal and hope it's enough or you can do the thing that you think could be a little bit too much but you know the bridge will be long enough.

And I lived in this real time and I'm glad that we chose to do what we thought was going to be necessary to get as many people over. If history judges that the bridge was a little bit too long to me that's a very little mistake to have made. I would not be able to live as easily with having built a bridge too short because I was afraid that we might be too long. Does that make sense?

MR. ORSZAG: Makes sense. So final question and you already mentioned that you've accumulated a lot of stuff during the pandemic. Part of that goods demand.

But any other silver linings for you personally in terms of having lived through this pandemic? Did you pick up a new skill? Was there some part of the pandemic that, you know, you're grateful for in some unexpected way?

MS. DALY: So I'll separate it into new skills and what I'm grateful for. So new skills, I learned to box, shadow boxing.

MR. ORSZAG: Wow.

MS. DALY: And I got better at golf. So both of those things are good. You need one because boxing let's off steam. Golf just creates steam and stress.

And what am I most grateful for? What am I grateful for? You know, my wife and I spent more time together in two years because I didn't have travel. And she didn't have to travel. And while you think, oh, gosh. We're cooped up in the house together. We spent years together, two solid years together that I will remember for the rest of my life. And I think that's true of so many families and friends.

You just -- we make connections in ways that we weren't able to because we spent loads of time together. So if we have to look for a silver lining in the pandemic that's my silver lining.

MR. ORSZAG: What a great answer. Well, Mary, thank you so much for joining us. And to the rest of the people who listened in or will be listening in later when this is available on the web. Thank you for joining this Hamilton Project episode. And look for the new research out from the Hamilton Project. And again, thank you all for joining us. And, Mary, thank you in particular for such insightful answers to the questions.

MS. DALY: My pleasure.

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