The Economic Club of New York

114th Year
618th Meeting

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Webinar

Moderator: Vonnie Quinn
Anchor, Bloomberg

Introduction

Barbara Van Allen, President and CEO

Good afternoon and welcome to the 618th meeting of The Economic Club of New York in our 114th year. I'm Barbara Van Allen, President and CEO of the Club. As many of you know, The Economic Club of New York is the nation's leading nonpartisan forum for discussions on economic, social and political issues, and our mission is as important today as ever as we continue to bring people together as a catalyst for innovation and conversation.

A special welcome to members of the ECNY Class of Fellows – a select group of very diverse, rising next-gen leaders. This morning they actually had a one-hour session with Dan Schulman, which was terrific. A special welcome also to our graduate students joining today from Fordham University and Columbia University.

It's a pleasure for me to now welcome our special guest and Club member, Nancy Lazar. Nancy is Partner and Co-Founder of Cornerstone Macro, where she leads the Economic Research Team. Nancy's work is well-known for being comprehensive, highly-detailed and unbiased.

Before founding Cornerstone, she was Co-Founder and Vice Chair of ISI Group for more than 20 years. She's been an *Institutional Investor*-ranked economist for the past 17 years, ranking in the top two for the past nine years. In 2015, she ranked #1. Nancy has also been named to *Barron's* 100 Most Influential Women in U.S. Finance in 2020 and 2021. Prior to founding ISI in 1991, Nancy was an SVP at C.J. Lawrence. Nancy is a member of New York Forecasters, Money Marketeers, NYABE, NABE, and Women in Finance & Housing.

The format today will be a conversation, which we're fortunate to have Club member and news anchor at Bloomberg, Vonnie Quinn, doing the honors of moderating. We're going to end promptly at 2:45, and as a reminder, this conversation is on the record and we do have a fair amount of media on the line. So without further ado, Vonnie, the mike is yours.

Conversation with Nancy R. Lazar

VONNIE QUINN: Thank you so much, Barbara, and thank you to everybody at the ECNY for putting on these events and keeping us connected through the pandemic. I know that we'll be back in person at some point, hopefully in the fall, and thanks to everybody, and welcome – as you say – to everybody. I'm excited to be interviewing Nancy. She's a rock star in the field, and we're going to hear some very interesting thoughts from her today on a day where we're seeing bond yields move. We're hearing

comments from the Fed chair. We have fresh comments from the President on the Fed and from Janet Yellen, the Treasury Secretary as well, so lots to get into.
Nancy let's begin with your outlook just for GDP growth in general. Obviously, we'll get fresh data at the end of the month and economists are broadly looking for 8% GDP growth in the last quarter. Your great handoff theme, you're actually even more enthusiastic about how the economy is recovering.

NANCY LAZAR: We've been very excited about the success of all of the stimulus that's been put in place. And importantly, that stimulus has fueled big drivers of growth. It's not as if, that lower interest rate, a lot of cash from the Fed, obviously the fiscal stimulus from the government has helped to really reinvigorate the economy, creating a lot of positive momentum. We've been very, very optimistic on growth, expecting this V-rebound. We're still a little stronger for even 2-Q GDP growth. We're closer to 10% for the second quarter. We think on average this year you're going to get about 8 ½% GDP growth, which is also still more than consensus.

And the reason for that is that, again, to emphasize, the stimulus, the fuel moved big drivers of economic activity, important drivers of economic activity – technology, manufacturing, capital spending in general, which is underappreciated as a driver of growth. And then obviously it was led by housing way back in the spring. We just learned today, NBER said that this was only a two-month recession. The trough was in

April. How can that be? And again, I think that's because we are a very healthy economy going into the crisis and the stimulus was appropriate and it fueled these drivers of growth. And we're now finally seeing it show up clearly in jobs.

VONNIE QUINN: So I do want to get into some of your great handoff themes, but before we do, when do we see peak GDP? And is there a danger that with some new variants or the possibility of maybe lockdowns again – we really don't know what's going to happen over the next few months – that this outlook has to shift?

NANCY LAZAR: Peak GDP is probably 2Q, 2Q - 3Q. But the question is where do you go from here? I mean is it going to be a crash back down to 2% GDP growth, or have we created a potentially even healthier economy driven by capital spending and productivity where GDP can be stronger than generally expected? We're using 4% for next year. So peak growth right now is certainly, but it doesn't mean – I'm a skier – it doesn't you're going over a Double Black Diamond. It could be just a gradual moderation in growth. You are getting handoff, as you suggest, into new areas. Maybe we now have all bought too much furniture and we're ready to go out and do some traveling. So within consumer spending, you are getting this handoff. Consumer spending growth will start to slow, but indeed with the job market, I think growth could end up being better than expected, particularly in 2022.

VONNIE QUINN: So we have to talk about inflation clearly. It's the dominant concern for markets and for everybody right now. What do you see in terms of inflation and then perhaps I'll prod you a little bit on that outlook?

NANCY LAZAR: So, as I wrote yesterday, it's good news we're seeing peak stimulus. It's good news we're seeing peak growth because that increases the odds we're going to see peak inflation. That is, it was sort of expected to have the V-rebound in economic activity with the stimulus and the reopening. Obviously, the inflation – we thought we were going to get some inflation – it was more than what we expected. But our view is still very, very much that it is transitory. Just as growth can't continue to be 8 to 10%, inflation – in our view – cannot be 4 to 5% for a sustained period of time and won't be 4 to 5% for a sustained period of time.

And let me define what I mean by inflation specifically, I mean CPI or the core PCE deflator. We can come back and talk about wages in a minute. And so just as you've had a handoff in economic activity, you're having a handoff in pricing, which is early on there was demand-supply imbalance as the economy reopened. Demand was very strong, for example, in housing, and that created very, very strong housing starts which then fed into house prices and obviously fed into lumber prices.

And so what happened over the past year with lumber, this may be a sense of minutia, but I think it's – too much minutia, but I think it's important – lumber prices surged. Over time, production finally caught up with lumber new orders. Over time, you started to see an increase in lumber inventories and lumber prices have crashed. So having really led this whole expansion, both activity and inflation, now we're arguing housing is leading us in the other direction. If you are a sector where you've raised prices too much, used cars, you are very vulnerable right now because the consumer is fighting those price increases. You're getting demand destruction very clearly in housing. Actually longer term I'm bullish on housing, but near-term I'm cautious on housing.

So I use the housing example, where what's going to happen over the next six months? One of the keys over the past year is not to look here, but to look at the bigger picture. Consumers are protesting these higher prices. You clearly saw it in housing. You're starting to see it in cars. My guess is you're going to see it in furniture and anything else that's gone up in price. This is not the 70s where you buy in anticipation.

And that's in part because the stimulus that we saw put into the economy was just for a very short period of time versus the 1960s, you had multiple years of aggressive monetary and fiscal stimulus, whereas this was a one-year phenomenon with monetary stimulus now fading as is fiscal. So this year, yes, inflation by the end of the year could still very well be something 4 to 5%, but by next year we think inflation will be back down certainly with a 2 handle and maybe even less than that. Listen to housing. And we think you're going to have declines in goods-producing prices that were benefitted from the Covid recession.

VONNIE QUINN: So we shouldn't listen to Larry Summers too closely, the likes of Jamie Dimon and, say the PepsiCo CEO who is talking about putting up prices. They're missing something or they'll reverse course very soon.

NANCY LAZAR: Well, those are all brilliant men and so I certainly would listen to them. I just tend to disagree with them. Again, no question right now. But if you got too caught up a year ago, for example, if you got too bearish because of where we were and missed the growth trajectory recognizing the stimulus and the health of the U.S. economy was going to turn things around, obviously you missed the rally.

So now let's look ahead. So to be sure, if there was another aggressive fiscal stimulus package, I might change my tune. And I don't mean another trillion-dollar infrastructure package. If we were to see a $3.5 to $4 trillion fiscal stimulus package, which increased the size of government and longer term reduced productivity, well, of course, I would become concerned about inflation. But that's where right now, right now we don't have another massive fiscal stimulus package and my colleague, Andy Laperriere, doesn't think we're going to get one. And that actually started to unfold this Spring.

Right now, federal outlays, if you dissect the data, which we do, federal outlays are declining. Nobody knows it because you all look at the data on an annual basis. Essentially, federal outlays have declined because the last big bucket of stimulus was in March and what drove the federal deficit this year was not a sustained shift up in the size of government as a share of GDP, it was a one-time fiscal booster shot to the consumer. And now it's gone.

On the monetary side, money supply growth has clearly accelerated very rapidly, up over 25, 30%. It's now slowing very quickly. So first you have to understand why it accelerated. Well, it accelerated because one, the FED eased very aggressively. It lowered rates and increased its balance sheet. It also accelerated because a lot of people were given a lot of money. People were still working. They didn't spend their money. They parked it in their checking accounts. This is common event during a crisis. And the combination of those three things exploded money supply growth.

But now what's happening? The economy is reopening. The fiscal stimulus checks are obviously no more. Fed balance sheet, although still growing rapidly, is not growing as rapidly as it was a year ago, and the interest rates have stopped going down. The combination of those forces are actually now slowing money supply very quickly. It's not the 1960s where you had that guns and butter program that was put in place for years that then erupted obviously by further policy mistakes in the 1970s. Now if we're wrong and there is another massive fiscal stimulus package, I might have to review the outlook.

VONNIE QUINN: Well, I know you're – as you said – Andy Laperriere and Don Schneider are the team that thinks that if we do get a reconciliation bill, no matter what's in it, it'll likely be deficit-neutral and they will only be a very, very small impact on GDP from any infrastructure package. Do you want to expand just a slight bit on that?

NANCY LAZAR: So I'm bullish on infrastructure because the private sector is reinvesting in this country. And if you have the private sector creating new facilities, from a warehouse to a factory, to a new bank building, the localities classically reinforce that and put in place infrastructure. You see it around the country. But specifically, the federal government, quite frankly, is likely to do something relatively small, maybe a 0.23 tenths GDP for 2022, is incremental. Government spending programs that are complementary to what the private sector is doing are classically successful.
And so I'm bullish on infrastructure spending even without an infrastructure bill, but if we get it, it would just further increase the odds. But, no, it's not big enough to really get us concerned about a bigger government, and at the end of the day obviously infrastructure spending could improve productivity and could be more positive for the economy. So that's kind of, productivity-enhancing government spending incrementally would actually be good news.

VONNIE QUINN: Let's talk a little bit about the labor market more specifically and the idea that, you know, we're seeing some inflation right now, how long does that last? At what point does it affect wages? And could that be a little bit of a good thing for the economy as Ken Rogoff suggested over the weekend in the FT that perhaps the economy can sustain quite happily a little bit of higher inflation if it is to feed into wages? And then I want to ask you how that impacts the gig economy.

NANCY LAZAR: So at the end of the day, I think we are ending secular stagnation. So I agree with a lot of the conventional thought today. And I think the reason you're ending secular stagnation has nothing to do with the temporary increase in prices that we've seen today. Again, this is, just as we had a temporary V-rebound in economic activity, we're having a temporary surge in CPI prices. I do believe wage inflation troughed back in 2010 at just 1.4% and is on its way back over 3%, and I'm using specifically the employment cost index. It is going to be important to watch the appropriate measure of wage inflation.

And the acceleration in wage inflation actually did start in the back half of 2020, the back half of the last expansion, about 2015. Why did it start? Because we had a capital spending recovery, which led to an increase in blue-collar jobs, which lured people back into the labor market, and you saw a shift up in the prime age labor force participation rate. There's been an under-appreciation – I've said it once, I'll say it 1,000 times – in the importance of capital spending in creating jobs, and therefore taking us out of secular stagnation.

So the real reason, I think, wage inflation is moving out of stagnation, i.e. something below 2% or less, which is where we were from 2000, roughly 2008 through 2015, 2% or less in wage inflation, is because the demand for jobs was deteriorating because blue-collar jobs were declining. Blue-collar jobs are at the heartbeat of this economy. They disappeared from 2000 through 2010 as China, as investment moved from the United States to China. Blue-collar jobs are coming back to this country. We had one of the biggest increases in goods-producing jobs in the last expansion since the 1970s. And, as a result, over 60% of industries in this country are hiring. Back in 2010, it was below 50.

The demand, my point is, that with the reinvestment cycle in the United States, the demand for jobs are going up. We see that in JOLTS. Broad-based increase in demand from manufacturing, for restaurants, and so it's that breadth of demand for jobs that is actually putting upward pressure on wages. And one has to appreciate it as a tremendous positive, and we think that is actually ending secular stagnation in this country, not the incremental price increases we're seeing associated with the imbalances from the Covid crisis.

VONNIE QUINN: So, just laterally a little bit then, just for self-curiosity, what does that do to something like the gig economy, which has been sustaining, you know, a whole level of worker that we had never seen before in this economy, wages that are very difficult to even discern what they are and people taking on two and three and four gig economy-type jobs, you know, with VC and venture and private equity backing? Does that go away?

NANCY LAZAR: It wouldn't go away, but it's a little bit of a, maybe it was a little bit of a bubble that's now shrinking some. We potentially aren't as in need of people working three or four jobs if you can indeed see a more sustained increase in wages. So the gig economy isn't going to go away, but as we see in any sector, a little creative destruction is normal and potentially just wouldn't grow as quickly as it had been. I mean you're seeing people consciously decide, eh, I don't want to work at a restaurant anymore. And guess what, they can get a higher paying job.

This idea of allowing a high-paying, blue-collar, goods-producing jobs, manufacturing, construction jobs to leave this country, whose idea was that? And then, oh, well, they'll be transitioned over to the service sector. Well, gosh, those are lower-paying jobs. Oh, well, everybody will go to college. Not everybody wants to go to college. I grew up in a blue-collar factory town. Not everybody wants to go to college. They enjoy working in factories and then going fishing in upper Michigan. So you need a broad footprint of industries hiring, which is what we have. Building room for gig economy workers and there's going to be room for factory workers along with economists and newscasters. This is actually quite a healthy economy.

VONNIE QUINN: So what should we make of the Federal Reserve at the moment then? Has the Fed met its goals for employment and inflation? And, if so, why is Chair Powell still looking for substantial further progress even if he allows, you know, for a lot of uncertainty in the coming months?

NANCY LAZAR: So you haven't yet seen a sustained period of inflation rising about the Fed's target. I mean this has been obviously, the last six months you've had this extreme pop in both headline and core CPI, it's not yet sustained. And I do agree with the Fed that it is transitory. As demand and supply gets more in line as you're already seeing with lumber and we think in other sectors of the economy, you will see prices come back down. Again, we're thinking next year inflation is going to be less than 2.5% and we're actually writing a report about that tomorrow. So, one, on inflation.

Now two, the labor markets, they are very concerned about the participation rate. I tend to look at the prime age labor force participation rate for the demographics and it certainly has declined significantly. It's also now starting to recover significantly, in June anyway. One month doesn't make a trend, but you had a nice pop in the prime age labor force participation so people are returning. The Fed would like to see that return back to its pre-Covid level, in particular the overall participation rate and the prime age labor force participation rate. So, no, not yet, they've not met.

And I can understand, it's one thing for me to make a forecasting error that doesn't affect the economy. It's another thing for the Fed to make a forecasting error. So I can understand their concern about the still-depressed level of the labor force participation, but I would suspect they're going to be pleasantly surprised over the next year, and that we think we do, by the end of 2022, see a full recovery in the prime age labor force participation rate.

VONNIE QUINN: So I know your Cornerstone's Roberto Perli has some kind of an announcement, either Jackson Hole or potentially the September meeting. Do you agree that we will see something that might move the market? And what is the bond market signaling to us now anyway? We saw it breach its July low today to go to 117 and change on the 10-year.

NANCY LAZAR: So Roberto does expect the Fed to announce some sort of taper. I found it interesting that if you read that article last week that the Central Bank of Canada has decided to pull back on its tapering. So we're now moving into that period. And again, I would argue that the U.S. economy is healthy enough. Look at corporate profitability. One of our themes when you say it's a handoff is it's a handoff from the public sector to the private sector. And we're lucky as an economy that we have that. We've had a V-rebound in corporate profits. We've had a V-rebound in private sector compensation growth because of jobs and wages. And so we can now have a successful handoff from the public to the private, to the private sector.

And so we think the Fed has room to start to taper. There's plenty enough liquidity in our banking system today. So companies, corporate profits, consumers, banks, there's plenty of liquidity in this economy. Now, to be sure, that could create some incremental increase in interest rates. It wouldn't be a surprise. Roberto doesn't think there's going to be too much because the Fed is telegraphing this far enough in advance.

But as far as why have bond yields come down, again it correlates beautifully with our theme, because federal outlays peaked in March and are now declining. Money supply growth is flowing significantly. Again, the theme is the reflation trade is over and that's not a negative. It's a positive because it implies that indeed this inflation is not engrained. It's transitory. So I think the bond market has figured out, one, long-term growth rate obviously isn't going to be 8 to 10. And two, inflation is not going to be 5. And, if anything, a year from now we're going to be talking about disinflation again when you talk about the CPI.

VONNIE QUINN: Nancy, President Biden came out today and actually spoke about the Federal Reserve and inflation, which is interesting, perhaps walking back some previous signaling or what have you. But he mentioned the word transitory as if to give Chair Powell a little bit of support. And I'm curious, does Chair Powell have another term? Does he get reconfirmed? Does he want to get reconfirmed? And will we see further Powell moves at the Fed?

NANCY LAZAR: Again, that's from Roberto. If I were the administration I wouldn't, given the concerns and uncertainties in this current economic environment, despite my pre-extreme bullishness, I don't think you want to do anything to rock the boat right now from a financial market perspective. But obviously I don't know. I would hope that he would be reappointed. I think he's done a very incredible job pulling us out of this crisis, helping to pull us out of this crisis.

VONNIE QUINN: So let's move a little bit to Treasury now. We have Janet Yellen, previously of the Fed, at Treasury. She seems to be, you know, enjoying maybe making a little foreign policy as she goes as well, which is interesting. Today, we had some comments about China and how perhaps those tariffs that were initially introduced under Trump were maybe not so thoughtful so she obviously has a bit of skepticism. That said, she had already said that, you know, there was no point in continuing with strategic dialogues with China. Where do you see U.S.-China relations going as it relates to, you know, economic relations with Yellen at Treasury?

NANCY LAZAR: Well, it's clear, both the Democrats and the Republicans agree on one thing, that China has increasingly become a bad actor for many reasons – from human rights to corporate IP theft, etc. So there seems to be a unanimous opinion in Washington on we have to make sure we're putting in place the appropriate policies for China.

I think the world has to adjust to a very different U.S.-China relationship. This is, I don't think this is, this is not transitory. We think this is a secular shift in many ways, a secular shift down in China's growth. I'm not bearish on China's economic activity. China's economy is going to be fine, but it's changing. It's not going to grow as robust as it had early in the last expansion. It is a sustained shift down in growth. That has huge global implications to other countries and companies that have depended upon that growth.

Second, China is increasingly embracing Buy China, made by Chinese companies. And so the western world had gotten used to having China – kind of like fishing in a barrel – they could sell anything and it would boom in China. That era is over. China is very focused, from airplanes to EVs, buying Chinese manufactured goods. The question is will it one day be the luxury goods that they also then make? So China is secularly changing, we would argue becoming more inward on their own choice. They're inward.

They want to support their own.

And importantly, Beijing is putting in place tough regulations. The community in the United States was worried earlier that indeed Washington might go down that path. Well, we still might. It's happening in China. You could take their heavy, you could use the phrase, heavy hand, which I use a lot, but I think, let's call a spade a spade. China is implementing draconian regulations on the national champions, the technology sector. And that, longer term, does make me concerned about the economy.

Those national champions, those technology companies have been major reasons for the health and strength in the Chinese economy. The last thing you want to do is deter innovation in China. They have a huge demographic headwind. They need innovation. And I worry by putting in the draconian regulations from raising capital to sharing information amongst one another, giving information to the government, limiting their growth, that they're going to squash innovation. And that, longer term, is a big headwind to their secular growth trajectory because the only thing they have driving growth longer term is productivity. They don't have the demographic background.

VONNIE QUINN: Yes, you have to wonder how, you know, China intends to proceed because surely China doesn't want to squash its own innovation either and clearly they're keeping a very close eye on the economy as they always do. We had that triple-

R cut last week, there's micro-management there. But beyond what China does for itself, how does the ripple effects come to the United States? How do we feel these changing times in China here in the domestic economy?

NANCY LAZAR: I worry about multinational companies, therefore multinational profits, that have been too dependent on China's boom – from technology companies, manufacturers, the auto industry to Wall Street – and that the way it comes home is through corporate profitability. We happen to be much more optimistic on domestic profits than we think multinational.

So if China's secular support for global growth is fading, it's going to be less than it otherwise would be, if they're increasingly buying more Chinese-made products, which they're making clear they are, then U.S. multinational earnings, which have been the darlings many, many times during the decades, are going to have some significant headwind because it doesn't stop in China. If China ends up being weaker than expected, then other EM growth in general will also be weaker than expected. So it comes down through multinationals.

VONNIE QUINN: And I guess that's a little bit of a longer-term outlook, perhaps a five-year outlook.

NANCY LAZAR: And maybe not quite five years, but the market has a funny way of discounting things ahead of time.

VONNIE QUINN: For sure. Just in terms of multinationals, as you bring it up and we're speaking about the Treasury, does the global minimum tax succeed? Do more corporate headquarters come back to the United States? And ultimately, are there more receipts for the U.S. Treasury?

NANCY LAZAR: The best way to grow corporate tax receipts, as we've just seen over the past year, we have not had corporate tax increases. Yet one of the reasons the CBO lowered their budget deficit estimate for fiscal year 2021 is because tax receipts are $500 billion higher than they thought they were going to be just three or four months ago. And so the best way to generate tax revenue for this country is to encourage the private sector to grow, and I would argue you don't do that by meddling with corporate tax, meddling with corporate tax rates. We're now competitive around the world. I'm not too keen on government regulations that – I don't know what the right word is – impact business decisions. And so I'd rather the corporate tax rate around the world be left alone and left up to each individual country, but that's a personal view.

VONNIE QUINN: It is a very interesting move on the part of Treasury. We'll leave that for the next conversation to see where we are by then. Back to the immediate impact of

Covid. Obviously, you know, there's a lot of vaccination going on in the United States. We're sort of cresting, hopefully, with vaccinations. You know, generally anyone who wants one can get one now. It's not the case in the rest of the world. There are many, many countries that are still suffering Covid to a tremendous degree. What happens if we see countries stop and start, open and close their economy? Britain even is opening its economy today, but there's really no telling how that experiment is going to go because Britain certainly is nowhere near the level of vaccination that it would like to be at.

NANCY LAZAR: So I have about a half dozen risks for the U.S. economy. We're cognizant that there are still risks for global growth. And I keep waiting to move Covid down from the number one risk and unfortunately it's not. It's still probably, it's still the number one risk. And I think it's really the number one risk indeed for the EM world in general, and I would add that to the maybe near-term headwind, for multinational earnings is the EM world is obviously the most behind when it comes. And I have to also add that the Chinese vaccine, which has been used in some of the EMs, not all but in some of the EMs, is also not very effective. And that, to me, is also an important negative mark on some of the lack of success China has made in certain areas, so the EM world in particular.

And it is going to be very interesting to see how governments react. We've already seen, I think L.A. mandate masks, mandate masks again. But the bigger issue is are we going to have another major global lockdown, and I would guess certainly within the major DM economies, I don't think so. I think it's been perfectly clear how destructive those lockdowns in and of themselves were and that we are indeed getting decent vaccination rates in most of the DM world. So it's still there. It's going to create economic waves. We're seeing it in the markets. You're seeing it some of the travel and leisure stocks over the past several weeks actually. And so it's still unfortunately an incremental headwind through the global economy. I just don't think it's going to be detrimental particularly for the DM world. More so to the EM world.

VONNIE QUINN: You know, I remember when Janet Yellen was at the Fed, she would talk a lot about, you know, feedback loops, and central banks obviously around the world are on high alert. You know, the RBNZ, the Bank of Korea, all of these banks, moving or waiting to move or about to move, keeping a very, very close eye on how Covid is affecting their economy. If we get a series of EM central bank moves, does that tip the Fed in any particular way? Do we have to watch those just as closely as we're watching the Fed these days?

NANCY LAZAR: You clearly have to watch what's going on around the world. And China, actually again, may be leading the pack as you and I were talking about earlier. They did cut the triple-R last week more than expected. There's a chance they're going to cut interest rates incrementally tomorrow. And so we actually are, had been prior to China's move, in an EM tightening cycle. We had roughly a dozen EM central banks raise rates over the past six months. China has been ahead of the curve on a lot of these moves. That changed obviously last week. The question is what will lower interest rates, what will more stimulus do to fight the temporary effect of the Covid crisis? It's not clear that the central bank policy really needs to change much.

Actually, China is experiencing also an uptick in Covid cases, and that could create wider easing, but we also think that they're easing because – on the other hand – they are tightening regulation. And they don't want the economy to slow down, they want it to maintain some sort of constant momentum. So to be sure, we have to watch central banks around the world.

VONNIE QUINN: Nancy, I'm very aware that we have many, many members dying to ask you questions. Unfortunately, they can't do it in person and, you know, I'm here, so I get to ask some very intelligent questions on behalf of the very intelligent ECNY members to you. We have touched on some of these already but let's take the first question here because it talks to productivity and we only just barely touched on that a little bit. And I'll read the words of the ECNY member.

Looking back at Robert Gordon, where do you see productivity in the future?

NANCY LAZAR: I'm very bullish on U.S. productivity growth, and I have been for about, I guess six, seven years now. The only way, and this is classic economics, the only way you can have a sustained shift up in productivity growth is if, first and foremost, you have a sustained shift up in business investment. And from 2000 to 2010, as companies shifted investment from the United States to China, we had a deterioration in productivity growth. It was directly related to – I'm all for globalization, but we could potentially have handled it a little bit better by somehow not penalizing domestic companies with the highest corporate tax rate in the world, basically in the industrial world, from 2000 through 2015. So companies, rightly so, shifted production to China to lower their costs and boost their profit margins. But the destruction that created to the economy is underappreciated.

And this is actually a passion I have. I wish policymakers would embrace; they made a mistake. When I make a mistake, you admit it. We made a mistake in not incrementally supporting, encouraging in some fashion – I would argue lowering the corporate tax rate because that also would have been a good idea – to balance, to make it a fair fight between more companies the FICA choose. Because again goods-producing jobs, blue-collar jobs, from 2000 to 2010 dropped seven million. A lot of heartache about all these restaurant workers, to be sure. I'm sorry, I don't hear many people complain about the blue-collar jobs that disappeared in which there's a whole group of people that that's all they, quite frankly, wanted to do and there's nothing wrong with that.

So globalization, as it was, actually destroyed capital spending, labor force participation, and productivity. If you don't invest domestically, you destroy domestic productivity. The companies that went to China, to be sure they improved their productivity. That's Chinese productivity, not U.S. So what happened was productivity deteriorated. Labor force participation deteriorated. Potential GDP growth deteriorated. And you can all link it back to China joining WPO and this government doing nothing.

Now, had the manufacturing renaissance started in 2010, China decides in 2010, eh, I've got enough investment. Almost 50% of GDP. At the same time, the United States became an increasingly competitive place actually to put new facilities and then you had the energy renaissance. So capital spending started to pick up and by mid, mid-the last cycle, about 2016, we started to see productivity improve, labor force participation improve. It was led by the e-commerce world and again we think it's being led by the e-commerce world.

So prior to Covid, you were getting improvement in productivity. Just look at the data. You were going from something less than 1 to 2, 2, 2, almost 2%. We smoothed things out. During Covid, more and more industries are embracing digitization, from restaurants, factories, to banks, to the travel industry. We think we've come out of the Covid crisis at even a higher growth rate, 2 ½% to 3% productivity growth. That's probably the only good thing that's come out of this. And that helps support wage inflation, but also keeping labor costs tame and core inflation tame. I remain very optimistic on U.S. productivity growth.

VONNIE QUINN: And that all leads, of course, then to profits being protected I guess and company margins being protected.

NANCY LAZAR: If you are a company and you've not invested in your business and you've not improved your productivity, you're going to have a problem because wages, even the strong demand for jobs, because of a healthy U.S. economic backdrop and many strong companies, you're going to have to pay higher wages. And if you haven't improved your productivity, you've got a problem. But net, yes, profit margins stay stronger longer because overall productivity does accelerate.

VONNIE QUINN: So here's another one. We talked a little bit about lumber, but somebody asks do you have any sectors that you watch for fun. And what are they telling you? And this person actually mentions autos, and we didn't mention autos and I do want to because we're seeing sort of the pandemic effect come out of autos a little bit as well.

NANCY LAZAR: I think autos are very important to watch early cycle, to be sure. If they can be strong, be it after 9/11, obviously with some fiscal stimulus help, but Covid, they're two areas in which, I remember having a conversation with one of my colleagues about, oh, my God, when are car sales going to get back to 18 million units? A lot sooner than anybody expected. To be sure, for a good reason, we didn't want to take mass transportation, etc., but we also had the finances to do that.

So housing and autos indeed are at the leading edge. I'd add one more and that would be rail. And quite frankly, all three, particularly housing and autos are softer. We would argue that's a reflection of, well, for both, in part supply constraint. We need more houses and we need more cars and because of the supply and demand imbalance we can't get them as quickly as we have, but also because prices have gone up too high.

The housing industry, the NAHB has suggested that indeed consumers are protesting these higher prices. We think used car sales are just going to plunge given the 45% increase you've had in used car prices. So I'm watching both in activity and I'm watching housing and autos for both inflation. And they both also confirm this idea that the inflation acceleration is transitory.

What the rail industry is suggesting is that similar to everything else, that growth is peaking. New orders are peaking. I know there's still a lot of congestion within a lot of the ports which could be also creating that kind of status. Don't look at rail year over year. You've got to look at rail activity sequentially. I worry that rail is also telling us that new orders are peaking and I must, one other little thing I worry about is that there's been a lot of double ordering, and I know I saw it in lumber. There was an article in the paper last week about Popeye double ordering chicken. I worry that there's some double ordering going on and I'm watching real closely for a sign that maybe new orders start to fade.

VONNIE QUINN: To fade, wow, that's fascinating. Nancy, I know that crypto is not something that you concentrate on, given that you're deep into the economy, but there is, you know, an interesting question to ask, I suppose. You know, if it's not crypto causing an extreme, do you worry about extremes in the market anywhere?

NANCY LAZAR: We were talking about this the other day. There are always bubbles – let's call it what it is. In every expansion, there has always been an excess that builds. You can go back, you know, obviously in the 70s it was commodities. You had the junk bond bubble in the 80s, in the 90s, commercial real estate, 2000s, housing. So for every cycle, there is an excess, to be sure in part because of extreme stimulus in the system or risk taking in the system. And so be it crypto or SPACs, yes, for sure there's going to be an excess so there's going to be a bubble in this expansion. Always is. And when the Fed starts to tighten, it's always popped, and it always creates turmoil. I've seen this game too many times.

VONNIE QUINN: Do you want to make a prediction as to where we might see it?

NANCY LAZAR: No.

VONNIE QUINN: I didn't think so. I see Barbara is back on, and you did touch a little bit on some of the other questions for the members at least. So maybe not exactly how they've phrased them but we did touch on trade policy and so on. So, Nancy, I would like to thank you, fantastic comments, and I know that people can probably get in touch with you directly should they want to know a little bit more. Thank you very much for today.

NANCY LAZAR: Thank you very much for your great questions.

PRESIDENT BARBARA VAN ALLEN: Thank you, Nancy and Vonnie. Wow! That was a great conversation. I hope you all enjoyed it as much as we did listening. I'm pleased to report we have a few more great speakers lined up this summer, and as always, we encourage you to invite guests. Next up we have Floyd Abrams, Senior Counsel at Cahill, Gordon & Reindel. He's going to touch base on the timely First Amendment issues that are in the news today. That will be followed up – that's July 26th – by Tony Malkin, the Chairman and CEO, President of Empire Trust Realty, along with Gayle King, CBS Morning Show host. They're going to talk about New York City and what we see there in the commercial real estate market as well as the broader New York City return as we go into what looks like might be a new normal. And then we have a kind of super closing on August 2. We have Scott Gottlieb of the American Enterprise Institute, the 23rd Commissioner of the FDA, in conversation with Becky Quick. He's going to provide an update on Covid-19 and the implications of the fast-spreading Delta variant as we head into the fall. And then that same day in the afternoon, we will have Steve Cadigan, who is the Founder of Cadigan Talent Ventures, discussing his new much-talked about book, *Workquake*, and the suggestions it holds for coming back to work also in the new normal. So, again thank you.

I also just want to mention real quickly, we're excited about the fall. We're hoping to come back together in person, and we're making plans to do so. We start out with our first in-person element, September 13, with Hans Vestberg, the Chairman and CEO of Verizon. We'll also be offering that virtually as well of course. John Williams, the President and CEO of the Federal Reserve Bank and our Chairman, September 19th, is going to talk about the U.S. economic outlook. If you joined as a guest today and you're interested in membership, you can see the email to learn more on the screen.

And finally, I want to thank our Centennial members that may have joined us today as their contributions make a big difference in terms of our ability to provide our wonderful, diverse programming now and in the future. Thank you again. Again, Nancy, Vonnie, wonderful conversation. Everyone, please stay healthy and safe. Thank you.