The Economic Club of New York

ESTABLISHED 1907

The Economic Club of New York

117th Year
766th Meeting

Dr. Lisa D. Cook
Member, Federal Reserve
Board of Governors

June 25, 2024

In-Person/Hybrid Event

Moderator: Jason Furman
Aetna Professor of the Practice of Economic Policy
Harvard University

Introduction

President Barbara Van Allen

Good afternoon. I think we all have to confess that it's nice to be in the air conditioning. It's quite warm again and being indoors is a wonderful thing sometimes. So good afternoon and welcome to the 766th meeting of The Economic Club of New York. I'm Barbara Van Allen, President and CEO of the Club. And I'm happy to have all of you here today as well as the large virtual audience that we have.

We are recognized as the premier nonpartisan forum in the nation for discussions on social, economic, and political issues. And for more than a century, the Club has hosted over 1,000 prominent guest speakers, and that tradition continues up to and includes today.

I'd like to extend a warm welcome to students who are joining us virtually from Rutgers University, NYU Stern School of Business, my alma mater, the Graduate Center there, as well as members of the largest-ever Class of 2024 ECNY Fellows – a select group of diverse, rising, next-gen business thought leaders.

We're honored to welcome back Dr. Lisa Cook as part of our Equity and Inclusion programming. As you may know, in 2020, the Club launched its Inclusion and Equity

programming with support from corporate partners, which included, and includes Mastercard, PayPay, S&P Global, Taconic Capital and others.

Lisa took office as a Member of the Board of Governors of the Federal Reserve System on May 22, 2022. Prior to her appointment to the Board of Governors, Lisa was a Professor of Economics and International Relations at Michigan State University where she also served as the Director of the American Economic Association's Summer Training Program. While at the helm, she championed increased diversity in the field of economics by preparing talented undergraduate students in economics and related disciplines.

Previously, she was on the faculty of Harvard University's Kennedy School of Government, a Deputy Director for Africa Research at the Center for International Development at Harvard, and a National Fellow at Stanford University. From 2011 to 2012, she served as a Senior Economist on the Council of Economic Advisors for President Barack Obama, who she worked with on issues related to the eurozone, financial instruments, innovation, and entrepreneurship. From 2000 to 2001, she was a Council on Foreign Relations International Affairs Fellow and served as Senior Adviser on Finance and Development in the U.S. Department of Treasury's Office of International Affairs.

She served on the Boards of Directors of the Federal Reserve Bank of Chicago and the Federal Home Loan Bank of Indianapolis as well as on advisory boards of the National Science Foundation, the Opportunity and Inclusive Growth Institute of the Federal Reserve Board of Minneapolis, and the Lemelson Center for the Study of Invention and Innovation at the Smithsonian Institution in Washington.

The format today will begin with prepared remarks from Lisa followed by a conversation in which we're honored to have Jason Furman doing the honors of moderating. Jason is the Aetna Professor of the Practice of Economic Policy jointly at Harvard's Kennedy School and the Department of Economics at Harvard University. As a reminder, this conversation is on the record. We do have quite a bit of media, both in the room and online. Time permitting, we'll take audience questions from those in the room. Without further ado, please join me in welcoming Lisa to the stage.

Opening Remarks by Dr. Lisa D. Cook

Thank you, Barbara. It is a fitting time to be speaking again to The Economic Club of New York because this month marks two years since my first Federal Open Market Committee meeting. At that meeting, we kicked off a series of large interest rate increases, all of which I supported, because I am fully committed to bringing inflation sustainably back to our 2% target.

As I said when I joined the Board, I care about both sides of our dual mandate – maximum employment and stable prices. When inflation was well above target and the unemployment rate was historically low, we prioritized restoring price stability. Over the past year, inflation has slowed and labor market tightness has eased, such that the risks to achieving our inflation and employment goals have moved toward better balance. I think now is a good time to assess how the economy has evolved after rates have held steady at our restrictive level for nearly a year.

Today, I will provide a progress report on disinflation, give you my outlook on the economy, and share my views on how to ensure that monetary policy brings inflation fully back to 2% over time while being attentive to the risk of a slowing labor market. I will conclude my remarks with a few words about my role as Chair of the Board's Financial Stability Committee.

As the U.S. and global economy recovered from the pandemic, rebounding demand came up against still constrained supply, and inflation rose to the highest level in many years. In the past two years, 12-month inflation in the PCE price index has fallen from a peak above 7% to 2.7% in April, and it likely moved a bit lower in May based on consumer and producer price data. However, after rapid disinflation in the second half of last year, progress has slowed this year. My focus remains on making sure inflation is on a path to return sustainably to 2%. How do I think about making that determination?

To respond, I think it is helpful to look at the underlying data.

Some price components have clearly improved. Food and energy price increases moderated significantly over the past two years as global commodity supplies recovered from the shock of Russia's February 2022 invasion of Ukraine. When excluding often-volatile food and energy costs, 12-month inflation in core goods prices is down from 7.6% in early 2022, returning to the trend of slightly negative inflation observed before the pandemic. The increased availability of computer chips and other material inputs has led to a recovery in motor vehicle production and, along with restraint in aggregate demand, likely reduced supply-demand imbalances for durable goods, more generally.

Inflation in services, a spending category that accounts for about two-thirds of household budgets, has slowed significantly, although it remains noticeably above pre-pandemic rates. Specifically, housing services inflation has eased quite gradually, as it takes time for the moderation of increases in market rent – what a landlord charges a new tenant – to show through to broader measures of shelter costs. One possible explanation is that landlords raise rents for existing tenants only gradually over several years and are still moving those rents closer the market rate.

Outside of housing, 12-month services inflation slowed over the course of last year from above 5% to below 3.5% but has stalled near that rate this year. That is still about one

percentage point above the average pace during the two years before the pandemic. Some of the largest contributors to recent services inflation are imputed prices, including portfolio management fees that are affected by equity price increases. Other components of services inflation that are more reflective of supply and demand conditions in the economy have continued to ease. Prices of hotel stays, airline tickets, and restaurant meals are illustrative.

I expect that the longer-run disinflation trend will continue as interest rates weigh on demand. Anecdotal reports, including from the Fed's Beige Book, suggest consumers are pushing back on price increases. Several national retailers have announced plans to lower prices on certain items, and there is increasing evidence that higher-income shoppers are trading down to discount stores. Two other important factors supporting this trend are well-anchored long-term inflation expectations and short-term inflation expectations falling back to near pre-pandemic levels.

My forecast is that three- and six-month inflation rates will continue to move lower on a bumpy path, as consumers' resistance to price increases is reflected in the inflation data. I expect 12-month inflation will roughly move sideways for the rest of this year, with monthly data likely similar to the favorable readings during the second half of last year. Beyond that, I see inflation slowing more sharply next year, with housing-services inflation declining to reflect the past slowing in rents on new leases, core goods inflation

remaining slightly negative, and inflation in core services excluding housing easing over time.

Turning to the other side of our dual mandate, the labor market has largely returned to a better alignment between supply and demand. Many indicators suggest the job market is roughly where it was before the pandemic – tight but not overheated. The unemployment rate was still low at 4% in May, but it has gradually risen over the past year since touching a more than half-century low of 3.4% in April of 2023. Last month's rate was also modestly above readings just before the pandemic took hold.

Layoffs remain low, and payroll growth has been solid so far this year, adding an average of 248,000 jobs a month, essentially matching last year's pace. Labor supply has expanded, partly reflecting a rise in immigration. Labor force participation has broadly rebounded from pandemic lows, except for those aged 65 or older. Women between the ages of 25 and 54 led the rebound, with their participation reaching 78.1% in May, the highest ever recorded.

With more workers entering the economy, the monthly job gains needed to keep the unemployment rate steady likely has risen from just under 100,0000 to nearly 200,000. Although these estimates are uncertain, such a breakeven pace may be a bit higher than the true pace of recent job gains, when taking into account data from the Quarterly

Census for Employment and Wages. These data suggest that payroll job gains were overstated last year and may continue to be so this year. Thus, even the robust payroll numbers are consistent with a tight, but not overheating, labor market.

Signs of better balance in the labor market have come into focus. For example, the ratio of job vacancies to unemployment has fallen from a high of 2.0 in mid-2022 to 1.2 in April, in line with its pre-pandemic level. Workers are also less likely to leave their jobs in search of new ones. The quits rate has fallen from 3% in April 2022 to 2.2% in April and is now below its 2019 average. This decline suggests a normalization following a period of high churn. Wage growth is outpacing inflation but is also moderating. Data from the Federal Reserve Bank of Atlanta show that the wage-growth differential between job changers and stayers has narrowed. Wage growth reflected in postings from online job boards, such as Indeed, has returned to pre-pandemic levels. These measures tend to adjust quickly to changes in labor market conditions.

Turning to the broader picture, the U.S. economy has rebounded robustly since the short but deep pandemic recession. Overall, gross domestic product, or GDP, eased in the first quarter from the rate at the end of last year. However, much of the first-quarter weakness was in net exports and inventories, noisy components from which I do not take much signal, while growth in private domestic final purchases remained solid. Going forward, I expect economic growth to remain near the rate of potential growth,

somewhat above 2%, which is boosted by the increase in the size of the labor force.

American consumers have driven the current expansion, bolstered by strong income growth. But recent data, including first-quarter household spending and retail sales for April and May, suggest that growth is slowing. And, in April, the total amount of credit card balances and other types of revolving consumer debt declined for the first time since 2021. Signs of strain continue to emerge among consumers with low-to-moderate incomes, as their liquid savings and access to credit have increasingly become exhausted. Credit-card delinquency is on an upward trend, and the rate at which auto loans are transitioning into delinquency is at a 13-year high. These rates are not yet concerning for the overall economy but bear watching.

Offsetting some of the slowing in consumer spending, investment spending for equipment and intangibles such as intellectual property and software, has been strong this year. After growing at about only a 1% pace last year, equipment and intangible spending grew at more than 4% annual rate, at a 4% annual rate in the first quarter. If that strength continues, it has the potential to increase productivity over time.

Productivity growth is one factor that could change the pace of both the expansion and inflation. Last year's GDP growth of 3.1% came alongside more moderate employment gains, implying strong growth in productivity. The economy may have benefitted from

investment undertaken in response to strong demand when the labor market was tight. Productivity growth is volatile and difficult to measure, but if it remains strong, then a faster pace of economic growth might not be inflationary.

While the pace of gains may have cooled from last year, I still lean toward optimism on innovation and productivity. Looking ahead, I see adoption of artificial intelligence, or AI, technology as a potentially significant source of productivity growth, keeping in mind that breakthroughs, such as effective generative AI, will take time to fully reach their potential and disseminate throughout the economy and for complementary investment to bear fruit.

Considering the full view of economic data available at this time, my colleagues on the FOMC and I decided to maintain the target range for the fed funds rate at 5-1/4 to 5-1/2% when we met earlier this month. I believe our current monetary policy stance is restrictive, putting downward pressure on aggregate demand in the economy. With disinflation continuing, albeit at a slower pace this year, and the labor market having largely normalized, I see the risks to achieving our employment and inflation goals as having moved toward better balance. Given our data dependence, we will closely monitor incoming information to determine the future path of policy.

Returning inflation sustainably to our 2% target is an ongoing process and not a fait

accompli. In considering how restrictive policy is, I look at a broad range of indicators from financial and credit markets. For instance, the two-year real rate, derived from Treasury Inflation-Protected Securities, or TIPS, remains around 2.7%, up from an average of about ½% in the couple of years before the pandemic, while the 30-year mortgage rate is around 7%.

Meanwhile, banks have significantly tightened credit standards over the past two years. In particular, small businesses and some small banks and community development financial institutions are experiencing diminished access to credit. Many of these businesses also face short-duration loans that need to be refinanced at higher interest rates. With rising delinquencies, a number of low-to-moderate income households are also likely experiencing diminished access to credit. On the other hand, the largest firms and the largest banks do not report a lack of access to funding. Larger firms, like many homeowners, were able to lock in low interest rates for longer terms a few years ago, before rates rose.

Of course, the economic outlook is always uncertain. One way to address such uncertainty is to consider a range of scenarios and not just the baseline forecast. One scenario is the possibility that persistently high inflation durably increases inflation expectations. While this appears less likely than a year or two ago, I am very attentive to the evolution of inflation expectations. Such a risk would imply keeping monetary

policy restrictive for longer, and another scenario would be that the economy and labor market weaken more sharply than expected in my baseline forecast. In that case, monetary policy would need to respond to such a threat to the employment side of the dual mandate.

Considering the balance of risks related to these scenarios, I believe that our current policy is well positioned to respond as needed to any changes in the economic outlook. With significant progress on inflation and the labor market cooling gradually, at some point it will be appropriate to reduce the level of policy restriction to maintain a healthy balance in the economy. The timing of any such adjustment will depend on how economic data evolve and what they imply for the economic outlook and balance of risks.

Before I conclude, I would like to say a few words about the financial system's resilience. Following the 2007-2009 financial crisis, a broad set of reforms was put in place to bolster financial stability. To ensure an ongoing focus on that area, the Board established the Committee on Financial Stability as a venue to discuss related developments and policy issues. Earlier this year, I was named Chair of that committee.

Consistent with some easing of financial conditions since late last year, valuations for some asset categories have risen. Home prices, for example, have outstripped rent

gains for several years. That leaves measures such as the price-to-rent ratio high relative to historical averages. Yet, these valuations have not led to an appreciable increase in risk taking. While house prices have grown rapidly, mortgage debt has not, and most households have ample equity cushions. As I said earlier, some households are experiencing financial strain, and rising delinquency rates suggest some caution. Borrowing by businesses and households has been expanding at rates below GDP growth for several years. I use ratios of their debt to GDP as a rough proxy for whether the sectors are overleveraged, and those stand well below pre-pandemic levels.

Financial institutions and markets appear broadly robust, with high capital and liquidity levels at the largest and most interconnected banks. While there is less visibility into nonbank financial institutions, this tightening cycle has seen markets absorb a number of risk events, suggesting that leverage does not appear too great. A subset of banks has a high concentration of CRE, CRE loans, and supervisors are working closely with those banks. As the CRE market adapts to the shifting preference for downtown office space, prices for some buildings will likely continue to fall, and more loans will need to be worked out as they come due. However, markets have broadly taken the bumps in stride so far, without notable spillovers.

In sum, I see a system that has some vulnerabilities but also important sources of resilience and, on balance, is not currently positioned to unusually amplify any shock. A

stable and resilient financial system is critical to the well-being of households and firms, allowing them to access credit, and it is essential for the Federal Reserve to achieve its dual mandate of maximum employment and price stability.

Thank you. It is a pleasure to be back at The Economic Club of New York. I look forward to continuing our conversation.

Conversation with Dr. Lisa D. Cook

JASON FURMAN: Okay, well, Governor Cook, thank you for that terrific set of remarks. You covered just about everything I would have wanted to talk about and more. So this is a chance for us to go into greater depth. We were, Governor Cook and I were together just a couple of months ago when she kindly came to my Introductory Economics class at Harvard. And the student questions, I thought, were great, so I'm going to try to remember some of what they asked and repeat them to you.

Let's start with the short-run outlook, and I want to push a little bit harder on some of the arguments I hear for rate cuts and why, at least so far, they don't seem to have been persuasive to you based on your votes. The first is that we are already at 2% inflation if you ignore lagged housing. Do you think we've already succeeded? Do you think it makes sense? The Europeans don't include housing in their measure of inflation.

Should we be doing it? Is it a mess? Is it lagged? Are we already at 2%?

DR. LISA D. COOK: No, I think that's a really good question. So we use the PCE index. That's our target. And it is 2%. Certainly there are problems associated with measuring housing inflation, absolutely. One of the biggest problems is finding comparable rent in owner-occupied neighborhoods. Right? So this is one of the big measurement problems, and that is a concession. However, the national academies did a big report on the measurement of CPI and thought that it was best, best for measurement, to include owner-occupied housing, so the measure of owner-occupied housing. So I think including OER is a defensible thing to do. So I think that we're on the right path, that this is a defensible measure. And not every European central bank includes it in its calculation on housing inflation, of inflation includes housing in that measure. There's a lot of heterogeneity. And ours is the PCE index that we pay attention to.

JASON FURMAN: Got it. Related, some people have argued that higher interest rates are actually raising inflation by reducing supply, especially the supply of housing. Do you see any evidence that high rates are causing inflation?

DR. LISA D. COOK: Well, let's think about the recent history of housing supply. Certainly after the GFC, there was a shortage of housing that started. Building slowed. And we've had more multi-family housing supply to come online recently, and we've

seen those rents falling. But they haven't shown up as one would have anticipated in official data. Not yet. So I think that there's a longstanding shortage of housing. That's part of the issue, part of what's raising prices. But certainly consumers report on surveys that they are facing higher interest rates and this may help them postpone or cause them to postpone purchase of durables, of housing. So that's understandable. But I think there's a more historical part that has nothing to do with higher interest rates right now.

JASON FURMAN: Got it. The other part of the case on getting to rate reductions faster was your, I think it was your second scenario of maybe the economy starts to weaken. I wanted to ask you what you make of a lot of the soft data, which is showing a much greater slowing than you see in the hard data? Also the fact that the unemployment rate has gone from 3.4% to 4.0% and we've rarely seen the unemployment rate rise a little bit without it rising a lot. Is that side of the mandate an even bigger concern than you made it out to be?

DR. LISA D. COOK: Well, if I'm thinking about the bigger picture, if I'm thinking in the long-run about the unemployment rate, we had almost 30 consecutive months of the unemployment rate at 4% or lower. And that's, for modern history, that's a record. And it moving up to 4% is obviously something that we're paying attention to, but by historical standards that's still low. And if you're thinking that the unemployment rate has to

increase significantly, let's say you have in mind a Phillips curve, a pre-pandemic Phillips curve that would show that maybe unemployment would need to increase dramatically, we're not seeing that.

We've seen a slight adjustment from 3.4 to 4.0 today, and we see still lots of jobs available. We see lots of movement in the labor market. But we're seeing some signs of softening. I certainly would say that's a factor. And we have the tools to adjust in case there is a rapid movement in the unemployment rate. We prioritized one side of the dual mandate in the fight against inflation, and we'll prioritize the other if we see softening in that realm.

JASON FURMAN: And the last question in terms of the short-run and the rates is just the lags in monetary policy, and two parts to that. One, I don't think you're arguing this, but when can you start cutting rates? It's not when inflation gets all the way to 2. And the second question is do you think those lags have gotten shorter? Or are you still worried about how long they might be? And does that debate have any implication for how quickly you go about rate cuts?

JASON FURMAN: Well, first I think monetary policy is restrictive. If we're looking at mortgage rates, we see they are hovering near 7% if we're looking at 30-year mortgage rates. If we talk to small businesses and small banks, they're facing tighter credit

conditions. So I think that monetary, this monetary policy is restrictive.

Now, with respect to lags, I think we all know, as economists, and in general it's accepted that it takes some time for our monetary policy actions to show up and slowed activity, economic activity in the labor market. So I think that those lags are real. But we're not backward looking. We're not just backward looking. Certainly some of our models rely on past relationships, official data appear with a lag, sometimes quarterly, sometimes monthly. But we're not just paying attention to past relationships and past data. We're talking in real-time to our colleagues on the FOMC, presidents of reserve banks. We are out in the community talking to firms, talking to individuals, households. I was just up in the rural part of the upper peninsula of Michigan talking to Native American communities about their experience of the economy. So we're using real- time data. So yes, the issue of lags is a longstanding one. But we will move when it is appropriate to move. We're data-dependent.

JASON FURMAN: Great. You told us a lot about the consumer sector, a lot about investment, including housing and real estate more broadly. You didn't talk that much about the international context for all of this. What type of risks does that pose for the U.S. economy? And what does it mean that other central banks have started to cut rates already? The ECB has already cut. The Bank of England is widely expected to cut soon. Swiss National Bank has. We haven't gone yet. That lack of synchronization in

the rates, how does that weigh on your thinking?

DR. LISA D. COOK: Well, you know, I rarely comment on other central banks' decisions. However, I would say under normal circumstances there's going to be variation among central banks. Let's take, for example, the Bank of Canada and the ECB. The economic conditions are going to vary in all three jurisdictions, in the U.S., Canada, and the eurozone. And therefore, the response to those economic conditions may differ among the three.

But also their mandates are different. We're quite unusual in having a dual mandate focused on maximum employment and stable prices. Most central banks have a single mandate of stable prices. So you would expect variation among central banks, that group or the group of central banks more generally, with respect to responses. So I would expect variation in terms of our data and responses to those data. So we are watching very closely, and we think our monetary policy stance is appropriate given our strong economy and labor market and other economic conditions that are different from the ECB and the Bank of Canada, the conditions they face.

And I just want to sort of point exactly what I mean. Economic activity on a quarter-by-quarter basis in the U.S. is 2.9%. In Canada, it's 0.5%. In the euro area, it is 0.4% With respect to inflation, somewhat similar. But with respect to unemployment, 4% for us.

And over 6% for those two central banks. So they are in a very different situation from the United States. So again, I think we should expect to see variation. On the other hand, market expectations for rate cuts are similar for those three central banks, for those three countries. So there are going to be some similarities. There are going to be some differences and that is true over time.

JASON FURMAN: Great. I want to now talk about some of the longer-term structural issues, but obviously they relate to the short term. You discussed productivity a lot. I guess the two follow-ups I'd have to what you've said is, first of all, if you want to say more about AI. I know you've thought a lot about it, so feel free, go ahead. Second, what about threats on the other side? Things like growing trade restrictions. Might they weigh on productivity? And then the last question is, what's the time scale on which all of this plays out? Is it the next six months so it helps you with monetary policy? Is it five years in the future so it'll help our children and grandchildren, but it won't affect the next couple FOMC meetings? How do we think about that?

DR. LISA D. COOK: That's a really good question. So just to look at the broader context of productivity growth, it is one of the most important sources of improvement in living standards, first of all. And secondly, it could, productivity growth could help with inflation while we have expanding economic activity. Expanding economic activity may not be inflationary if there's productivity growth. So that's the larger context.

Productivity growth is very hard to measure as you know. It is very volatile. So if we just look at the pandemic era, in 2020 it was about 4%. It was up by about 4% in 2022. It was down by 1.9%. And then last year it was up by 2.7%. So even in the pandemic era it was very volatile. And that's a microcosm of the long-term series. From 1948 to 1973, it was about 3%. Between 1973 and 1995, it was 1.5%. Between 1995 and 2007, it was 3% again. And since 2007, it has been 1.5%. So for productivity growth to get above 1.5%, which is the long-term average if you net out the volatility, it's going to be a big challenge. So while I am an optimist on innovation and AI, this is a very persistent series.

Now, if we turn to AI, as you know I've studied this for some time, and I think that generative AI is probably a general-purpose technology. That it is an invention that will lead to other processes changing that could alter the direction and the rate of arrival of new ideas and new inventions. And that depends on a number of different factors, including the rate of dissemination as I was saying in my speech. So I'm hopeful, but it's too early to tell when this will have an effect. It's too early to tell the impact that it will eventually have. But again, I'm an optimist on technology and innovation and its impact on the economy going forward.

JASON FURMAN: So, on the too soon to tell, in the 1990s, in the mid-1990s, Chair Alan Greenspan decided that productivity growth had increased. Most other people hadn't

realized it at the time. Should we think that this was, he was incredibly wise and you should aspire to that level of wisdom? Or he was incredibly lucky and it would be really reckless for you to try to get lucky and make a big bet on this type of noisy data the way he did?

DR. LISA D. COOK: In general, I think he was really wise in picking up on that. And I would say that because this has been my research in the past, of course this is something I'm paying very close attention to. So I would say that it is, it would behoove all of us to pay close attention to it. And, you know, we have some empirical studies thus far that are encouraging. Let's say, the Brynjolfsson paper on call centers or the Aghion paper on French firms. Both show increased productivity when AI is present. So I think obviously we're going to have to have a lot more research. There's going to have to be a lot more dissemination, but I think it holds promise for productivity growth.

JASON FURMAN: And can you tell me how the Fed is using AI? And in particular, are those FOMC statements written by generative AI because they all sort of look, they all sort of look roughly the same? You don't get that one a lot...

DR. LISA D. COOK: Okay, so there is a lot of thought, even though they may look the same. One thing I've learned at the Fed in my two years is that every single word is negotiated. Every single word is negotiated. And, you know, the most recent, very slight

change in wording, for me, the revelation between moderate and modest. I had no idea. And I have two...

JASON FURMAN: Which side were you on?

DR. LISA D. COOK: Well, neither. But I noticed when I wrote it down, it caused a lot of heartburn. And I had no idea why. So every single word is contested. So I don't think AI is going to be able to replace us in that sense, and not in the short run.

JASON FURMAN: Yes. No, I was actually asking a more serious question, but then I ruined it. How are you using it? How are you thinking about it? Do you have a group of people doing fundamental research into whether this will help us understand the economy? Are we talking about the privacy issues and security issues?

DR. LISA D. COOK: Well, there are two answers to that. In research, there is a lot of ongoing research on AI, among other topics, other potential factors affecting productivity growth. But on the supervision side, we're paying a lot of attention to how third-party vendors are using AI for example. But I think that along these two dimensions there's a lot more work to do. So this is just the beginning. Just as it probably is for many other enterprises and many other entities, many other regulators.

JASON FURMAN: Got it. The other really big hot-button long-term issue that you didn't address very much in your remarks, I did want to hear your perspective on, and that is the neutral rate. So, first of all, you cited what's happened to real short-run rates, that they're in the high 2s. But you look at the dots, the median dot thinks that's a passing fad and we'll go back to something pretty close to where we were before Covid. Do you have confidence that we will? What type of things are you looking for to figure out whether this is temporary or permanent? And then I'll ask a follow up.

DR. LISA D. COOK: Sure. So first let me say that I think that the current stance of monetary policy is restrictive, and I think that we have a lot of evidence of that from the housing market to the labor market as I said in my speech and just said. I think R-star is something that I have to write down in my Summary of Economic Projections, and it is dependent on a lot of different factors. Macroeconomic developments, like the ones we've seen during the pandemic and since the pandemic, are netted out when you are looking at the long-run real interest rate. So for real-time decision making, R-star is not the most important factor because the economic factors that are more short run, that may be long-lasting but are not permanent, are the ones that we are reacting to in real time. So that's what R-star is, and it depends, as you know, on many different factors, including long-run demographic factors. So I think that it is more useful with respect to thinking about the longest run and it's not as helpful in thinking about real-time decision making.

JASON FURMAN: You're probably on safe ground in saying that monetary policy is restrictive, but do you need to know the neutral rate to know how restrictive it is?

DR. LISA D. COOK: I don't think so. I mean I think I would like to know how restrictive it is and whether it is restrictive, but that's not something that R-star is going to tell me right now, and not in the short run. It's a long-term real interest rate.

JASON FURMAN: So I want to segue from this into the financial stability set of questions but ask the neutral rate question again in that context, which is for a lot of the financial system if rates come back, if short rates come back down to, I think, 2.7 is the median dot, that's one thing. If they stay at 5 or only fall back to, say 4-1/2 or 4-1/4, that's another thing. How much does the path of interest rates and this question about what neutral is matter for thinking about risk in the financial system? Is it risky if rates don't end up coming down as much as some people are hoping?

DR. LISA D. COOK: So that's a factor. But in our financial stability program, we're considering a broad range of indicators. We're considering, on the one hand, risks, so these exogenous shocks that happen to the economy. And we're thinking about vulnerabilities as well. The ability of the system to absorb those risks, to handle those risks. So that's one factor. Asset valuations is one thing that we look at, one vulnerability that we look at. So the path of interest rates is just one factor when thinking about the

broad financial stability program and the set of issues that we face.

JASON FURMAN: Then also on the interplay between financial stability and interest rates, in the past when there have been financial stability problems, the Fed has maybe cut rates. Last year, when Silicon Valley Bank happened, the Fed largely pursued a dual track. Interest rates were set for macro reasons and then it used other tools for the financial system. Is that the way it's going to be going forward? Or if there are more financial problems, should interest rates and monetary policy be in play as a tool to address them?

DR. LISA D. COOK: So I appreciate that question because in fact we do have two sets of tools, and we stand ready to use them – monetary policy tools as well as supervisory tools. Certainly I think we reacted very quickly in setting up the bank term loan, BTFP program. And we have also, you saw the Barr report, we have made recommendations with respect to, well, there were recommendations in the report with respect to, let's say, readiness at the discount window and helping banks to be more, to access credit more readily. So we are moving along two tracks, but I can't tell you what the future holds. We're data-dependent. But we're always monitoring, with our financial stability focus we're always monitoring these potential issues. But we have two sets of tools to be able to handle these issues.

JASON FURMAN: Great. And you talked about some of the risks in your remarks, but I just wanted you to elaborate a little bit more – commercial real estate, private credit. Should we still be worried about banks given some of the mark-to-market losses that are still on their balance sheet? What are missing? Where are you looking? And the answer is obviously everywhere, but you can list a few, you can double-tap on a few of the everywheres.

DR. LISA D. COOK: So with respect to CRE, we know that there are problems there. And our supervisory program is focused on helping banks to recognize those problems and to address them with loan loss provisions, for example, and those are concentrated largely in smaller banks. And there's a lot of heterogeneity with respect to CREs. As you know, the issues have largely arisen with respect to office, downtown office and retail. So we're keeping our eye on that.

With respect to private credit, we are watching the inter-linkages between the traditional banking system and those who provide private credit. And we know that it's growing rapidly, and anything that is growing rapidly, we are watching very carefully, so that's on our radar as well. And just smaller banks in general are saying how they may be facing more issues with respect to tightening credit, let's say community, CDFIs. So that's something we're watching very carefully as well from a financial stability perspective.

And our financial stability program is really focused on market functioning and spillovers, and we haven't seen, even though we've seen these issues arise, we think that they may be sizable but manageable in any of the categories that I just mentioned.

JASON FURMAN: Great. So I have two more topics before we have time for a few questions, or really just two more areas of questions. One is just how the Fed operates in terms of transparency. It sounded almost to me like you didn't like putting down that long-run dot. Are these dots a great way to communicate transparently? Are they confusing to people? Should you be making more speeches where you do the economic outlook? Should you be doing less of that? What's your view on Fed transparency and the way it communicates? Is that something that should be looked at over the next year as you look at the framework?

DR. LISA D. COOK: That's a really good question. And I think there is scope for entertaining that when we do monetary policy framework review. I probably shouldn't have changed my tone...

JASON FURMAN: I might have mis-characterized..

DR. LISA D. COOK: ...when I was talking about writing down the long-run real interest rate. But I did what I think is clearer with respect to Fed communication. I did that in the

speech. I think I agree with Ben Bernanke that using, you know, he's proposing this for the Bank of England, but I think it's good for us to do in general. The path of the economy is so uncertain, which means that our response to it, changing monetary policy, may also be uncertain. So why not entertain various scenarios rather than just the baseline. So I think that could be very useful. That could be a very useful tool.

And one thing I'll say about the dots is I would just caution that if you look at the dots, I think I would pay more attention to the distribution. I think the central tendency could be misleading because there was pretty much one-third, one-third, one-third, you know, 0, 1, 2. And think it is worth understanding that there are various views rather than focusing on the median dot. So there's always room for improvement.

JASON FURMAN: Great. So my last question before we have a chance to take a few from the audience is I would love to hear, we've just done, we've done all the substance, I want to hear about the way the economics profession is changing or isn't changing, the role of the American Economic Association Summer Program which you established and ran for so long, what the Fed is doing in this area. Take this wherever you want. I asked you, when I was in government, if I got a multi-part question, I just answered whatever part I wanted to answer.

DR. LISA D. COOK: So I appreciated the time that I had at Michigan State and with the

AEA, American Economic Association, working on the economics profession itself. Now, that arose, not because of, it was a reaction to something. It was a reaction in large part to the "Me too" movement. But I think a more positive view is that the AEA Summer Program that I was director of, or co-director of from 2016 to 2020, is focused on getting more people, encouraging more people to participate in the economics profession and preparing them to do so. And I'm not going to take credit for founding it. It was founded, we're celebrating our 50th year. We just did that.

JASON FURMAN: Right here in New York.

DR. LISA D. COOK: Yes, exactly, exactly, the beginnings of the AEA Summer Program, and it's moved all around the country. And I think that it has been really important. I think a broad set of ideas can come from anywhere. When I think about, when I'm thinking about invention, when I'm thinking about the patent teams that I worked on before I got to the Fed, I'm thinking about bringing the most ideas, the best ideas to the table to expand the rate of arrival of ideas. And I'm thinking the same is true for the economics profession. And I think for us to do more interesting work, to have that work sustained, we just have to have broad participation in the field.

JASON FURMAN: Great. Your chance. Oh, are you calling or should I? We'll start with...I guess introduce yourself.

QUESTION: First of all, thank you so much, Governor Cook. My name is Elisabetta Cavallo. You have described in your speech a fairly positive path for inflation going forward. So assuming your Scenario 1, which is the one where the labor market stays relatively steady and healthy, what is your baseline for rate cuts in 2024?

DR. LISA D. COOK: So I have said, and I started saying this in November consistently, that the path to 2% is going to be bumpy and uneven, but I am fully committed to getting back to, sustainably back to 2%. So, you know, we're data-dependent. There's no way I could say about, even myself, not including my colleagues, what they will do in the rest of the year or next year. So I'm data-dependent, and I look forward to receiving the incoming data and taking into account the totality of the data, not just one inflation, not just depending on one. I don't think it's going to stop being bumpy and uneven.

QUESTION: Hi...

JASON FURMAN: I don't see where you are but start talking. We'll figure it out. Oh, okay, great.

QUESTION: Hi. Marcy Syms. Thank you so much. Very informative, thank you. As a past-Chair of the Small Business and Agriculture Board of the New York Fed, I saw up close the data that we reviewed and how painful it was for a good segment of the

population in business and personally when interest rates change. And what, over the years, has become somewhat more available to us is understanding how the gray economy grows in those situations, particularly for the, if we look at two tiers of the economy – the lower tier of the economy. And I wonder if that's a consideration in discussion.

DR. LISA D. COOK: Well, certainly one purpose of the Beige Book and one purpose of my getting out of D.C. as often as possible is to talk to people and go where they are. So where I was in the upper peninsula of Michigan, you would see, you would potentially see – I saw evidence of it, I didn't talk to anybody who was telling me about the gray economy – but you would expect in rural areas that there would be a gray economy. And as you might know, before I came to the Fed, I worked on developing countries a lot. So I see, in our own economy, where there may be evidence of that. So we might get undercounts, for example, with respect to labor force participation or economic activity. So, yes, that we take into account. But making sure that we're talking to people in real-time should help us recalibrate what we're seeing in the aggregate data.

JASON FURMAN: Great. And one last question.

QUESTION: Thank you. I really appreciate your remarks and the entertaining Q&A as

well. My question, kind of going back a little bit to this topic of lags, the Fed in the face of very high inflation, raised rates pretty rapidly, over 500 basis points. And I think, my perspective and probably most people's perspective is the economy and the markets have been surprisingly resilient in the face of that, and the restrictiveness has played out very gradually. I'm curious, as we think about going in the opposite direction, if the economy shows additional signs of weakness, and you and your colleagues at some point later this year or next year decide to start making gradual reductions in interest rates, how concerned you are about how long the lags might be in terms of will the economy react positively quickly to those incremental cuts? Or is there symmetry to raising and cutting rates?

DR. LISA D. COOK: So that's a really good question. We're quite attentive to the potential non-linearities and the labor force and the labor market. So things could change very quickly and our tools stand ready to respond to such a change. So I wouldn't be able to answer your question for 2025 or later in 2024. We really are data-dependent, and we will rely on the incoming data. We'll rely on the totality of the data and make a determination at that time. But we are attentive to both sides of the dual mandate. And I'll say, again I acknowledge that there are long and variable lags. There's just a lot of uncertainty with respect to when and how our monetary policy actions show up. So we'll stay attentive to every part of the dual mandate and every part of the economy.

PRESIDENT BARBARA VAN ALLEN: Well, thank you for a great conversation. It was an honor to have you both here today. And as the discussion wraps up, I have to say this is our last event for this season. It's like 25 or 30 events later here. And we're going to take a break for the summer and look forward to bringing you an equally robust, if not more so, list of speakers joining us in the fall. So even though the back of the program says it's to come, believe me, it is coming. Also, I always like to mention, in presidential election years, that the Club does invite the two major party nominees after the conventions to address the Club on their economic platforms, and we'll be doing that again this year after the conventions. And so please stay tuned for that.

And then finally, as we always like to do, a note of appreciation to the members of the Centennial Society joining us today as their financial contributions represent the backbone, financial backbone, of the Club. So thank you to all of them. And then I guess in closing, thanks to everyone for attending today, and we hope you enjoy the rest of your summer. And for those in the room, please enjoy your lunch. Thank you.