Make Me Smart November 23, 2021 transcript

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Kimberly Adams: By the way, I've been getting all sorts of turducken cocktail suggestions.

Kai Ryssdal: I'm sure you have. Let me just say that you brought that upon yourself, sister.

Kimberly Adams: And I don't mind it. I don't mind it.

Kai Ryssdal: Fine, fine, fine.

Kimberly Adams: Hello, there. I am Kimberly Adams. Welcome back to Make Me Smart, where none of us is as smart as all of us. Thank you so much for joining us.

Kai Ryssdal: I'm Kai Ryssdal. Today is Tuesday, time for our weekly deep dive into a single topic with a person who knows lots and lots about it. And we will do that today about the Federal Reserve. You have heard by now, I'm sure, the President has renominated Jay Powell, the chair of the Fed, he's gonna make Lael Brainard the Vice Chair. And if you're a regular listener, you knew that already. But you might not know what exactly the Fed does, why and how. So that's what we're going to talk about.

Kimberly Adams: And even if you know, it's always more detail to get into and so regardless of who is leading the Fed, it's a good opportunity to talk about what it does, why the institution matters to everybody living in this economy, because it's not an institution that's very well understood for many reasons, which we are going to get into. And here to make us smart is Victoria Guida. She's an economics reporter and covers the Federal Reserve at Politico, and welcome to the show, Victoria.

Victoria Guida: Thank you so much for having me on.

Kimberly Adams: Awesome. So what does Powell's reappointment mean at this particular moment in the American economy?

Victoria Guida: So basically, it means continuity at the Fed, which is, you know, what the President said was important because the economy is such a, is at such a fragile time period where on the one hand, the economy is recovering, but on the other hand, we have all of this inflation that's causing a lot of difficulties for lower income Americans. So, you know, good news and bad news. And the President decided that it was most important to have someone who was experienced and could, could keep going in the direction that we're going to make sure that the economy does as good as possible.

Kai Ryssdal: I'm going to ask a foundational question here, which is why do we need a Fed?

Victoria Guida: So the reason why we originally decided to have a Fed--actually, there were a couple of attempts at a central bank before the Fed. You'll remember that Andrew Jackson was very anti central bank. But um, you know, the main reason why the Fed itself was created was because in the lead up to 1913, which is when it was created, there were a bunch of bank runs. And so basically, it was sort of every bank for itself back then, where banks would issue their own money, there wasn't a central source of money printing. And so, you know, if one bank maybe ran into trouble, people would run and pull their money out. And then people would also panic about other banks. And there wasn't any institution to kind of back up and lend to these institutions when they ran into those situations. And so the Fed is what's called a lender of last resort, where basically it's supposed to be there when things go wrong to make sure that everybody kind of calms down.

Kimberly Adams: But now the Fed does a lot more than that. And it means more than that in the economy.

Victoria Guida: For sure, yeah. So, you know, even though it does maintain that emergency role, I mean, the big thing that the Fed does, and the thing that I think most people if they know anything about the Fed, they know that it controls borrowing costs. And basically, that is something that controls how expensive debt is, which controls how much actual economic activity there is, because the easier it is to borrow money, the easier it is to, you know, invest and spend more money, you know, but they also regulate banks, they also regulate the payment system to make sure that our money gets from point A to point B. So yeah, the, the role of the Fed is extremely expansive.

Kai Ryssdal: And then what is this whole thing about regional Reserve, Regional Federal Reserve Banks, right, cause you got the Fed Fed, but you've also got a dozen others that are like, city specific and region specific. Explain that a little bit.

Victoria Guida: Right. Yeah. So this is, this is the federal part of the Federal Reserve. So there are, there are seven board members in Washington that are, you know, appointed by the president, confirmed by the Senate. That includes Jay Powell, who was just reappointed, as you said, but there are also 12 Reserve Bank presidents. And basically, the reason it was designed this way is because, you know, policymakers wanted to make sure that the, you know, geographical diversity of the country was represented, they wanted to make sure that in economic decision making when there were different conditions on the ground in different places, that those would be represented. There was also a little bit of politics going on, which is why you have--there, so there's a reserve bank in St. Louis and a reserve bank in Kansas City.

Kimberly Adams: And also because St. Louis is awesome.

Victoria Guida: Yes, but the speaker of the house at the time was from St. Louis. So that's one of the reasons why there's a reserve bank there.

Kai Ryssdal: That's awesome. Kimberly, go ahead. I'm sorry, I could do Fed history history all day. But, but I'm only one guy. Anyway.

Kimberly Adams: Well, you know, the history part is very cool. But I mean, back to this whole controlling the cost of borrowing, it feels like people ask the Fed to do a lot of things when the economy is in trouble. And how much power does the Fed really have? And what tools does it have to move the levers of the economy?

Victoria Guida: Yeah, so I mean, the Fed does have a lot of power, but it doesn't have a lot of nimbleness necessarily in how it does it. So if you think about an anvil, right, an anvil is really good at crushing things, but it's not very good at cutting things. So, you know, it's, you, you can use it to achieve a really powerful economic outcome, but it has to be well suited to what the Fed has powers to do. And part of the reason why, you know, the Fed is asked to do a lot of things in an emergency is because its tools and its mandates are so specific that what it has to do. It's, it's very, very sophisticated at doing. Whereas, you know, Congress basically has jurisdiction over any number of things. And so, you know, it might be better or worse at some or other things, whereas the Fed just has very specific jobs that it does. And, and it's, it's considered to be by many policymakers very effective at doing it.

Kai Ryssdal: So along those lines, could you talk a little bit about the independence of the Fed? I mean, Janet Yellen talked about it the other day, obviously a former Fed Chair herself, Powell talks about it a lot and, and why independence matters with this agency?

Victoria Guida: Yeah, so the short answer of why independence matters is because the Fed makes decisions that affect the long term of the economy. So, you know, there are policies that it can do, such as lowering interest rates that will increase economic activity. And that can juice the economy in the short term, which for political purposes, presidents might really like right, you're more likely to get reelected. And this is actually what exactly what happened with Richard Nixon, where he actually pressured the Fed to keep rates low for this reason. But the Fed is supposed to be making decisions that are good for the long term. And, you know, that's not to say that the Fed isn't involved in politics. You know, it's, its existence as an institution depends on how it does its job, how Congress reacts to what it's doing. But basically, it's supposed to not be partisan. And it's supposed to be thinking about things, like I said, and sort of a longer term way.

Kimberly Adams: But you just gave an example of a time when it was partisan. How effective has the Fed been at sort of staying above the fray?

Victoria Guida: So I think comparatively, it's a very nonpartisan institution. I mean, in terms of Washington today, I think that that's demonstrated, for example, in what you saw as the reaction when Jay Powell was named for a second term, he has support from someone, you know, who's a progressive Democrat like Sherrod Brown, or. But you also, he also has support from, you know, Republicans who are very ideologically conservative like Pat Toomey. And so I think that that demonstrates that the Fed does try and sort of take into account the, you know, political and policy views of people across the spectrum in, in sort of its decision making. So I would say, I would say comparatively, it is very nonpartisan.

Kai Ryssdal: Every now and then, though there are members of Congress, Rand Paul is among them, his father, Ron Paul is another one who were like, let's get rid of the Fed. Let's get back on the gold standard. What's the question out of that--do you suppose that at all within the realm of like, possibility? Not the gold standard part, the get rid of the Fed part.

Victoria Guida: Get rid of the Fed, um, so that, you know, I mean, never say never, especially these days. But, um, I think that that is especially unlikely right now in this political moment. I mean, you know, we came out of a four years of a Donald Trump presidency, when the Fed was actually an area where Republicans sort of bucks what Trump wanted because they were trying to protect the independence of the Fed because basically, they care about the long term health of the economy. And it was, it was one of the very few areas where we actually saw Republicans doing that. And then you also saw, you know, sort of bipartisan approval for a lot of what the Fed did to, you know, in its emergency response to the Coronavirus pandemic. So I would say we're in a moment right now, where policymakers seem to really appreciate the value of the Fed. But that kind of, that kind of waxes and wanes depending on what's happening in the economy.

Kai Ryssdal: Do you suppose--sorry, sorry to jump in here, Kimberly--but do you suppose they appreciate the value of the Fed because the Fed is willing to do things where, you know, until the pandemic, right, you had fiscal policymakers, which is to say, Congress, not being able to agree on what day of the week it was, let alone figuring out an aid package or whatever, and Bernanke and Yellen and all went, okay, fine. We'll do it. Right? I mean, that, that plays into the appreciation of the Fed at this moment.

Victoria Guida: Yeah, no, I think that's absolutely true. It's actually one of the reasons why Congress created the Fed, you know, the thinking goes. Well, just to kind of back up for a second, right, the reason why the Fed exists is because Congress created it. It is, it is delegated authority from Congress. And so, you know, the thinking goes that part of the reason why Treasury wanted to have a Fed is because the Fed could do things that Congress maybe didn't want to do because they were politically unpopular, and then Congress would have the ability to sort of scapegoat them.

Kimberly Adams: How has the Fed evolved in the way that they've approached their dual mandate, especially in recent years? And can you talk a little bit about the dual mandate first?
Victoria Guida: Right, yeah. So this is, this has changed a lot. So the Feds jobs are basically price stability and maximum employment. So price stability, the Fed says that means an average of 2% inflation and maximum employment, they're a little bit murkier as to what that

means. But the, the sort of shorthand definition is, you know, anybody who wants a job can get a job. That's what a state of maximum employment would look like. So in the 70s and early 80s, we saw, you know, very high inflation. Paul Volcker, who was then the chairman, very famously had to hike interest rates extremely high, and to sort of break the back of inflation. And so ever since then, the Fed has been really skittish about wanting to preempt inflation before it gets to that kind of point because it's really damaging for the economy to have to do that. In fact, we saw multiple recessions as a result of that, in order to get inflation back under control. And so the Fed sort of took a lesson from that, that they needed to be extra paranoid about inflation and make sure that, you know, it didn't get to that point. So, in, in recent years, in the wake of the 2008 financial crisis, you saw a lot of people expecting inflation to show up before it actually did. And, you know, Janet Yellen waited until December 2015 when she was chair of the Fed. They waited until December 2015 to actually raise rates. And, you know, there at the time, there was intense political pressure, people thought the Fed was way, way behind, and that inflation was going to go crazy. And then looking back on that experience, inflation never really picked up in a significant way. It was actually under the Feds 2% target. And so the Fed said, hey, we're maybe hurting people's job prospects and wage prospects by reacting so early to when we think inflation might show up. So instead, we should wait until we see inflation show up and they formalized that policy change last year, and that was, that sort of a, you know, a sea change that's been a very long time in the making.

Kai Ryssdal: So when, when, I mean, I said this yesterday on the pod and, and I believe it to be true, but it's an easy thing for me to say so I need you to explain it. I said, you know what the Federal Reserve does affects every single person in this economy. Do you buy that?

Victoria Guida: Yes, I do. Um, so the Fed, you know, prints the money, right? So they control the money supply. And it's, it's interesting, because it's, you know, one of the criticisms of the Fed is that they contribute to wealth inequality. And one of the reasons is, it's a lot easier for the Fed to impact the wealth of someone who has more assets. So the Fed, you know, probably does potentially have a bigger impact on someone who has a stock portfolio because the Fed can, you know, its actions can indirectly make stocks go up a lot, or even directly make stocks go up a lot. But, but when it comes to, you know, lower income people, their assets are their income, and their job. And when the Fed can, you know, is in charge of setting how difficult it is to borrow money, that also affects hiring, and, and wages. And also, I mean, fighting inflation.

Kimberly Adams: Wait, can you explain that a little bit? How the, the terms of borrowing affect hiring and wages?

Victoria Guida: Yeah, sure. So if you think about investing, right, so if you're, if you're a business and you have money, you can, you know, invest it in hiring people, you can invest it in equipment, all of that things, all those things create growth, theoretically, right, if you're doing something productive. So if you think about what the point of debt is supposed to be, the point of debt is basically you take the money now, so that you can invest it into something, and then it'll pay off over the long term. That's sort of like, the ideal form of debt. And so if you make it harder for companies to borrow, you make it harder for them to invest, which both, you know, makes, reduces growth opportunities, and it also can sort of like, put a damper on both wages and jobs.

Kimberly Adams: So there are a lot of people who just straight out say that the Fed makes inequality worse. And that, you know, we've talked about this K shaped recovery and how income inequality increased during the pandemic, like you said. Does the Fed make inequality worse? And how can they address that?

Victoria Guida: Yeah, so I mean, as I was alluding to, because the Fed can affect asset prices, if you invest in stocks and bonds and all sorts of things like that, then you're going to get richer as a result of some of these Fed policies that, you know, increase growth, right, because if you think about one of the, one of the reasons why stock goes up is--not the only reason stocks go up, but one of the reasons stocks go up--is because there are better prospects for growth. And, you know, it's just, it's just crazy when you compare, right, wage growth to stock price growth, right? Like, if you look at it that way, rich people are getting helped much more. Now, there, there are two sort of caveats to that. So one is, lots of people will tell you that it's not better for the Fed to not help the economy just because then like, rich people’s stock portfolios won't be doing as well, right. Because you still, you still want people to be able to get jobs and have higher wages. And so, you know, it's the question, one of the questions is, you know, okay, rich people are better off than poor people are because of what the Fed does. But does that mean that enough, like, poor people themselves are better off than they would be if the Fed weren't doing what it's doing? So there's that. There's also, you know, another argument that comes up is, well, you know, the Fed just works through the channels that exist, right, we have an unequal society. And so when the Fed sort of supercharges everything, it's basically just making, its operating through channels that are unequal. And so, you know, it's, it's sort of limited in what it can do redistributionlly. Now there, there are people that would argue against that point, they would say that the Fed could be, you know, could purposely try and make its outcomes less unequal. But that's, that's a little bit more complicated.

Kimberly Adams: Victoria Guida is an economics reporter and covers the Fed for Politico. Thank you so much, Victoria.

Victoria Guida: Thank you.

Kai Ryssdal: Victoria, thanks so much. I really appreciate it. Good stuff. Yeah, Fed, man. I can do it all day. I love the Fed.

Kimberly Adams: Yeah. And I just like, I'm very curious about this, this question of what exactly full employment is, you know, because this is something that has really been batted around quite a bit during the pandemic when we saw just the way that wealth inequality was exacerbated and the fact that, you know, you pre pandemic, you had Black unemployment that was double white unemployment, but that was still considered full employment, you know, and we haven't quite gotten away from that yet.

Kai Ryssdal: No, in fact, the gap is as bad now. I mean, yeah.

Kimberly Adams: And so there's all this pressure for the Fed to take the foot off the gas. But that's no, that's not a different measure of full employment than we had before. So, are we okay with that?

Kai Ryssdal: Yeah. I don't know. I don't know. I mean, the short answer is no, it's not okay. The longer answer is, you know, people are yelling and screaming about this for a lot of different reasons.

Kimberly Adams: Yeah. Okay. If you are still confused about the Federal Reserve and have more questions for us, let us know, our number is 508-827-6278, also known as 508-82-SMART, or you can leave us a voice memo at makemesmart@marketplace.org. And we'll be right back.

Kimberly Adams: Okay, we are back.

Kai Ryssdal: We are.

Kimberly Adams: And now it's time for the news fix. You go first.

Kai Ryssdal: Alright, so mine was chosen number one, because it's a kind of a wild economic story, but also because it fits into the theme of the day, which is central bank. So in Turkey, the lira is just crashing, losing value right and left in no small part because President Erdoğan is messing with the independence of the central bank. And he's forcing interest rates to be artificially low for his own political reasons. But that's driving inflation up. And so people are pissed and prices are going up and they can't figure out how they're going to make ends meet. And if you want an example of why you should not mess with a central bank, even though the political pain will be bad for you, whoever's in the executive management of whatever country you're in, this is it, man. This is it. The story I picked was Reuters. But it's, it's all over the place. This is a big story. And look Erdoğan had a history over the past, like 8, 10 years-ish of messing with the Turkish central bank and its independence, but it's not a game, right, because people's livelihoods and people's ability to pay for the cliched example of a loaf of bread hinges on this stuff. So, you know, we'll put in the show notes but, but yeah, Turkey is a good object lesson today.

Kimberly Adams: Yeah, I'm just looking at some of these charts in this story and they're grim, grim looking charts. Oh my gosh, you know, so every day when you do the numbers, you talk about the yield on the 10 Year T Note, right? So, and it's usually like one point something or the other. Right. So in this story, it says, for the Turkish Lira, the 10 year benchmark bond yield rose above 21%.

Kai Ryssdal: Think about that. Think about that.

Kimberly Adams: For the first time since the start of 2019, right?

Kai Ryssdal: Right, so look, that's the government being able to borrow at 21%, regular people are not getting the low rate that the government gets. So if you need to buy a car, or a house or whatever in Turkey, no, you're not, you're not gonna be able to.

Kimberly Adams: Well, also on the theme of the Fed, and its, and its mandates, I have a story from CNN about Dollar Tree, which was sort of the last actual dollar stores in the US in terms of stuff actually being $1. But now, it's actually not going to be, they're going to be raising prices from $1 to $1.25 on the majority of products by the first quarter of 2022. You know, that's inflation. And, and this is, this is the thing and, and, you know, it's easy to sort of be dismissive of that. But many, many people in various parts of this country really do rely on dollar trees and other dollar stores for their staples, especially in places where there aren't a lot of shops and resources, and these price hikes are going to be felt. And so, you know, everyone, you know, screaming about inflation, some people are worried about it for big business reasons. Some people are worried about it because it actually affects their ability to buy the things that they need to get day to day, get by day today. And so, you know, when you think about macro issues, you know, like unemployment and whether the movements of the Fed will do one thing or the other. This is what it really comes down to and like you said, affecting every person in this economy.

Kai Ryssdal: Yeah, it's real. Inflation is real. I don't know whether it's transitory or not, but right now, it's real. Real, real, real. Alright, let's move on, shall we, Mr. Jostad?

Kai Ryssdal: Okay, we talked about onshoring last week with Megan Greene at Harvard Kennedy School. And after that, we asked all y'all to tell us whether the supply chain is affecting how you shop. And we got, among others, this.

Ryan: Hi, this is Ryan from San Diego. My family got together to think about Christmas gifts this year. And rather than supply chain issues, we looked at climate issues. And that affected our purchasing. So we decided not to buy gifts from all the big stores this year. But instead either shop locally, by reused gifts or thrift store gifts. And that kind of goes in line with the supply chain, but really different intention for us. So it really changed us, how we're going to be buying gifts this year, and hopefully it'll make a difference in the years going forward. Thanks a lot. Enjoy listening.

Kai Ryssdal: That's cool. That's cool. Actual concrete steps. I haven't done any shopping yet. I'm not a good shopper, and I've got time yet so leave me alone, please. It's bad enough in my house that I'm a bad shopper.

Kimberly Adams: Oh, touched a nerve there!

Kai Ryssdal: Am I a little sensitive? Yes, I am. Yes, I am!

Kimberly Adams: I was just gonna say, I said screw it. Everybody's getting cash. I'm not even trying. I'm not even trying. I make no pretense. Okay, and yesterday we talked about turducken inspired desserts, and I asked you to send us your turducken cocktail ideas. I've been seeing some on Twitter, but we also had this one.

Becca: Hi, this is Becca calling in from DC. Isn't a turducken cocktail a Long Island Iced Tea? It just has everything, right? Tequila Sunrise because it's layered. Your thoughts on this are most welcome.

Kai Ryssdal: Much like turduckens, I never understood Long Island Iced Teas. Here, pour a bunch of liquors in a glass and drink it.

Kimberly Adams: The point is to get drunk, Kai.

Kai Ryssdal: I know, look, I've been 21, come on. But back then, even back then they were never my thing. But that's a whole different podcast.

Kimberly Adams: Several, several folks have suggested the Long Island Iced Tea. Um, I do think it needs some layers. I've gotten a couple of suggestions. I think a Tequila Sunrise is a little bit too bright. I need like, some brown-ish layers in there for the various like, I don't want to think about meat. But I also need to like, get the Thanksgiving colors in there.

Kai Ryssdal: There's a lot of thought going into this. I'll tell you what, you know.

Kimberly Adams: Some things I make time for, Kai.

Kai Ryssdal: Good for you. All right. We are gonna make time for today's answer to the make me smart question. Once again, what is something you thought you knew you later found out? You were wrong about? Here you go.

Tiffany: This is Tiffany Osbourne from Dripping Springs, Texas. I'm calling for something that I thought I knew but it turns out that I was wrong. I've been listening for several years and this whole time when Kai mentions his dog, particularly, I guess only during the pandemic, I've always thought his dog's name was Bonds. So I thought how clever for an economics reporter to name his dog Bonds, that’s just so cute. And so last week when Kai referred to his dog as Bonzai, I just laughed out loud in a public place. And you know, while Bonzai is still cute, you know, it surprised me. So, thanks.

Kai Ryssdal: That's pretty funny. Tiffany, I kind of love that, I kind of love that.

Kimberly Adams: So now you need to get a puppy and name it Bonds.

Kai Ryssdal: Right, legitimate Bonds. Yeah, yeah.

Kimberly Adams: Best excuse for a puppy, ever. All right. Don't forget to send us your answer to the make me smart question. Consider calling us and leaving a voicemail message just like Tiffany did. Our number is 508-82-SMART, or you can write us, we're at makemesmart@marketplace.org.

Kai Ryssdal: That is it for us today and for the week. Molly and I are back next week. She's back for a couple of days. And, and look, have a happy Thanksgiving and just relax. Just everybody, just relax. That's what everybody should do.

Kimberly Adams: And be thankful for something.

Kai Ryssdal: And if you're working, thank you, but if you're not, relax. This podcast, Make Me Smart, is directed and produced by Marissa Cabrera. Our intern is Grace Rubin. Tony Wagner does our newsletters.

Kimberly Adams: Today's program was engineered by Drew Jostad with mixing by Juan Carlos Torrado. Ben Tolliday and Daniel Ramirez composed the theme music and the senior producer is Bridget Bodnar. Donna Tam is the director of on demand and Marketplace’s vice president and general manager, and general manager is Neil Scarborough I can say words. I can say words. I guess I actually have to try some of these cocktails.

Kai Ryssdal: Yeah, well look. That’s on you, pal. That's, that's on you.