**MEDIA: Television**

**STATION: Bloomberg**

**MARKET: National**

**DATE: 2023-11-01**

**TIME: 01:47 PM ET, 02:04 PM ET, 02:11 PM ET, 02:20 PM ET**

**PROGRAM: Markets**

**SUBJECT: Rich Clarida - US Economy**

**PAGE COUNT: 9**

**TOM KEENE, BLOOMBERG:**

We're going to go quickly here. We have two wonderful guests now to prepare us for the Fed meeting and then Michael McKee at the press conference as well. Richard Clarita is with PIMCO. He's Global Economic Advisor. Yes, the former Vice Chairman of the Federal Reserve System, but far more holding coat at Columbia, curbing Nobel laureates for Columbia economics and also providing original research on the dynamic natures of our American economy. Matt Luzzetti out of UCLA is Chief U.S. economist at Deutsche Bank on a tight timeline here. Vice chairman, let me go to you first here. As you look at this meeting and as Bill Dudley says with Bloomberg Opinion today, this is a meeting and a set of meetings fraught with risk for Chairman Powell. What is the major risk the Chairman faces?

**RICH CLARIDA, PIMCO:**

Well, Tom, I think he has a communications risk. I don't think we're going to get any news in terms of either the decision or the statement at two o'clock, but I do think this is a high stakes press conference because there's a meeting coming up in just six weeks in December and September, 12 folks on the committee thought they'd need to hike once more. That's the camp I'm in. If I were still there, I would think at least one more hike is needed. But right now the market is not really pricing that in. And so I think he needs to discuss today's meeting, but also to tee up his outlook for the next meeting.

**KEENE:**

Matt Luzzetti, we'd Priya Misra with a great call on deep inversion early in the year. You have the mother of all calls. You were out front saying recession is distant. I've got a GDP-Q3 going to a GDP-Q4, which is in the Luzzetti recession direction. Do we have a recession coming up as we address this meeting?

**MATTHEW LUZZETTI, DEUTSCHE BANK:**

Look, I don't think it's going to be the focus of today's meeting. I think the focus will be the strength in the data that we've really seen since September. We've had a strong jobs report, a strong retail sales report, an inflation report that was showing some strength. Just this week, we saw job openings remaining high and the employment cost index with some strength. So I think it really is about the Fed not raising rates today, keeping up with our optionality to raise rates in December. And really, if they do need to raise rates again, I'm convinced that they are just one and done. You could see some resilience in the data that remains, and it'll depend on whether or not financial conditions remain very tight and continue to do the Fed's work.

**LISA ABRAMOWICZ, BLOOMBERG**

Matt, what's your one question to Fed Chair Jay Powell?

**LUZZETTI:**

I think an interesting one from my perspective is there's a lot of parallels today to what happened back in March, which is that the Fed is not raising rates or being less aggressive because they're looking at the timing of financial conditions that are taking place. What we learned back in March is that it didn't come through and flow through to the economy as much as we might have thought. And so, is there a risk here that they are moving in a somewhat more dovish direction to the financial conditions, that they're anticipating it doesn't feed through to the economy and risk that they have to do more later?

**KEENE:**

Matt Luzzetti, one final question. Is this a collegial board or are there deep divisions as we see at the Bank of England and among the nations of Europe?

**LUZZETTI:**

Look, I think they've been remarkably cohesive in decisions over the past 18 months. I think as we look ahead, it's just natural that there's going to be more disagreement. I think you're getting to the point where two-sided risks are more real. The risk of overtightening will become more significant. The risk of under-tightening will be more significant. And so, I anticipate that as we look ahead, there will be more disagreements. But I think Chair Powell is very clear. The number one metric from their perspective is that they get inflation back down to target over time. I think what we're seeing today is that it might take further tightening from their perspective, and that while getting inflation down to 3% didn't take much pain, getting from 3 down to 2% might take a little bit more pain within the economy and labor market.

**ABRAMOWICZ:**

And that's definitely what's keeping up a lot of people at night. Matt Luzzetti, thank you so much for being with us. This is the countdown to the Fed Decides on Bloomberg TV and radio. We're moments away from a Fed-rate decision. Still with us, we are so glad to say, Rich Clarida, the former Fed Vice Chair. Rich, I want to pose that question to you that Matt Luzzetti was just talking about. Are we on the brink of another March 2023 moment, where the Fed pulls away from raising rates even in the face of hotter than expected data?

**CLARIDA:**

Well, obviously other things were going on in March later on. We had SVB and the like. I do think, and I give the committee credit for getting off the rate hike hamster wheel. And so they've shown that they can both hike and pause, and I certainly, if I were there, would be okay with a pause today. But I hope it's a hawkish pause, because I'm with Matt. The progress that we had seen on inflation has stalled a bit. The labor market is still red hot, which is a good thing, but wage gains are really not consistent with the inflation target. So I think the messaging needs to convey that determination.

**KEENE:**

Rich Clarida, April 4th of this year, writing for the Economist, the former Vice Chairman. “But it is likely to be something more like two points something than 2.0”. Drag us forward from April 4th when you shook the economic world. Is two point something 2.5, or does John Williams need to get used to 2.9?

**CLARIDA:**

Well, look, what I'm trying to communicate is that the Fed's primary goal since March of 2022 has been to get inflation substantially lower. It was running at five. It's now running in the low threes. I am of the view that if next year in 2024, inflation's running at two point something, and point something could be point five, point six, or point seven, they will say, look, we've made a lot of progress. We can start to dial back and start to adjust rates downward. Chris Waller's done a good job of explaining that. It will be a nuanced message, but I think it will be the correct message. But we can't put the cart before the horse. We have to get inflation down to two point something on a year over a year basis, and we're not there yet.

**KEENE:**

Richard Clarida, we'd say lower Milton Friedman, we're going to go out longer with variable lags and all this. That's from another time and place. Forward here for Chairman Powell in all, do we have an America that is together where we have a common economic theory? Or is this a Fed making it up as they go, including here at 2 p.m.?

**CLARIDA:**

Well, Tom, I think you may be on to something. Maybe I wouldn't put it quite that way, but I do think central banks, the Fed and other central banks, are about to enter a period where there is going to be an active public debate on the merits of the inflation target. Right now, inflation is very unpopular. Everybody wants lower inflation. But so far, we haven't really seen any consequences in terms of higher unemployment. At some point, the Powell Fed may run into that trade off, and given the nature of what else is going on in the country right now, that could be a divisive discussion.

**ABRAMOWICZ:**

Right now, we're looking at a myriad of issues, including geopolitics. We heard Jay Powell talk about this in the past number of weeks where he did raise this as something they're watching and seem to indicate that it was disinflationary, non-inflationary potential shock, the way the others have been received. What do you make of that? What do you expect him to say today on that front?

**CLARIDA:**

I think that he probably won't try to break a lot of new ground. Fed officials always want to acknowledge the geopolitical tensions. They don't want to get too into the details of how they're factoring that in. Typically when there's war in the Middle East, it tends to lead to higher oil prices. And so there's a pretty standard playbook for thinking about that. But also over time, if it accumulates, it gets into risk appetite, it gets into animal spirits. I frankly think it's too soon to tell how this is going to play out. So I think he would stay away from it.

**KEENE:**

Richard Clarida, at this meeting, at this press conference, to the December meeting on January 31, I would suggest post-pandemic we find a new science of monetary policy. You wrote about this years ago. What is our new science of monetary policy that Chairman Powell right now has to confront?

**CLARIDA:**

Well, I think he has to confront that in the rearview mirror, inflation has been too damn high. The Fed and other central banks want it to be around 2%, and the longer inflation remains above that target, the more central bank credibility is threatened. And so, so far, I think the Powell Fed has done a good job of keeping inflation expectations anchored. But to your point, Tom, in Clarity Galley-Gurtler, our model essentially looked at a situation where central banks were credible, because in the past they'd achieved their goals. It's a little bit more complex model when you've not done that for three years.

**KEENE**

Right. But the heart of the matter, post-pandemic, as Bill Dudley says, we have a risk of becoming unanchored. At this meeting, does that need to be addressed? That confidence building, does that need to be addressed in the press conference?

**CLARIDA:**

Tom, I don't think so at this press conference, because I think so far, inflation expectations are reasonably well anchored. But I think the chair will say, as he has many times, including with David Westin not too long ago, that they are determined ultimately to bring inflation down to 2%, but no, I don't think he needs to address that specifically today.

**ABRAMOWICZ:**

He does, though, maybe have to nod at his belief, which is a huge academic question of whether we need to see more pain in order to get inflation down under control. We're kind of addressing this from all different angles. What do you think the answer is? Have we gotten anything that gives you a sense of whether we've seen the kind of pain in the U.S. economy to get us back to 2%?

**CLARIDA:**

Well, Lisa, I am in the camp that it's going to take somewhat more slack in the labor market, which is a euphemism for pain in the labor market than the Fed's September projection. In September, the median participants saw the unemployment rate peaking around 4.1. That would be great, but I think given how hot the labor market is and how stubborn inflation appears to be in the threes where they want it in the twos, I think we are going to need to see some more slack. Now, it may just be slower growth, maybe Governor Waller is right, and the adjustment can occur in job postings and quits, but you saw today the JOLTS numbers are also going in the wrong direction. So I do think it's going to probably take somewhat more pain than the committee seems to think right now.

**ABRAMOWICZ:**

And just quickly, what do you think the risk is that the Fed is losing its credibility and is behind the curve in a more meaningful way and needs to take an even more aggressive stance to counteract that?

**CLARIDA:**

Lisa, I don't think we're here now and I don't think we're likely to be here in December, but I think it is a real risk in 2024. We could be sitting going into the May Fed meeting with inflation moving up, not down with the labor market hot and with a committee that may need to re engage. I don't think that's the most likely case, but I think it is a significant risk. And I think implicitly you heard that from Lizetti, and I think that's in Dudley's piece as well this morning.

**KEENE:**

Richard Clarida is still with us. He is with PIMCO and Columbia University. Richard Clarida I look at cumulative and that just tells me we're going out there. Draghi would have put a date on it. Can professor Clarida put a date on this longer Fed at this level?

**CLARIDA:**

Well I don't think so. I think the language community has clearly been there for several meetings and it does recognize that the path forward depends upon how much they've done in the past. As I've said these are always balancing acts. I think the Fed's baseline outlook makes a lot of sense but if there is a risk the risk is that inflation is too stubborn. If I were recommending or talking to Jay Powell I would recommend that he leave the door open to doing more. He doesn't have to commit to it. Every meeting is live but I definitely don't think he wants to walk away today with markets seeing the headline as Fed is done.

**ABRAMOWICZ:**

That seems to be certainly at least the initial read on this. One line that Michael McKee pulled out was “the tighter financial as well as credit conditions are set to weigh on the economy”. They added financial into this. How much do you think the Federal Reserve and the members are concerned about some of the volatility we've seen on the long end of the curve that maybe it's getting to something a little dysfunctional, a little bit less just nicely restrictive?

**CLARIDA:**

Yeah well the short answer is there's probably a range of opinions but certainly Chair Powell recently and Lorie Logan, the President in Dallas, have indicated that it is doing some of the Fed's job for it. They haven't pushed back against it. I do think that the challenge of having wordsmiths with some of these things, the challenge of putting the financial conditions in this statement is financial conditions can go up and down and be volatile for a lot of reasons and then at some point they may regret that they included it in the first place.

**KEENE:**

Rich Clarida, what's so important to me is again the analog that we're conveniently using of taking Powell back to Volcker. And as Bill Dudley wrote an hour ago for Bloomberg, he says the arch fear was Arthur Burns who allowed inflation to get out of control in the 1970s. I believe we have a disinflation vector, but should we fear that inflation is out of control?

**CLARIDA:**

Well, the analogy I would use, which I think the Fed would want to avoid at all costs, is 1966, LBJ had guns and butter inflation was moving up, the Fed hiked, and then they blinked. And they cut in 1967, and what we now call the great inflation, I think, stems back to a hiking episode that got cut short and the Fed did not re-engage when inflation went up. I don't think the Powell Fed would make the same mistake, but that's the part of the history book I'd be looking at and trying to avoid.

**KEENE:**

Rich Clarida, what's so important here, and I'm thinking of your conversations and your counsel to the portfolio managers at PIMCO. And in the moment we're in, there are select people out, they're saying bonds out in maturity are a screaming buy. How do you frame that at PIMCO? Given what the Fed is doing, post-pandemic, can you say price up, yield down, and go out in maturities to get total return?

**CLARIDA:**

Well, exactly. And in the sense that investors can earn returns that they would have been drooling over three years ago, by not moving all that far out on the curve, certainly, if you look at investment grade corporate or mortgage-backed security. So what we're saying is that there is a menu of opportunities available to investors, but when you can get returns, real rates, where they are now, and because we're in the camp that thinks the Fed will succeed and ultimately bring down inflation, that this is a great entry level, and you don't have to take a lot of duration risks. Some investors, because of their business model, do have more duration risk. But there are opportunities, even if you don't want to add that.

**KEENE:**

This is great. The Dean of Columbia Economics is a bond manager. I think Rich Clarida had just got out of bond tickets and said let’s go long.

**ABRAMOWICZ:**

Which is the reason why he's currently at PIMCO, though I do want to just get a sense from you, Rich, about the balance sheet question, about whether the Fed's balance sheet needs to be a lot bigger than people previously had imagined. And if we're kind of bumping up against that level.

**CLARIDA:**

I don't think we're bumping up against that level, Lisa. Remember, the Fed has something, another acronym, the Reverse Repo Facility Program that's got a trillion dollars in it. That money, once it leaves that facility, will then flow back into reserve. So I think if you factor that in, I think there is more road for the Fed to travel to shrink its balance sheet. I do agree with your previous guest. It is interesting that the Fed has talked about continuing QT even after they potentially adjust rates. When I was there in 2019, we stopped QT before we caught rates. So that would be an interesting difference.

**KEENE:**

Professor Clarida, thank you for your generous time today here at this Fed meeting. We're going to let Rich Clarida go here, six minutes away from this important press conference.