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*Monthly condensed analyses of crucial real estate and economic issues offered by the UCLA Anderson Forecast and UCLA Ziman Center for Real Estate. Here, Stephen Oliner, Senior Fellow at the UCLA Ziman Center for Real Estate, deflates the myth that Fed Chair candidate Janet Yellen is “soft” on inflation. He also argues that Yellen is the safer bet to assume this crucial position.*

## The Myth That Janet Yellen Is ‘Soft’ On Inflation

### The President Should Beware Rolling the Dice With Summers; Yellen Is a Safer Bet.

*By Stephen Oliner, Senior Fellow at the UCLA Ziman Center for Real Estate*

Press reports suggest that President Obama could soon announce his nominee to replace Ben Bernanke as the Chair of the Federal Reserve. Larry Summers, the Harvard professor and former Treasury Secretary with strong ties to the Obama administration, appears to be the favorite over Janet Yellen, the current Fed Vice Chair. Before the choice is made, let's take a close look at one of the main knocks on Yellen -- that she may be too willing to let inflation rise in an effort to reduce unemployment. The charge that she's soft on inflation has been repeated so many times that it's now taken as fact.

**“Every word uttered by the Fed Chair has the potential to roil markets. Yellen chooses her words very carefully, while Summers is less cautious ...”**

If this claim were true, you'd expect to find supporting evidence in Yellen's many speeches as President of the Federal Reserve Bank of San Francisco and then as the Fed Vice Chair. These speeches provide a substantial public record of her views. To assess this issue, I read the 42 speeches she has given over the past five years, focusing on her comments on inflation. This reading leads to only one conclusion: Yellen is not soft on inflation.

Let's start with the speech that could be read as most favorable to the opposite view. On April 4 of this year, Yellen said: “With unemployment so far from its longer-run normal level, I believe progress on reducing unemployment should take center stage for the FOMC, even if maintaining that progress might result in inflation slightly and temporarily exceeding 2 percent,” the Fed's target rate of inflation. Given Yellen's premise that unemployment was well above normal, the rest of the quote is entirely in line with the FOMC's statement of longer-run monetary policy goals and strategy that was adopted in January 2012. All of the inflation hawks on the Committee approved the strategy statement, which recognized that circumstances may arise in which the Committee has to balance the attainment of its inflation target against the objective of keeping employment near its maximum sustainable level. Yellen's April 4 speech and the FOMC's strategy statement simply reflect the Fed's dual mandate.

Importantly, the quote also makes clear that Yellen would accept only a slight and temporary rise in inflation above the 2 percent target, not more than that. Yellen is expressing the shared conviction of all FOMC members that the Fed cannot jeopardize its credibility as a low-inflation central bank. As further evidence of Yellen's aversion to high inflation, consider the following statement from a speech delivered on April 11, 2011: "The FOMC is determined to ensure that we never again repeat the experience of the late 1960s and 1970s, when the Federal Reserve did not respond forcefully enough to rising inflation and allowed longer-term inflation expectations to drift upward."

Two other speeches, delivered on April 11 and June 6 of last year, also deserve comment. Both speeches contained a lengthy discussion of why Yellen felt it was appropriate for the FOMC to keep the federal funds rate close to zero until 2015, a highly accommodative policy. In the models she discussed, leaving the funds rate near zero until 2015 produced a faster transition to full employment than an earlier normalization of policy, as advocated, for example, by John Taylor of Stanford University. The accommodative policy also generated a bit more inflation than Taylor's prescription. However, the projected inflation rate under the accommodative policy topped out at less than 2½ percent, only a shade above the Fed's target. Nothing in the speech suggests that Yellen would have been comfortable with a higher rate of inflation.

Yellen's policy stance has been consistently dovish in recent years because she sees an economy with a stubbornly weak labor market and subdued inflation. If her outlook for the economy were different, her policy recommendations would be as well. As she noted in remarks made while serving as President of the San Francisco Fed (September 14, 2009): "I can assure you that we will be ready, willing, and able to tighten policy when it's necessary to maintain price stability. But, until that time comes, we need to defend our price stability goal on the low side and promote full employment."

The choice of the next Fed Chair should be based on accurate information, not loose notions parading as facts. The President should not pass over Yellen because he thinks she could be soft on inflation. That's a canard.

Taking a broad view of the choice between Summers and Yellen, both are prominent economists with more than enough expertise for the job. But, on balance, I think Yellen would be the safer bet. Every word uttered by the Fed Chair has the potential to roil markets. Yellen chooses her words very carefully, while Summers is less cautious and has gotten into trouble in the past for his controversial comments. I also believe Yellen would be better at managing the FOMC. She listens well and is respectful, which is important for the functioning of such an unwieldy committee, while Summers can be dismissive of those who disagree with him. These points notwithstanding, it appears likely that the President will be rolling the dice with Summers.

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