



Three Observations about Central Banking in the US, and Compared to China

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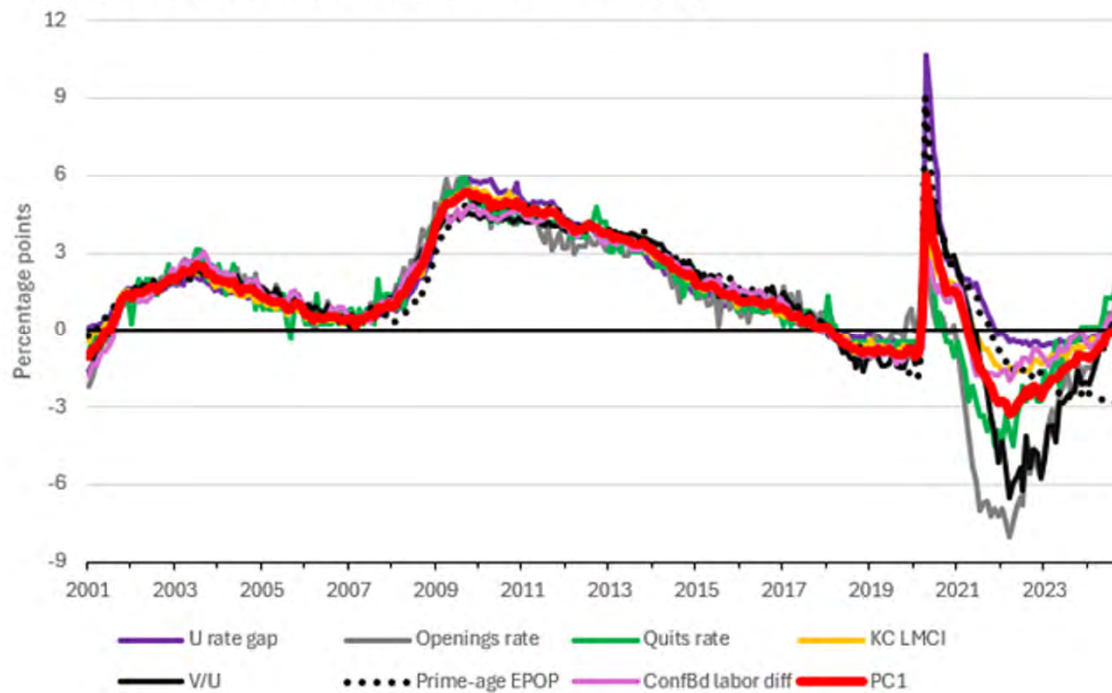
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Topics:

1. Is the labor market still too hot?
2. How could President-elect Trump shape the Federal Reserve more to his liking?
3. The governance of monetary policy is very different in China and the US. Why does it seem to work in both places?

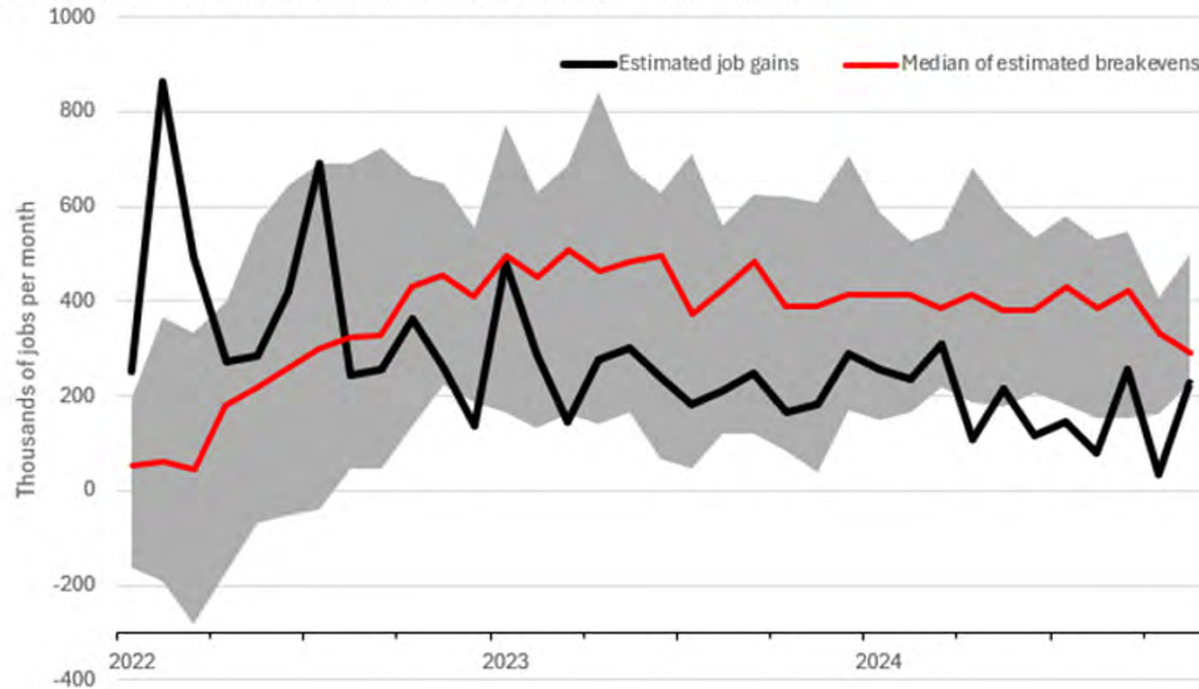
Is the labor market still too hot?

Most Indicators Show the Labor Market as Cooling



Job gains has been too slow to prevent cooling

Breakeven Pace of Job Gains Much Faster Than Actual



2. How could President-elect Trump mold the Federal Reserve more to his liking?

- Level 1: Appoint new members to the Board.
 - But all seven slots currently full
 - Vacancies will occur in January 2026 and January 2028; strategy required
 - Other slots could come open if current members resign
- Level 2: Attempt to demote Chair and two Vice Chairs to ordinary Board members
 - Has never been tried before
 - Would certainly be challenged in court
 - Powell has indicated he wouldn't go easily
- Level 3: Abolish the concept of an independent agency

3. The governance of monetary policy

In the US:

- Institutions are designed to keep the President and the President's team at arm's length from monetary policy
- Federal Reserve Board members have long, overlapping terms (14 yrs)
- Board members can't be fired by the President over policy disagreements
- Federal Reserve Bank presidents are chosen by their local boards of directors

In China:

- Monetary policy is fully integrated with the rest of the government's decisionmaking powers
- The PBOC Governor is not present when the most important monetary policy decisions are made
- There is no concept of monetary policy being "independent"

3. The governance of monetary policy (2)

- The systems are very different, and yet monetary policy appears to work well in both places
- Here's one theory for how that can be:
- The fundamental challenge is “time inconsistency”: A stimulative policy generates growth first, inflation later

3. The governance of monetary policy (3)

- The American approach deals with this problem by granting monetary policymakers independence
 - Give them long horizons, detach them from the political party controlling the White House
- In the Chinese system, the time-inconsistency problem never arises because policymakers have long horizons anyway
 - In that case, it makes sense to exploit all available tradeoffs
- Same problem, two different solutions



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