Economic Club of New York

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February 6, 2019
New York City

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Co-Host, Bloomberg Markets: European Close
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Introduction

Vice Chairman, Peter Henry

Good morning and welcome. It's not quite as cold as last week but we have a Fireside Chat for you, nonetheless. I'm Peter Henry, Vice Chairman of the Economic Club of New York and Dean Emeritus and Professor at the NYU Stern School of Business. I'm very pleased to introduce our guest speaker this morning – fellow member and former Club board member, Ed Hyman.

Ed is Chairman of Evercore ISI, Vice Chairman of Evercore, and heads Evercore ISI's Research Economic Team. For the past 43 years, Ed has been ranked by the Institutional Investor poll of investors for Economics and has been ranked #1 for 38 years. Prior to joining Evercore ISI, Ed was the Chairman and Founder of ISI Group, LLC which is the broker dealer and ISI, Incorporated on the funds management side. As many of you know, ISI Group has employees around the world with headquarters in New York and offices located in Boston, Fairhope, Houston, London, Los Angeles, St. Louis, San Francisco, Shanghai, and Washington, DC. ISI's broker dealer clients are institutional investors in the U.S. and abroad.

Before forming both of these companies in 1991, Ed was Vice Chairman and a member of the board of C.J. Lawrence, Inc., which he joined in 1972. He was an economic consultant at Data Resources, Inc. from 1969 to 1971. And he has previously served as a board member of the International Tennis Hall of Fame, Capital Trust, Said Holdings Limited, 10 Gracie Square, Saint

David's School, Collegiate School's Finance Committee, as well as our own Economic Club of New York.

Ed is a board member of the China Institute and is a member of the Advisory Committee for the New York Public Library's Financial Services Leadership Forum. He also serves on the Finance Committee of Bowdoin College. He earned a BS in Engineering from the University of Texas in 1967 and received his MBA from MIT in 1969.

As I said, our format today is a conversation and we're delighted to have as our interviewer one of our newest club members, Vonnie Quinn, who is the co-anchor of Bloomberg Markets: European Close and the anchor of Bloomberg Markets Americas on Bloomberg Television weekdays from 10 am to 1 pm Eastern Time. You've probably seen Vonnie on the air in the past interviewing U.S. and global central bankers, presidents, prime ministers, and other legislators, CEOs, entrepreneurs, and strategists about macroeconomic themes and controversies, the direction of policy and markets, along with the leading stories of the day. Vonnie joined Bloomberg in 2006 after completing an MA and an MS in Journalism from Columbia.

As Ed and Vonnie take their seats, and I'd ask the to please come up, I'd like to remind everyone that this conversation is on the record and we do have media in the back of the room. After Vonnie and Ed's conversation, I'll moderate questions from members and their guests. And as is our practice, we'll wrap up sharply by 9 a.m. Please give a big hand to Ed and Vonnie.

(Applause)

Conversation with Edward S. Hyman

VONNIE QUINN: Thank you. I'm so excited to be here. I have to say I almost didn't turn up because Ed was so kind to give me $5 trillion just a few minutes, but it happened to be Zimbabwean dollars. So, Peter said a lot of what there is to say about Ed, but obviously this 38 years as #1 ranked economist with Institutional Investor is just a phenomenal record. And I don't know anyone who has done anything for 38 years, never mind do it well and at the top of their game. I know you all know his worth and his value, and I hope I can do some justice to your views today. So, let's get going. You're one of the best, if not the best market and business cycle economist out there with the econometrics model that you, you know, learned at MIT and then put into practice at Evercore ISI is just world famous. Let's begin with something very current. You've said yourself that President Trump uses the stock market as a "report card." We had the State of the Union last night in which he called the U.S. an economic miracle, mentioned many, many statistics. We didn't hear much in the way of new policies. And I'm wondering if you see anything fiscal on the horizon that might keep the so-called Trump Trade in place.

EDWARD S. HYMAN: The only thing that could come up would be the infrastructure, but that looks – it's not that likely so there's not a lot coming up. And that brings up the 2020 election. And the economy is slowing right now and the only thing that could happen is if it was to slow in

‘19 and ‘20 and start to pick up in the latter part of ‘20. So it could be good timing, but right now it looks as though it’s going to be a slower pace than it has been. That said, the economy has increased about 50% in the past decade, which – I don’t know if you think that’s a lot – but it’s notable. And I travel constantly and every place I go to you can just see the prosperity, not in rate of change, but just that it’s so much better. Like Boston, for example, is really strong and you can just see it everywhere. I was on the West Coast last week. It’s very strong. I got a kick out of the Super Bowl because you’ve got Atlanta, that beautiful stadium, and Atlanta is just booming. LA is booming, but its real estate has weakened quite a bit. And Boston, I think the Patriots are from Boston, and it’s booming too.

VONNIE QUINN: You did mention the other day when we were speaking where we are in the business and economic cycle and you had a good reference to the Super Bowl.

EDWARD S. HYMAN: Yes, so that’s what I’m, one of the things I’m most interested in right now is this topic. The economy probably grew in the first quarter. If it grew in the second quarter, if the U.S. GDP increased, it will be the longest expansion on record. It would be 40 quarters. The longest was 39 quarters in the 90s. And that will get tongues wagging. Peter, you interviewed Larry Summers and when you were discussing with him when the next recession would be, he mentioned Australia, and Australia, as you know, has been at it for 28 years. And you said, Larry, this is being recorded. I don’t want you to give people the impression you think the next recession is 15 years out. But once you get into the second quarter and it’s the longest

ever, you'll be asking the question what's what. And this is what I think is happening. China, this is the first expansion that China has dominated. China really became China as an economic force in 2007. And so this is the first time they've been really driving global growth which they have been .Second, these forces are now in place for two decades – competition, technology, and globalization. They're driving growth and keeping inflation down. And they're always getting stronger and that's now a force in the current episode. And so those things are making the cycle longer than has been in the past. And so we'll have to cope with that. I don't see a recession, it'll be a couple of years out, if not longer.

VONNIE QUINN: I think you called it the Tom Brady of biological...

EDWARD S. HYMAN: Right. So I say, I'm into any performer that's old so we're chronologically old and biologically young, or let's say, I would say that we're Tom Brady when he's 50.

VONNIE QUINN: Wow! Okay, excellent. So I'm sure a lot of you know, but one of the things that Evercore ISI does and that you pioneered specifically were these surveys. You put out 400-odd surveys to different industries effectively surveying business and manufacturing, airlines, banking, retail, you name it, and Evercore ISI and Ed has its finger on the current pulse. You get responses every week. First of all, during the partial shutdown, did those responses keep coming? And what were they telling you?

EDWARD S. HYMAN: Well, they definitely, so the responses definitely kept coming. So we started these surveys 25 years ago. We asked the same companies – we started first with retailers – and we asked the same companies the same question. How is your business compared to what you expected? 50 is as expected. We do an airline survey and the week of 9/11, they rated business as a 3 on a 0 to 100 scale. There wasn't any business. And that survey has gotten as high as 70. So we do that every week for maybe 25 industries. So we started that. And then Jason Trennert took it to a new level and then Oscar Sloterbeck is now pushing it ahead. At the moment, the surveys are clearly weakening. Our trucking survey, for example, was 65 six weeks ago, now it's 55. So the economy is weakening. I don't think it's going to go into a recession, but it's definitely weakening.

VONNIE QUINN: Well, it's fascinating because the last bull set of GDP data that we have is for the third quarter of last year. It shows 3 ½% growth, definitely slowed in the fourth quarter. What are you looking at now for the first quarter, now that we're starting to get January data? And honestly, you know, a lot of the government data that we're getting now, it's not terribly weak.

EDWARD S. HYMAN: It's not terribly weak. The last data we've gotten is we got the survey of bank loan officers. It came out yesterday. It had a significant drop. And then we got the PMI which had a drop. And I got a trucking survey which was down four points in four weeks. So I look at, you know, the government data and the industry data and our company surveys and so

they're weak. GDP, in the first quarter, will probably be about 1 ½% on a quarter to quarter basis. But that will still be 2 ½% year on year. So it will still be a pretty solid increase down from maybe 3, 3 ½% at the peak last year.

VONNIE QUINN: Now you also survey hedge funds and you have technical analysis as well as fundamental analysis. We'll get to some of that in a little bit because the stock market, I'm sure, everybody wants to know about that. But let's dig in a little bit more to the economy and the health of the economy. Hourly earnings averaging 3.2% year over year. Kevin Hassett saying that that will get to 4%. Do you see that happening? Because that seems to be what's necessary for inflation.

EDWARD S. HYMAN: So that's one of the strongest likelihoods is that wages will keep accelerating. We just got this week the Atlanta Fed wage tracker and it is 3.8 so it's already close to 4%. And all the wage numbers, like the Employment Cost Index came out last week, it's clearly accelerating. There's little doubt that wages are getting stronger and stronger. And for a business person, whether you run a bank or an auto dealer, whether employment increases or your customer wages increases, you're sort of indifferent. You're just in for an income increase. And so in the employment report that came out on Friday, income was up 5.7. If inflation was, say 2, that's a 3.7 increase. So income looks, it's the real star at the moment. And then the question is, does the star become an enemy if you start to get inflation out of it? And so far, inflation has been restrained by the factors I've mentioned – technology, globalization,

competition.

VONNIE QUINN: Is that what's holding back wage gains? Because by now, with unemployment so low and not just in the U.S. but in many of the major advanced economies, and we still took until now to see a certain amount of healthy wage growth, what held that back, Ed?

EDWARD S. HYMAN: Well, those things. So competition in so many areas, whether it's airlines or autos or retail, then technology, whether it's Uber or Airbnb is such a drag. And then globalization, you always can get labor cheaper outside the U.S. And so those things are holding back what would be a stronger, but they're still accelerating. And I assume they'll keep accelerating and you'll get a business cycle – at some point inflation will pick up and the Fed will over-tighten and that will be it. It's not for now I don't think.

VONNIE QUINN: What about the relationship with productivity? Because again you're at the cold phase there. How has that relationship broken down? What's causing productivity to stay so muted?

EDWARD S. HYMAN: I think productivity is weak because the economy has been slow. Ken Rogoff had the, this time it's different, after a financial crisis the economy doesn't snap back. It's slow for a decade. And it was slow. It was 2% growth for a decade. As a result, productivity was slow. And it's still, to me, been disappointing. I thought it was going to be better last year. I

thought growth would be maybe 4% and it was only 3 ½ or 3. Now productivity has picked up. It was just reported this morning – or will be reported at 8:30 – it's picked up from maybe ½% to 1 ½%. But that's still not great, but it's getting better. But at this point, with the economy slowing back down, productivity will be weaker again so I'm not particularly betting on anything big there.

VONNIE QUINN: Which brings us to the question of monetary policy and there was obviously a huge brouhaha recently about the change in language and about the balance sheet. First of all, is the Fed at a point now where we don't know what direction the next interest rate move is?

EDWARD S. HYMAN: I think that's the point they would like for us to be where they say we're data-dependent. Read my lips, we're definitely data-dependent. The *New York Post* had this great headline: Trump Feeds the Fed, when they had the dinner with Powell. But the Fed had those two steps where first we were a long ways from normal and that, you know, crushed the market, and then the automatic pilot on the balance sheet just drove them crazy. And usually when you make two mistakes you're pretty cautious on the next step. And so the Fed, I think, is cautious on what they do next. As a result, the market right now is assuming that even if you get stronger data, the Fed is going to be slow to react at that. And that's why the market is having such a big run here because they think there's a free pass here for a bit.

VONNIE QUINN: So you're quite sanguine about inflation. You're sanguine about the

possibility of a next recession any time soon. And it seems like you're quite relaxed about the economy.

EDWARD S. HYMAN: I am relaxed.

VONNIE QUINN: Well, that's good. The yield curve is pretty flat though and there are a lot of worries out there that this is signaling something and that the Fed maybe shouldn't stand so pat given that, you know, there is the potential for wages to get to 4% and that could happen pretty soon. Could there be a jump condition in inflation, therefore, making the Fed wrong?

EDWARD S. HYMAN: Okay, so when the Fed said we're a long ways, we could keep tightening, people said if they tighten another two or three times, we'll have an inverted yield curve. And if that happens, we could have a recession. And that was the thing, back in October, that set the market off. That's a little bit off the table. My number one worry is that Europe goes into a recession. My second worry is that the yield curve inverts. And it's close enough that, and on that, I worry because the world economy is slowing and inflation is low, and you could get into deflation without a lot of trouble. And if the bond yield were to come down like some expect it to, you could get an inverted yield curve. And if we got an inverted yield curve, even if it was for unusual reasons, I would still think that you'd probably get a recession out of that. So that's a worry for me.

VONNIE QUINN: Why are yields anchored so, last November we saw the 10-year at 3.24%, we're right back to the 2.70 range for the 10-year and the 2-year is going nowhere either, 2.38 or so?

EDWARD S. HYMAN: So my hindsight is usually perfect. (Laughter)

VONNIE QUINN: Well, that's why people read your research, Ed.

EDWARD S. HYMAN: Or close to it. My foresight, you know, comes and goes. But, you know, 20 basis points probably does it. You know the German bond yield is, I don't know what it is...

VONNIE QUINN: Yes, about 17 or something..

EDWARD S. HYMAN: I mean it's just so low and Germany, zero. And it's hard for the U.S. yield to get up very much, plus inflation is not that high. So I've looked, you know, the market had that huge drop in the fourth quarter, and I looked to see, trying to prepare, could I avoid it if it happened again? And one of the things that happened was that the dollar went up 7% in a short period of time. So I'm watching that really closely. Second, oil went up $30 to $70. So I'm watching that closely. And thirdly, the bond yield went over 3%. So if the bond yield were to go over 3% which might be a good sign for the economy, but that trifecta could get us back to another correction in the stock market. At the moment, you know, like you pointed out, yields

are still quiet, oil is up but not that much, and the dollar is sort of stabilized at the current level.

VONNIE QUINN: Speaking of the stock market, you said a few moments ago that you saw your surveys in January slow quite substantially. It was a 10-point drop, I think you said, in some of the industries. Was that due to the partial federal government shutdown? Will that bounce back? Or are you seeing something a little broader here?

EDWARD S. HYMAN: Yes. So, first, the government shutdown, you know, pushed the economy down and you'll get a bounce back. You'll probably get half a point down in the first quarter, half a point rebound in the second, roughly speaking. But in the work I do, consumer net worth, which is driven by the stock market and house prices, it was up 10%, now it's unchanged, roughly speaking. That knocks a point off of real GDP growth in the econometric work I do that I started doing at MIT. Second, spreads, BAA spreads in particular, widened out 100 basis points. And that knocks a point off of GDP growth. So that's how I got from 3 ½% and the 2 ½ down to 1 ½. And so I think the economy is slowing for those fundamental reasons. Now since then, the stock market has come back some – Trump's report card. And the spreads have narrowed some. So it's looking a little bit better and the economy might pick up some. The other gorilla in the room is China. And I'm out and about all the time plus I have the advantage of working with our teams, and China has put in a ton of stimulus. Don Straszheim says it's the most stimulus they've ever put in, in modern history. I'm not sure what other history he is referring to for China. But they've put in 51 easing moves. And we think they're going to pick

up some in the second half of the year, which if they did, you know, Trump would get a free pass on that. We survey 21 companies that do business in China and that survey has hooked up a little bit. We survey 28 multi-nationals that do business in Europe. That survey has dropped two points in the past two weeks. So one is going straight down, the other looks like it might be bottoming a little bit.

VONNIE QUINN: Let's stick on China for a moment before we get to Europe. China is a bugbear and it's one of your main concerns and you only have three. So, with trade first, how important is it that we get a trade deal done this month? Because it looks like it's going to be this month or not for a long time.

EDWARD S. HYMAN: So, Vonnie, I'm pretty short-term oriented with a long-term view, but I'm trying to – as Powell put it – I'm walking very slowly in a dark room trying not to fall over. And on China, it really seems to me like it's likely to pick up in the next little bit.

VONNIE QUINN: When you say pick up, do you mean China growth?

EDWARD S. HYMAN: Yes, China growth.

VONNIE QUINN: Why? Why do you think that?

EDWARD S. HYMAN: Because they put so much stimulus into the economy.

VONNIE QUINN: And you don't see any problems with the shadow banking sector or with...

EDWARD S. HYMAN: There are a ton of problems, which is why they put in 51 easing moves.

VONNIE QUINN: What about if this trade deal doesn't get done?

EDWARD S. HYMAN: Sorry, on the trade deal, so I'm out and about, I don't know if this room would agree – I can maybe let you know, I guess I can nod – roughly 100...people think the odds of a trade deal are 100%.

VONNIE QUINN: Do we want a show of hands? Who thinks the odds are above 80%?

EDWARD S. HYMAN: They have to be just above, they have to be like 55% because I survey people all the time. Most people think the odds are now that we'll get a trade deal. Then they put deal in quotes...(Laughter) and it's whatever Trump says is a deal. So that's, one of the reasons the market is moving is because people now assume that there will be a trade deal. And for, you know, a variety of reasons. Trump is desperate to get a deal. Xi is probably interested in getting a deal. But that is the prevailing view at the moment...and our team, I think, puts the odds at 90%.

VONNIE QUINN: And therefore there will be good economic relations with China that will be beneficial to both countries?

EDWARD S. HYMAN: Yes. But this is also, I don't want to give the impression that people think that this is going to be good forever, that it is just we'll move the ball to the next place and then we'll see if we can enforce intellectual property and have a true improvement in trade.

VONNIE QUINN: Would it make a meaningful impact on U.S. GDP?

EDWARD S. HYMAN: I don't know. I've talked to some people that say that if they start buying U.S. goods in the quantities that they're talking about and increased it 10% a year, it could become very meaningful, but I'm not counting on that. That would be something, I'm not even sure I'm hopeful for.

VONNIE QUINN: Trump has said that he wants structural changes in order for this to happen. What would China allow?

EDWARD S. HYMAN: I don't know. I mean...will intellectual property open up China to U.S. companies? Those are things that are more problematical. And, you know, China, I have many, as mentioned, I'm on the board of the China Institute. I have many close friends who are Chinese. And they are, they've sort of soured on China because it's a dark place and you have to, they have now, they have like continuing education. So if you're working at a company like

Evercore, you have to do continuing education about the Communist ideal. And young people in particular are like, no, thank you, and so there's a lot of tension in China right now.

VONNIE QUINN: So let's move to Europe. You said you saw a 2-point drop in Europe. Obviously Italy went into a recession at the end of last year, the gilets jaunes in France, and it looks like other countries could very potentially do that too. You don't seem to be as concerned about Europe impacting things as you do about China, for example, or at least at putting an end to the bull market?

EDWARD S. HYMAN: I have nothing to say for Europe. They have no, in the case of monetary policy, you're moving, you're making a transition from Draghi so that sort of leaves a bit of a moment. And on the political structure, the Eurozone might not work in the long term. And so if there's a problem with Italy being in recession or Brexit has an impact on the Eurozone, there's nothing, I can't point to anything in Europe like you can in China where they've already started to stimulate aggressively. And so right now it's just sort of weakening. And that gets you to the next point of reflexivity, which is that central banks are now very aggressive. So the Fed, which I take my cue from Krishna Guha, the Fed is now signaling that they have a balance sheet target, Krishna believes, of as much as $3.7 trillion. Before this, maybe a month ago or two months ago, it was maybe $1.7 or $2.7. So this is a much bigger number. And at $40 billion a month, they get there by December. And we think that before they get there – they don't want to do 40, 40, 40, 40, 40, zero – they'll start to taper. So the Fed could be moving away, or moving to a QT taper

in the second quarter. And, you know, China is aggressive and Japan is still expanding their balance sheet and Europe has to worry about their economy there. So you have a very stimulative monetary regime at the moment.

VONNIE QUINN: So a couple of questions on that. Given that the Fed is now is sort of pause mode except for the balance sheet, which it's continuing, but which – at least the New York Fed says, you know, why is everybody concerned about the balance sheet? This is just technical, it's not a monetary policy tool right now. Do other central banks have to delay their actions? Will the Bank of Japan, for example, ever get away from zero interest rates?

EDWARD S. HYMAN: Probably not. I mean that's the scary thing. If you sit down in the evening and start reading about the world economy, Japan is a real troubling spot because they've done all this stimulus and they still have basically zero inflation. And then Europe doesn't have much inflation. And so that's where you get to this aggressive policy response that's going on now by the central banks. And what a switch from like September of last year when we were all tightening and now we're all easing. But that's, you know, that's the way the cycle goes. And right now people are assuming that we've got a trade deal, the Fed is friendly, and China is going to pick up and so the market is on the move up.

VONNIE QUINN: What does a balance sheet that size now mean to you? I mean listening to the Federal Reserve representatives, it's just a larger balance sheet. That's always the way it was

going to be after the financial crisis and it's now at least providing liquidity to the global environment and that should be a good thing and nothing to worry about.

EDWARD S. HYMAN: It's funny the way things change. You know right now we're going through a moment where we're starting to say, well, budget deficits don't matter. And it's like, well, wait a minute, Ed, please. But that's the new-new. And now we're going to the point where we say, well, maybe we don't need to have a $1 billion or $1 trillion, $2 trillion, maybe we could have 3.5 or 3.7. And I don't have any particular thought. In the long, long term, I figure we're in real trouble because of the debt levels and we don't really have any ability to fight a recession. But in the short term, it looks like we're going to be doing what I have covered so far this morning.

VONNIE QUINN: Let me stop you there. We don't have any ability to fight another recession, that sounds a little scary.

EDWARD S. HYMAN: Well, it is a little scary.

VONNIE QUINN: But we do have interest rates that have risen a little bit so there is still...

EDWARD S. HYMAN: A little bit of room.

VONNIE QUINN: What about companies? Can Corporate America save us from the next recession or what happens there? Are companies done spending?

EDWARD S. HYMAN: No, I don't think companies are done spending. As I mentioned, I think the next recession is years out. And so you have time for people to buy more and more Bloomberg terminals. And time heals a lot of things.

VONNIE QUINN: I was asking for a friend, not for me. (Laughter)

EDWARD S. HYMAN: And one other thing I'd mention is that at the moment we don't have a tech bubble like we had in '99. We don't have a housing bubble like we had in '05. And we don't have a valuation bubble like we had in 1929. I'm picking carefully my shots there. So we're not at a risk like that. And the first two I mentioned were recent. At the moment, there are problems like corporate debt is a little high, student debt, but I don't see any deep problem at the moment, which is phenomenal given that we're just entering the longest expansion in history. And we still don't have any, at least for me, any visible thing that could blow up in the next year or two.

VONNIE QUINN: So you're not at all concerned about lower quality credits, you're not concerned about the FANG stocks. You're not concerned about any of the little things that have come up.

EDWARD S. HYMAN: Well, not concerned is a little bit – I live in a state of tachycardia. (Laughter) I can only have one cup of coffee a day because I'm so concerned about everything. But you have to sort of, you know, balance, my Rosetta Stone of, you know, what is. And right now the dominant things is that the central banks are easing, the Fed is easing, China is likely to turn up, and a trade deal is likely. And so that's, you have to shift with those things and those things were very different. And like I mentioned, on sort of a short-term basis, I'm watching bond yields, oil prices, and the dollar to tell me if I should get more concerned about the risk in the system.

VONNIE QUINN: We're coming fairly towards the end of this earnings season. We've had a really great run it seems. Even yesterday some of the consumer discretionary stocks did fantastically well and that was on the outlook for Asia. So what about earnings? Do we continue to see decreased expectations? What happens, you know, with companies? Do they continue to buy back? Do they continue to raise dividends?

EDWARD S. HYMAN: So I think that, you know, one of the risks out there is a decline in earnings because growth is slowing pretty sharply and earnings could decline. We're estimating earnings, we're forecasting earnings to go up 5%. And one of my dear friends here today keeps reminding me about buy-backs. So there's a tailwind for earnings but we are forecasting a slowdown from 25 to 5 and that's obviously a slowdown. Now in the fourth quarter, earnings – like you say – they were good. They were 15% four weeks ago and now they're almost 18%,

they're 17 ½%. So companies guide down and then beat, guide down and beat. The first quarter will be a bit of a test because that will be the first quarter without the tax cut in there. So it'll probably slow down dramatically. But at the moment I think earnings are likely to increase some, but that's a risk because the global economy is weakening.

VONNIE QUINN: So I want to get your thoughts on active management? This is something slightly different, but I know that you have your finger on that pulse too. And I'm curious as to Alpha Generation and whether it's still possible, whether it's getting more and more difficult? Obviously it is.

EDWARD S. HYMAN: Vonnie, we were doing pretty well until we got to this one.

VONNIE QUINN: But does that change again? I mean if we see the return of volatility, you know, the spreads widening...

EDWARD S. HYMAN: I don't know, I don't know. When a dollar goes from active to passive, trading volume goes down 90%, and my business is 100% trading volume. So this is a question that I am very interested in.

VONNIE QUINN: You're a little biased.

EDWARD S. HYMAN: A little biased. I will tell you that when I ask a group of people like this, do you think active will outperform passive in the next year, like 70% say yes. It's like hope springs eternal. But I don't have a dog in the fight except my whole life. (Laughter)

VONNIE QUINN: Let me ask you a different way.

EDWARD S. HYMAN: I don't know if it's going to...

VONNIE QUINN: Market concentration then, are too many investors piled into the same assets, the same risky assets?

EDWARD S. HYMAN: I don't know. It's just gotten to be very tough. I think that if interest rates were to get back to a more normal level, that active management would have a much better chance of outperforming. And I thought bond yields would be much higher – if you'd ask me five years ago, I thought they would be much higher and I've slowly given up. And so with that, you have to work really hard to get active to outperform passive.

VONNIE QUINN: Speaking of, you know, the profession and the fact that several years ago you wouldn't have predicted, you know, what's happening now exactly – things have changed over the last few years – how have your econometric models held up? And not just yours, but just generally the profession's models?

EDWARD S. HYMAN: Well, when I first started doing that work in the 70s, the econometric models collapsed. They simply stopped working completely. And I haven't found that in this episode. Like I mentioned, consumer net worth, the spreads, price of money, the price of oil, those have continued. So the models that I use forecasted growth to slow to about 1% in 2016. They forecasted growth to pick up 3 ½% in 2018. They forecast growth...slow to 1 ½% this year. And I decided that it's not happening. It's not slowing to 1 ½%. So I moved it up to 2%. So in that sense it's not working and I decided that it's not working because of fiscal stimulus which there's about as much fiscal stimulus this year as last year. But I haven't found, I'm not giving up on the sort of scientific approach to analyzing the economy. I'm not a slave to it, but I find that the relationships still are working to a large extent.

VONNIE QUINN: Are there new strands to the profession or new strands of thinking that you have started to incorporate just in the last, since the financial crisis?

EDWARD S. HYMAN: The strands that I'm thinking about mostly right now is where are we in the cycle? Because it's so hard to know when you're, the longest ever, where are we? And so I'm doing, and that's new work. Like I mentioned, I think we're still biologically okay but that's one thing. And then I'm also, I mentioned 1929 and 1999 and 2005, the way in which psychology plays a role in shaping the business cycle and investments, I'm very interested in. And I find that at the moment most people are fairly pessimistic. Whether they're pessimistic in their forecast or not, they're sort of pessimistic in general. Like Davos, I couldn't watch it anymore. There was

just so much sort of negative feeling coming out. And so I don't think this is the end of a cycle because I think people are a little too cautious for that to be the case.

VONNIE QUINN: And then just a broader overview question, we're hurtling towards 2020 it seems. What if there is a change in economic thinking? And so, you know, all of these new ideas, they're not new but, you know, things like Medicare for All, things like a wealth tax, they're gaining traction and a lot of people are very supportive of those ideas. Can an economy just reverse course like that? What would happen in that situation?

EDWARD S. HYMAN: So, Vonnie, you're very perceptive. I don't, this is like sort of an unspoken question. It comes up, you know, after a couple of glasses of wine or something. But there's a fair chance that we're going to have a complete regime change. We'll have a 70% tax rate. I've worked for a long part of my career with a 70% tax rate. You know, one for me, three for you. And I don't know, I seem to be okay. And then a wealth tax. I mentioned I was in California, and I think, I always ask people, do you think Trump will be reelected? And in New York, it's about 50/50. In California, it was 20% yes. And so then you just think, well, gosh...

VONNIE QUINN: That's a lot for California.

EDWARD S. HYMAN: Who's the 80%? A question like that is unfair, do you think Trump will be reelected, because you're not presenting who he's going to be running against. So it's really

not a fair question. But, you know, I lay awake at night thinking about that and what the stock market response would be if that comes up. And I assume it would be pretty bad or the work-up to it would be pretty bad. And then I had the jarring experience, I was in Tokyo the election night when Trump won. And I was giving a speech to 250 people who I meet with once a year at 3:00 on Thursday afternoon in Tokyo. And so I was all set, and then Trump won, so I had to completely…I was a panic. But that could happen again. It could look like Trump is going to win and then suddenly you get whoever...so that's, I won't say it's a risk out there, but it could be a big change out there. Maybe Bloomberg will be the next president.

VONNIE QUINN: Well, just finish that anecdote. Tell us what happened.

EDWARD S. HYMAN: Well, I had very good coaching – I must say – from my Democratic friends at Evercore. And Ralph Schlosstein, in particular, who is a big D Democrat. And I love the guy, he said, Ed, he said, well, I'm disappointed, but they're going to ring-fence America and it's going to be great for business. That's what I told them and it worked out fine, so far.

VONNIE QUINN: I think we're coming very close to the end of our time. But I do want to thank Ed first before you get to the questions. Ed Hyman, fantastic conversation, and it's really wonderful to have your insights.

EDWARD S. HYMAN: Thank you, Vonnie, so much. (Applause) And I believe we're not done

yet. You all get a chance to ask some questions.

VICE CHAIRMAN PETER HENRY: The floor is open. Questions for Ed. Table 13 in the back.

Hi. This is Dan Robbins. How do you think about automation's effect on jobs, if any, when you look at the long term?

EDWARD S. HYMAN: So I'm in the technology is good for us. I've had a long relationship with Andy McAfee at MIT – not long, but a good relationship with him – and his first book, *The Second Machine Age*, was quite negative that robots will replace people. And his second book was much more positive, and you saw that jobs have been created now for 100 months. How many months are we going to create jobs when we keep thinking that robots are going to replace people? So I'm in the camp that there will be definitely – people that make buggy whips are going to be out of luck. They'll have to do something totally different and maybe they'll never get another job. But I think that creative destruction will rule the day on that. And at this point, you know, going into the longest expansion ever with 100 months of job creation, it seems to me as though the facts are on that side. Not to say there won't be displacements, but I think on balance it's good and should, Vonnie, should help with productivity.

VONNIE QUINN: Well, I just, can I add to that and ask you – we didn't have time for it – obviously robots and artificial intelligence are one element, but you have this gig economy now

where people are working several jobs and they're not registered as unemployed, but they're still finding it so hard to make ends meet. Does the gig economy become sustainable?

EDWARD S. HYMAN: I think all this is a revolution that's going on – the gig economy and also people working like in Nashville. You can work anywhere. So I see a lot of people now that are working, you know, in places that are much more economically attractive. My son worked for Epic Games in Raleigh. Why he's in Raleigh I have no idea. But it's booming and they also have Red Hat Theater. So these cities that you thought wouldn't be much of anything are now doing quite nicely. And it's because people can work anywhere and have the gig economy. But I also say, I also find that when I travel around, I get the impression that the bottom of our income strata is picking up and also I see Walmart sales are better than they have been. So it's not just, you know, visual inspection. The CBO had a paper out last week that said that the bottom tenth of income brackets are improving, which makes sense to me given how long the economy has improved.

VICE CHAIRMAN PETER HENRY: Let's take the next question.

You finished your formal comments by talking about the U.S. being ring-fenced. The U.S. has been ring-fenced for a long time. It's actually a fairly closed economy. We're not terribly dependent on trade. But you listed at the top of your worries European recession. Given some of the political issues in Europe and the lack of policy tools, do you think that Europe could drag

the U.S. economy into a recession?

EDWARD S. HYMAN: That's why I have it, yes, that's why I have it as my biggest worry. I don't have any, it's certainly big. And I don't have any way to really track, you know, how bad it could get. You have, you know, Brexit. You have immigration problems there. You have a political structure that's not as cohesive as it is here. So that leaves really ECB. And you have a bit of a change there, plus ECB is already maxed out. So I'm not, you know, I'm not, it's easier for me personally to be bearish than bullish, which is why I can feel that about Europe. But, in general, I think right now, you know, China is going to pick up and I think the U.S. can pick up a little bit in the second half of the year. And with policy where it is and trade working where it is, I'm more looking up. Can I add one more thing that's not to your question? So, the correction last year in '18 was the fourth correction in this expansion. We had one in 2010, 2011, 2016. And so last year to me felt like it was a disaster and out of nowhere. But it's actually something that's happened, you know, four times now. And after each of those, the stock market bounced back about 20% in the next six months, in each case because there was a move by central bankers to turn it up. And so I think that's what's happened. And I'm going to revisit your question in maybe three or four months.

VICE CHAIRMAN PETER HENRY: Another question, or Vonnie, do you need a follow-up?

VONNIE QUINN: I was just going to say it's number one in your three negative risks, Europe

economy weakens significantly.

Dave Duebendorfer, Artemis Wealth Advisors. I was wondering if you can sort of quantify your comment on the debt concern with regards to timing of the long term. In other words, at what stage does debt servicing at the state and the federal level crowd out discretionary spending?

EDWARD S. HYMAN: You're asking me these questions that have no answer. (Laughter) But I mentioned I'm intrinsically more able to be, you know, glass half empty. And every quarter when the debt numbers come out, I do a debt to GDP, and it just keeps getting worse and worse and worse. My assumption is that I'll face the devil, as the book covered, I'll face the devil when inflation picks up and the yield curve inverts. And that may be my Achilles' heel. Maybe something else will happen different this time. But I'm assuming that things will go on and somewhere down the road, we'll get an inverted yield curve and then we'll get into a recession. At the moment, I think the popular view is that the next recession will be mild. I think if I was to ask people, that's sort of the inside baseball. And I'm not so sure about that. I think the next recession could be as bad as the last one. But I'm not going to try and get there until those circumstances that I mentioned unfold. And, as I mentioned, Vonnie, I think that this expansion could last for quite a while longer. And if it does, I'd be premature to get off at the moment.

VICE CHAIRMAN PETER HENRY: Next question.

Hi. Charlie Garland with Hamlin Capital Management. The question is in the next recession, whenever it happens, do you assume more QE? And if you do, will it eventually be problematic for inflation and the dollar?

EDWARD S. HYMAN: I want to stick to my wheelhouse. I mean you know me pretty well and I don't know when the debt thing is going to be an issue in Europe and I certainly don't know what the policy response would be in the next recession. But we're in an economy where we are very reflexive, like the move from October by the Fed to now. We move. And so if we get into a recession, I assume if it's a bad recession, you know, they'll pull out all the stops. They'll have tax cuts and spending increases and the Fed will be creative and try QE I assume.

VICE CHAIRMAN PETER HENRY: In the back, Table 11...

Yes, do you see this Fed as following any kind of a familiar pattern? Normally you think of the Fed as trying to be broadly cyclically anticipatory. Is this a change in how they are responding to data? And how do you see them acting if something unexpected happens? Is there any kind of a risk of a shock as a result of a turn in Fed policy?

EDWARD S. HYMAN: Well, it seems we've just gotten the answer to your second question. They react aggressively and quickly when it looks like they've moved off in the wrong direction. And I think the Fed is a very well-intentioned institution, a voice respected, you know, back to

Marriner Eccles, the very beginning, or certainly Stan Fischer. These people are trying to do the right thing. But forecasting is, you know, virtually impossible. And so I think the Fed is usually sort of lagging events. Not because that's their intention but it's just because it's so damn difficult. And also monetary policy takes such a long time to work through the system, so what they're doing now, you don't really see. In the models I use, it's one and two years, what the Fed does and what actually happens. And so I was – right or wrong – I was totally opposed to the Fed tightening this last move. And I remember in 2007 the Fed tightened in the spring I think, and at that point, house prices had been going down for two years. And, you know, the people that were involved with the sub-prime crisis, they were all over it. And that tightening move in '07 was like really, it was not the best thing. So I think the Fed, by the nature of an institution, they tend to be more of a lagging thing than leading.

VONNIE QUINN: Just a quick word on the evolution of transparency. We've had a Fed that's been more transparent, even just in the last month, than probably ever in its history. It used to be that you'd have to parse a statement and then wait for the next Fed speech, and now they're just bombarding us. That has a negative connotation. I didn't mean it that way. But is it a good thing?

EDWARD S. HYMAN: I don't have a strong view. I grew up first with Paul Volcker who is an absolute legend. And he liked to keep, as he said, keep the cards close to his vest. And the German central bank like to actually fake people out. They say I think we might be easing next month and then they'll tighten. There was Volcker and then you got into Greenspan and now we

moved to total transparency. The feeling I get is that we're trying to move away from the Fed predicting what they're going to do next, the dot plot. Just to say, look, at each meeting we'll take a look at it and we'll do what we think we should do, but I couldn't tell you today what I think we're going to do in September. And I think they're moving away from that.

VICE CHAIRMAN PETER HENRY: Well, no one knows what the Fed is going to do, but Ed, we thank you for your hindsight.

EDWARD S. HYMAN: Thank you Peter.

VICE CHAIRMAN PETER HENRY: And Vonnie, thank you.

VONNIE QUINN: Thanks Peter.

(Applause)