What's on Nouriel's Mind: Larry Summers: Underdog in Race for Fed Chair May Now Be Frontrunner

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By Nouriel Roubini Jul 26, 2013 11:00:00 AM [Read this analysis on Roubini.com]

- The most important economic policy decision that President Barack Obama will have to make in the fall will be naming a replacement for Fed Chairman Ben Bernanke. We take an out-of-consensus view that Larry Summers will be the next Fed chairman.
- Both the frontrunner, current Fed Vice Chair Janet Yellen, and former Treasury secretary Summers are eminently qualified with both the intellectual/academic skills and broad policy experience needed for the job, but we would argue that Summers is battle-tested, having worked at the Treasury during the Asian Financial Crisis and the many EM crises between 1994 and 2000, as well as during the systemic downfall around the LTCM hedge fund. Yellen outmatches Summers on central bank experience, but Summers' extensive policy experience more than compensates. Yellen is not very close personally to Obama and his senior aides, while Summers has close friends in the White House and worked directly for Obama.
- Yellen's weaknesses include an excessively dovish position on monetary policy (there is concern about this among some market participants and even Fed hawks), her distance from the Obama White House, a lack of financial market experience, a soft-spoken management style that could suggest weak leadership, and a lack of concern about financial stability relative to economic growth.
- Summers' perceived weaknesses include the perception among some that he is intellectually arrogant and in rare occasions a careless communicator; that he is perceived as a friend of Wall Street and does not have the support of the left wing of the Democratic Party; that his relationship with the Obama administration was partially rocky while at National Economic Council (NEC), even if everyone has great respect for him; and his lack of direct monetary policy experience, even if he has a very broad policy experience. Summers will face harder questioning than Yellen during the confirmation hearings even from some Democrats, but Yellen's dovishness would likely be challenged by conservative Republicans.
- Both candidates are very well qualified for the job and would be an excellent

choice for the Fed chairman position. At the margins, the weakness of Yellen—who until recently was the frontrunner for the race—are now being discussed more openly. Meanwhile, Summers, the underdog, is now becoming the candidate most likely to win this race.

- In terms of impact on monetary policy, both candidates care about growth in the framework of inflation stability and while there is a significant fiscal drag, but Yellen is more dovish than Summers—more dovish even than the doves on the FOMC—on how aggressively monetary policy should be used to boost growth and jobs. Summers would support less frontloaded fiscal austerity as the leading tool to achieve more sustained economic growth. Given the current divisions within the Fed Board and FOMC, and given that the Fed chairman is no longer a near-king who can impose his/her views on the other Fed members, both would have to work hard to convince other FOMC members on the right path for monetary policy. The leadership styles of the two are quite different, with Yellen taking a more consensus-driven approach. Given RGE's forecasts on growth and inflation, the Fed will normalize policy rates very slowly regardless of who is chosen as the next Fed chair.

*To read the full analysis, visit Roubini.com.*

**We should pay attention to Nouriel's thoughts because of his disclaimer. He knows both of the candidates personally:**

*A necessary disclaimer: Janet Yellen was my boss as head of the CEA when I was the international economist for the CEA in 1998-99. Larry Summers was a teacher of mine at Harvard during my PhD studies and brought me from the CEA to Treasury in 1999-2000 as the Senior Advisor to Tim Geithner when Geithner was the Under Secretary for International Affairs while Summers was Treasury Secretary. So I know and have worked closely with both of them. Summers was also an external advisor to the Board of RGE in 2009-10 before going to the White House NEC.*