

NATIONAL PRESS CLUB LUNCHEON WITH CHRISTINA ROMER

SUBJECT: THE EXTRAORDINARY CHALLENGES AND POLICY ACTIONS OF THE FIRST TWENTY MONTHS OF THE OBAMA ADMINISTRATION

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ALAN BJERGA: (Sounds gavel.) Good afternoon, and welcome to the National Press Club. My name is Alan Bjerga. I'm a reporter for Bloomberg News, and President of the National Press Club. We're the world's leading professional organization for journalists and are committed to our profession's future through our programming and by fostering a free press worldwide. For more information about the Press Club, please visit our website at www.press.org. To donate to our professional development and training programs, please visit www.press.org/library.

On behalf of our members worldwide, I'd like to welcome our speaker and attendees to today's event, which includes guests of our speaker as well as working journalists. I'd also like to welcome our C-SPAN and Public Radio audiences. After the speech concludes, I will ask as many audience questions as time permits. I'd now like to introduce our head table guests.

From your right John Wordock with Market Watch. Jennifer DePaul, Reporter for the Fiscal Times, Paul Page, Journal of Commerce, Cecilia Rouse, Member of the President's Council of the Economic Advisors, and a guest of the speaker; Diana Gregg with BNA, Jason Furman, Deputy Director of the National Economic Council and a guest of the speaker. Skipping over the podium we have Andrew Schneider, Chairman of the

Speakers Committee at the National Press Club, and an Associate Editor at Kiplinger Washington Editors.

Skipping over our speaker for the moment, Deborah Silimeo, Senior Vice President with Hager Sharp, and the Speaker's Committee Member who organized today's luncheon. Austin Goolsbee, a member of the President's Council of Economic Advisors, and a guest of the speaker. Patty Giglio, President of PSG Communications, Tim Holman with Bloomberg. And finally Eric Meltzer, Producer with New Tang Dynasty Television.

Dr. Christina Romer, Chair of the President's Council of Economic Advisors, is making her first appearance as the Head of the White House In-House Think Tank at the National Press Club. At the same time she's making her last appearance as the Head of the White House In-House Think Tank.

She's leaving her post this week to return to teaching economics at the University of California at Berkeley. Her tenure at the Council is surely one for the history books. When Christina Romer came to Washington, just after Barack Obama was elected President, she arrived with a long list of credentials in studying the ups and downs of the economy.

She sat on the committee that decided when the economy was officially in or out of recession. She directed a program on monetary policy at the National Bureau of Economic Research. But what she was really known for was her expertise on the Great Depression, what worked and what didn't, in getting our country out of it.

She contributed to President Obama's proposal for the largest economic stimulus package in U.S. history. At the time Dr. Romer thought that this could keep the unemployment from going much higher than 8%. It's now 9.5. Today the economy is front and center as an issue in the mid-term elections. A new *U.S. Today* gallop poll showed that 59% of Americans do not approve of the way the President has handled the economy. And experts are starting to worry about a double dip recession.

Dr. Romer returns to Berkeley with her husband, David, who's also an economic's professor at the University. Once asked by a reporter, "What book is on her bed stand?" she confessed that she was reading, "*CBO Budget Options*." She won't be far from the action in California, however. The President has asked her to serve on his Economic Recovery Advisory Board. And just this week, he announced he will be proposing some new economic recovery efforts, which we're looking forward to hearing more about today.

So please welcome to the National Press Club, Christina Romer. [applause]

CHRISTINA ROMER: Thank you, Alan, for that kind introduction. And it is lovely to have a chance to finally speak at the national Press Club before I return to California. You know, because I am stepping down from The Council of Economic Advisors at the end of this week, today's talk is a sentimental one for me. So I brought my own audience with me. You know many members of The Council of Economic Advisors are here with me today. And my husband, David Romer, is also here with me today.

And as Alan has already described, I brought three special friends to the head table, my two colleagues from The Council of Economic Advisors, C.C. and Austin, and of course Jason Ferman, from The National Economic Council, both a great friend of the CEA and a great economist.

The first recession that I really remember is that in 1981 and 1982. Now I began graduate school just as the economy peaked. And over the next year and a half output plummeted and unemployment rose dramatically. Now that recession was personal. My father lost his job at a chemical plant in the spring of 1983, shortly after the trough of the recession. And I vividly remember the phone call when he told me that he had been sacked. He was careful to say that I shouldn't worry about my wedding, which was scheduled for that summer. There was money put aside for that.

Just before the wedding my mother learned that her teaching job was also uncertain for the next year. David and I, nevertheless, got married as planned. And the wedding was probably all the more special because my mother and her two sisters did much of it themselves.

But what I really remember is the tremendous sense of relief when I returned from my honeymoon to hear that my mother's school district had found the money to continue her position. And soon after my father found a less well paying, but very stable job. And by Christmas our family's economic health was almost fully recovered.

1981/82 was a terrible recession, but it was a recession that economists understood. Like many other post-war recessions it was started by a difficult decision by monetary policymakers to raise interest rates to bring inflation down. The suffering of ordinary families, like my own, was very real and costly. But once inflation had been reduced and the Federal Reserve lowered interest rates, construction spending, purchases of durable goods and business investment came surging back.

Unemployment which peaked at 10.8% at the end of 1982 fell to 8% by early 1984. The current recession has been fundamentally different from other post-war recessions. This is not my father's recession. Rather than being caused by deliberate monetary policy actions, it began with interest rates at low levels. It is a recession borne of regulatory failures and unsound practices that contributed to a housing bubble, and eventually a full fledged financial crisis.

Precisely what has made it so terrifying and so difficult to cure is that we have been in largely uncharted territory. An all out financial meltdown in the world's largest economy, and the center of the world financial system, is something that the world has experienced only once in the past century, in the 1930's. Thus the President took office in the midst of a recession of historic proportion, but for which history provided little guidance.

This afternoon I want to talk about the tremendous economic challenges the country faced back in January of 2009. And the challenges that we continue to face as we reach the second half of 2010. I want to discuss what I think we've learned over the past 20 months about the causes of our economic difficulties. What we've accomplished through extraordinary policy action. And the tremendous work that remains before the economy is fully recovered.

Well, according to the National Bureau of Economic Research the recession began back in December of 2007. It's now clear that the popping of the housing bubble had serious consequences. The dramatic decline in house prices, and the related drop in stock prices, destroyed \$13 trillion dollars of household wealth in 2008. Not surprisingly, the fall in house prices and the decline in wealth reduced consumer spending and investment, particularly in residential construction.

As a result, even before the collapse of Lehman Brothers in September of 2008, the U.S. economy had lost than a million and a half jobs, and GDP had fallen by more than the average in the previous two recessions. The fact is we all know the worst was yet to come. As declines in house prices accelerated, fears about the solvency of firms holding mortgage back securities set off a genuine financial panic. The collapse of Lehman sent credit spreads skyrocketing and credit availability plummeting. Had the Federal Reserve not responded as rapidly and creatively as it did, the crisis would have been catastrophic. As it was, it was as severe as anything we have experienced since the Great Depression.

Though it was clear that the strain on our financial markets was intense, what was not clear at the time was how quickly and strongly the financial crisis would affect the economy. Precisely because the severe financial shocks have been rare, there were no reliable estimates of the likely impact. To this day economists don't fully understand why firms cut production as much as they did, or why they cut labor so much more than they normally would, given the decline in output. A firm so dependent on short term finance that the temporary freezing of credit flows forces them to cut back immediately. Or did the fear engendered by a wholly unknown type of recession leave firms to hunker down in a way they hadn't previously. These are questions that economists should, and surely will be investigating over the coming years. But in any event, almost all analysts were surprised by the violent reaction.

The other thing that few anticipated was the degree to which the recession would be worldwide. I can remember early discussions of the economic's team about whether economic stability in the rest of the world might help to sure up our economy. Previous financial crises in Sweden, Japan, East Asia can have largely localized effects. It was only after the data for 4th quarter GDP for countries such as Japan, Korea and the United Kingdom started being reported in late January and February of 2009, it was clear that almost every other economy was also declining, in many cases at a more rapid pace than we were.

Now despite the fact that we were in uncharted territory, the new economics team back in December of 2008 was painfully aware that the economy was facing a terrible downturn, and that we were fast approaching the edge of a cliff. At a meeting we had with the President Elect in Chicago in mid-December I began by saying, "The economy is very weak and deteriorating fast."

The weekend before the meeting, the team had sent a memo to Rahm Emanuel echoing that sentiment, and laying the groundwork for a larger stimulus package. Whereas most analysts and congressional policymakers had been contemplating the stimulus of \$500 billion dollars or less, we urged that it grow substantially because of the severity of the downturn.

Well, just as the recession was unprecedented in post-war American history, so was the policy response. The American Recovery and Reinvestment Act was passed less than a month after the inauguration. The legislation was large, well diversified, temporary and fast acting. Now many would have liked to have seen a more iconic bill, a moon shot that concentrated spending on a single activity, such as building a nationwide smart electrical grid, or a comprehensive high speed rail network. But as happened with many decisions, pragmatism won out.

We agreed that many of the things that would improve the economy fastest were unglamorous measures such as state fiscal relief and tax cuts for working families. Because the final bill was a mixture of hundreds of measures, many of which don't come with recovery act signs or easily identifiable links to the Act, it's been hard for people to see what the act has done. But it is precisely because of works through existing programs, and spreads the funds widely, that it could get out quickly and reap large benefits.

Now despite its pragmatism, the Recovery Act reflects many of the President's top priorities for forward looking investment. It invests more than \$90 billion dollars in clean energy, and so provides a down payment on the transition towards renewable energy and greater efficiency. The aide to state and local government struggling with terrible budget difficulties is focused on health and education. And the education funds include incentives that are encouraging greater accountability, and widespread quality improvements. And the middle class families, who've gotten the short end of the stick for

the past decade, are getting tax cuts, unemployment relief and support that have helped keep food on the table and the mortgage paid as the economy slowly recovers.

Now our policies for financial stabilization were similarly pragmatic. We opted for continued system-wide support through bond guarantees and joint credit provision plans with the Federal Reserve, but not an aggressive federal takeover of troubled institutions. The stress test formed the centerpiece of the response. Implemented as scientifically as possible by the Federal Reserve and the other regulators, it was designed to give an honest accounting of the state of our largest financial institution, and to determine what further actions were needed, to ensure solvency and stability.

These unprecedented pragmatic policy actions have made an enormous difference. On the financial side, the stress test reassured investors and set off a wave of private capital raising that was exactly what the system needed. Credit [23:48] an indicator of perceived risk have returned almost to pre-crisis levels. And while credit remains tight for consumers and small businesses, lending standards have stopped tightening and are gradually starting to loosen. Large firms are able to borrow at favorable rates and get the credit that they need for investment in day-to-day operations. And the financial industry has paid back the U.S. taxpayer at a rate few thought possible.

For the real economy, the turnaround has been dramatic. Real GDP went from falling at an annual rate of nearly 6%, the end of 2008 and beginning of 2009, to growing steadily over the past four quarters. Likewise employment went from falling at a rate of 700,000 jobs per month to growing at the beginning of 2010. These swings from horrifying negatives to positive are a testament to the speed and effectiveness of the policy response.

But compared to the problems we face, the turnaround has been insufficient. So the unemployment rate has come down six-tenths of a percentage point. It is still 9.5%, an unacceptable level by any metrics. Real GDP is growing, but not fast enough to create the hundreds of thousands of jobs each month that we need to, to return employment to its pre-crisis level.

Now it's clear that the Recovery Act has played a large role in the turnaround in GDP unemployment. In a report that Jerry Bernstein and I issued during the transition, we estimated that by the end of 2010, a stimulus package like the Recovery Act would raise real GDP by 3.5%, and employment by about three and a half million jobs, relative to what otherwise would have occurred.

As the Council of Economic Advisors has documented in a series of reports to Congress, there is widespread agreement that the Act is broadly on track to meet those milestones. The non-partisan Congressional Budget Office, the CEA's own estimates, and estimates from a range of respected private analysts, suggested the Act has already

raised employment by approximately two to three million jobs, relative to what it otherwise would have been.

Now what the Act hasn't done, as Alan alluded to, is prevent unemployment from going above 8%. Something else that Jerry and I projected it would do. Well, the reason that that prediction was so far off is implicit in much of what I've been saying this afternoon. An estimate of what the economy will look like if a policy is adopted contained two components: a forecast of what would happen in the absence of a policy, and an estimate of the effect of the policy. As I've described, our estimates of the impact of the Recovery Act have proven to be quite accurate. But we like virtually every other forecaster failed to anticipate just how violent the recession would be in the absence of policy, and the degree to which the usual relationship between GDP and unemployment would break down.

Now the report was very clear that there was a great deal of uncertainty about the no-policy baseline. And noted that some private forecasters anticipated unemployment as high as 11% in the absence of action. Yet that chart we presented did not show the uncertainty, and so allowed critics to take it out of context, and falsely claim that the spike in unemployment early in 2009 is somehow evidence that the Recovery Act didn't work.

If I were doing this again I would not focus on the policy and no policy projections. Instead what I'd emphasize would be the important part of the analysis, which is the estimated impact to the Recovery Act, a part that has been broadly accepted and corroborated.

But I certainly don't regret having done the study. During the transition that little paper helped to build the case, both internally and externally, by a stimulus of unprecedented proportion. Only in retrospect saying that our best guess was that the unemployment rate would rise to 9.5% without aggressive action was rosy. At the time it was scary as hell. It helped convince both our team and Congress to go for as big a program as possible. And laying down a firm marker that the legislation had to save or create three and a half million jobs helped to prevent the package from shrinking greatly during congressional negotiations.

More generally, I will never regret trying to put analysis and quantitative estimates behind our policy recommendation. Macro economic policymaking is incredibly hard. If policymakers, scholars and private analysts can't discuss design issues, impact estimates and baseline forecasts, I can't imagine how we will ever manage to get policy remotely close to right. We need more numbers, more policy papers, more competing analysis, not fewer.

The thing that I do regret is that there is still so much unfinished business. I would give anything if the unemployment rate really were down to 8% or lower. The American

people are suffering terribly. Policymakers need to find the will to take the steps needed to finish the job and return the American economy to full health. And no one should be blocking essential actions for partisan reasons.

But the economy remains as trouble as it is despite aggressive action, reflects the fact that this has not been a normal recession. Just as the downturn was uncharted territory, so is its recovery. Because the recession began with interest rates at low levels, we can't just have interest rates fall and housing investment and other interest sensitive sectors, come roaring back as they typically do in recoveries. Now they're because of over-building and housing and commercial real estate during the bubble, construction is likely to remain subdued for some time.

Indeed the economy faces numerous headwinds not normally present in recovery. In addition to the over-supply of housing, households have been through a searing crisis that's likely to make them more prudent for years to come. In much the same way that the Great Depression gave rise to a generation of high savers and cautious investors.

Likewise, the decline in wealth is likely to lead to increased savings, replenish retirement accounts and payoff debt. But saving [1:35] are healthy for the economy in the long run. But in the near term they mean that consumer spending will likely be less robust than before the crisis.

State and local governments have also been hit particularly hard by this recession. The tax revenues are notoriously cyclically sensitive. And the decline in house prices has further impacted property tax revenue. State and local budget cutting, reduced GDP over the past year, and it's likely to continue to be a drag on GDP going forward. And while the private sector has added jobs every month so far this year, state and local governments have reduced employment by 169,000 since last September

Now the administration understood that the recovery would be difficult, precisely because many of the usual drivers of growth were missing. That's why we included \$266 billion dollars of additional temporary recovery measures in our 2011 budget. Congress has taken some important steps, including extending unemployment insurance, allocating funds to prevent teacher layoffs, and passing the higher tax credit to encourage firms to hire unemployed workers. However, it has enacted substantially less than what the administration proposed. As a result the economy has not had all of the additional support that it needed.

Early in the spring there was hope that new drivers of growth, particularly investment and exports, would substantially compensate for some of the headwinds. Business investments in equipment and software rose at an annual rate of more than 20% in the first two quarters of 2010, and exports grew rapidly. Unfortunately, both those sources of demand have taken a hit in recent months. The recent Greek debt crisis and

anemic growth in much of Europe, contributed to a decline in both stock prices and confidence, and to a rise in the value of the dollar.

The latest data on durable good shipments suggest that equipment investment is only growing modestly in the third quarter. And last Friday's GDP revision for the second quarter, indicates that our exports are growing substantially less rapidly than our imports.

The results of these powerful headwinds and recent developments is that the United States still faces a substantial shortfall in aggregate demand. GDP, by most estimates, is still about 6% below trend. This shortfall in demand, rather than structural changes in the composition of our output, and a mismatch between worker skills and jobs, is the fundamental cause of our continued high unemployment. Firms aren't producing and hiring at normal levels simply because there isn't demand for a normal level of output.

Now in the long run the transition to a higher saving, higher investment, higher export economy can restore demand, and hence output and employment to normal. But at the moment, as the recent data emphasizes, that process is operating painfully slowly. The pressing question that is what can be done to increase demand, and to bring unemployment down more quickly. Failing to do so would cause millions of workers to suffer unnecessarily. And it also runs the risk of making high unemployment permanent as workers' skills deteriorate with lack of use, and their labor force attachment weakens as hope of another job fades.

Now policymakers should certainly try innovative, low cost policy. The President's National Export Initiative is an excellent example. Given the fixed costs associated with exporting the new market, small investments in information provision and commercial diplomacy can bring about a substantial increase in our exports. Likewise responsible new trade agreements can help open markets and increase trade in the short run and over time.

Policymakers should also take sensible actions to increase confidence. While some in the business community talk about regulatory uncertainty as one reason that they're cautious about hiring and investing, I suspect that uncertainty about future sales is a much larger determinant of the firm's action. We can, however, do more to highlight and codify our pragmatic approach to regulation. As [6:06] administrator has detailed in his recent congressional testimony, the estimated net benefit, that is the benefit minus the cost of the Obama's administration regulatory actions during its first year, far surpass those of the first years of the previous two administrations. For the health of the economy we should, and continue and should trumpet this prudent regulatory approach.

Now what we would all love to find the inexpensive magic bullet to our economic troubles, the truth is it almost surely doesn't exist. The only sure fire ways for

policymakers to substantially increase aggregate demand in the short run, or for the government to spend more and tax less, in my view, we should be moving forward on both fronts. The measures should be carefully chosen so that they have the highest bang for the buck possible. The state fiscal relief, to prevent teacher layoffs that just passed is an excellent measure. The Small Business Tax Cut and Lending Bill is also likely to have excellent job creation effects, and should be passed.

As the President said in his Rose Garden remarks on Monday, there are a range of other sensible measures that deserve consideration. Such as tax cuts for struggling middle class families and businesses willing to invest in the United States. And much needed additional investments and infrastructure. The key is that we need to take action and we need to do it quickly. Given our long run fiscal challenges, any additional support should be done in a responsible way. It makes sense to [7:45] some temporary support as an emergency measure. Most actions, however, should be paid for over time with future spending cuts, or appropriate future revenues.

But concern about the deficit cannot be an excuse for leaving unemployed workers to suffer. We have tools that would bring unemployment down without [8:07] our long run fiscal outlook. If we could only find the will and the wisdom to use them.

On election night, almost two years ago, my husband and I did a most uncharacteristic of things. We had friends over to watch the returns and had celebrated the Obama victory with a sedate glass of champagne around 8 o'clock California time. By 8:30 our friends had gone home, and we were left wondering what to do with our joy. I finally declared that I needed to be part of a crowd. So we hopped in the car and followed the sounds of honking horns into downtown Oakland. We stopped at the first street corner where people were gathering. And there we were two middle aged economists dancing in the streets with an Oakland teenager.

Like so many that evening we were celebrating the promise of a new President who shared our values and our dreams for a better America. What we didn't realize that November evening was just how large an economic nightmare lay before the new President and the American people. It would require actions few would have contemplated that evening just to keep the unemployment rate from rising beyond low double digits.

It has been an honor beyond any I could have imagined to be part of the team that President Obama selected to help diagnose the situation, and craft the policy response. I am proud of the recovery actions we have taken. I believe they have made the difference between a second grade Depression, and a slow but genuine recovery. And the passage of healthcare reform and financial regulatory reform, our accomplishments that will be with us long after the recession is over. They will ensure that our children inherit the future in which families can afford the healthcare they need, and where workers and firms never again have to face the specter of a cataclysmic economic meltdown.

But I desperately hope that policymakers on both sides of the aisle will find a way to finish the job of economic recovery. We have already navigated through miles of difficult, uncharted waters. Surely we can go the rest of the way. The American people deserve nothing less. Thank you. [applause]

ALAN BJERGA: And thank you very much for speaking to us today. And thank you for having time to answer questions from our audience. Please keep questions coming up. I know we have several good ones already in the queue.

Just starting out, in your address you talked about an immediate need to spend more and tax less to continue to work toward an economic revival. And that of course being mindful of that later on, because you are exacerbating the deficit. That at some point there needs to be a responsible way to cut spending and pair that down. What would be the signal that the U.S. economy is at that point where you can transition from one strategy towards another? How will we know when we're out of the woods?

CHRISTINA ROMER: An excellent question. I think the obvious thing is to say we know that we need to do more now. So certainly looking at the unemployment rate of 9.5%, it is clear that additional action is needed. And as I described, doing it in a fiscally responsible way is incredibly important.

You know, how do you know when you can make the transition? I think what the President's often described as, we need to be working on both the problem of the deficit, and the fact that we need to get the unemployment rate down together. That's why he set up the bipartisan fiscal commission, to be talking about the long run and medium run fiscal situation, at the same time that we're of course thinking about what can you do in the short run.

What I also suggested is, even as you're thinking about short run policies, you can be mindful of the long run deficit. And think about pay for it either in terms of lower future spending or additional future revenues, as you're crafting the measure today. So I think that is, in many cases, the best policy for them.

ALAN BJERGA: What are the odds of the U.S. slipping into a double dip recession?

CHRISTINA ROMER: If my colleague, Larry Somers, he would know exactly the numbers to the decimal point. The important thing is to say I think they are very small. I think that the American economy, we're clearly going through a rough spot that I think as I described, in the spring it looked as though we were really starting to grow more strongly. The troubles in Europe definitely I think caused some turbulence, especially took a hit on confidence and on stock prices and things like that.

My prediction is we come through this period of turbulence and go back to steady growth again. I think the important thing is even that scenario, or even the scenario before we hit this period of turbulence, wasn't good enough. We know that often coming out of a recession this bad, you'd have GDP growth of four, six even eight percent. And so to have a forecast where you're growing at normal, or a little bit above normal, that's dramatically better than having GDP fall at a rate of almost 7%. But it's not good enough to bring the unemployment rate down quickly.

ALAN BJERGA: You made reference to the European debt crisis. And we have a question on that topic. How concerned should the U.S. be about a resurgent sovereign debt crisis in the [13:49]? What can or should the U.S. do to prevent the debt problems of Greece, Spain or other European economies from threatening the global recovery?

CHRISTINA ROMER: Well, certainly I think we've been very encouraged by the actions that the Europeans have taken to deal with the situation in Greece. Certainly their stress test was something that I think was very helpful in getting the read on the state of their financial system, and was reassuring to market. I think the most important thing that you know all the countries of the world should do is to be thinking about a balanced program of both what do we need to do to get people back to work now? And what do we need to do to be thinking about making sure our long run fiscal house is in order.

And I think the really important thing is to again emphasize that those two things do not have to be in conflict over a period of time. That a sensible economic policy can match more expansion now with credible measures to get the deficit down as you go forward. And one of the things I think again that we often lose sight of is how important growth is, not just for people, not just for dealing with what is obviously a terrible unemployment problem, but for dealing with the deficit. It obviously helps tremendously in the short run because tax revenues are down. But it even matters in the long run. Because as I alluded to in my talk, one of the things you worry about when the unemployment rate is at 9.5% for a long period of time, when the long term unemployment rate is as high as it is, what you worry about is that workers start to lose skills, that they start to drop out of the labor force. And that some of that unemployment becomes permanent. And that is obviously terrible for the people involved, but it's terrible for your long run deficit, because those are people that aren't going to be paying taxes as we go forward. If all you care about is the deficit, I think dealing with the short run economic problem is also incredibly sensible and good economic policy.

ALAN BJERGA: Because there will inevitably that tradition towards withdrawing a certain amount of stimulus from the economy, and going into more of a budget cost cutting environment in terms of getting the deficit down, is the U.S. committing itself to a long term path of slower economic growth than what might normally happen in the recovery from a recession?

CHRISTINA ROMER: I think the most important thing is, we don't do that. You know, as an economic historian, one of the things that I started talking about at least a year ago was thinking back to the Great Depression and what happened in 1937. That if you remember your Depression history from 1929 to 1933 the economy declined dramatically. Then it started to grow again with the New Deal and action on the monetary side. But one of the things that happened in effect grew strongly, almost an average of 10% in those years from '33, '34 and after.

One of the things that happened in 1937 is there was a little bit of a collective sigh of relief. The economy was growing again. It certainly wasn't fully recovered. The unemployment rate was still quite high. But there was a tendency for the Federal Reserve to say oh good, we can draw back on our actions. There was the fiscal side passed tax increase started to get its fiscal house in order. And the lesson was the recession of 1938 where unemployment shot up again. We had a big setback. And part of the reason why the 1930's is as bad as it is, is that recovery was cut short by I think very natural policy actions. We can see where they come from, right. We're living through them now. We've lived through extraordinary actions. We had to take actions nobody ever would have thought, or wanted to take. They were the appropriate thing for the economy. And there is a tendency to say, as soon as possible let's stop that. And I think it's important to say, let's get this recovery much more firmly established, much closer to all the way done before you then start to pull back.

Because I think what you mentioned, the biggest risk to our long term growth is not that we've been through the crisis. I think that is not had a permanent affect on our productivity or anything like that. But if we make policy mistakes going forward, if we leave the unemployment rate very high for a very long period of time. I think that's where you run the biggest risk of causing a permanent scaring to the economy, and obviously to people.

ALAN BJERGA: And looking at your historical example, I think even after the '38 recession, there was a bit of a recovery, but unemployment was still in the double digits when World War II began. And that leads to the next question that we have here, is about the structural rate of unemployment. In the 1990's the natural rate of unemployment was believed to be about 4%, more that you hear about 6%. As you see the changes in the economy, economically in terms of economic model that the U.S. is following in terms of skills in the job market, in terms of structural changes in employment trend, is the natural rate of unemployment inching upward? And what would be expected in the future?

CHRISTINA ROMER: Obviously an incredibly important question. What I was trying to argue in my talk is I think we're not seeing that yet. That the rise in unemployment that we're living with, the 9.5% unemployment that we have is almost entirely a cyclical phenomenon. It is a reflection of the fact that GDP is dramatically

below trend. That we don't yet have demand back to where it needs to get. And I think that is the overwhelming source of the unemployment that we have.

But certainly there has been a lot of discussion about some sectoral changes in the economy, the fact that finance and construction may well be a smaller part of the economy going forward. And obviously other things are going to need to grow to fill that space. One of the things to realize, those kind of sectoral changes are happening all the time. Likewise, there's a lot of talk—you know the sectoral decline in manufacturing, something that's been going on in several decades. That's something that—we had that going on when the natural rate of unemployment was 4%. So I think those kind of sectoral changes I think the evidence that they're driving anything of what we're seeing now I think is very weak, just simply because those are a pretty common phenomenon.

Likewise, even the high rate of long term unemployment, at some level that is simply a consequence of the fact this has been a terrible recession that has gone on for a long time. And if you lose your job really in this recession, we haven't been creating a lot of jobs, so you naturally tend to eventually become long-term unemployed. But even that, I would expect, as the economy recovers as the overall unemployment rate comes down, you'd expect that rate to come down as well.

ALAN BJERGA: You discussed some permanent sectors of the economy that may be smaller in the long term. You were talking to that. Two that you cited were finance and construction. Is it a good thing that the financial industry may be a little bit smaller? They did a heck of a job with those collateral obligations and the sub-prime loans.

CHRISTINA ROMER: That probably is my least politic statement ever. I was at a speech in New York where I said something about, "And it will be a good thing if all of those people that went into finance do something useful, like medicine or science." It did not go over well with that audience.

I think it is certainly—The perspective that I bring to this is that market economies are wonderful dynamic things. And that one of the great strengths is that as new opportunities come up, as certain doors close, other doors open. And I think that's an important part of the process. And if some things are going to be smaller for awhile, like construction because we've had—as my colleague Austin [42:21] talks about a lot, we have a big over-supply of housing, some over-building now. What's going to be important is that other things fill that gap. And especially fill that gap for the kind of workers that were in that sector. And so I think that's something, certainly I know is very high on the President's list of concerns. And something that we are certainly thinking about.

ALAN BJERGA: How many people do you know who are unemployed or under-employed? And what have you learned from their experiences?

CHRISTINA ROMER: I think that is—I often talk about when we would go back to California periodically, and you think you’re having the innocent walk out to the mailbox, and there’s your neighbor who you’ve known for years who comes out and says, “My daughter’s unemployed. My son-in-law is about to lose his house. Why aren’t you doing more?” So no, absolutely, you can’t go anywhere and not know that there are many people who are struggling incredibly.

You know earlier this spring one of the nicest things that I’ve done was a two day road trip to Ohio where Julie and Nan and I visit a Ford Motor factory where we met with the union representatives, where we looked at my old hometown in Canton, Ohio. What was really striking, especially in talking to the workers, they were looking at this Ford plant where half of it was a gleaming new factory that had just come in, and they were so thrilled about that. And then they kept pointing to the other half that was empty. And they kept saying, “Can’t you get us another auto assembly, something to go in that, because my brother-in-law is unemployed.” Or, “There are 3,000 of us working at this plant now; there used to be 13,000 of us at this plant.”

So I think everyone of those interactions is the reason why I wake up every day, like the President wakes up every day and says, “For heaven sakes can’t we be doing more to get this rate down?”

ALAN BJERGA: Following on your manufacturing examples, this questioner asks, “How can we work to revive American manufacturing? Are there incentives that might be effective?”

CHRISTINA ROMER: I think it’s an incredibly important question. And as Jason and CC and Austin will tell you, it is again one that the President and the Vice President are so incredibly concerned with. So I think the right thing is a mixture of policies. Probably the number one thing you could do to help manufacturing is the same thing you do to help services and everything else, which is to get the overall economy going. So the general recovery measures, one of the things that does is to affect the whole economy. Because manufacturing is inherently more cyclically sensitive. Anything you do to get the overall economy going disproportionately helps manufacturing.

But you know what the President has been trying to saying is also, you know, we do know that things like getting our exports going. One of the main things that we’re good at is high tech manufacturing. So if we can do things that make it easier for those firms to export, that can be something that would certainly help them. But also, you know, he’s identified one of the areas where there might be a market failure. We can see the future coming, which is we need to get cleaner energy. We need to be more energy efficient. And so one of the things that he’s identified, and we started it in the Recovery Act, is can we do more to help the economy make that transition?

If the market system isn't doing enough to realize that that's what the future is going to hold, can we do some targeted investments? Can we do tax incentives for renewable energy? There was, as I mentioned, about \$90 billion dollars of that in the Recovery Act, including some tax incentives particularly for clean energy manufacturing. And that's been one of the biggest success stories I think for the Recovery Act. And something again, when we're talking about additional measures, something that the President has emphasized, you know that program was sold out very quickly. You know, if we got some more money for that, we've got the applications there, there'd be good work that could be done that would help to rebuild manufacturing and help us become more energy efficient going forward.

ALAN BJERGA: How should Congress approach the question of renewing the Bush tax cuts? Should they all be extended temporarily? Or should some of them not be renewed?

CHRISTINA ROMER: As the President made very clear on Monday, the important thing is to renew those tax cuts for the people earning less than \$250,000 dollars. We certainly believe strongly that middle class folks have had a tough time. They need this money for them and for the economy. But what the President and the economics team has said consistently is, the high income tax cuts, we're talking about \$34 billion dollars in 2011. That is money that we should not spend, especially because one of the things we worry about is if you renew them once, the chance that they become permanent becomes much higher. And over a ten year period it may be only \$34 billion dollars in one year, it's about \$750 billion dollars over a ten year period. That is fiscally irresponsible measure that we just simply can't afford.

The other thing that I feel very strongly, you know tax cuts can absolutely be an important recovery tool. That's why we had the Making Work Pay Tax Credit in the Recovery Act. That's why there were some \$300 billion dollars of tax cuts in the Recovery Act. But all of the economic literature says tax cuts for very high income earners don't do nearly as much as ordinary tax cuts. And so even on stimulus grounds, I think it's a pretty bad bargain. You want to spend \$34 billion dollars, I guarantee you, I can find some much better ways that will create a lot more jobs.

ALAN BJERGA: Last night President Obama announced the formal end of U.S. combat operations in Iraq. What benefits do you see to the U.S. economy as the war winds down?

CHRISTINA ROMER: One of the things that just always strikes me—One of the things about this job is as an economist there's an area that you know a lot. And then when you become CEA Chair you suddenly discover there are all of these other areas that you need to know just about the economy. And every once in awhile then I look at the President and say, he has to know everything I know, and then this whole other realm of

things. And that's certainly what, every time we have a major foreign policy movement, realize just how complicated his job is.

But certainly for the overall economy, obviously one of the things that as combat winds down in Iraq, the President has said, you know, he sort of moved that towards, we need to be focusing on our own economy. And certainly there's a budget cost that's been associated with the war that then can be usefully be put to work here, or helped to bring down the deficit and the debt. But also I think just in general to give us the opportunity and the resources to be focusing on everything possible that we can do to be creating jobs. And that is certainly his focus. It's been his focus since the day he took office. And as he announced in the Rose Garden, it is a tremendously his focus as we go into the fall. Because it's obvious that we need to do as much as possible to bring this unemployment rate down.

ALAN BJERGA: A couple of questions about consumers, companies and cash. First question, how do you get companies who are now sitting on so much cash to invest more of it?

CHRISTINA ROMER: Alright, so I think there are a couple of things. This is actually a topic that the Council of Economic Advisors looked into some. We do know that firms are holding a lot of cash. One of the things that I think was helpful for us to get some historical perspective, to see that that's a not unnatural thing as you come out of recoveries, or as you come out of recessions. There's a strong cyclical component to cash holdings. And it goes back a little bit I think also to what I said about consumers, right?

Consumers have been through an incredibly searing, frightening two years. And the same has been true of firms. And I think a big part of why firms are sitting on the sideline is just simply they've been through a searing crisis like the rest of us. So I think the main thing you do to give firms the confidence to invest is again, it's like the answer to manufacturing, it's the answer to almost everything, is get the overall economy going. And that's going to be the main thing that makes a firm want to build a new factory is that they see customers out there.

And so you know what you might think of as not an investment related policy, like a tax cut for consumers, well that can be very important for investment because it gives firms more certainty about their sales, about the overall economy. But it is also true, I mean, one of the things we've tried to do in the Recovery Act is to give firms particular tax incentives to invest. I'll put in a plug for the Small Business Jobs Lending and Tax Cuts, because that bill has been sitting in Congress. One of the things it does is a big chunk of bonus depreciation for firms, something that gives them a very strong financial incentive to do more investment, to take some of the cash and put it into buying durable goods, putting it in to putting people to work.

ALAN BJERGA: And on consumer cash. Is there any danger that the American consumer could go too far the other way and actually be saving too much?

CHRISTINA ROMER: One of the things that—I'll put in a plug now for the Economic Report of the President—Because every February we put out a comprehensive volume, which again my colleagues will tell you is a very big job. But one of the things that we did in that was to talk about again, not the immediate period, but as we go forward, what do we expect for the American economy?

And one of the things I think, you know, the President has been very strong in emphasizing is, we don't want to just go back to where we were, right? That we know before this crisis came—I always find it helpful to remember the President was running for President on economic issues before there was a recession, before there was Lehman Brothers, precisely for things like we weren't investing enough as an economy. That we were living in a bubble and bust consumers saving almost nothing. And we've seen some of the consequences of that kind of unbalanced growth.

And so certainly what our estimates, when we started thinking about what's the world going to look like when we come through this recession, what we anticipate is consumers to be saving more. We anticipate that how we're going to fill that gap. We're going to expect firms are going to need to be investing more. They're going to need to be exporting more. That's part of why we've had such an emphasis on investment and export.

Right now the reason this long digression is in that economic front, we did some empirical estimates of what do we think consumers are likely to do given the state of the economy, given what's happened to their wealth, given to their expectations. And the current savings numbers are dead on. That very much they're following our predictions. And what I would say is as we come back to normal, probably the saving rate will be in kind of the 4-7%, rather in kind of the 0-2% that it was before. I think fundamentally that's healthy for the economy. I think what we'd all like obviously is for consumers to be a little more robust now to help us get people back to work. But certainly them coming back to that very sensible place, I think will ultimately be good for the economy.

ALAN BJERGA: We have several questions about your upcoming life and your future role teaching at Berkeley. And how your experiences in Washington will be informing your contributions here on out. The first question. How is your experience on the Council of Economic Advisors informed your plan syllabi as you return to academia? That's the first one.

Second one, your husband who's also an economics professor, is known to offer his students Chicken Soup for Economist: Advice for Living. As you prepare to leave Washington, can you offer chicken soup for all of your colleagues, some of them are at this table, who will still be working to turn the economy around?

CHRISTINA ROMER: Alright, let me start with what I've changed about my syllabi. Let's be clear, I've changed the whole course. So in fact, in the spring of next year I'm going to be teaching a course on macro economic policy from the Great Depression through the Great Recession. And I think that will be—The whole thing is to take what I've learned, what I think economists in general have learned from the crisis that we've been through, to show sort of what's worked, what hasn't worked, what questions still remain. So I think that's going to be hugely important.

On the chicken soup, I'm not sure—I mean, David is much better than I am at giving wisdom. I will tell you what I say to anyone I'm thinking of bringing to the Council of Economic Advisors, because it has been—As I've said, it's been an honor above anything I could have imagined. But it's also been for me, it's been very important. And I often describe it as sometimes you hit 51 and you're not sure you can still learn again, right? So as an economist you tend to get narrower and narrower. And I got very good at one kind of research. And what was very helpful is to be brought into the Council of Economic Advisors and said, "I don't care if you're a macro economist, healthcare is the issue, learn it." And it has actually been incredibly liberating to find that those skills that you learned in graduate school come back to you. You can throw yourself into an other area. And so I think that is certainly for every policymaker I think, to be open to that ability to learn and to embrace it. It can be terrifying at times, but I think important to realize that it is what makes the job both so important and so incredibly rewarding, is that it is a chance to learn about so much that we need to know about.

ALAN BJERGA: We're almost out of time. But before asking the last important questions, we have a couple of important matters to take care of. First, to remind our members and guests of future speakers. On September 13th we'll have the Rev. David Beckman, the President of Bread for the World, and this year's Laureate of the World Food Prize, will discuss Eliminating Hunger: the People and Congress. On September 30th Senator John Cornyn, Chair of the National Republican Senatorial Committee, and Senator Robert Menendez of the Democratic Senatorial Campaign Committee will disagree on things. And October 12th General Norton Schwartz, the Chief of Staff of the U.S. Air Force will be talking about challenges dealing with that service branch today.

Second, we'd like to present our guest with what will soon be the most coveted item in Berkeley, the traditional National Press Club mug. [applause]

And thank you again for spending time with us today. Our final question comes from an anonymous questioner from the audience who may wish to stay anonymous after this question is asked, or maybe not. Dr. Romer, you seem like you'd be a lot of fun at parties. Are you? What is the party persona of Christina Romer? And will it change now that you're getting out of here?

CHRISTINA ROMER: I don't know, this morning Jason Ferman said, "And are you and David going to reenact dancing in the streets?" So, you'll have to just take it for granted, take it on my word that we can be the life of the party. And certainly I'll have a lot more sleep once I'm out of this job, so I won't fall asleep at parties nearly as much.

ALAN BJERGA: Thank you once again. [applause]

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