NATIONAL PRESS CLUB LUNCHEON WITH CHAIRMAN BEN BERNANKE

SUBJECT: THE BURGEONING ECONOMIC RECOVERY

MODERATOR: MARK HAMRICK, PRESIDENT, NATIONAL PRESS CLUB

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MARK HAMRICK: (Sounds gavel.) Good afternoon, and welcome to the National Press Club. I'm Mark Hamrick and I cover business and economics news for the Associated Press, and I'm President of the National Press Club. We are the world's leading professional organization for journalists and we are committed to our profession's future through our programming and by fostering a free press worldwide. For more information about the National Press Club, please visit our website at www.press.org. You can also find information about how to donate to our library.

For all of our members worldwide, I'd like to welcome our special speaker and all those attending the 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. And you can follow the conversation on today's luncheon on Twitter with the hashtag NPClunch. After the speech concludes, I'll ask as many audience questions as time permits. And I'd now like to introduce our head table guests from your right.

We begin with Keith Epstein. He is managing editor for the Center for Public Integrity, recently merged with the Huffington Post investigative fund; Scott Spoerry, he's a senior producer with CNN; Rick Dunham, one of our former presidents here, Washington bureau chief with the *Houston Chronicle*; Donna Leinwand, reporter for *USA Today* and also a former NPC president; Timothy Ahmann is the Washington economics editor for Reuters; and Michelle Smith, assistant to the Chairman with the Federal Reserve.

Melissa Charbonneau, over the podium, with Newshook Media and chairman of the Speakers Committee. We'll skip over the speaker for a moment. Bob Carden with Carden Communications, and he's the Speakers Committee member who organized today's event, thank you Bob; Dave Skidmore, public affairs with the Federal Reserve Broad; Alison Fitzgerald, a reporter and she is with Bloomberg. She's also Vice Chair of the NPC Speakers Committee; Darren Gersh, bureau chief, "Nightly Business Report"; and Steve Beckner, senior correspondent with Market News International. That's our head table, and you can give some applause now. (Applause)

It has been quite a journey for our guest speaker today. The middle class son of a pharmacist and schoolteacher, he has been an economics professor, the head of the Council of Economic Advisors under President Bush, and now our nation's chief central banker. He became Chair in 2006 just in time for the great recession. He was later re-nominated by President Obama to serve another four-year term as Chairman. And reflecting his stewardship in the face of crisis, he was named *Time* magazine's Man of the Year in 2009.

But this journey started well south of Washington, D.C. If you've ever driven south on I95, you can't help but notice the colorful billboards and screaming letters as you approach the border been North and South Carolina, hawking an unusual sprawling roadside enterprise known as South of the Border. That's where our guest waited tables after graduating from high school in Dillon, South Carolina. He got his bachelor's in economics from Harvard and a Ph.D. from MIT. He taught at Princeton and Stanford, as well as NYU and MIT.

Along the way, Chairman Bernanke became an expert on the causes of the Great Depression, and that expertise was key in responding to the 2008 economic meltdown. Mr. Bernanke's willingness to creatively use the power of the Fed to intervene in the financial markets is credited by many with keeping the great recession from becoming the great depression. Those measures have been controversial. Texas Congressman Ron Paul has reintroduced legislation that would require a full audit of the Fed. And his son, Rand, the newly elected Senator from Kentucky is joining in, and this legislation is seen as a challenge to the Fed's goal and its tradition of political independence.

Some conservative economists, and even some of his fellow governors, think that Mr. Bernanke's efforts may have gone too far, including the decision to inject another $600 billion into the economy to foster the recovery. At issue is whether the Fed is courting inflation as it responds to persistently high unemployment. Just today, the European Central Bank expressed the view that longer-term price pressures remain contained despite rising energy and commodities costs. President Jean Claude Trichet repeated the very close monitoring of inflation is warranted.

I am particularly grateful that Chairman Bernanke agreed to be our first luncheon series speaker of my National Press Club presidential term. Please give a warm National Press Club welcome to Chairman Ben Bernanke. (Applause)

BEN BERNANKE: Thank you. Thanks, and good afternoon. I'm very pleased to have the chance to be here at the National Press Club, and I'm especially glad to have a conversation with journalists who write about economic policy from our nation's capital. Your job's not easy, but it is essential. Virtually every American is affected by developments in economics and economic policy. But contemporary economic issues are highly complex and few non-specialists have the time or the background to master these issues on their own. The public has to rely on diligent reporting, clear thinking and lucid writing of reporters determined to go beyond dueling bumper stickers and sound bites to help people understand what they need to know to make good decisions, both in their personal finances and at the polls. These are weighty responsibilities and the journalists that I know take them very, very seriously. So, thank you for what you do.

Today, I'm going to provide a brief update on the economy and how I expect it to evolve in the near term. And then I'll turn to some implications for monetary policy. And finally, I'd like to briefly discuss some of the daunting fiscal challenges that we face as a nation.

The economic recovery that begin in the middle of 2009 appears to have strengthened in recent months, although to date growth has not been fast enough to bring about significant improvement in the labor market. The early phase of the recovery in the second half of 2009 and in early 2010 was largely attributable to the stabilization of the financial system, the effects of expansionary monetary and fiscal policies, and a strong boost to production from businesses rebuilding their depleted inventories. But economic growth significantly last spring as the impetus for inventory building and fiscal stimulus diminished, and as Europe's debt problems roiled global financial markets.

More recently, however, we've seen increased evidence that a self-sustaining recovery in consumer and business spending may be taking hold. Notably, we learned last week that households increased their spending in the fourth quarter in real terms at an annual rate of more than four percent. Although a significant portion of this pickup reflected strong sales of motor vehicles, the recent gains in consumer spending looked to have been reasonably broad-based. Business investment in new equipment and software also grew robustly over most of last year as firms replaced aging equipment and as the demand for their products and services expanded.

In contrast, in the housing sector, the overhang of vacant and foreclosed homes continues to weighs heavily on both home prices and residential construction. Overall, however, improving household and business confidence, accommodative monetary policy and more supportive financial conditions including an apparent increase in the willingness of banks to make loans seems likely to lead to a more rapid pace of economic recovery in 2011 than we saw last year.

While indicators of spending and production have, on balance, been encouraging, the job market has improved only slowly. Following the loss of about 8 ½ million jobs in 2008 and 2009, private sector employment showed gains in 2010. However, these gains were barely sufficient to accommodate the inflow of recent graduates and other new entrants to the labor force, and therefore not enough to significantly reduce the overall unemployment rate. Recent data do provide some grounds for optimism on the employment front. For example, initial claims for unemployment insurance have generally been trending down, and indicators of job openings and firms' hiring plans have improved. Even so, with output growth likely to be moderate for a while, and with employers reportedly still reluctant to add to their payrolls, it will be several years before the unemployment rate has returned to a more normal level. Until we see a sustained period of stronger job creation, we cannot consider the recovery to be truly established.

On the inflation front, we have recently seen significantly increases in some highly visible prices, notably gasoline. And these prices of many commodities have risen lately largely as a result of the very strong demand from fast growing emerging market economies coupled, in some cases, with constraints on supply. Nevertheless, overall inflation remains quite low. Over the 12 months ending in December, prices for all the goods and services purchased by households increased by only 1.2 percent, down from 2.4 percent over the prior 12 months. To assess underlying trends in inflation, economists also follow several alternative measures of inflation.

One such measure is core inflation, which excludes the more volatile food and energy components, and therefore can be a better predictor of where overall inflation is headed. Core inflation was only 0.7 percent in 2010, compared with around 2 ½ percent in 2007, the year before the recession began.

Wage growth has slowed as well, with average hourly earnings increasing only 1.8 percent last year. These downward trends in wage and price inflation are not surprising given the substantial slack in the economy. In sum, although economic growth will probably increase this year, we expect the unemployment rate to remain stubbornly above, and inflation to remain persistently below, the levels that Federal Reserve policymakers have judged to be consistent over the longer term with our mandate from the Congress to foster maximum employment and price stability. Under such conditions, the Federal Reserve would typically ease monetary policy by reducing the target for its short-term policy interest rate, the federal funds rate. However, the target range for the funds rate has been near zero since December 2008, and the Federal Reserve has indicated that economic conditions are likely to warrant an exceptionally low target rate for an extended period.

As a result, for the past two years we've been using alternative tools to provide monetary accommodation. In particular, over the past two years, the Federal Reserve has further eased monetary conditions by purchasing longer-term securities on the open market. From December 2008 to March 2010, we purchased almost $1.7 trillion in longer-term Treasury, agency and agency mortgage-backed securities. In August 2010, we began investing the proceeds from all securities that were matured or redeemed into longer-term Treasury securities so as to keep the size of our security holdings roughly constant.

Around the same time, we began to signal to financial markets that we were considering providing additional monetary policy accommodation by considering further asset purchases. In early November, we announced a plan to purchase an additional $600 billion in longer-term Treasury securities by the middle of this year. All these purchases are settled through the banking system with the result that depository institutions now hold a very high level of reserve balances with the Federal Reserve.

Although large scale purchases of longer-term securities are a different monetary policy tool than the more familiar approach of targeting the federal funds rate, the two types of policies affect the economy in similar ways. Conventional monetary policy works by lowering market expectations for the future path of short-term interest rates, which in turn reduces the current level of longer-term interest rates and contributes to an easing in broader financial conditions. These changes, by reducing borrowing costs and raising asset prices, bolster household and business spending and thus increase economic activity.

By comparison, the Federal Reserve's purchases of longer-term securities have not affected very short-term interest rates which remain close to zero. But instead, put downward pressure directly on longer-term interest rates. By easing conditions in credit and financial markets, these actions encourage spending by households and businesses to essentially the same channels as conventional monetary policy, thereby strengthening the economic recovery.

A wide range of market indicators supports the view that the Federal Reserve security purchases have been effective at easing financial conditions. For example, since August when we announced our policy of reinvesting maturing securities, and signaled that we were considering more purchases, equity prices have risen significantly, volatility in the equity market has fallen, corporate bond spreads have narrowed, and inflation compensation is measured in the market for inflation index securities, has risen from low to more normal levels. Yields on five to ten year Treasury securities initially declined markedly as markets priced in perspective Fed purchases. These yields subsequently rose as investors became more optimistic about economic growth and as traders scaled back their expectations of future securities purchases.

All of these developments are what one would expect to see when monetary policy becomes more accommodative, whether through conventional or less conventional means. Interestingly, these developments are also remarkably similar to those that occurred during the earlier episode of policy easing, notably in the months following our March 2009 announcement of significant expansion of securities purchases. The fact that financial markets responded in very similar ways to each of these policy actions lends credence to the view that these actions had the expected effects on financial markets and are thereby providing significant support to job creation and the economy.

My colleagues and I have said that we will review the asset purchase program regularly in light of incoming information and will adjust it as needed to promote maximum employment and stable prices. In particular, it bears emphasizing that we have the necessary tools to smoothly and effectively exist from the asset purchase program at the appropriate time.

In particular, our ability to pay interest on reserve balances held at Federal Reserve banks will allow us to put upward pressure on short-term market interest rates, and thus to tighten monetary policy when required, even if bank reserves remain high. Moreover, we have developed additional tools that will allow us to drain or immobilize bank reserves as required to facilitate the smooth withdrawal of policy accommodation when conditions warrant. And, of course, if needed we could also tighten policy by redeeming or selling the securities that we owe.

Let me turn to fiscal policy. Fiscal policymakers also face significant challenges. The federal budget deficit has expanded to an average of more than nine percent of gross domestic product over the last two years, up from an average of about two percent of GDP during the three years prior to the recession. The extraordinarily wide deficit largely reflects the weakness of the economy along with actions that the administration and the Congress took to ease the recession and to steady financial markets.

However, even after economic and financial conditions return to normal, the federal budget will remain on an unsustainable path with the budget gap becoming increasingly larger over time unless the Congress enacts significant changes in fiscal programs. For example, under plausible assumptions about how fiscal policy might evolve in the absence of major legislative changes, the Congressional Budget Office projects the deficit to fall from about nine percent of GDP currently to roughly five percent of GDP by 2015, but then to rise to about 6 ½ percent of GDP by the end of the decade. After that, the CBO projects the budget outlook to deteriorate even more rapidly with federal debt held by the public reaching almost 90 percent of GDP by 2020 and 150 percent of GDP by 2030, up from about 60 percent at the end of fiscal year 2010.

The long-term fiscal challenges confronting the nation are especially daunting because they're mostly the product of powerful underlying trends, not short-term temporary factors. The two most important driving forces for the federal budget are the aging of the U.S. population and rapidly rising healthcare costs. Indeed, the CBO projects if federal spending for healthcare programs, which includes Medicare, Medicaid and subsidies to purchase health insurance in new insurance exchanges, will roughly double as the percentage of GDP over the next 25 years. The ability to control healthcare costs while still providing high quality care to those who need it will be critical for bringing the federal budget onto a more sustainable path.

The retirement of the baby boom generation will also strain Social Security as the number of workers paying taxes into the system rises more slowly than the number of people receiving benefits. Currently, there are about five individuals between the ages of 20 and 64 for each person aged 65 and older. By 2030, when most of the baby boomers will have retired, that ratio is projected to decline to about three. Overall, the projected fiscal pressures associated with Social Security are considerably smaller than the pressures associated with the federal healthcare programs, but they are still notable.

The CBO's long-term budget projections, by design, do not account for the likely adverse economic effects of high debt and deficits. But if government debt and deficits were actually to grow at the pace envisioned, the economic and financial effects would be severe. Sustained high rates of government borrowing would drain funds away from private investment and increase our debt to foreigners with adverse long run effects on U.S. income, output and standards of living. Moreover, diminishing investor confidence that deficits will brought under control would ultimately lead to sharply rising interest rates on government debt, and potentially to broader financial turmoil. In a vicious circle, high and rising interest rates would cause debt service payments on the federal debt to grow even faster, causing further increases in the debt to GDP ratio and making fiscal adjustment all the more difficult.

How much adjustment is needed to restore fiscal sustainability to the United States? To help answer this question, it's useful to apply the concept of the primary budget deficit, which is the government budget deficit excluding interest payments on the national debt. To stabilize the ratio of federal debt to the GDP, a convenient benchmark for assessing fiscal sustainability, the primary budget deficit must be reduced to about zero. Under the CBO projection that I noted earlier, the primary budget deficit is expected to be two percent of GDP in 2015 and then to rise to almost three percent of GDP in 2002, and six percent of GDP in 2030. These projections provide a gauge of the adjustments that will be necessary to obtain fiscal sustainability.

To put the budget on a sustainable trajectory, policy actions, either reductions in spending or increases in revenues, or some combination of the two, must be taken eventually to close these primary budget gaps. By definition, the unsustainable trajectories of deficits and debt, as the CBO outlined, cannot actually happen because creditors would never be willing to lend to a government whose debt relative to national income is rising without limit. The economist Herbert Steins has simply described this type of situation. He said, "If something can't go on forever, it will stop." (Laughter) One way or the other, fiscal adjustments sufficient to stabilize the federal budget must occur at some point. The question is whether these adjustments will take place through a careful and deliberative process that weighs priorities and gives people adequate time to adjust to changes in government programs or tax policies. Or whether the needed fiscal adjustments will be a rapid and painful response to a looming or actual financial crisis.

Acting now to develop a credible program to reduce future deficits would not only enhance economic growth and stability in the long run, it could also yield substantial near-term benefits in terms of lower long-term interest rates and increase consumer and business confidence. Plans recently put forward by the President's National Commission on Fiscal Responsibility and Reform, and other prominent groups, provide a useful starting point for a much-needed national conversation. Although these proposals differ on many details, they demonstrate that realistic solutions to our fiscal problems are available.

Of course, economic growth is affected not only by the levels of taxes and spending, but also by their composition and structure. I hope that in addressing our long-term fiscal challenges the Congress and the administration will seek reforms to the government's tax policies and spending priorities that will serve not only to reduce the deficit, but also to enhance the longer-term growth potential of our economy. For example, by reducing disincentives to work and to save by encouraging investment in the skills of our workforce, as well as the new machinery and equipment, by promoting research and development, and by providing necessary public infrastructure.

Our nation cannot reasonably expect to grow its way out of our fiscal imbalances, but a more productive economy will ease the tradeoffs that we face. Thanks for your attention, and I look forward to taking your questions. (Applause)

MARK HAMRICK: Thank you, Mr. Chairman. First of all, we're extremely grateful for your decision to return to the National Press Club where you were here just a short time ago. We think it's very important as a journalism organization that we have transparency in government and to give reporters and others, the American public, the opportunity to hear your thinking and to respond to questions in sort of real time as you're doing that. So thank you.

In that regard, I understand these discussions are also sort of occurring behind the scenes at the Fed with your colleagues, and there was a notation from a video conference of October 15th where it said-- and I love how some of the official language is displayed here-- but it's "participants discussed whether it might be useful for the Chairman to hold occasional press briefings to provide more detailed information to the public regarding the committee's assessment of the outlook and its policy decision making than is included in the committee's short post-meeting statements." So it seems as if that's a very official way of saying, "Should we be holding more news conferences? Should we be going to places like the National Press Club?"

Your colleague in Central Banking, so to speak, in Europe, holds a news conference. What is your thought about regular news conferences as opposed to the somewhat piecemeal approach that we're seeing right now?

BEN BERNANKE: Well, first I think that sentence particularly spoke for itself, don't you?

MARK HAMRICK: Absolutely.

BEN BERNANKE: Let me say first that I think that transparency is very important. It's important because we live in a democracy and the public needs to know what we're doing and why we're doing it. It's important because our policies work better if markets anticipate and understand the actions we're taking and what's likely to cause changes in those policies and the like. And the Federal Reserve has come an enormous distance. You may not be aware, but in 1994 the Fed didn't even announce when it changed the federal funds rate target. And now, of course, we have an after-meeting statement with votes, unlike the European Central Bank, and almost any other central bank, we have detailed minutes that are released three weeks after the meeting. We release full transcripts with a five year lag. We have extensive speeches and testimonies and other mechanisms. So we are a transparent central bank and we have made a lot of progress in that front.

On press conferences, it's been a difficult decision as we thought about it. On the one hand, real time transparency is very important and valuable. On the other hand, we don't want to create unnecessary uncertainty, unnecessary volatility in financial markets by saying things that may be misinterpreted if they're too ad hoc. That being said, as I said, I put a lot of value on transparency. We've moved very substantially in that direction and we are looking very seriously at whether-- we have a committee, in fact, headed by Vice Chair Janet Yellen which is looking at the whole range of communications. And I know they're looking very seriously at the idea that I would give a more regular press conference in the hope that that would further increase the Fed's transparency.

MARK HAMRICK: So just to sort of update us on where that stands, how far off into the future do you think a decision might come on that?

BEN BERNANKE: Not too far. The committee is working on it, and I think they'll have some recommendations pretty soon. And whatever comes out, there will certainly be additional steps to try and make us more transparent and more clear about what we're doing.

MARK HAMRICK: And they'll share those with us, right?

BEN BERNANKE: Absolutely.

MARK HAMRICK: Okay. And the next question is sort of about the personal side of this question, and that is-- this comes from the audience-- what are the three-- you don't have to go three-- but what are the most frustrating things about being Chairman of the Fed? Is it that the world is hanging on your every raised eyebrow and the possibility of an overreaction in the financial markets, i.e., irrational exuberance as your predecessor had to deal with way back when?

BEN BERNANKE: I think I want to answer that question seriously. This is a very challenging job and we faced a very challenging period. We've had enormous problems, issues with the financial markets, with financial stability, we've had to address those. I believe we addressed them adequately in terms of stabilizing the system. Now we have to implement a new set of laws, a new set of rules to make sure that in the future we don't have this kind of instability again.

At the same time, the economy, although it does look to be growing more quickly, is still in a deep hole, is still very far from where we'd like to be, and we need to manage policy, both monetary policy and, as I talked about today, fiscal policy, to try to bring us back to full employment and get people back to work in a way that's consistent with stability, and in particular with continued low inflation. So it's a very challenging job. I have a great staff at the Federal Reserve, I have great colleagues on the FOMC and in that respect, it’s tremendously challenging and interesting from my perspective. But it is frustrating because it takes a long time. It takes a while to make the kind of progress in the economy that we’d like to make.

MARK HAMRICK: And then from today’s headlines, a question from the audience, do you believe that any of the growing political unrest around the world, especially Tunisia and Egypt, is linked to higher food prices, which the questioner says results from the Fed’s large scale asset purchases?

BEN BERNANKE: Well, I'm not going to address the first part of that, I don't have much insight into the sources of the unrest. I would guess, thinking about Egypt, for example, that there's a lot going on there including issues about democracy and representation, issues about the broader economy and the like. So, I'm not sure I accept the premise of the first half of the question.

But I'll talk about food prices in general and the Fed’s policies. When you talk about food prices or other commodity prices, you need to talk about supply and demand. And in some cases, in food for example, there are some constraints on supply, there have been weather issues, and so on. But the most important development globally is the fact that the world economy is growing more quickly, particularly in the emerging markets. We have essentially a two-speed recovery where industrial economies like the United States are growing relatively slowly. And in fact, the industrial economies are just now coming back to the level of output and demand that we were in before the crisis three years ago. So the industrial countries are growing slowly, the emerging markets are growing much more quickly.

Now, the Federal Reserve’s monetary policy is aimed at stabilizing the United States economy. And in the United States, I don't think anybody can argue that our economy is overheated, that it’s growing too quickly, that it’s short of resources. We are using our policy to address stability in the United States. So then the question is where's that demand coming from? As I said, it’s mostly coming from emerging markets. Emerging markets are growing very quickly for a couple of reasons. One is just the fact that there has been a long-term trend now for emerging markets to develop very quickly and that on the whole is a very positive development because it means that millions of people who were in poverty are now moving closer and closer to a more middle class standard of living, which is of course a very good thing.

But as people’s diets become more sophisticated, as they eat more beef and less grains, and so on, the demand for food and energy and the like grows. And that's the primary long-term factor affecting the real price of commodities and food.

The other factor is that in some cases, some of the emerging markets are facing inflationary pressures because their own economies are growing perhaps even faster than their capacity. That is, their policies have not been such to keep growth and capacity balanced, which means that inflationary pressures are arising from those emerging markets. But I think it’s entirely unfair to attribute excess demand pressures in emerging markets to U.S. monetary policy because emerging markets have all the tools they need to address excess demand in those countries. They can, for example, use monetary policy of their own. They can adjust their exchange rates, which is something that they've been reluctant to do in some cases.

So it really is up to the emerging markets to find the appropriate tools to balance their own growth. That being said, even ignoring the inflationary pressures in emerging markets, their continued growth is going to continue to put pressure on the prices of commodities, including food, around the world.

But just one final comment on why Federal Reserve policy cannot be primarily responsible is just that you asked about Middle East, food in Egypt is priced in Egyptian pounds, not in dollars. If the dollar is weaker, the Egyptian pound is stronger. So clearly what's happening is not a dollar effect, what's happening is a growth effect primarily in emerging markets which is creating this tremendous demand for commodities, which is driving up the relative prices of those commodities.

MARK HAMRICK: So to leave the correlation or the causality question aside for the moment, as you look at these events unfold around the world, you see the price of oil rising. How do you see that as presenting risk to the U.S. economy as you try to do your job?

BEN BERNANKE: Well, we pay very close attention to oil prices and to other commodity prices because they do present really two kinds of risks. The first is that higher oil prices are kind of a tax. We're trying to stimulate the economy, we're trying to get consumers to become more confident, be able to spend more, and to help put people back to work to the extent that part of their income gains are drained away by higher gas prices, for example. That's going to be a negative and it’s going to slow the recovery. And so as international factors lead to higher oil and commodity prices, that's definitely a negative from the perspective of consumers and household budgets and economic growth.

The other place where it’s an issue and we are watching very carefully, notwithstanding that I think that commodity price increases are primarily coming from the global economy rather than from the U.S. per se, nevertheless we have to pay attention to that because we also have a very strong commitment to stable prices and low inflation. Right now, inflation overall, including food and energy prices, is quite low in the United States, quite lower, in fact, than in almost any other industrial country, not to mention emerging market economies.

That being said, we got to make sure it stays that way. Higher energy prices add to headline inflation because they raise the price of heating oil and gasoline and the like. And even more serious, if they begin to feed into other prices. So for example, if they begin to feed into wages or goods and services that are produced using energy, then you might get a broader inflation problem. And we are absolutely determined that we will do whatever is necessary to keep inflation low and stable. In that respect, that is a challenge that we have to address.

MARK HAMRICK: Certainly in your speech you talked about the bond buying program. There was a time when QEII was thought to have referred to an ocean liner and now it's first reference as to the program. Somebody's asking would you attribute the stock market's rise since late August to QEII? And if not, why not? And just as a follow-up to that, I might say how do you see sort of the process of helping the U.S. economy filtering through various sectors of the economy as you go about engaging in that process?

BEN BERNANKE: Well, first to be very clear, the purpose of the monetary policy easing is not to increase stock prices per se. The purpose is to strengthen the U.S. economy, put people back to work and create price stability. But the way monetary policy always works is through interest rates and asset prices, that's how it always works, by changing those prices in financial markets. So yes, I do think that by taking these securities out of the market and pushing investors into alternative assets, we have led to higher stock prices and to lower stock market volatility.

By the way, the last time we did this in March 2009, was about a week before the absolute minimum where the Standard & Poor was in the 600s and following our actions, Standard & Poor, the stock market, rose quite considerably. So yes, the policy is affecting the stock market really in two ways. One is by lowering essentially long-term yields and forcing investors into alternative assets. But also because as this process has been working through, and as we have seen both in the earlier episode a few months after we began the process we began to see a stronger economy, this time we really began this process in August and now four or five months later, we're seeing a stronger economy. As the markets see the stronger economy materializing, that's incorporated into expectations about future profits and future economic activity. And that causes the market to rise as well, so it's a virtuous circle in that respect.

So as I described in my remarks, the whole idea here is to move interest rates and move asset prices in a direction that will stimulate more economic activity, put more people back to work and get rid of risk of deflation and create a stable price environment. And if you look at the developments since August, I think things have moved very distinctly in the right direction.

MARK HAMRICK: And then, of course, the extension from that is people want to know what you look at to decide whether to extend the program. Is there a QEIII, IV, et cetera? I think you've said that it's possible that there would be an extension beyond the current end of the program. So what kinds of things do you look at to decide where to go from here?

BEN BERNANKE: Well, first of all as we've noted in our statements, in our commentary, we are reviewing the program on a regular basis. We want to make sure that it's working as intended, that it's not having any adverse side effects. But to answer your question more generally, the approach is more or less the same we always use for monetary policy. I mean, how do we make decisions about the federal funds rate? What we do is we do our best to create an outlook for the economy; say where are things going, where is employment going, where's output going, where's inflation going? And we ask ourselves given the level of monetary combination we have now, is the economy on a trajectory that will give us the best possible outcome in the medium term? If not, if inflation looks to be very low or deflation risk is there, or if output is too low and unemployment is too high, then that would be a situation that requires more stimulus.

Vice versa, if inflation becomes an increasing problem, the economy’s growing quickly, that would be the reason for us to scale back. So in the same way that we adjust monetary policy under normal circumstances with a short-term interest rate, by looking at the outlook and trying to gauge whether the economy is growing at a pace that's consistent with eventually returning to full employment and stable prices, by the same approach we look at that outlook and based on that we will either provide more stimulus if necessary, or scale back or stay with what we have. So, it's really not a simple answer. But we have to use the best we can in terms of our forecasting models to try to assess where the economy’s headed.

MARK HAMRICK: And at the same time, perhaps on the most politically charged question, that of the unemployment situation, you've said that you think it may be a matter of years before the unemployment rate goes down to a level that's considered to be more normal. Is that something you look at as you decide whether to extend or not?

BEN BERNANKE: Well, certainly. I mean, half of our mandate is maximum employment and we want to get the labor market working again, better if we can. It’s very important because not only is 9 ½ percent unemployment a very large waste of human resources and a very taxing burden on many families around the country, but about 45 percent of all the unemployed have been unemployed for six months or more. And what that means is that if they don't find work in the next six months or year or two years, if they find work again in the future, it could very well be at a much reduced wage, or part time. People who are not employed for long periods of time, they lose their skills, they lose their connections, they lose their knowledge of what's happening in their particular line of work. And so the consequences could last a very long time.

And so it is very important to put people back to work as quickly as we can. It’s going to take a while. The very nature of this is that the economy has to grow about 2 ½ percent real terms just to accommodate people coming into the labor force. And so in order to keep the unemployment rate constant, we need about 2 ½ percent growth. Back in August when we were thinking about this policy, growth was looking like it was around two, and so we were looking at a situation in August where we thought the unemployment rate would actually begin to rise again. And so in order to get growth above that 2 ½ percent mark, we embarked on these new policies. And we're looking forward into 2011, we think it will be above 2 ½ percent, and therefore we expect to see unemployment declining over time.

Now, it's not going to be as fast as we would like, but on the other hand, as I mentioned, there is some good news. I think there are a lot of indicators, including we had once again this morning on new claims for unemployment insurance, which is a pretty good number. Looking at the whole range of statistics on the labor market, the sense is that employers are becoming more willing to hire and I think we'll start seeing some stronger payroll reports and some lower unemployment rates pretty soon.

MARK HAMRICK: Another question from the audience talking about the same program. So do you announce the purchases before the Congress passed the tax cut extension, the payroll tax holiday and several other significant stimulative measures. Has that given the Fed any reason to consider ending your latest purchase program early?

BEN BERNANKE: As I mentioned earlier, of course we try to make an assessment of the outlook. And based on that, we decide whether or not we're about where we should be, or we should do more or should do less and so on. In this particular case, when we were making our projections, we had already taken into account most of what is in that package. We had anticipated that the Bush tax cuts would most likely be extended, at least in large part. We had anticipated that the UI insurance would be extended, at least in large part.

The part of the package that was surprising to us, and which does create a little additional stimulus, is the payroll tax rebate. So we factor that into our analysis and of course on the margin we'll respond to the way that affects the outlook. But it wasn't that we were surprised by this package, we expected a lot of it to happen and that was already built into our forecast when we made our policy decisions.

MARK HAMRICK: You referenced the jobless claims numbers and obviously data flows on a nearly daily basis. What do you think is the single biggest thing, if there is such a thing, holding back companies from increasing their hiring right now?

BEN BERNANKE: Well, there are a lot of factors, it isn't simple. Certainly one issue is, and perhaps very key issue, is uncertainty about how much demand there's going to be. Remarkably, at the beginning of the downturn, firms laid off large numbers of workers and they were able through very significant productivity gains to meet existing demand with many fewer workers. And only as demand has begun to grow beyond the level where it was when the recession began has there been really any pressure on firms to begin to add to their workforce. And so I think only now, firms are beginning to say, "Well wait a minute, we're now seeing enough increase in our sales that-- and we have already exhausted the obvious productivity gains, that it's time now to start bringing on new workers."

So that uncertainty about the duration and sustainability of the recovery, I think, has been the key factor and explains why, for example, firms have been using a lot of temporary workers, because they can bring temporary workers on and if the economy weakens again, they can let them go. It'll be a really good sign when we see those temporary jobs being converted into permanent jobs, and I'm hopeful that that's where we're going to be heading in the next couple of quarters.

MARK HAMRICK: So you've been exhorting Congress, and essentially the federal government to attack this fiscal situation sooner rather than later. And we've seen what happens in Europe if you don't do that. What do you think the risk is that, indeed, the financial markets force the solution before our lawmakers and our administration do it themselves?

BEN BERNANKE: It’s really impossible to give any projection. Right now, the markets seem to be behaving as if they think these problems will be addressed in the sense that the U.S. government can still borrow for long periods of time at reasonable interest rates. So evidently, investors believe that the U.S. economy is strong enough and that our political system is able to deliver stability in our budget situation over the medium term.

In one respect, certainly they're right in that this is a very, very wealthy productive economy and there is in no sense that we are economically unable to find the solution to these problems. We're rich enough, we have enough resources, that we can find those solutions, there's no question about that. And some of the commissions we've seen, for example, have put out some plausible possibilities. I'm not endorsing any particular one, but they just demonstrated that here are some various ways that we could go about doing this without ripping apart our social safety net and without radically raising taxes, et cetera, et cetera.

So it can be done. I think the question will be do we have the political capacity, the political will to do it? And I think that's what the markets will be following. Indeed in Europe, indeed it’s been less a question of resources. Everyone believes that Europe as a whole has the resources to meet sovereign debt claims. It’s really been a question of will the countries there demonstrate that they have the will to collaborate to work together to solve these problems? I believe they will, but it’s really that political uncertainty which is the key issue for the markets, not so much the economic capacity.

MARK HAMRICK: Have you seen any evidence any time in the recent past that there is political will of that magnitude to attack a problem of this size in the United States?

BEN BERNANKE: Well, it’s difficult to say. I think there's a lot of interest. There certainly have been a number of members of the Senate and House who have for years been talking about these issues and have pressed for taking steps to address them. And clearly, there's considerable interest in the general public in trying to address these questions. So I'm not a political prognosticator, I wouldn’t try to make an assessment. But I know that there's an increasing understanding among representatives in Congress and in the administration and in the public that these are important issues and there's only so far we can kick the can down the road. We have to address this, and the sooner we do it the less painful it’ll be and the better it’ll be for our economy.

MARK HAMRICK: Then there are more near-term issues. One questioner says we know that you make monetary policy, not fiscal policy. But would Fed policy have to be adjusted if there were a shutdown of the government, as some politicians are threatening? Does the Fed have enough options left to make a difference if a government shutdown cascaded through the private sector, through contractors laying off workers and adversely impacting other channels?

BEN BERNANKE: Well, just to be accurate, I think what's being contemplated is not a shutdown of the government, but a refusal to ratify the debt limit extension. And this is a very serious matter because under current law, if the debt limit is not extended for a time, the Treasury has various resources that it can use to make payments on a national debt. But beyond a certain point, it would not have those resources and the United States could conceivably-- I think this is very remote but it's not something you want to play around with-- the United States would be forced into a position of defaulting on its debt. And the implications of that for our financial system, for our fiscal policy, for our economy, would be catastrophic.

So I would very much urge Congress not to focus on the debt limit as being the bargaining chip in this discussion, but rather to address directly the spending and tax issues that we all have to deal with if we're going to make progress on this fiscal situation. The debt limit itself is, again, something where we need to be very careful that we don't create any impression that the United States is not going to pay its creditors the interest on the national debt. That would be, again, a very bad outcome.

MARK HAMRICK: So we talked earlier about some of the legislation that's percolating on Capitol Hill to audit the Fed. Can you talk about where the policy stands now by virtue of the Dodd-Frank legislation and why you think some of the proposed legislation isn't the right thing to do?

BEN BERNANKE: So, the Dodd-Frank legislation with Fed cooperation and with a lot of other Fed initiatives, has basically created a completely transparent Fed as far as the financials are concerned. When people say audit the Fed, what they mean is open the Fed's books. What is the Fed's transactions? Currently, every program that we initiated during the crisis has been completely open to the GAO, all the information has been provided to the public. On December 1st, we put out a complete record of all 21,000 loans that we made during the crisis. All 21,000 of which, by the way, were paid back with interest. Explaining what the program was, what the criteria were, who was the borrower, what was the collateral, how much was lent, when was it repaid. All that information was provided.

We provide weekly statements of our balance sheet, we have an outside auditor, Deloitte and Touche, which comes in and audits our books and publishes all that information every year. So, every aspect of the Fed's financial dealings are wide open, wide open. And we have invited the GAO to come in and look at all of our activities, both extraordinary activities during the crisis and all of our ongoing financial activities.

So there is no sense in which the Fed has secret financial dealings. All of our assets, all of our transactions are open to the public and will be open to the public. And I have committed to that transparency.

Now, what audit the Fed means in the language that has been used by some members of Congress is not about the financials of the Fed. Rather, it's about auditing monetary policy, which means that the GAO would be assigned by the Congress to look at monetary policy decisions to take the materials prepared for the meeting, to depose potentially the members at the meeting, to essentially provide an evaluation to the Congress at very short horizons of whether or not the Fed was making the right monetary policy decision.

I think this is very different from what most people think about when they think about an audit. And what this is, basically, is a very significant challenge to the notion that while the Congress has every right to set the goals and objectives of the Federal Reserve and the tools of the Federal Reserve, it should be up to the Fed to make monetary policy decisions independently of short-term political influences and with an eye towards long-term objectives of the economy.

And what that kind of legislation would do has nothing to do with financials. It would be very much a significant step towards direct Congressional oversight of the decision process itself, and personally I think that would be a very bad outcome. We have seen around the world that-- and there's a great deal of evidence, empirical and practical evidence to support this-- that central banks that are independent in their decision making and have a clear mandate provide a much better outcome, both in the economy and in financial markets than a central bank which is dictated by-- whose decisions are dictated by short-term political considerations. So that's something which I think is an extremely important principle.

MARK HAMRICK: Is this sort of pressure coming from the outside helping to unit you with your colleagues on the Federal Reserve Board at all?

BEN BERNANKE: On this issue, every member of the Federal Reserve, both current and past, I think, would be extremely united. This is a fundamental bedrock principle of central banking and if the Federal Reserve becomes essentially an arm of Congress in making monetary policy decisions, I do think that would lead to much worse outcomes in terms of inflation, in terms of stability in the U.S. economy.

MARK HAMRICK: Here's a banking question. Bankers say that while leaders and regulators in Washington are telling them to lend more at the bank level, the examiners and regulatory staff they deal with on a day to day basis are more concerned with the financial health of banks and less concerned with promoting lending. What are you doing about this disconnect?

BEN BERNANKE: This is an issue that we have been very, very focused on for quite a long time. There's a problem here, which is we don't-- obviously, we don't want banks to make bad loans. We don't want them to make loans that are not going to get paid back, we want them to make sounds loans. On the other hand, when you have a creditworthy borrower coming and asking for credit, it's in the interest of the bank, it's in the interest of the borrower, it's in the interest of the whole economy that that loan get made. And so we need to find the appropriate balance between loans that are appropriately prudent and safe on one hand, but under which good borrowers, creditworthy borrowers, are able to get credit.

And we have working together with the other bank regulators, going back several years now, we have been providing extensive guidance both to the banks and to our examiners about how to make that appropriate balance. We've done large numbers of training classes, we have had phone-ins, ask the Fed phone-ins where banks call in and talk about their concerns. We have had meetings all across the country to meet with bankers and small businesses to talk about issues that have arisen. So we have put an enormous amount of institutional resources into trying to find that right balance. And I think we've made a lot of progress, frankly. And I would suspect that as we look forward into 2011 and on, that we will see increasing willingness of banks to lend and the examiners will not be an issue. If there are good loans to be made, it's very clear that banks should be allowed to make them and we will, in fact, encourage them to make them.

MARK HAMRICK: Just some sort of housekeeping matters. We're almost out of time, but before asking the last question, a couple of very important matters to take care. I want to remind our members and guests of future speakers Harry Shearer the comedian and humorist, the voice of The Simpsons will discuss media myths on March 14th, and we might even try to get him to do a few voices for us. And then the voice of taxation, Douglas Shulman, the commissioner of the IRS, will be here before the tax deadline day.

Second, I have some walking-away gifts for you, more than one. I'd like to present you with the traditional NPC coffee mug, which I understand you had once before. But nevertheless, we'd love for you to perhaps share that with a loved one. We will be watching eBay to make sure it doesn't show up there.

But then we thought you've been so kind to join us on multiple occasions, we wanted to present you with-- and this is very unusual-- the highly coveted National Press Club baseball cap. (Applause)

So our last question, I have to say that having you here today is a big deal for us, for me, since I've been covering business and economics news for many years now. It's a little like the Super Bowl for business journalists, speaking of which, the Super Bowl's this weekend. And I'm wondering, first of all, do you watch football? And do you have a favorite in the game between Pittsburgh and Green Bay, which will be in Dallas?

BEN BERNANKE: I definitely do watch football when baseball season isn't around, anyway, and I'm looking forward to the game. But, the Redskins didn't make it this year once again, unfortunately, so I will be studiously objective, although I do note that one of the teams has a quarterback named Ben. (Laughter) But I'm looking forward to the game and I think GDP will drop to nothing during that three-hour span.

MARK HAMRICK: Thank you, Mr. Chairman. (Applause) Thank you for being a good sport, we really appreciate it. We'd like to thank the National Press Club staff including the library and broadcast center for organizing today's event. And for more information about joining the club or how to acquire a copy of today's program, please go to our website at www.press.org. Thank you, we're adjourned. (Sounds gavel.)

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