Speeches by Bob McTeer

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I'd like to thank NABE for inviting me today. And for giving me back my research director—Harvey Rosenblum. I don't know how good a job Harvey's done as president over this past year—my hunch is a good job. But I can vouch for how hard he's worked on your behalf, as measured by the number of days he's been AWOL from his day job. Of course, that's measuring output by input.

On a more serious note, I know Harvey was affected profoundly by his experience at the World Trade Center Marriott last year, an experience he shared with many of you. September 11 helps us put our work life into perspective. And our personal life.

For a while after September 11, I felt awkward talking about the economy. I didn't want to give the impression that I thought its economic impact was important in the total scheme of things.

On the other hand, when it began to look like consumers thought the patriotic thing to do was to curb their spending, I felt compelled to write an op-ed piece pointing out the obvious to you: that one person's spending is another person's income and job. But even that message creates some angst. Perhaps a moral dilemma.

At the individual level, most American consumers probably should be consuming less and saving more. But if too many do that, we fall victim to the paradox of thrift. (Just a small Keynesian moment there.)

Back to Harvey's year as NABE president. I hope you haven't ruined him by drawing him too deeply into the macroeconomic mainstream, the mainstream of official statistics and econometric models. We may need to reintroduce him to the world of anecdotes as an antidote to all that. Get him rebooted with some factory tours and mall crawls and maybe a trip down to Laredo to count the number of northbound trucks versus the number of southbound trucks crossing the border.

This business about anecdotes is sort of an inside joke at the Dallas Fed. I once asked an economist at the New York Fed what he thought of some of the essays in our annual reports.

He said, "Well, they are pretty anecdotal."

I don't think he meant it as a compliment, but I'm not sure why it couldn't have been. If history is just one damned thing after another, you could call the "things" in question "anecdotes." Someday, I'm going to the mall and have a T-shirt made that says, "Life is anecdotal."

Anecdotally, we know that something is wrong in this economy when it's surprisingly easy to get an upgrade to first class. We know *what* when we look back in coach and see room to stretch out and take a nap.

We know something is wrong when our computer gurus start keeping regular office hours and coming to work in clean black shirts.

We know something is wrong when we can suddenly get our choice of colors on a new Lincoln Navigator in the heart of the Telecom Corridor just north of Dallas. The Lincoln Navigator, as you may know, is the unofficial official car of the Telecom Corridor (or was).

We know something is wrong when we can get a hotel room in Austin, the high-tech capital of Texas. There's no despair yet, however, because the live music venues on 6th Street are still too crowded. Texas country soul, or blues, is a countercyclical industry.

I don't mean to suggest that we at the Dallas Fed rely entirely, or even primarily, on anecdotal evidence. But I do

agree with Yogi Berra when he said you can observe a lot just by watching.

I like to use real-world observations to temper the theoretical stuff. I identify with Glen Campbell's answer when he was asked if he could read music. He reportedly said, "Yes, I can read music. But not so much as to interfere with my picking."

I guess I have the shortcomings of statistics on my mind because of the many recent revisions that seem to have taken the luster off the New Economy. As a cheerleader for the New Economy, I feel a bit like a Dallas Cowboys cheerleader when the Cowboys lost to the new Houston Texans in the first game of the season.

Well, what do I have to say for myself? I'm tempted to follow the example of President Kennedy, who told a campaign aide what he planned to say on his second campaign trip to Philadelphia. The aide said, "You can't say that."

"Why not?"

"Because it contradicts what you said in Philadelphia last month."

Kennedy said, "I'll deny I was ever in Philadelphia."

Unfortunately, I did speak to this group in Chicago two years ago, and some of you may remember. On September 11, 2000, to be exact.

You may recall that the really strong numbers of the "New Economy" period ran from around 1995 through mid-2000.

September was the third month of the third quarter, which we later learned had slowed significantly from previous quarters. We first learned, only at the end of October, that the third quarter had slowed. That number was revised down at the end of November and again at the end of December 2000.

So the extent of the slowing was not appreciated until three months later, and by that time the fourth quarter had slowed even more—we learned later. Hence the January 3, 2001 intermeeting easing, almost a month before the next scheduled FOMC meeting. The rest, as they say, is history, as we pushed the target federal funds rate down from 6 1/2 percent to 1 3/4 percent over the next year.

The overall economy grew slowly but positively in the first and second quarters of 2001 and was on its way to more of the same in the third quarter—before September 11 tipped it into negative territory. I'm an optimist, but even I assumed the fourth quarter of 2001 would be worse than the third because of the timing of September 11. But as you know, growth turned positive in the fourth quarter. So the third quarter turned out to be the only negative quarter. Or so we thought.

Years ago I heard someone say the future isn't what it used to be. I thought that was a great line. Well, it turns out that not only is the future not what it used to be, but the past isn't either. Massive revisions have shuffled the deck in an obvious conspiracy against us New Economy cheerleaders. We now think we had a mild three-quarter recession. It turns out that there was more foam and less beer during that period than we thought. Well . . . shucks!

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It was the acceleration of productivity growth in the second half of the 1990s that enabled the economy to grow faster and drive the unemployment rate lower without accelerating inflation.

Faster productivity growth raised the so-called speed limit for policymakers and stiffened their backbones enough to tolerate faster growth and lower unemployment at levels that used to cause inflation to accelerate.

Traditionally, central banker courage meant the courage to tighten before the need was obvious to others. The new courage was the courage *not* to tighten when established economic opinion suggested a preemptive strike was needed. Fortunately, Chairman Greenspan possesses both kinds of courage: the courage to do something, as well

as the courage to just stand there.

Of course, there is a lot of second-guessing about all that these days. Many of those who chided the Chairman for suggesting the possibility of "irrational exuberance" in late 1996—and many who objected to any tightening or talk of tightening at the time—now wonder why we didn't tighten enough to curb the stock market. I'll leave that touchy topic to the Chairman, but I can't help wondering out loud what the reaction would have been to an announcement that the Fed was tightening monetary policy to depress stock prices.

As the public record shows, I preferred not to tighten as early as June and August 1999. I suspect that if we took a poll here—which I'm definitely not suggesting—a majority of you would argue, with the benefit of hindsight, that the tightening should have begun earlier, rather than later. That may or may not be true; I'm not conceding anything here.

But one problem I have is that the rationale for tightening earlier, while inflation was decelerating, could have been made earlier in 1999, or in 1998 or 1997 or 1996. If the preemptive tightening argument had prevailed early on, we would have been enforcing the old speed limits and choking off the productivity-enhanced growth potential of the New Economy. If we had done that, there is a good chance that the productivity boom and all the good things it produced would never have taken place. The New Economy may have had more foam and less beer than we thought, but there was still more beer than foam.

So as the latest data revisions show, productivity growth did not almost triple during the late 90s. But it did double, from around 1.4 percent per year to around 2.8 percent per year. So our standard of living doubles in half the time—approximately. That's still pretty good.

As you know, after the surprising fourth-quarter upturn last year, headline GDP grew at a 5 percent rate in the first quarter this year. But momentum was lost in the second quarter, when it grew at a 1.3 percent rate. Moreover, job growth has been anemic so far, making comparisons to the previous recession's "jobless recovery" inevitable. While the unemployment rate has held up remarkably well so far, we can't continue to count on discouraged workers and declines in the labor force to sustain that number. Unfortunately, the pain of recession and slow growth is not shared evenly.

The really good news is the continuation of productivity growth during the recession and the recovery period so far. But while recoveries fueled by productivity growth augur well for the future and for the long term, in the short term they place an inordinate burden on unemployed and discouraged workers.

Everyone knows that economic growth is good. But few appreciate how pervasive its beneficial effects are. At the last meeting of the Dallas Fed's board of directors, we had a presentation on how cyclical forces affect minority unemployment, poverty status, crime, welfare and charities.

The higher growth rate of the 1990s, of course, improved all these measures.

In the decade prior to the 2001 recession, the gap in the unemployment rate between blacks and whites fell from 6.7 percent to 4 percent, while the gap between Hispanic and white unemployment rates fell from 3.3 percent to 2.3 percent. During the 1990s, minority unemployment and poverty rates fell to their lowest rates in recorded history.

Well, what has happened since the recession started? The black–white unemployment gap has gone back up from 4 percent to 5.5 percent, and the Hispanic gap has stopped narrowing.

The 1990s boom—along with favorable demographic trends, especially with respect to age—helped reduce crime rates, especially crime such as robbery, burglary, larceny and motor vehicle theft. The declines were as much as 50 percent in some cases. As the economy slid into recession in 2001, the crime rate stabilized and then started rising again in most regions of the country. If growth remains insufficient to reduce the unemployment rate, increases in crime seem inevitable.

Rapid growth helped welfare reform reduce welfare rolls by almost 60 percent between 1994 and 2000. The recession produced a sharp slowing in that reduction, and the rolls had stabilized by the end of last year. Most states' welfare rolls actually increased during the first quarter of this year, a trend that is likely to continue absent an early

resumption of more rapid growth.

The impact of the economy on charitable giving has been dramatic. To quote from our board presentation:

In the first half of the 1980s, real charitable contributions per person rose at an annual rate of 1.5 percent. In the second half of the 1980s, contributions rose at a 2 percent rate. But during the boom of the 1990s, giving rose at a whopping rate of 4.5 percent per year as New Economy workers shared their prosperity . . . . In contrast…contributions actually declined by 3.2 percent in 2001.

To quote from the conclusion of the board presentation:

Everyone knows that economic growth matters. Almost everyone knows that economic growth can give them a job or cause them to receive a higher wage. But few people know how much economic growth affects other aspects of their lives that are just as important but aren't usually thought of as being related to the economy.

Taken together, the evidence supports the idea that economic growth has a substantial impact on crime, welfare, charity and minority well-being. It also underlines the importance of . . . policymaking at this vital time. Should U.S. economic growth accelerate in the quarters to come, Americans would reap benefits in the form of less crime, less welfare recipiency, more charity, smaller deficits, and greater earning power . . . . Economic growth matters more than most people think.

Of course, I suppose, as a central banker I should say something about inflation. Well, it's low and conditions are already ripe for it to go lower. Especially if growth picks up.

If you focus on demand, demand is weak and growth is below potential, and we have slack in both labor and product markets. That is disinflationary.

If you focus on productivity, and its impact on labor cost, the way productivity growth has held up since the recession began is surely disinflationary, and productivity growth does not seem to be abating.

If you focus on the supply side, and the influence of rapid output growth on inflation, the potential of growth to accelerate, if realized, is surely disinflationary**.**

I've used the word "disinflationary" a lot. I don't know at what point welcome disinflation might morph into unwelcome deflation. I don't think we are there yet, but that doesn't matter much. Because I do believe faster real growth is essential.

And a policy to promote growth is consistent with a policy to combat deflation. There is no conflict.