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Remarks by

Alan Greenspan

Chairman

Board of Governors of the Federal Reserve System

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One day during the 1984 reelection campaign, a television correspondent, Andrea Mitchell to be exact, shouted a question across the Rose Garden to President Reagan: “What about Mondale’s charges?” Without missing a beat, the President paused as he was returning to the Oval Office and replied, “Tell him he should pay them.”

Ronald Reagan brought a lightness and benevolence to the serious business of the Oval Office that few have been able to match. He had inherited a dysfunctional economy and dealt with global dangers, but his spirit never wavered.

Though such one-liners and anecdotes were indeed humorous, many also communicate politics or policy. A classic was candidate Reagan’s memorable quip during his 1980 campaign for the presidency: “A recession is when your neighbor loses his job. A depression is when you lose yours. And a recovery is when Jimmy Carter loses his.” I presume that former President Carter was not amused, but as a skilled politician himself, he could not but admire the wit.

My favorite anecdote, as I remember it, starts with Mikhail Gorbachev, accompanied by his usual coterie of underlings, reviewing the Soviet Union’s military might parading by Lenin’s tomb. The phalanx of missiles, tanks, and troops was most impressive as it passed the reviewing stand.

Next in line came a straggle of disheveled civilians wholly out of step, a clearly dissonant note in an otherwise well-orchestrated performance. This sight evoked major distress from a Gorbachev aide who pleaded forgiveness for allowing such riffraff to mar the meticulous show of Soviet military might.

“Do not be concerned, comrade,” counseled Gorbachev. “I am responsible for them. They are our economists, and you have no idea how much damage they can do.”

Underlying the humor is President Reagan's long-held distrust of those economists who promoted what he perceived as destructive government intervention in the marketplace.

Throughout his professional life, the President understood the self-correcting tendencies of free markets and the fundamental wealth-creating capacity of capitalism. He trusted Adam Smith's invisible hand to stimulate creativity and innovation and to produce outcomes that he perceived as generally fair.

A great deal of what Reagan saw in the America of the 1970s was not to his liking, and he changed much of it when he became President. Yet for all that he accomplished in those remarkable eight years, one could argue that he had an even greater effect after he left office, when a whole generation of people who were proud to be identified as Reaganites moved into positions to influence policy.

If he was ever discouraged, I suspect it was because not even Ronald Reagan could fully rein in excess government spending and significantly pare the size of the bureaucracy. To be sure, no American President, with constitutionally limited powers, has been able to mold a nation as complex as the United States to his set of values. But Ronald Reagan surely stands in the first rank of American Presidents measured by the breadth of their legacy for good.

In his eight years in office, President Reagan transformed the country's self-image. Instead of a people believing they were a once great power, they regained their self-confidence, sensing that it was indeed "morning in America." Although we have not yet wholly leveled the playing field, Ronald Reagan believed that, more than in any other country, every individual in the United States is given an opportunity to succeed.

The revival of the American spirit, which became evident in the 1980s, was the result not of the President's cheery disposition but rather of his implementation of important changes that continue to manifest themselves in our society and economy.

Ronald Reagan started the sequence of geopolitical initiatives that led Mr. Gorbachev to figuratively tear down the Berlin Wall. President Reagan's rhetorical demand, as he stood at the Wall in 1987, is the most vivid image I have of his presidency.

He sensed a progressive economic rot in the Soviet Union, despite official appraisals from within the U.S. government of continuing Soviet economic strength. He also did not believe, contrary to much conventional wisdom, that per capita gross domestic product in East Germany by the 1980s had drawn close to that of West Germany. In fact, after the dismantling of the Berlin Wall, the figure was estimated to be less than half.

As a consequence, President Reagan was convinced that the economy of the Soviet bloc could not sustain the pace of its arms race with the United States. A surprisingly large number of western economists, including many in our government, disagreed. They were largely relying on an array of statistics from Soviet bloc central planning authorities that, in the light of freedom, turned out to be grossly exaggerated.

The President's Foreign Intelligence Advisory Board in 1984 gave me the task of evaluating economic data from the Soviet bloc and our intelligence estimates of the economic strength of the Soviet Union. The data's quality was poor, and their implications were contradictory. The President cut through the ambiguity with the simple premise that an authoritarian and corrupt government cannot foster economic vitality. He had it right, though it was still years before his insight became evident to all.

President Reagan applied the same straightforward approach to domestic economics, setting in motion several initiatives that facilitated an economic trend resulting in the exceptionally flexible U.S. economy that we observe today. That increased flexibility has allowed us to absorb and, at least to date, fend off a series of economic shocks in the last three years that in an earlier period, in my judgment, would have been debilitating.

My predecessor at the Federal Reserve, Paul Volcker, embarked in the fall of 1979 on an aggressive monetary tightening that attempted to arrest a dangerously accumulating set of inflationary forces. Presidential candidate Reagan also perceived inflation as a danger, and, then as President, afforded Volcker the political support that is so essential to a central bank when its pursuit of long-term stability risks some worsening in near-term economic activity. That support began the process that has led today to the virtual elimination of inflation from the U.S. economy.

A second key support to today's flexible markets has been the bipartisan deregulation initiatives that began in the Ford and Carter years and were extended by Ronald Reagan. In January 1981, disregarding warnings that the action might renew upward pressures on inflation, President Reagan dismantled the remaining controls that had debilitated our oil markets. By 1986, crude oil prices had reached their lowest levels in real terms since 1973. Deregulation in finance, trade, and transportation was pressed forward.

But perhaps the most important, and then highly controversial, domestic initiative was the firing of the air traffic controllers in August 1981. The President invoked the law that striking government employees forfeit their jobs, an action that unsettled those who cynically believed no

President would ever uphold that law. President Reagan prevailed, as you know, but far more importantly his action gave weight to the legal right of private employers, previously not fully exercised, to use their own discretion to both hire and discharge workers. There was great consternation among those who feared that an increased ability to lay off workers would raise the level of unemployment and amplify the sense of job insecurity.

It turned out that with greater freedom to fire, the risks of hiring declined. This increased flexibility contributed to the ability of the economy to operate with both low unemployment and low inflation. Whether the average level of job insecurity has risen is difficult to judge, but, if so, some offset to that concern should come from a diminished long-term average unemployment rate.

The notion that lowering barriers to discharging workers reduces the long-term unemployment rate has gained widespread acceptance even beyond our shores. The European Council, meeting in Brussels last month, urged member states to “maintain the momentum of reform of national labor markets” by among other things, “relaxing overly restrictive elements that affect labor market dynamics.” That is not the way that Ronald Reagan would have put it, but analytically it is moving in a Reagan direction. In a recent speech, Chancellor Schröder, a Democratic Socialist, made specific proposals to reduce the cost of hiring and firing German workers. He proposed making protection against dismissal “less unwieldy.”

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Ronald Reagan was one of our most successful Presidents in part because he fervently believed in, and acted on, a small number of important principles. To be sure, he knew how to

compromise to advance his legislative agenda. But in the process he always kept sight of his essential principles.

Those principles included a wholehearted embrace of capitalism and a rule of law. He understood that no market system--no exchange of goods and services--can function without a rule of law rooted in individual rights, especially the right to own property. Indeed, societies that do not sanction and protect ownership rights are invariably rife with bribery, corruption, and violence. Little wealth is created in such an environment.

A society riven with violence cannot organize a viable market economy. It obviously cannot prosper if violence is unchecked, but it also cannot prosper if the amount of violence that has to be checked is large. The high risk and cost of enforcement imposed on an economy subject to random violence will raise the cost of capital and inhibit productive economic growth.

The constancy of Reagan's policy goals helped his administration construct legislative and budgetary recommendations. Most veteran Reagan staffers found that they could press their priorities by demonstrating their consistency with one or more of the President's goals. That approach resulted in a greater coherence of policymaking.

Ironically, it also helped coalesce the opposition to his policies because the President's positions were a good deal less ambiguous than those of most other politicians. Many disagreed with elements of Ronald Reagan's philosophy of freedom and markets, but few have had difficulty understanding where he stood on the question of how to organize an economy.

I will leave a fuller analysis of that philosophy to historians and biographers. Instead, let me focus this evening on one pillar of free-market capitalism, the model that Reagan embraced so enthusiastically.

I refer to an old-fashioned human virtue--trust.

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Although a rule of law is necessary to a vibrant and efficient market economy, it is not sufficient. We rarely consider, for example, that a law of contracts, an integral part of any rule of law, operates because everyone assumes that only a very small share of legally contracted transactions will require adjudication. If it were otherwise, our courts would be overwhelmed, and our economy severely impaired.

Hence, an effective law of contracts, as part of a rule of law, requires that the vast majority of transactions be voluntary. That outcome necessitates that the buyer of a good or service trust the explicit or implicit warranty on the offered product. The buyer needs assurance that, if an agricultural equipment dealer certifies that a harvester is in mint condition, he is being truthful and his warranty is to be trusted. Similarly, the dealer needs assurance that the buyer's check is good. If trust in the word of counterparties is lost, any exchange that takes place will need to be administered by a court or some third party. It is a costly use of real resources if one is required to engage in the memorable admonition of one great statesman in a different context, "Trust, but verify."

Trust in the promises and performances of counterparties to a trade is thus an essential pillar of free markets and, hence, free-market capitalism. Because trust is so valued, it is often capitalized and recorded explicitly as "goodwill" on business balance sheets. Our system works fundamentally on individual fair dealing. We need only look around today's world to realize the rarity and value of such an underpinning.

Trust has had an important role in American economic development. In fact, through much of the nineteenth century, laissez-faire reigned and caveat emptor was the prevailing prescription for guarding against the wide-open trading practices of those years. A reputation for honest dealings was thus a particularly valued asset. Even those inclined to be less than scrupulous in their private dealings were forced to adhere to a more ethical standard, or they risked being driven out of business.

To be sure, the history of business is strewn with the Fisks, Goulds, and numerous others treading on, or over, the edge of legality. But they were a distinct minority. If it were otherwise, the United States at the end of the nineteenth century would never have been poised to displace Great Britain as the world's leading economy.

Reputation was especially important to early U.S. bankers. It is not by chance that in the nineteenth century many bankers could effectively issue uncollateralized currency. They worked hard to develop and maintain a reputation that their word was their bond. For these institutions to succeed and prosper, people had to trust their promise of redemption in specie. The notion that "wildcat banking" was rampant before the Civil War was an exaggeration. Certainly, crooks existed in banking, as in every business. Some banks that issued currency made redemption inconvenient, if not impossible. But they were fly-by-night operators and rarely made it beyond the first swindle.

In fact, most bankers competed vigorously for reputation. Those bankers who had a history of redeeming their bank notes in specie, at par, were able to issue substantial quantities of notes, effectively financing their balance sheets with zero-interest debt. J.P. Morgan marshaled

immense power on Wall Street in large part because his reputation for fulfilling his promises was exemplary.

But as the nineteenth century came to a close, the view that the federal government should eschew any role in altering free-market forces started to change. The dishonest practices of some less-scrupulous business people seriously eroded the valuable reputations of the many more ethical business people. The Granger laws of the 1870s began the process of regulating the marketing practices of the railroads. But they were not very effective and were followed by the much broader Interstate Commerce Act of 1887. The Federal Trade Commission Act of 1914 backed up the Sherman Antitrust Act of 1890 by specifying illegal trading practices. Caveat emptor was in retreat as federal enforcement of appropriate business practice had the collateral effect of diminishing the value of hard-earned private reputation.

Over the past half century, the American public has embraced the protections of the Securities and Exchange Commission, the Federal Deposit Insurance Corporation, and the myriad other federal agencies that have largely substituted government financial guarantees and implied certifications of integrity for business reputation. As a consequence, the market value of trust so prominent in the nineteenth century seemed, by the 1990s, to have faded to a fraction of its earlier level.

Perhaps we are better protected and, accordingly, better off as a consequence. But corporate scandals of recent years have affirmed the view that the plethora of laws of the past century had not eliminated the less-savory side of human nature. I anticipate that recent legislation holding chief executive officers more responsible for the integrity of their companies will help.

But I am pleased to see a re-emergence of market value placed on trust and personal reputation governing business practice. Moreover, after the revelations of corporate malfeasance, the market punished the stock prices of those corporations whose past behaviors cast doubt on the reliability of their reputations. I hope and anticipate that trust and integrity again will be amply rewarded in the marketplace as they were in earlier generations.

I cannot help but believe that Ronald Reagan would consider that the right outcome.

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Our forefathers bestowed upon us a system of government and a culture of enterprise that has propelled the United States to the greatest prosperity the world has ever known. We elect Presidents to protect and expand that bequest. Ronald Reagan will go down in history as one President who superbly fulfilled that obligation.

Contributing far more to that success than most realize was Nancy Reagan. The critical importance of her loving support of her husband, especially in periods of great stress, was evident to all of us who had the privilege of serving the President. And besides, she added a certain sparkle to the Reagan White House and to Washington that few of us can forget. I particularly remember her bravura surprise performance to a standing ovation at the 1982 Gridiron Club dinner. I do not know how many congressional votes she garnered for the Administration from that performance, but she certainly won mine.

The Reagan presidency was a remarkable one for Americans. In the words of the nation's fortieth President, "We meant to change a nation, and instead, we changed the world." He did indeed, and we are grateful.