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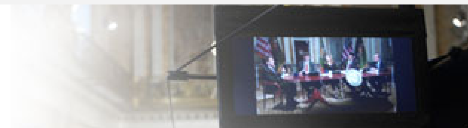

Remarks by Secretary Geithner before the Economic Club of Chicago

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As Prepared for Delivery

CHICAGO - Good morning. Thank you, Mayor Emanuel. I want to thank John Canning and Donna Zarcone for hosting this event. It is a pleasure to be here at the Economic Club of Chicago to discuss some of the fundamental economic choices we face as a country.

The President arrived in Washington at a particularly dark moment in American history. The U.S. economy was contracting at an annual rate of 9 percent. Growth around the world was collapsing.

The actions taken by Secretary Paulson, Chairman Bernanke, and the FDIC in the fall of 2008 had broken the back of the financial panic, but the financial system was frozen and the economy was still deteriorating at an alarming pace.

The President did not sit around hoping the fire would burn itself out. He did not commission a bunch of studies. He did not play politics with the crisis. He chose to act, and he acted forcefully.

The President's strategy to repair the financial system, combined with the Recovery Act, the restructuring of the U.S. auto industry, the coordinated global rescue he led in the G-20, and the actions of the Federal Reserve, was very effective in restoring economic growth.

Within three months of his taking office, the pace of decline in growth began to slow. By the summer of 2009, the American economy was growing again.

Let me make that clear. In about six months, the economy went from contracting at an annual rate of 9 percent to expanding at an annual rate of nearly 2 percent, a swing of almost 11 percentage points.

In a remarkably short period of time, we were able to not just avert a second Great Depression, but also to begin the long and fragile process of repairing the damage and laying a stronger, more durable foundation for economic growth.

How has the economy performed since that early start?

Since the summer of 2009, the economy has expanded at an average annual rate of 2.5 percent, adding 3.9 million private sector jobs over the last two years.

Growth has been led by private demand, including strong gains in investment and exports. The balance sheet of the business sector is exceptionally strong, and the economy as a whole is more productive than before the crisis.

These are promising developments, but we still face some very tough challenges.

Unemployment is very high, the housing market remains weak, and growth is not as fast as we would like. These are tragic legacies of the financial crisis.

And we live in a dangerous and uncertain world, one reason gas prices are higher today.

What does the recent pattern of growth tell us about the economy?

Most viewed the moderate pace of the recovery and the slowdown in 2010 and 2011 as justification for pessimism. But if you look at the *causes* of the slowdown, there is reason to be much more optimistic about the strength of the economy and the private sector.

Most importantly, growth was dampened in the early stage of recovery by headwinds that follow all financial crises.

Recoveries that follow financial crises are slower, as Carmen Reinhart and Ken Rogoff have famously written. They are slower because the causes of financial crises—typically a large rise in borrowing by households and the financial sector and too much investment in housing and real estate—act to hold down growth as they are unwound.

As people bring down their debt burdens and raise their saving rate, they spend less. As banks are forced to reduce risk and restore more prudent credit standards, they lend less. These forces work against the impact of lower interest rates, dampening the otherwise potentially powerful effects of monetary policy.

There is a paradox in this, in that the changes necessary to unwind the causes of the crisis and lay a more lasting foundation for future growth necessarily slow the pace of expansion.

Our economy is still in the process of deleveraging, dealing with significant household debt, excess investments in real estate and other forms of debt.

But we are making a lot of progress in working through those adjustments. Household debt is down 17 percentage points relative to income since before the crisis. Financial sector leverage is down substantially and credit is expanding. Housing and commercial real estate construction is starting to pick up after five years of contraction.

Overall, we have done a better job than many economies in making these adjustments—as Martin Wolf has written in *The Financial Times*, "The U.S. economy is the most advanced in deleveraging."

Apart from these difficulties, we have faced a series of other challenges to growth.

There were three large external shocks in 2010 and 2011—the situation in Europe, the effects of the earthquake and tsunami in Japan, and higher oil prices. These shocks were large enough to take about a percentage point off GDP growth in the first half of 2011.

Their effects are now receding, although Europe and oil still present risks. But the U.S. economy proved quite resilient in the face of those pressures, and growth strengthened quickly as those shocks receded. Despite the resilience of the economy, high gas prices do remain a challenge for average Americans.

On top of this, President Obama inherited very large fiscal deficits, swollen to levels well beyond any experienced since World War II. That erosion in our fiscal strength left the nation with less room to maneuver and increased the political opposition to fiscal actions beyond the Recovery Act.

And while the Recovery Act provided absolutely crucial support for the economy, state and local fiscal contraction offset a significant part of its effects. But that drag is receding as revenues have started to rise with economic growth.

Finally, the debt limit debate last summer caused huge damage to confidence. But that was a blow caused by political threats of default by the President's opponents—not something produced by weakness in the economy or by economic policy.

Much of the political debate and the critiques of business lobbyists misread the underlying dynamics of the economy today. Many have claimed that the basic foundations of American business are in crisis, critically undermined by taxes and regulation.

And yet, business profits are higher than before the crisis and have recovered much more quickly than overall growth and employment. Business investment in equipment and software is up by 33 percent over the past 2 ½ years. Exports have grown 24 percent in real terms over the same period. And manufacturing is coming back, with factory payrolls up by more than 400,000 since the start of 2010.

The business environment in the United States is in numerous ways better than that of many of our major competitors, as measured by international comparisons of regulatory burden, the tax burden on workers, the quality of legal protections of property rights, the ease of starting a business, the availability of capital, and the broader flexibility of the economy.

The challenges facing the American economy today are not primarily about the vibrancy or efficiency of the business community. They are about the barriers to economic opportunity and economic security for many Americans and the political constraints that now stand in the way of better economic outcomes.

These challenges can only be addressed by government action to help speed the recovery and repair the remaining damage from the crisis and reforms and investments to lay the foundation for stronger future growth.

This means taking action to support growth in the short-term—such as helping Americans refinance their mortgages and investing in infrastructure projects—so that we don't jeopardize the gains our economy has made over the last three years.

And it means making the investments and reforms necessary for a stronger economy in the future. Investments in things like education, to help Americans compete in the global economy. Investments in innovation, so that our economy can offer the best jobs possible.

Investments in infrastructure, to reduce costs and increase productivity. Policies to expand exports. And reforms to improve incentives for investing in the United States—including reform of our business tax system.

A growth strategy for the American economy requires more than promises to cut taxes and spending.

We have to be willing to *do* things, not just cut things.

To expand exports, we have to support programs like the Export-Import Bank, which provides financing at no cost to the government for American businesses trying to compete in foreign markets.

To make us more competitive, we have to be willing to make larger long-term investments in infrastructure, not just limp forward with temporary extensions.

Any credible growth agenda has to recognize that there are parts of the economy, like the financial system, that need reform and regulation. Businesses need to be able to rely on a more stable source of capital, with a financial system that allocates resources to their most productive uses, not misallocating them to an unsustainable real estate boom.

Cutting government investments in education and infrastructure and basic science is not a growth strategy. Cutting deeply into the safety net for low-income Americans is not financially necessary and cannot plausibly help strengthen economic growth. Repealing Wall Street Reform will not make the economy grow faster—it would just make us more vulnerable to another crisis.

This strategy is a recipe to make us a declining power—a less exceptional nation. It is a dark and pessimistic vision of America.

The President has a different strategy for economic growth. He believes that while our long-term fiscal problems are formidable, we can address them over time with a balanced package of reforms that preserve room for investments that will help us grow.

There is no economic or financial case for using the fear of future deficits to cut as deeply into core functions of the government, to weaken the safety net or fundamentally alter Medicare benefits as do the Republican proposals.

Our fiscal commitments are unsustainable over the long run, but we cannot put our long-run fiscal challenges above all others, and we have to confront them carefully and wisely, with a balanced mix of spending cuts and modest revenue increases such as the President has proposed.

We are gradually getting stronger, but we still have very tough challenges ahead.

Yet, as tough as they are, these are manageable challenges for the United States. And I would prefer our challenges to those of any economy anywhere in the world.

We can afford the investments that are important for future growth. We can adjust to the changes that will be compelled by the need to bring our long-term deficits down.

As we face the great political and economic choices ahead, remember how terrible the crisis was. Remember that Americans are still living with the damage that is the legacy of that crisis. When you listen to the debate about taxes and Medicare and Medicaid, or when you hear politicians tell you that they will protect even the most fortunate Americans from higher taxes, remember that even before this crisis, about 20 percent of children in the United States were living in poverty and about 40 percent of children were born to parents covered by Medicaid.

Remember that the fortunes of children born in America today, the quality of public schools they attend, the quality of health care they receive, the chance they have to go to college, still depend significantly on the wealth of their parents and the color of their skin.

But also remember that we are a country of great strength and resilience. We have successfully navigated the most dangerous phase of the worst economic crisis in generations. We need to bring the same creativity and force and sense of national purpose to the challenges ahead. And that will require better choices from our political system. No economy can be stronger over time than the ability of its political leaders to come together to make tough decisions.

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