

U.S. DEPARTMENT OF THE TREASURY

Press Center

**Remarks of Assistant Secretary Jan Eberly before the National Association of Business Economists (NABE)**

7/31/2012

2012 ECONOMIC MEASUREMENT SEMINAR*As prepared for delivery*

Thank you for inviting me to speak to you today. As you know, NABE's mission is to provide leadership in the use and understanding of economics. And the research and analysis that NABE economists provide is valuable both in understanding the state of the economy and in understanding policy options.

Today I am going to discuss a topic near and dear to the heart of every economist: data. Now that is the kind of statement that gives economists our reputation for being dismal and dry and analytical, but in my not-very-objective view, it's quite the opposite. The data help us set priorities and design policies and evaluate the outcomes that have a huge impact on people. In many cases, that's why we wanted to become economists – not to look at data and the discipline of economic thinking in isolation, but rather to understand and make a difference in the world. Those policies range from health care to housing to global finance. So today, I want to discuss a few specific ways in which data inform policy-making.

Coming from an academic background, the policy world presented some new challenges in balancing rigor and timeliness. In academia, the pendulum swings more toward thoroughness, leaving no stone unturned. However, in the policy world, there are times when “the data are the data”, and we have to make time-sensitive decisions based on the information available and in front of us.

I want to focus today on three key areas in which data can inform current policy-making. First, understanding the past: assessing the current state of the U.S. economy and fiscal policy. Second, investing in the future, through education policy. And third, a topic that is a crucial issue in the recovery right now: housing.

Macroeconomy and Fiscal Policy

Turning first to the macroeconomy: As you know, the U.S. economy is in the process of recovering from a severe financial crisis and associated recession. History teaches us that recovery from such crises is gradual, as households and businesses must correct the imbalances that initially caused the problems. Despite the deleveraging process, real economic activity has resumed. The U.S. economy has been growing now for 12 straight quarters and GDP now stands nearly 7 percent above its recession low. Private-sector payrolls rose by 84,000 in June and have increased by 4.4 million since the employment trough in February 2010.

However, as is typical following a financial crisis, growth has been uneven. U.S. economic activity has moderated in recent months. Real GDP rose 1.5 percent at an annual rate in 2012Q2, following a 2.0 percent gain in Q1 and a 4.0 percent gain in 2011Q4. In interpreting the recent data, it is important to keep in mind that a number of temporary factors have weighed on growth over the past several months, including the run-up in energy prices earlier this year, the unusually warm winter weather which pulled forward activity from Q2 into Q1, and an intensification of the sovereign debt problems in Europe. That said, the underlying pace of demand also appears to have weakened. This recent slowdown serves to illustrate to us again the difficult path that economies tread as they emerge from financial crises.

Although growth has been uneven following the crisis, the volatility of GDP growth in the current expansion has actually been lower than is typical, although in line with the reduction in the variability of GDP growth over the past 25 years known as the Great Moderation. Over the period covering the economic recovery (2009Q2 through 2012Q2), the standard deviation of GDP growth is 1.1 percentage points. During all the previous recoveries in the post-war period, the standard deviation of GDP growth averaged 3.2 percentage points.

Going forward, there are both positive and negative factors influencing growth. Several factors in the private sector are supportive of continuing growth. As I noted earlier, households have made progress in deleveraging, and as most families' largest asset is their home, the improvement in house prices should support wealth accumulation going forward. In addition, gasoline prices have substantially retraced their rise this winter, which has boosted real income growth in the past few months. All these factors should provide some support for consumption going forward.

On the business side, the conditions are supportive of further increases in investment. Interest rates remain very low, making it relatively inexpensive to invest, and access to credit is improving, although certain firms may still find it difficult to qualify for a loan. The corporate profits of domestic industries rose by \$195 billion over the four quarters ended in Q1 and stand at a record level, and corporations have record levels of cash on hand with which to fund desired investment.

I will talk about the housing sector in more detail later, but for now it is worth discussing how recent developments in housing fit into the U.S. macroeconomic picture. The housing sector – while still very fragile – has also shown signs of improvement. According to a variety of nation-wide measures, house prices have risen in recent months and are even showing year-over-year gains. The FHFA purchase-only house price index rose 0.8 percent in April, and it has risen 3¾ percent over the past twelve months. Prior to February, there had not been a year-on-year increase in almost five years. The 20-city S&P/Case-Shiller home price index climbed 1.3 percent in April after seven months of decline [see slide 1].

Even with this slight improvement in house prices, affordability remains near record levels, as mortgage rates are still at record-low levels [see slide 2]. When the index equals 100, a family earning the median household income has just enough income to qualify for a loan on a median-priced home.

And while the inventory of unsold homes remains high, the number of seriously delinquent mortgages has been declining, which should result in fewer foreclosed homes on the market in the coming months and years. Meanwhile, the number of foreclosures has stabilized [see slide 3].

Share of Loans Delinquent and in Foreclosure

These improvements have translated into improved sentiment on the part of prospective homebuyers. According to the Reuters/Michigan Survey, the share of respondents saying that it is a good time to buy a house is at its highest level since early 2009. A summary measure gauging consumer home buying attitudes (that nets out the share who think it is a bad time to buy a home) is currently at its highest level since 2004.

These improvements have also translated into increased buying and construction. New home sales have been on a modest upward trend since last fall. Existing home sales are also up relative to last year. This figure shows single-family new home sales [see slide 4]. Sales of new single-family homes rose 7.6 percent in May to 369,000 at an annual rate. New home sales have risen nearly 20 percent from a year earlier.

Residential construction has made a positive contribution to GDP growth in each of the last five quarters. Going forward, there is a considerable pent-up demand for housing: The NAHB estimates that 2.1 million household formations were postponed between 2007 and 2010, and the level of PCE housing services is well-off its trend from 1980 to 2007, leaving room for an increase in housing demand to return to what had been a very stable long-run trend, after more than working-off the excess demand from the housing bubble.

Taking all this into consideration, private forecasters project GDP to rise about 2.0 percent for the year as a whole, up about ½ percentage point from the pace in 2011. This is consistent with GDP rising at about a 2.5 percent pace in the second half of the year.

But while the pieces are in place for a pick-up in economic activity going forward, the economy still faces many challenges. The unemployment rate remains unacceptably high at 8.2 percent and too many Americans are still looking for work. Despite the substantial progress already made, households will continue to deleverage. In addition, the sovereign debt crisis in Europe continues to weigh on financial markets, and global growth has slowed, which restrains demand for exports of American goods.

On top of that, the economy has faced an unprecedented amount of fiscal tightening given the amount of slack that remains in the economy, primarily from state and local governments, but also more recently from the federal government, which has dampened the recovery. On average over the past four decades, state and local government spending has contributed about ¼ percentage point to real GDP. However, since 2010, the contraction in state and local government outlays has subtracted an average of roughly 0.3 percentage point from growth per quarter. Moreover, state and local governments have shed a total of 618,000 payroll jobs since the recession ended. While the finances of state and local governments are improving, most states will still need to cut expenditures in the future to meet balanced budget requirements. The federal government has also been a net drag on GDP growth since the end of 2010, as the fiscal stimulus enacted to counteract the recession has receded.

I want to stop here for a moment and emphasize that it is only from this type of review – a careful, consistent monitoring of the incoming data – that we are able to understand the path our economy has taken since the financial crisis, as well as our trajectory going forward. Having a solid grasp of the data represents the difference between being intrigued and being informed. It is the mechanism through which we have come to understand our fundamental challenges at this critical time—supporting growth now while implementing long-term reforms.

The President's FY2013 Budget is designed fulfill both of these mandates. All of these proposals were developed with the state of the economy I just described in mind. For example, to determine how much belt-tightening is required to bring the deficit into primary balance—putting our debt on a declining path as a share of the economy—we look at data. Specifically, we consider the extent to which different fiscal reforms would affect the deficit; data on expected tax revenues and spending in future years; and data on the size of the deficit that brings it into primary balance.

In the current year, the Budget includes more than \$350 billion in measures to boost economic activity and encourage job creation. Of these, the Administration and Congress have already extended the 2 percentage point payroll tax cut and an extension of emergency unemployment benefits until the end of 2012, and the Administration has been urging Congress to act on other job creation programs.

In addition to these near-term measures to boost economic activity, the FY2013 Budget also includes a strategy to cut the deficit in half and achieve primary budget balance before the end of the decade. It does so through a balanced package of tax reforms and spending cuts that still leaves room for us to make necessary longer-run investments – in infrastructure, education, and research and development – that will determine our competitiveness and productivity, and ultimately our standard of living.

Education

Data analysis tells us that education is one of our highest-payoff long-run investments. I must say that when I think about my students who couldn't get to an 8:30 class on time, who begged for extra time, and extra credit, and extra points, I sometimes find this a little hard to believe. But these also turn out to be the same students who later spend the summer building houses in Indonesia, and getting up at 4 am for the Asia trading session.

I have lots of anecdotes about this from a career in education, but we all know that anecdotes are basically single data points. More systematic data tell a very compelling story – showing that the returns to higher education are large; that these gains accrue not only to individuals but also to society at large; and that therefore the government can and should play a role in creating policies that encourage individuals to seek higher education.

But setting aside the positive externalities, even at an individual level the data make clear that education has never been more valuable. The earnings gap between those with a college degree and those without one is the highest it has been since 1915, the earliest year for which such estimates exist. This gap, however, doesn't even capture all of the benefits: college-educated workers are far less likely to be unemployed and are more likely to have jobs that provide additional benefits such as employer-provided health insurance, paid vacation, and sick leave. In particular, the reduction in the unemployment rate is quite significant, as those with only a high school diploma are nearly twice as likely to be unemployed as those with a college or advanced degree [see slide 5].

The Returns to Education

Higher education is also critical for economic mobility. Recent work from the Pew Foundation found that without a college degree, children born in the bottom income quintile have a 45 percent chance of remaining there as adults [see slide 6]. With a degree, they have a roughly equal chance of attaining each income quintile, which means an 80 percent chance of being in a higher income quintile than their parents.

Intergenerational Mobility

Given the growing returns to higher education, an economist would expect to see a response in the demand for education. Indeed, this has shown up in the data. As you can see [in slide 7], this response has come in the substantial growth in college enrollment. The Department of Education estimates that of the 2.9 million people who finished high school in 2009, 70 percent (approximately 2.1 million) enrolled in college that same year.[1] One decade earlier, in 2000, only 63 percent of recent graduates enrolled in college right out of high school (1.7 of 2.8 million).

Total Enrollment Over Time

I would make two additional points based on this chart. First, the vast majority of higher education takes place at public institutions. Approximately 80 percent of new students enroll in a public institution. Second, while enrollment has grown across the board, growth is highest at private, for-profit institutions, although they still represent a small share of total enrollment. And even though public institutions are the largest player in higher education, they have still maintained higher growth than private, non-profit schools.

In addition to rising college enrollment, we have also seen rising tuition costs. As the next slide [8] shows, posted tuition has more than doubled in real terms over the last thirty years.

Published Tuition and Fees (1981 = 100)

Note that tuition has risen the most quickly at public, four-year colleges, increasing by more than 350 percent. Net tuition, defined as sticker tuition minus financial aid, has increased at a slower rate due to greater availability of financial aid, but the increase has nonetheless been substantial, especially for those students who do not receive financial aid.

Underlying the trend in tuition is a fundamental shift in education financing, especially at public institutions. As state support for higher education has been withdrawn, tuition has grown in importance as a source of funding at public institutions, doubling from only 20 percent of revenue in the late 1980s to over 40 percent today [see slide 9].

Share of Revenue at Public Four-Year Institutions

During that same time period, state and local government support has fallen by almost the exact same share. In fact, 2009 was the first year since we began keeping these statistics that tuition accounted for more revenue than state and local governmental support at public institutions.

At the same time, the federal government has increased its support for higher education by increasing the size of Pell Grants, and by enacting new tax credits, which assist students and parents in coping with increased tuition. While these programs soften the impact of higher tuition, they do not completely offset the substantial decline in support from state and local sources.

These data enable us to see the true trend: an on-going decline in state and local public support for higher education, with a shift to tuition-based funding which is partially offset by increased need-based financial aid. Low tuition was historically supplemented by public funding – the current generation of tax payers – supporting the education of the next generation of students. This cross-generational support is a classic example of a social contract: one generation invests in subsequent ones, which in turn uses the benefits of that investment to support the next, and so on. In contrast, our society is moving toward a situation in which individuals or their families are themselves responsible for making investments in human capital.

Family wealth might be a cushion against this ongoing shift in education financing. High-quality data on family wealth are rare – most wealth data are self-reported measures, and linking parents' wealth to children's wealth is even more challenging. In spite of these limitations, the evidence shows that, as a result of the crisis, there is less available in home equity for the current generation to pass along to future generations, about which I'll say more when we discuss housing. Hence, linking educational access to family resources is even more problematic, as fewer families can tap home equity to provide the resources to fund their children's education.

Housing Policy

And this brings me to my final topic for today: housing. As many of you know, for most American families, their home is their single largest asset. Through this store of wealth, many families were able to invest in their children's future.

However, the housing crisis erased much of this wealth. In the wake of a crisis, economists often wonder whether there were any tell-tale signs that were missed, or if they were just reading the tea leaves incorrectly. Unsurprisingly, one of the root deficiencies can be traced back to the data. The early to mid 2000s were characterized by rapid innovation in the financial services sector but the existing data infrastructure could not effectively analyze many of these new products and appropriately quantify the risks. Private-label securitization – which refers to securitization by entities other than Fannie Mae, Freddie Mac, or Ginnie Mae – grew. The composition of these securities varied wildly, but their opacity did not initially raise alarm bells – in part because strong housing price growth and benign economic conditions muted any appreciable differences.

Then, in 2006 and 2007, housing prices fell precipitously, and cracks began to appear in the value of the assets that secured trillions of dollars of debt. Mortgage delinquencies began to mount. While it is not possible to know the exact ramifications of the loss in housing wealth, the total figures are substantial by any measure. On average, house prices have fallen by more than 30 percent from their 2006 peak and housing wealth has fallen by roughly \$7 trillion. This has led to 11 million homeowners who owe more on their mortgages than their homes are worth, an amount totaling about \$700 billion.

Loan-to-Value (LTV) Distribution

While the downturn has been widespread, its severity has varied – and continues to vary – by geography. In some areas – such as the so-called “sand states” – the housing boom years were characterized by price-escalation and furious building. In these areas, widespread delinquencies reflected severe negative equity combined with accelerating job losses. Some areas, such as Michigan, never experienced the bubble dynamic that characterized the sand states, but poor housing market performance was the culmination of decades of job and population loss, exacerbated by the recession. The share of mortgages that are non-current (i.e., delinquent or in foreclosure) is one measure of the severity of current housing problems [see slide 11]. Outside Nevada, much of the non-current population is in the Southeast and along the Rust Belt.

Even within regions, the impacts of the housing market downturn varied dramatically. The decline in housing has hurt low-income families disproportionately, since homes with lower prices and larger mortgages also lost disproportionately more equity. In each of the 16 cities surveyed by Case-Shiller tiered home price index, the lowest-priced homes had the largest decline in value. For example, in Los Angeles, overall house prices fell 40 percent since 2006, but the highest value homes fell 31 percent and the lowest value homes fell over 50 percent. The gap is even more pronounced in Atlanta, where on average house prices have fallen 35 percent since 2006, but the lowest-priced homes fell in value by 64 percent. Moreover, research from Pew and Treasury show that Hispanic and Asian households are more likely to live in the states hurt most by the housing crisis – such as California, Nevada, and Florida – and their home equity has fallen by 50 percent and 32 percent, respectively. So while overall home values have fallen by about a third, the hit to families' wealth is not evenly distributed. Indeed, for some families the decline has been catastrophic.

While aggregate information helped characterize the scale of the losses, it was immediately clear from more granular data that any policies addressing housing would require precise targeting in order to be efficient and reduce the cost to the taxpayer. In the depths of the housing crisis and with this perspective, the Administration developed housing policy that was grounded in and informed by the available data and that strived to protect the taxpayer. The Making Home Affordable (MHA) programs are numerous and address a wide

variety of housing market issues – including mortgage modifications, second lien modifications, refinances, principal reductions, and foreclosure alternatives.

One program was the Home Affordable Modification Program (HAMP), developed in early 2009 to support payment-reducing mortgages for distressed borrowers with economic hardship and high mortgage payment-to-income ratios, when doing so was in the interest of both the investor and the borrower. To encourage mortgage investors to participate in HAMP, the program needed a data-driven, impartial decision-making tool that investors could trust to yield an unbiased economic assessment of the modification. Along with economists from other agencies including the FHFA, Fannie Mae, Freddie Mac, and FDIC, Treasury used data on borrower behavior and local housing market features to calibrate a model to evaluate the net economic benefit of the HAMP mortgage modification for the mortgage investor. The HAMP program now covers over 90 percent of the mortgage market, and its widespread adoption suggests the value of standardization and harmonization around this model. Of course, data were crucial in informing and improving this policy tool.

To date, the HAMP program has produced more than 1 million permanent mortgage modifications. And the program itself has become a valuable source of data, as we learn more about the income profile of applicants, update their credit scores, and get a new read on their home values to inform our understanding of borrower behavior in various degrees of negative equity. We have used data from this program, including performance data on successful modifications, to inform and develop our other housing policies targeted at distressed borrowers. As we have come to better understand housing market dynamics through this program and through the increasing and constantly-improving stream of housing market-related data, we have expanded eligibility to other groups of borrowers, and we have enhanced certain features of the program, such as principal reduction.

Conclusion

In conclusion, economic analysis and data have played a crucial role in addressing the challenges of the past, present, and future. Importantly, amidst these challenges, the Obama administration is building new institutions to monitor the data and avert future crises. When President Obama signed the Dodd-Frank Act in 2010, he established the Financial Stability Oversight Council and the Office of Financial Research—also known as FSOC and OFR—which are actively monitoring and mitigating threats to the stability of the financial system.

Since its first meeting in October 2010, the FSOC has met regularly to discuss market developments and potential threats to stability. One of the duties of the FSOC is to facilitate data-sharing and coordination among its member agencies. In the run-up to the crisis, fragmentation in our regulatory system allowed many risks to slip through the cracks. As Chair of the FSOC, Secretary Geithner continues to make it a priority that the work of the regulators is well-coordinated.

The Dodd-Frank Act also established the OFR to collect and standardize financial data, perform essential research, and develop new tools for measuring and monitoring risk. Currently, the OFR is working on a number of projects with the FSOC, including developing metrics for

and indicators of financial stability. One ongoing priority, for example, is establishing a legal entity identifier (LEI), or unique, global standard for identifying parties to financial transactions. The LEI can improve the quality of financial data, especially in identifying firms' largest and most complex exposures, and thus help to detect a buildup of risk in the system.

They say that knowledge is power. That is certainly true in economic policy. The data inform our understanding of the economy: How did we get here, where are we headed, and what can we do about it?

It is this perspective—a perspective fundamentally informed by data—that we bring to bear on the policy debate in which we are engaged. An economy that supports measurable improvements in standards of living is one with productivity growth, driven by investments in human capital and education, research and innovation, and the infrastructure to support growth.

If you'll indulge a little history in addition to recent data: this is not the first time that our country has faced difficult long-run challenges alongside near-term stresses. In many previous cases, we have risen to the occasion: The high school movement of the early 20th century increased high school completion from 9 percent to 40 percent in just 25 years, land-grant universities, polio vaccinations, food safety regulation built across many administrations – begun by Harry Truman's 1947 signing of the Federal Insecticide, Fungicide, and Rodenticide Act of 1947, and continuing to the Safe Drinking Water Act of 1974 (Ford) and the Food Quality Protection Act of 1996 (Clinton) – the National Park System, and the Eisenhower interstate highway system. These were all investments made knowing that they had potential long-run benefits, and required costly and risky initial investments, without knowing how large or how lasting their legacy would be.

We have been through a terrible crisis, and while the economy continues to improve, the legacy of the crisis is still wrenching for many families. The data show us just how difficult that crisis has been, both at the aggregate level and looking at the experiences of individual households and families. You all know that behind the statistics are anecdotes and people, individual stories and families. The data show us how far we have come to date in combating and recovering from that crisis. And they point toward the further steps we can take to support the economy in the short run and to make the necessary and crucial investments in our nation's long-run future.

Thank you.

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[1] Table 208, *DES 2010* (Snyder & Dillow, 2011). High school completion, as measured by the ratio of high school graduates to the population that is 17 years old, increased between 1990 and 2010 (from 73 percent to 77 percent) (Table 110, *DES 2010*).

[NABE Speech](#) 