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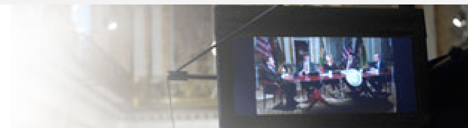

Remarks by Deputy Secretary Sarah Bloom Raskin at the Economists for Peace and Security Symposium

11/18/2015

WASHINGTON - Good morning. Thank you, Professor Galbraith, for that kind introduction and for inviting me to speak here this morning.

Economists for Peace and Security has helped our country make progress on a wide range of issues by cutting across academic disciplines and policy areas, and bringing the best economic thinking to bear on our greatest security challenges. And that is part of why it is such a privilege for me to be able to participate in this year's Schwartz Symposium.

The approach of my remarks today is to start with one of the four topics—namely the topic of economic growth, which is the traditional macroeconomic metric that we focus on, to elaborate upon the ultimately important topics suggested by the other three headings—inequality, austerity, and jobs.

When economists discuss growth, we mean GDP growth—the rate at which our economy's output is expanding over time. To be sure, and as the thinkers here well know, GDP growth is an imperfect metric for capturing and quantifying all the many important things that bear on social welfare and common good.

In fact, the risks associated with a focus on macroeconomic growth that is unhinged from inclusive growth are significant. Speaking purely from the perspective of the macroeconomy, inclusive growth is necessary in order to achieve more sustainable macroeconomic growth over the long term.[1] A growing body of research provides evidence suggesting that less heterogeneity in income and wealth may actually facilitate higher and more durable economic growth, contradicting the conventional view that greater heterogeneity—in other words, inequality—had a silver-lining purpose of achieving better growth. In the traditional model, economists believed that more income flowing to high-income households meant greater overall savings and investment, which, in turn, meant greater growth.[2] But, these considerations are only part of what determines how an economy shrinks or expands. In particular, by limiting broad access to engines for wealth creation like housing and education, non-inclusive growth can limit macroeconomic growth and make it less sustainable in the face of adverse shocks.

Think of it this way: When it comes to the potential for macroeconomic growth to advance broad-based prosperity and well-being, inequality hampers it, austerity thwarts it, and you will have fewer quality jobs without it. And achieving inclusive growth that breaks us out of anemic and insufficient short-term macroeconomic growth will not be possible, in my view, by just the "invisible hand." Importantly, government must help to foster and enhance it.

Today, I want to talk about policies that promote inclusive growth, and the questions that inclusive growth raise in terms of government policy in an economy driven more and more by technological change.

To frame this challenge, I want to share two scenes from my summer, involving my car and me.

In the first scene, I am driving south on 95 with two dogs, an aging car on a rainy dark day. My car starts making ominous noises, and I see that I am passing a New England town where—in the not too distant past—hardworking factory workers flourished. I am in one of those towns where pay-day lending shops and "We pay cash for your jewelry" trucks have sprung up between abandoned buildings. I was in one of those desolate downtowns that is a shell of a once vibrant community.

Before its final gasp, my car valiantly struggles to reach a gas station with a bustling set of activities occurring in its garage. I am approached by the garage's mechanics and thanks to their extraordinary and expert intervention, with skills honed over decades, the car is repaired, and I am back on my way.

Now for the second scene: Later that same week, I am on the other side of the country, traveling again in a car, but this time behind a driverless car in California. Here, where the economy is speeding into the future, a car is just as likely to be repaired by a computer programmer as an auto mechanic, and lines of code have become as important to vehicles as brake pads. As I watched the small, futuristic pod whiz along, I thought back to the New England mechanic, and all of the other skilled laborers across the country, and wondered about jobs in the economy of the future.

To achieve sustainable macroeconomic growth, we need to make sure that the economic opportunity and security promised by technological advancement is within reach of all Americans. We need to make sure the prosperity of our future economy is broadly shared.

This is the challenge of achieving inclusive growth, and I do not see how it is to be achieved without a steer from government.

Economic Snapshot

Before we discuss the challenge, let me review where we stand today.

Seven years ago, the worst financial crisis since the Great Depression plunged our economy into recession. Real GDP shrank 4.2 percent between the final quarter of 2007 and the second quarter of 2009. When the President took office in early 2009, the economy was still shedding 750,000 jobs per month. In total, 8.7 million Americans lost their jobs, 5 million Americans lost their homes, and $13 trillion of household wealth was destroyed, wiping out two decades of gains.

The recovery took hold midway through 2009, and since then the economy has expanded at an annual rate of 2.1 percent. Since employment hit bottom in February 2010, the number of jobs has risen by 13 million. During this time, the unemployment rate fell by half, from ten percent to five percent. Today, consumer confidence is near an eight-year high, real hourly earnings are rising—2.6 percent over the past twelve months ending in September—and consensus forecasts expect real GDP growth of 2.6 percent next year.

We have come a long way.

But there are other metrics we must consider as well. The share of the population below the poverty level—14.8 percent in 2014—was unchanged from its 2012 level and remains more than a full percentage point above its level in 2008. The share of workers who are working part-time but would like to be working full-time, at 3.6 percent last month, has come down, but is still high relative to its pre-recession average of 3.0 percent. The labor force participation rate for prime age workers, which stood at 80.8 percent last month, is at its lowest point since 1984. Too many young men are neither working nor enrolled in school—the highest percentage in three decades—and fourteen percent of young adults between 25 and 34 continue to live with their parents. For those who have a job but lack a college degree, average earnings are only $28,000 per year, four thousand dollars less in real terms than they were in 1979.[3]

Thus, despite the progress we have made in terms of the overall economic recovery, not all Americans are sharing in this progress. To do that, we are going to have to make growth more inclusive, which means reducing poverty, increasing youth employment, and raising wages.

Fostering Inclusive Growth

Achieving sustainable growth involves many factors. Economists' models may dwell on labor, capital, and natural resource endowments, but studies comparing growth in different countries show that institutional factors are also critical. Having a fair legal system, appropriate regulation, and sufficient government investment are essential to promoting inclusive growth. It is clear that a vibrant private sector, animated by cooperating economic agents, and thriving commercial activity, is necessary to stimulate growth. But it is also essential to have a meaningful rule of law, including judicial processes that are fair and transparent and accessible.

Financial instability also stifles growth. On the one hand, risk-taking and leverage are vital components of a healthy and growing economy. But, when the rules meant to calibrate safe levels of risk-taking and leverage are set incorrectly, or are not appropriately enforced, these activities can precipitate a collapse that sets the economy back years. After the recent financial crisis, for example, it has taken years for households and businesses to rebuild their balance sheets. The economy experienced trillions of dollars in lost output. Even now, residual effects from households and businesses feeling their future prospects are more uncertain may be weighing on economic activity. In other words, inclusive growth requires prudent financial regulation so that households and businesses can reap the benefits of economic opportunities.

Beyond creating the legal and regulatory preconditions for growth, a distinguishing feature of government is its ability, and indeed its responsibility, to invest in the common good with a long term perspective. We need to design those government institutions that focus on the economy to consider the unquantifiable costs associated with government inaction as well as the unquantifiable benefits that enhance the common good; we need to refine our government institutions to contemplate for the long-term, rather than the short-term. Examples of failures and successes in all these regards come readily to mind: a monetary policy, like the one we had in the 1930s, that is inflexible and unable to take into account changing conditions rather than one that provides needed countercyclical support to economic activity; a fiscal policy that veers toward shutdowns of government rather than long-term planning for a sound fiscal future. The design of how our economic policy levers get pulled by government entities in both the legislative and executive branches, as well as the independent agencies, is relevant to inclusive macroeconomic growth.

More obviously, we set ourselves up for inclusive economic growth when we make long-term investments to build bridges and when we open airports or when we open a new pre-school in an underserved community. We make them when we reform our healthcare system so that millions of Americans have access to regular medical care, enhancing labor mobility and supporting productivity. And we support growth when we reform and safeguard our financial system to reduce the risk of instability so that our economy can operate on a firmer footing and so that, if another financial crisis hits, our economy can withstand the harm.

Responding to the Financial Crisis

The recent economic downturn set growth back, both here and abroad, spurring contractions in private commercial activity around the world.

In the United States, rather than let the economy sink into another Great Depression, the President responded quickly and forcefully to support all segments of the economy. The legislative response was comprehensive and included support for aggregate demand, help for struggling homeowners and the unemployed, measures to realign the financial sector toward confidence-enhancing financial intermediation, assisted by attention on individual consumers and financial markets for consumer financial products.

These expansionary fiscal steps played an important role in shortening the downturn and restoring growth. The American Recovery and Relief Act released hundreds of billions of needed dollars into the economy—supporting the labor market, assisting state and local governments to avoid deeper cutbacks, and investing in new research and development and better infrastructure. The Administration also pursued targeted measures such as investment in the automobile industry, which independent estimates have shown saved more than two and a half million American jobs.[4]

Another essential component of the US response to the economic downturn was the fiscal expansion triggered by the usual counter-cyclical provisions of government programs such as Social Security, unemployment insurance, Medicare, and Medicaid. These core programs acted as automatic stabilizers, and accounted for a meaningful percentage of our fiscal expansion, especially between 2010 and 2012.[5] By enacting the Affordable Care Act in 2010, we added to the set of tools that automatically mitigate a downturn because the ACA protects families' access to health care and cushions their budgets in the face of job and income losses.

Monetary policy as well was appropriately accommodating, and through successive rounds of large scale asset purchases, the recovery gained traction. The effect of monetary policy on inclusive growth is a topic for another day.

Investing for Inclusive Growth

Given where we are now in the recovery, what types of additional investments would promote inclusive growth going forward?

Let's briefly look back to look ahead: Eighty five years ago—also following a financial collapse—John Maynard Keynes wrote an essay entitled "Economic Possibilities for Our Grandchildren." In the face of a massive depression and global retrenchment, Keynes thought that technological change and continued advancement would allow the economy to grow to multiples of its current size, but that that growth would create significant challenges as well.[6]

Aspects of this perspective are still relevant. Technological changes continue to come at a breakneck pace. The internet revolution has brought more than just texts and tweets; it has brought new advances in manufacturing, health sciences, and information services. Computers can now help diagnose an illness, identify and eliminate inefficiency throughout production and distribution processes, and answer complex questions by searching huge stores of data and information. Machines can now communicate performance data instantly, report and assess malfunctions within their own systems, and improve their own energy efficiency. With each advance, it costs less to produce more.

But, there is evidence that this technological change has contributed to rising inequality.[7] Over the last several decades, as the US economy has grown, that growth has not translated into similar gains in middle class incomes. The middle three quintiles of households saw their income grow by 16 percent in real terms between 1979 and 2011. In contrast, earnings for the top ten percent of households have more than doubled over the same period, and market incomes for the top one percent have almost tripled.[8]

At the same time, in the most recent recovery, real median hourly wages declined two percent. Those real wage losses were broadly shared: workers in the bottom 25th percentile saw their earnings decline the most, an average of 3 percent, and those in the 75th percentile saw their earnings decline by 2 percent.[9]

As I've noted before, while more than half of all job losses in the recession were in middle-wage occupations, only one-third of subsequent job growth has been in these areas.[10]

There are several policies, which could help make our growth more inclusive. One which would directly address this, is a proposal to raise the minimum wage from $7.25 per hour to $10.10 per hour. If adopted, this raise would benefit 28 million workers and move our minimum wage closer to its past inflation-adjusted value.[11] Even higher levels, like one proposal in Congress to raise the minimum wage to $12, would have even greater benefits.

If growth is currently being propelled by innovation in the technology sector, then we need to determine how to make the benefits of that growth shared. The car mechanic who fixes my car needs to have the skills to fix a driverless car. The government—if it can be incentivized to balance between the short view and the long view—has the ability and responsibility to support the development of those skills through grants and loans for education and job training. At the same time, government needs to ensure that investment is productive – that schools work to ensure that students don't just enroll, but complete their studies and earn their degrees, that they receive an education that produces meaningful advancement and return on investment.

Conclusion

Choosing investment over austerity was the right choice in the face of the financial crisis, and recognizing the role of public spending in driving inclusive growth remains critical to our future.

If it is true, as some argue, that our economy is on the verge of reaping benefits from technological breakthroughs, then we need to lay the groundwork in the design and activity of our government institutions to determine how everyone in society is to participate fully in this transformation. As we look ahead to the drivers in the next business cycle and beyond we must continue to ask Keynes' question: "What can we reasonably expect the level of our economic life to be a hundred years hence: What are the economic possibilities of our grandchildren?" We must, as Keynes put it, "disembarrass" ourselves "of short views and take wings into the future." I trust that it will be through gatherings such as these that we will continue to explore what these "wings into the future" mean and together chart a path forward toward a more inclusive, and therefore stronger, economy.

Thank you.

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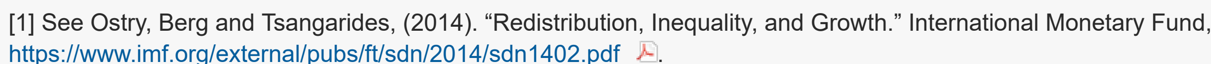
[1] See Ostry, Berg and Tsangarides, (2014). "Redistribution, Inequality, and Growth." International Monetary Fund, https://www.imf.org/external/pubs/ft/sdn/2014/sdn1402.pdf.



[2] See, for example: Berg, Ostry, and Zettelmeyer, (2012). "What Makes Growth Sustained?", Journal of Development Economics. Cingano (2014), "Trends in Income Inequality and its Impact on Economic Growth", OECD Social, Employment and Migration Working Papers, No. 163, OECD Publishing.

[3] Pew Research Center (2014) "Education and Economic Outcomes Among the Young" available at http://www.pewsocialtrends.org/2014/02/11/chapter-1-education-and-economic-outcomes-among-the-young/.

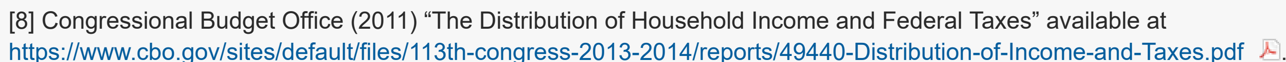
[4] McAlinden and Menk (2013) "The Effect on the U.S. Economy of the Successful Restructuring of General Motors." Center for Automotic Research Research Paper. available at http://www.cargroup.org/?module=Publications&event=View&pubID=102.

[5] The Economic Report of the President (2014), p. 102.

[6] Keynes (1930), "Economic Possibilities for our Grandchildren."

[7] See, for example, Acemoglu and Autor (2011) "Skills, Tasks and Technology: Implications for Employment and Earnings," Handbook of Labor Economics, Volume 4 available at http://www.sciencedirect.com/science/article/pii/S0169721811024105 and Van Reenen (2011) "Wage inequality, technology and trade: 21st century evidence," Labour Economics, Vol 18 Issue 6. Available at http://www.sciencedirect.com/science/article/pii/S0927537111000613.

[8] Congressional Budget Office (2011) "The Distribution of Household Income and Federal Taxes" available at https://www.cbo.gov/sites/default/files/113th-congress-2013-2014/reports/49440-Distribution-of-Income-and-Taxes.pdf.



[9] Current Population Survey and Treasury Staff calculations.

[10] Current Population Survey and Treasury Staff calculations.

[11] Council of Economic Advisers, "The Economic Case for Raising the Minimum Wage," February 12, 2014, available at https://www.whitehouse.gov/sites/default/files/docs/final_min_wage_slides_-_no_embargo.pdf.