REMARKS BY TREASURY SECRETARY TIM GEITHNER
BEFORE THE ECONOMIC CLUB OF NEW YORK

As Prepared for Delivery

NEW YORK - Good evening. It is a pleasure to be back at the New York Economic Club, this great forum for national debate about economic policy, at a moment when we face some fundamental choices about politics and economics.

I left New York for Washington in November 2008 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 Treasury Secretary Henry Paulson, the Federal Reserve, the FDIC, and Congress earlier that fall were essential to stemming the worst of the financial panic, but the economy was deteriorating at an alarming pace.

Our banks and financial markets were still in a state of shock, sucking more oxygen out of the economy, helping push the U.S. and global economies into the worst crisis since the Great Depression.

Businesses were failing at a record rate. Those able to survive were laying off hundreds and hundreds of thousands of workers each month. House prices were falling rapidly and were projected to fall another 30 percent.

As the President prepared to take office in January 2009, it was clear the situation was grave. The President understood that additional actions were urgently needed. He did not sit around hoping the crisis would burn itself out. He was not paralyzed by the complexity of the choices or the terrible politics of the potential solutions.

He decided to act early and forcefully. And his strategy to stabilize and then repair the financial system, combined with the $800 billion of tax cuts and emergency spending in the Recovery Act, the restructuring of the U.S. auto industry, the actions of the Federal Reserve, and the coordinated global rescue he led in the G-20, was very effective in restoring economic growth.

Within three months of 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.

- Over the last two years, the economy has added 3.9 million private sector jobs.
- Growth has been very broad-based, with strength in agriculture, energy, manufacturing, services, and high tech.
- Growth has been led by business investment in equipment and software, which has risen by 33 percent over the past two and a half years, and by exports, which have grown 25 percent in real terms over the same period.
- Productivity has risen at an average annual rate of about 2.25 percent over the same period, a little above its average over the past 30 years.
- Households have made significant progress in reducing excessive burdens of debt, and the personal saving rate stands about 4.5 percent—well above its pre-recession level.
- Leverage in the financial sector has fallen significantly.
- Our fiscal deficits have started to decline as a share of the economy, and we are borrowing less from the rest of the world—our current account deficit is now half the level it was before the crisis relative to GDP.

Overall, the total amount of income and output generated by the American economy is now above the pre-crisis peak.

Millions of Americans now have health care with better coverage because of the Affordable Care Act, and health care costs are rising less rapidly. We are becoming more efficient in how we use energy, more reliant on clean energy sources, and less dependent on foreign sources of energy. And in communities across the country we are seeing promising reforms in education to improve the quality of teaching in science and math and to reduce the cost of and improve access to higher education.

The early shape of the expansion is encouraging for the future trajectory of the economy.

Growth is led by private demand, including strong gains in investment and exports. We have made real progress eliminating the economic imbalances—too much debt among individuals, too much leverage in the financial sector, and too much residential and commercial real estate construction—that created the unsustainable economic growth that preceded the crisis. 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, and is improving more gradually than any of us would like. While there have been some welcome recent signs of stabilization in the housing market, residential construction remains weak. Pension values have recovered much of the losses during the crisis, but house prices in many parts of the country are still very low.

Because their home is most families' single biggest investment, the value of household saving still has not recovered from the crisis.

These are the tragic legacies of the financial crisis. In addition to these legacies, we still face a dangerous and uncertain world, as the rise in oil prices demonstrates. Americans are feeling the effects of higher gas prices. There is no quick and easy fix to this problem, but it reinforces the need for more progress to develop additional sources of energy of all forms.

We have very high rates of poverty, and the median income has not grown in real terms for more than a decade. Our fiscal deficits—though falling—are still swollen by the crisis and the policies of the previous decade. And we face new competitive challenges as other parts of the world are getting better at creating the institutions that are necessary to make economies more productive.

Although the average rate of growth in the first 10 quarters of this recovery is faster than recoveries following the last two recessions, it is slower than previous recoveries from deep recessions. What explains this?

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.

President Obama inherited very large fiscal deficits, swollen to levels well beyond any experienced since World War II. The dramatic erosion in our fiscal position between 2001 and 2008 and size of the projected future deficits made the American people and their elected representatives uneasy about stimulus, and this diminished our capacity to legislate significant additional fiscal actions beyond the Recovery Act. State and local governments had to make severe cuts in employment and services and raise taxes, offsetting part of the substantial stimulus for the economy enacted at the federal level.

In addition, we were hit by a series of blows to growth from outside the United States in 2010 and 2011. The European debt crisis has been very damaging to confidence and growth around the world. Japan's crisis—the earthquake, tsunami, and nuclear plant disaster—hurt manufacturing growth here and around the world. High oil prices put additional pressure on both consumers and businesses across the United States. These three external shocks took about a percentage point off GDP growth in the first half of 2011.

On top of this, the fear of national default in the United States provoked by the debt limit crisis did terrible damage to business and consumer confidence in July and August of 2011. The fall in confidence at that time was quick and brutal, as large as the declines that happen in typical recessions.

These are the most important reasons why the pace of the expansion slowed after the first few quarters of this Administration. Without these challenges, the recovery would have been stronger.

Looking forward, then, what is the right economic strategy for the United States? What mix of investments and reforms will lay a more durable foundation for economic growth and broader economic opportunity?

The three primary economic imperatives we face today are supporting economic growth now, making the right investments and reforms to make our economy more competitive over time, and restoring fiscal sustainability. These imperatives require that that we resolve the fundamental political divide in this country about the appropriate role of government in the economy.

Economic Growth

First, we need to stay intensely focused on strengthening the economy in the short-term.

While growth is gradually getting stronger, we still have very high levels of unemployment, poverty, and other damage left over from the crisis. And we face additional challenges, with Europe confronting a severe and protracted crisis and the world engaged in a critical struggle with Iran, which is adding to upward pressure on oil prices.

For these reasons, we believe there is a compelling need for additional action by Congress to strengthen growth and get more Americans back to work. Congress should act on the President’s proposals to rebuild our nation’s infrastructure, help small businesses, and prevent more layoffs of teachers and first responders.

We need to continue to repair the damage to homeowners and the housing market, by helping Americans refinance their mortgages to take advantage of lower rates, to put more vacant homes into the rental market, and to help families stay in their homes or transition to more affordable options.

The President will continue to use his executive authority to help, for example, by streamlining approvals for new infrastructure projects and regulations which have large costs relative to their benefits. But these measures cannot substitute for action by the Congress.

As I discussed earlier, recoveries that follow financial crises are necessarily more tentative and uneven. The buffers that normally help to cushion families and small businesses from downturns have been run down or exhausted. Confidence, damaged so severely in the crisis, is more fragile—more likely to be hurt disproportionately by new shocks, like we saw in 2010 and 2011. It is going to take years to fully repair the damage caused by this crisis.
This is why it is so important that policy makers continue to work to get the economy growing faster in the short term and not shift prematurely to fiscal restraint or shift the focus of policy entirely to reforms with only long-term payoffs.

Education, Innovation, Investment, and Reform

Our second imperative is building a better foundation for future growth. This crisis came on top of a set of economic challenges that had been building up for years. Among these challenges: a long-term erosion in the relative quality of education for many Americans, a long period of stagnation in the real median income, diminished confidence in the ability of Americans to exceed the economic achievements of their parents, a substantial ongoing shift in the risk and cost of health care and retirement security away from employers and to individuals, poverty rates much higher than in any economy with comparable wealth, and a deteriorating public infrastructure.

These are relatively new challenges for the United States. We were remarkably successful over a long period of time in achieving better outcomes than many other economies on these dimensions of economic success. We were successful in part because we had leaders who put government policy to work in providing health care and retirement security for generations of retiring Americans, universal primary and secondary education, the GI bill, the great public infrastructure projects of Eisenhower and others in the last century, large investments in scientific research, and sensible safeguards over the financial system.

The challenges we face today are more difficult in part because other nations—China, Mexico, and Brazil, for example—are getting better at making market economies grow and develop. Their success, though it brings considerable economic benefits to us, has put a lot of pressure on large parts of the American workforce engaged in making things that other countries are getting better at.

The President's strategy for meeting this challenge is to combine investments with reforms in education, to support innovation, to encourage investment, and to expand exports. These are not challenges the private markets can solve on their own.

In education, the President has proposed a series of reforms to make it more affordable to go to college, to improve the quality of teachers, and to improve training opportunities across all industries where we are short of people with the necessary skills.

The moral case for doing a better job of giving Americans the opportunity to succeed is very compelling. The economic case is just as strong. If more Americans are educated, more will be employed, their collective earnings will be greater, and the overall productivity of the American workforce will be higher.

Greater investments in education should be matched by greater investment in innovation.

The economic case for government support for scientific research rests on the reality that the private innovator and the private investor can't always capture all the full benefits of research and development, so they tend to underinvest.

Since he took office, the President has proposed substantial investments in the National Institutes of Health, the National Science Foundation and the National Institute of Standards and Technology. He has proposed to expand and make permanent the Research and Experimentation tax credit. He has significantly increased government support for innovations in renewable energy.

These investments entail risk. They need to be carefully designed to focus primarily on research, and to maximize the role of the market in determining which technologies should ultimately prevail.

Support for innovation should be combined with strong longer-term programs for promoting public and private investment.

Infrastructure investment is one of the most efficient job-creation programs available. And investment in infrastructure helps increase productivity, increase economic activity, and lower costs for businesses and individuals.

Alongside a strong, multiyear program for public investment in infrastructure, we need to improve the incentives for private investment and to modernize the framework of institutions that help allocate those resources most efficiently.

This requires fundamental reform of our business tax system, which today is a complex and unfair mess of subsidies, temporary and permanent, with a very high statutory rate, and huge differences in the effective tax rates across companies in different industries.

The President proposes to reduce the overall rate to a more competitive level, by reducing or eliminating the corporate subsidies in the tax code, and to strengthen the incentives for creating and building things in the United States. We want a system in which businesses succeed or fail based on the quality of the products they make and the services they provide rather than on the creativity of their tax engineers and lobbyists.

Along with these tax reforms, we need to restore what were the great strengths of our financial system—the highest standards in the world for investor and consumer protection and the most creative and efficient market in the world for channeling savings to finance investment and innovation.

As a result of the reforms this President has put in place, our financial system is now in much stronger shape, with larger cushions of capital against risk and greater transparency over firms and markets, and is now a more resilient source of capital and credit for an expanding economy.

And we need to work to expand trade and exports. Building on the Korea, Columbia, and Panama trade agreements, we are negotiating new agreements to expand exports in Asia. We have been aggressive in using the safeguards within U.S. trade law to protect American companies from unfair trade practices.

Facing rising costs in China and other markets, American manufacturers have started to bring production back to the United States.

We want to see the market share of U.S. companies expand overseas, and we want to see a large part of the growing demand in the emerging market economies met by things we create and build in the United States.

This economic strategy, focused on education, innovation, investment and trade, is the most promising path to greater economic opportunity and higher economic growth.

Fiscal Sustainability

These investments and reforms need to be combined with longer-term reforms to restore fiscal sustainability.

Without more substantial steps to bring down our future deficits, then over the long run the incomes of Americans will rise more slowly and future economic growth will be weaker.

Fiscal reforms are necessary to ensure we have room for the investments we need to improve growth and opportunity in the future. In this new area of more limited resources, we have to be able to target those resources to investments with higher returns. We have to make sure we can meet our changing national security needs in a dangerous and uncertain world. And we have to agree on reforms to make sustainable our commitments to protect health care and retirement security for millions of Americans.

The recent debate about how to restore fiscal sustainability began with the Bowles-Simpson recommendations for a balanced mix of tax increases and spending reductions. And it will likely end there. The debate, when it ultimately concludes, will result in legislation that has roughly the same overall dimensions.

The case for balance should be obvious. To reduce our deficits to a sustainable level over the next decade, we need about $4 trillion in savings, $3 trillion on top of the cuts and caps we negotiated last summer. We propose an overall mix of roughly two and one half dollars in cuts for every dollar in revenue.

The President's plan forces savings across the government in programs we can no longer afford so that we have room for the investments we need. It forces savings in military spending, reallocating funding to better meet future threats. It reduces the rate of growth in healthcare spending, while preserving our commitments to retirement and health care security. And it proposes a modest increase in revenues from the most fortunate Americans.

If you do not raise revenues through tax reform, then you have to find another 1 percent of GDP or roughly 1.5 trillion dollars over 10 years in additional savings from defense, Social Security, Medicare, education, or low-income programs. As each of the bipartisan commissions have concluded, this is hard to do without sacrificing things that are important to large majorities of Americans.

The Republican budget proposals from last year showed quite vividly what it takes to restore fiscal sustainability without raising any revenue through tax reform.

In their budget, in order to preserve the present, historically low effective tax rate for the top 2 percent of Americans and in order to sustain higher levels of defense spending than the Secretary of Defense and the Joint Chiefs believe we need, the Republicans proposed cuts that would dramatically reduce the level of future Medicare benefits, cut even more deeply into the safety net for low-income Americans, and cause further damage to education, infrastructure, and other investments—reducing the total size of what are called discretionary spending programs to 1.6 percent of GDP within 10 years, a level more characteristic of Pakistan or Sub-Saharan Africa.

Some Republicans have proposed capping overall government spending at 20 percent of GDP or lower. Doing so, with 25 million more Americans relying on Medicare and Social Security over the next 15 years, would effectively end the decades-long bipartisan commitment to maintain health care and a basic pension benefit for retiring Americans or leave us unprepared to defend the nation, much less offer Americans a better education.

Remember these fiscal realities when you consider the competing proposals for restoring balance.

We can't cut our way to growth. Severe austerity now would be very damaging.

We can't offer Americans the illusion of tax cuts that pay for themselves. No responsible politician can offer the nation fiscal sustainability through trillions in unpaid-for tax cuts.

We can't go back to pretending deficits don't matter and make expensive commitments we don't pay for.

And if the politics of the moment prevent us from addressing our fiscal challenges before the election, both parties will have to work together very quickly after the election to start to make these tough decisions.

At the end of 2012, we face the simultaneous expiry of tax cuts and large across-the-board cuts in spending that together amount to about 5 percent of GDP. This should provide Washington with a strong incentive to agree on a balanced package of reforms.

We have a set of 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.

And thanks to the actions of this President, alongside the Fed, we are in a much stronger position to meet these challenges than we were three years ago.