New Policies for a New Century:
Recent Economic Actions through the Lens of the New Deal

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It is a pleasure to be with you this afternoon. I am honored to spend this important day with you and your families. I often tell my children that I wish I could live my life over again—not because I want to change things, but because it was so nice the first time around. What you have given me today is a chance to relive one very special day—my graduation from William and Mary some 29 years ago. I am delighted that my father is here to spend the day with me again; and this time, my husband and two of my three children can be here. I am sure that you will appreciate that our third child, who is a sophomore at M.I.T., had to pass on the trip because he has final exams next week.

My years at William and Mary went by so fast. They were a blur of tough classes, good friends, and far too many late night trips to the College Delly. By what I learned in those four years changed my life forever. I am guessing that the same is true for many of you. One amazing class in a new subject, some special professor, an all-night discussion with a roommate, and you finally realize what you love and what you want to be when you grow up.

I often tell students the story of how I became an economist. I was all set to major in government and go to law school. But, as part of the government major, we were required to take a year of economics. After about two weeks—I was hooked. Because of that one requirement and a brilliant introductory economics professor, I found what would become my passion and my life's work. Over my time here, I also got drawn into William and Mary's wonderful history department. I ended up blending the two subjects in my academic research, becoming a specialist in the economic history of the Great Depression.

Whoever would have thought that this specialty would turn out to be so relevant to public policy? But, in the fall of 2008 as our financial markets were rocked by a crisis reminiscent of the 1930s, that knowledge became frighteningly useful. My very first conversation with the President-Elect was about the role of monetary policy in the Great Depression. Almost before I knew it, I moved from studying the Great Depression to helping to prevent a second one. Serving as one of President Obama's economic advisers during this difficult time has been an honor and a challenge above any I could have imagined on the day of my William and Mary graduation.

In my remarks this afternoon, I thought I would return to my academic roots and take a stab at discussing the economic history of the first year of the Obama Administration through the lens of Roosevelt's New Deal. This idea of comparing recent actions with those of the 1930s has been percolating in the back of my mind ever since I walked into the Oval Office one day and the President said, "Christy, you're my Frances Perkins." (For those of you who are not up on your Depression history, Frances Perkins was Roosevelt's secretary of labor and the first woman to serve in the cabinet.)

There are many parallels between President Obama's response to the economic crisis and President Roosevelt's response 75 years earlier. The parallels arose not from a deliberate effort to follow Roosevelt's lead, but from the fact that we were facing similar problems and shared similar core values.

The economic situation facing the new Administration was unlike any we had seen since the Depression. In January 2009, the economy was losing more than three-quarters of a million jobs per month. Output was plummeting and businesses were closing their doors at an alarming rate. The financial system was seized with fear and key flows of credit, the lifeblood of our economy, virtually evaporated. Though not a depression, this truly was a Great Recession.

Like Roosevelt before him, President Obama realized that what we were facing was an all-out crisis that demanded an all-out policy response. In that response, ordinary families had to be the focus of our efforts. No matter where the recession began or what its causes, it quickly ended up on Main Streets throughout the country. Millions of Americans were losing their jobs, their savings, and their homes. We had to formulate policies that would restore their economic security. Like Roosevelt, the new Administration did not have time for ideological battles. The only question about a policy was whether it would put people back to work. That pragmatism and concern for American workers are the defining elements of President Obama's approach to the economy, just as they were of Roosevelt's economic policies.

Although at a philosophical level there are crucial parallels in the responses to the Great Recession and to the Great Depression, at a practical level they are very different. Ours is not the New Deal repeated, but new policies for a new century. Economic analysis has improved markedly in the decades since the Great Depression. In our policies, we sought to learn from past mistakes and apply new thinking. Perhaps most fundamentally, President Obama's economic policies were more market-oriented than

Roosevelt's. In area after area, we sought to strengthen and build on the market system, not override it. Equally important, this time around policymakers resisted pressures to take misguided steps that could ultimately slow the recovery and make the economy more vulnerable.

Let me talk about just a few of the specifics of the recent policy response to the Great Recession and describe their similarities and differences from the New Deal.

The signature action to fight the recession was the American Recovery and Reinvestment Act. This was simply the boldest countercyclical fiscal stimulus in American history. It was unquestionably bolder than the fiscal actions pursued in the New Deal. The Recovery Act included tax cuts and expenditures equal to more than 4 percent of GDP spread over two years. At its largest, the fiscal expansion under Roosevelt was just 1½ percent of GDP. And, that did not occur until the Depression had been going on for six years, and it was counteracted by an equally large fiscal contraction the very next year.

The Recovery Act was also structured differently. It included a large tax cut for working families—something that modern research shows is effective at stimulating spending, but was not understood or tried in Roosevelt's time. So far, more than $200 billion in tax cuts and support payments, such as unemployment insurance, have gone to households. And, we have seen consumer spending and retail sales rise strongly as a result.

The Recovery Act also included numerous tax cuts for businesses that were designed to leverage private spending. For example, the Clean Energy Manufacturing Tax Credit encourages firms to invest in high-tech factories and equipment to make things like solar panels and wind turbines. Over time, the $2.3 billion of government tax credit will be matched by more than $5 billion of private investment spending in this 21st-century industry. In contrast, Roosevelt's New Deal spending was largely direct government investment that did little to try to catalyze private spending.

The Recovery Act, though fundamentally designed to support the economy during the crisis and stimulate employment, was also about reinvestment and leaving the economy healthier than before. More than $90 billion is devoted to clean energy—investments that will help protect the environment, improve national security, and help reinvigorate our manufacturing sector. It also includes unprecedented investments in education and infrastructure, so that we will have the first-class skills and transportation system to be as productive as possible. In this regard, it is similar to the New Deal, which built the dams and irrigation canals that provided the power and water to supply the postwar boom.

A key difference between the financial crisis of the 1930s and the recent crisis was the response of the Federal Reserve. In the early 1930s, the Federal Reserve stood idly by and allowed banking panics to go unchecked. The result was widespread bank failures and devastating declines in the money supply. In the fall of 2008, the Federal Reserve and other financial policymakers responded aggressively to the financial crisis, taking crucial measures to provide liquidity, reassure depositors, and maintain key lending flows. Over those terrifying months following the collapse of Lehman Brothers, the Federal Reserve made the difference between hanging at the edge of a cliff and falling to the bottom of the ravine.

Despite the Federal Reserve's actions, the financial system was tenuous when President Obama took office. Figuring out the best way to stabilize and heal our financial markets was one of our greatest challenges. When the days weren't long enough to design the policy, we started having late-night working dinners at the Treasury, including, I remember, even one on Easter Sunday night. We ultimately decided that the best approach was a combination of transparency within the financial system and policies to stabilize the remainder of the economy.

The stress tests that were conducted in the spring of 2009 struck me as a modern version of Roosevelt's bank holiday. To stop the banking panic underway at the time of his inauguration, Roosevelt shut every bank and conducted a thorough check of the books. Banks were only allowed to reopen after they were deemed safe. This time around, we did a comprehensive review of the nineteen largest financial institutions and pledged to fill any capital shortfalls with government money if needed. But, we were able to do this review without the enormous disruption of shutting down the financial system.

The result of testing the soundness of our financial institutions was extraordinary. Few capital holes were found, which greatly increased confidence. With the disclosure of information and the urging of regulators, the institutions were able to raise billions of dollars of private capital. The stress tests and other financial measures bought time for recovery elsewhere in the economy to take hold. By the summer of last year, output was starting to rise and house prices had nearly stabilized. These developments made financial institutions stronger. The result has been a virtuous cycle of economic recovery aiding financial recovery further aiding economic recovery.

So far, I have discussed how the response to the recent crisis shared some similarities but also had important differences from the New Deal. But perhaps the strongest differences were not in what we did, but in what we did not do. In 1930, Congress passed a large tariff to try to shift demand to American goods. The result was predictable—other countries retaliated, leading to a further decline in our exports. Trade spiraled down to a trickle. In 2009, President Obama led a worldwide effort to keep trade relations open. The result is that as the countries of Asia and elsewhere have recovered strongly, our exports have bounced back faster than any other part of the economy. In this way, international trade has helped to reopen factories and encourage job creation.

Likewise, this time we did not resort to anti-competitive practices. One of the New Deal's wrong turns was the National Industrial Recovery Act, which suspended some of the antitrust laws and allowed firms to collude to raise prices. Most scholars believe this hampered the economy's natural healing mechanisms and so held back the recovery. President Obama, in contrast, sought to maintain healthy competition.

I have been describing the actions we have and have not taken to deal with the economic crisis. But, of course, the history of the Great Recession is not yet over. The economy is unquestionably on the right trajectory. The horrific job losses of last year have finally been replaced by job gains. Recently, we learned that we had added almost 300,000 jobs in April, the most in four years. But, while the economy is recovering, it has not yet recovered. It will take many months of robust job growth to replace the millions of jobs lost in the recession and to bring the unemployment rate down from its painfully high level. For the millions of Americans still waiting to be rehired—still struggling to provide for their families and make their mortgage payments without a job—this remains an economic crisis.

I worry that policymakers may take the return of growth as license to withdraw the support that has been essential to the recovery. That is exactly what happened in 1936 and 1937. President Roosevelt, Congress, and the Federal Reserve switched to fiscal and monetary contraction before the recovery from the Great Depression was complete. The result was a second recession in 1938 that pushed unemployment back up to 18 percent and delayed the return to normal for another three years.

What we need now is not the withdrawal of support, but further targeted actions that will help the private sector come back more strongly. For example, the President wants to create a lending fund to ensure that small businesses can get the credit they need to continue to grow and create jobs. He is also deeply concerned that state and local government budget deficits could lead to a rash of teacher layoffs that would hurt families, students, and the economy. He is anxious to work with Congress on measures that will blunt this destructive headwind to the recovery. We need to take these measures because, as President Roosevelt so wisely observed, "No country, however rich, can afford the waste of its human resources. Demoralization caused by vast unemployment is our greatest extravagance."

Now these further actions will need to be done while being mindful of our long-run fiscal challenges. We unfortunately began the recession and the new Administration with a large budget deficit, and we absolutely must get our fiscal house in order as we return to full employment. But sensible actions to get the unemployment rate down quickly are essential to making sure that high unemployment does not become the new normal. Permanently higher unemployment would not only be devastating to families, it would be destructive to our long-run fiscal health.

Another key piece of unfinished history from the Great Recession is financial regulatory reform. One of the great accomplishments of the New Deal was putting in place a regulatory framework that prevented financial crises for 75 years. And even when a crisis finally came in 2008, key New Deal innovations, such as deposit insurance, helped to prevent the crisis from becoming a cataclysm.

We owe it to ourselves and to future generations to take the trauma of the past two years and channel it into reforms that will help prevent future financial crises. We are so close to a genuinely bipartisan set of sensible new rules of the road for the financial system. We need to see these new rules through to the end—so that your generation and your children's never have to face another Great Recession.

In the policy response to our economic crisis, my generation of policymakers has both learned from the past and sought to improve upon it. We have used all that was learned in the decades since the Great Depression to forge a response that had the greatest chance of healing the economy and leaving it stronger than before. In doing so, I like to think we have taken the best of the New Deal and made it better. The policies couple President Roosevelt's passion for action with President Obama's pragmatism and a core belief in the importance of strengthening private industry, not supplanting it.

Your generation will surely face its own challenges—economic and otherwise. But in talking to many of you and your professors, I feel a wonderful sense of optimism. You are coming to the workforce with a first-rate education and with the values born of hard times. It is no accident that the generation that came of age during the Great Depression fought and won World War II, powered the postwar growth of the United States into an economic superpower, and gave us decades of innovation and stability. They had seen the alternative of economic collapse for themselves and did not want their children to face that again. I am confident that you will have the knowledge and wisdom to do the same for your children. You will be part of the next "Greatest Generation." And I am more proud than I can say to have been with you at this occasion—the end of your time at William and Mary and the beginning of your time leading our wonderful country into the heart of the twenty-first century.

Congratulations and my very best wishes!