Richard W Fisher: Connecting the dots – Texas employment growth; a dissenting vote; and the ugly truth (with reference to P G Wodehouse)

Remarks by Mr Richard W Fisher, President and Chief Executive Officer of the Federal Reserve Bank of Dallas, at the Midland Community Forum, Midland, Texas, 17 August 2011.

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The views expressed by the author do not necessarily reflect official positions of the Federal Reserve System.

Thank you, Kirk [Edwards]. It is great to be here in the cool climes of Midland, Texas.

I appreciate your having walked our friends today through the operations of the Dallas Fed. You know as chairman of our El Paso Branch board that we operate a well-run business as we provide services to the American people that only a central bank can provide, from making sure you have folding money, to lending to our community and regional banks, to supervising and regulating bank and thrift holding companies so as to protect depositors. As president and CEO of the Dallas Fed, I am responsible for a $100 billion bank, accountable to a board of local directors. That board is chaired by Herb Kelleher (you Midlanders will appreciate that Herb's immediate past predecessors were Jim Hackett, president and CEO of Anadarko Petroleum, and Ray Hunt) and consists of eight other citizens of our district; I am also advised by the private-sector directors of the El Paso, San Antonio and Houston branches of our bank.

I am not appointed by a president of the United States or subject to confirmation by the U.S. Senate. I, along with the 11 other Federal Reserve Bank presidents, operate the business of the Federal Reserve as efficiently as any bank in the private sector. And as Kirk mentioned, we make money for the U.S. taxpayer: We returned over $125 billion to the U.S. Treasury in 2009 and 2010. You are looking at one of the few public servants that make money from its operations, rather than just spending taxpayer money. This wouldn't be possible without a first-rate staff, led by my chief operating officer, Helen Holcomb, and the other senior officers that Kirk introduced. I love and admire these folks and too rarely get to single them out for public praise. So, please join me in applauding them.

Two matters

As Kirk has already said much of what I planned to say today about how the Fed works, I would like to address two non-operational matters.

First is the record of job creation in Texas. For obvious reasons, this has become a subject of intense interest to the national media; my staff and I are being hounded by the national press corps for data and commentary. Today I will try to separate fact from fiction, with a heavy focus on the data.

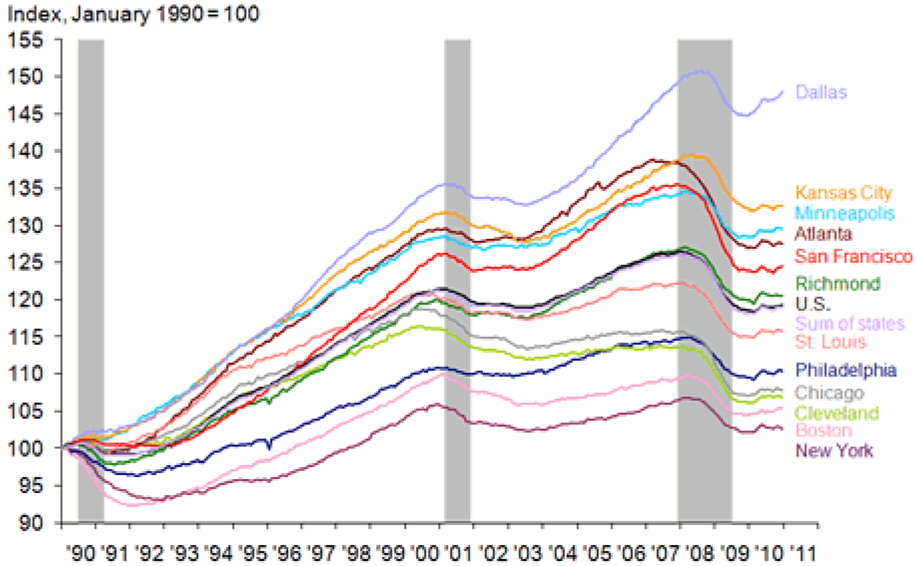
The second matter I wish to address is why I dissented from the consensus at the last meeting of the Federal Open Market Committee (FOMC).

The two would appear to be unrelated, but might well be – though not in a manner that would be readily apparent. I will conclude by trying to connect the two dots.

Texas' record of job creation

Here is a chart that displays nonagricultural employment growth by Federal Reserve Districts over the past 21½ years, using the employment levels of 1990 as a base of 100 and tracing job creation through June.

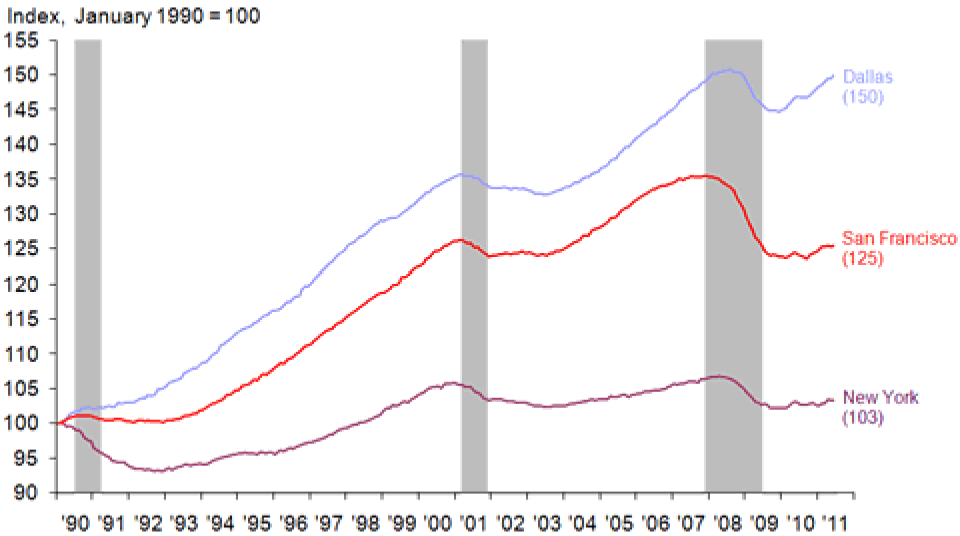
Total Nonagricultural Employment Growth by District



NOTE: Shaded bars indicate U.S. recessions.
SOURCES: Bureau of Labor Statistics; Federal Reserve Bank of Dallas

To illustrate a point, I am going to separate out three districts: the Second, headquartered at the New York Fed and consisting of New York, southwestern Connecticut, Puerto Rico, the U.S. Virgin Islands and a dozen counties in New Jersey; the Eleventh, represented by the Dallas Fed, made up of Texas, the wooded areas of eastern Louisiana and southern New Mexico; and the Twelfth, or the San Francisco Fed's district, which consists of California, eight other states, the Northern Mariana Islands, American Samoa and Guam. The state of New York produces 72 percent of the economic output of the Second District; Texas accounts for 95 percent of the Eleventh District's output; and California accounts for 62 percent of the Twelfth District's output. One might consider this second chart to be an imperfect but reasonable proxy for the employment growth over the past two decades of the three largest states in the country.

Total Nonagricultural Employment Growth by District



NOTE: Shaded bars indicate U.S. recessions.
SOURCES: Bureau of Labor Statistics; Federal Reserve Bank of Dallas.

Like the chart for employment in all 12 of the Fed's districts, the three districts' employment levels are indexed to 100 in 1990. You will see that, at the end of June, the index stands at 150 for the Eleventh District, 125 for the Twelfth and 103 for the Second. Nonagricultural employment growth in Texas has compounded at an annual rate of 1.95 percent over 21½ years; that of California at 0.57 percent; and New York's at 0.19 percent. If you are interested in the output of their workers over this same period, the compound annual growth rate of Texas GDP is 3.6 percent; California's is 2.59 percent; and New York's 2.06 percent.

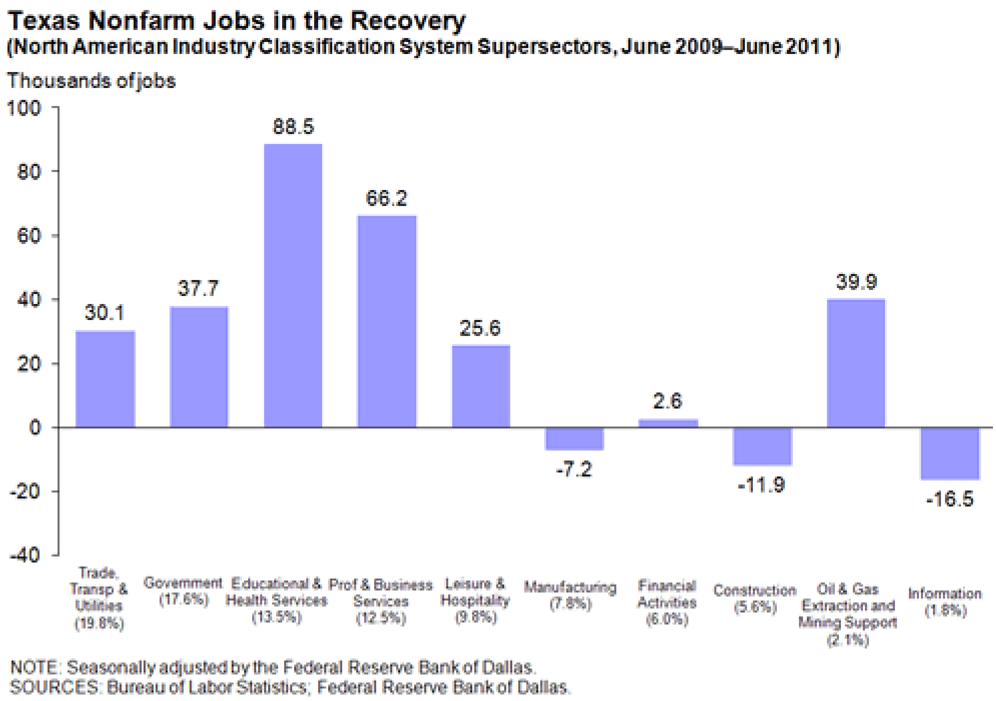
Now, let's look at job creation in Texas since June 2009, the date that the National Bureau of Economic Research (or NBER, the body that "officially" dates when a recession starts and ends) declared the recent economic recession to have ended.

There are several ways to calculate Texas' contribution to national job creation from June 2009 through the end of June 2011. One is to look at the number of jobs created by all 50 states, including those that have lost jobs since the nation's anemic recovery began. Using this metric, through June of this year Texas has accounted for 49.9 percent of net new jobs created in the United States.

Another way to calculate Texas' contribution to job creation is to lop off those states that have continued losing jobs and consider only those that have positive growth in employment these past two years. Using this metric, Texas has accounted for 29.2 percent of job creation since the recession ended.

These are the facts. You may select whichever metric you wish. Regardless, it is reasonable to assume Texas has accounted for a significant amount of the nation's employment growth both over the past 20 years and since the recession officially ended.

This raises the obvious question – what kind of jobs are being created in Texas? Here are two charts that might help you form an opinion.



Jobs and Wages
(Ranked in order from highest job-creating sectors, June 2009–June 2011)

Supersectors	Average Weekly Wage (2010)
Total Texas	$903
Texas government	$845
Texas private	$915
Education and health	$790
Professional & business services	$1,117
Mining	$2,271
Trade, transportation and utilities	$824
Leisure and hospitality	$347
Financial activities	$1,198
Manufacturing	$1,216
Construction	$947
Information	$1,298

SOURCE: Bureau of Labor Statistics.

The first provides a breakdown of employment growth by sector since the recession ended, listing each employment sector by its weight in the employment mix of Texas. The most jobs have been created in the educational and health services sector, which accounts for 13.5 percent of Texas' employment. The second-most jobs have been created in the professional and business services sector, which accounts for 12.5 percent of the Texas workforce. The mining sector, which includes support activities for both mining and oil and gas, employs 2.1 percent (yes, two-point-one percent) of Texas' workers. In the second chart, you will see that these jobs are not low-paying jobs. The average weekly wage in the education and health services sector is $790; in the professional and business services sector it is $1,117; and in the mining sector, the average weekly wage is $2,271. Together these three sectors account for 68 percent of the jobs that have been created in Texas in the past two years.

I should point out that in 2010, 9.5 percent of hourly workers in Texas earned at or below the federal minimum wage, a share that exceeds the national average of 6 percent. California's share was 2 percent and New York's was 6.5 percent. Texas and New York do not have a state minimum wage that is higher than the federal minimum wage.[1] At least 17 states do have minimum wages that are above the federal level of $7.25; California's minimum wage, for example, is $8.

The agricultural sector has a relatively high share of minimum wage workers. Approximately 2 percent of Texas' workers are in the ag sector, whereas 1.1 percent of California's workforce and a mere 0.5 percent of New York's workforce are employed in agriculture. This is true especially in the border area, which also has many migrant workers and where the level of education is relatively low. Finally, Texas has a younger workforce than the nation,

[1] See "Minimum Wage Workers in Texas," Bureau of Labor Statistics, March 28, 2011, http://www.bls.gov/ro6/fax/minwage_tx.htm.

further boosting the share of minimum wage earners in the state. For example, the leisure and hospitality sector employs a disproportionate number of young people, and the average weekly wage in that sector is a very low $347.

So those are the facts. The Dallas Fed will henceforth be providing monthly updates on employment in Texas through our website at www.dallasfed.org. We hope it will be a useful tool for everyone ranging from columnists who write for the *New York Times* to the pundits who provide commentary for Fox News, as well as serious economists.

FOMC decision

Now to the second matter I wish to discuss with you today: my decision to dissent from the commitment of the majority of my colleagues on the FOMC in their decision to hold the base interest rate for interbank lending – the fed funds rate, the anchor of the yield curve – at its current level well into 2013.

I have posited both within the FOMC and publicly for some time that there is abundant liquidity available to finance economic expansion and job creation in America. The banking system is awash with liquidity. It is a rare day when the discount windows – the lending facilities of the 12 Federal Reserve banks – experience significant activity. Domestic banks are flush; they have on deposit at the 12 Federal Reserve banks some $1.6 trillion in excess reserves, earning a mere 25 basis points – a quarter of 1 percent per annum – rather than earning significantly higher interest rates from making loans to operating businesses. These excess bank reserves are waiting on the sidelines to be lent to businesses. Nondepository financial firms – private equity funds and the like – have substantial amounts of investable cash at their disposal. U.S. corporations are sitting on an abundance of cash – some estimate excess working capital on publicly traded corporations' books exceeds $1 trillion – well above their working capital needs. Nonpublicly held businesses that are creditworthy have increasing access to bank credit at historically low nominal rates.

I have said many times that through the initiatives we took to counter the crisis of 2008–09, and the dramatic extension of the balance sheet that ensued, the Fed has refilled the tanks needed to fuel economic expansion and domestic job creation. Though I questioned the efficacy of the expansion of our balance sheet through the purchase of Treasury securities known as "QE2," I have come to expect that the Federal Open Market Committee would continue to anchor the base lending rate at current levels and also maintain our abnormally large balance sheet, now with footings of almost $2.9 trillion, for "an extended period."

I do not believe it wise to commit to more than that, or to signal further accommodation, when the cheap and abundant liquidity we have made available is presently lying fallow, and when the velocity of money remains so subdued as to be practically comatose. At the FOMC meeting, the committee announced that it "currently anticipates that economic conditions … are likely to warrant exceptionally low levels for the federal funds rate at least through mid-2013." In monetary parlance, that is language designed to signal that we are on hold until then.

I voted against that commitment-cum-signal. In the press' reporting of my dissenting vote and those of the other two members of the FOMC who voted against that commitment – Mr. Kocherlakota, my counterpart from the Minneapolis Fed, and Mr. Plosser, my counterpart from Philadelphia – there was substantial speculation as to the reasons for our dissent. I will let my other two colleagues speak for themselves; I can only speak for myself. Let me make clear why I was opposed to freezing the fed funds rate for two years.

First, in reporting my views to the committee, I noted my concern for the fragility of the U.S. economy and weak job creation. It might be noted by the press here today that although I am constantly preoccupied with price stability – in the aviary of central bankers, I am known as a "hawk" on inflation – I did not voice concern for the prospect of inflationary pressures in the foreseeable future. Indeed, the Dallas Fed's trimmed mean analysis of the inflationary developments in June indicated that the trimmed mean PCE turned in its softest reading of the year. The ***trimmed mean analysis*** we do at the Dallas Fed focuses on the price movements of personal consumption expenditures. It is an analysis that tracks the price movements of 178 items that people actually buy, such as beer, haircuts, shoe repair, food and energy prices. In June, the trimmed mean came in at an annualized rate of 1.3 percent, versus 2.1 percent for the first five months of the year. The 12-month rate was 1.5 percent.

My concern is not with immediate inflationary pressures. Core producer prices are still increasing at a higher than desirable rate. But I have suggested to my colleagues that while many companies have begun and will likely continue to raise prices to counter rising costs that derive from a range of factors – including the run-up of commodity prices in 2010 and increases in the costs of production in China – weak demand is beginning to temper the ability of providers of goods and services to significantly raise prices to consumers.

My concern is with the transmission mechanism for activating the use of the liquidity we have created, which remains on the sidelines of the economy. I posit that nonmonetary factors, not monetary policy, are retarding the willingness and ability of job creators to put to work the liquidity that we have provided.

I have spoken to this many times in public. Those with the capacity to hire American workers – small businesses as well as large, publicly traded or private – are immobilized. Not because they lack entrepreneurial zeal or do not wish to grow; not because they can't access cheap and available credit. Rather, they simply cannot budget or manage for the uncertainty of fiscal and regulatory policy. In an environment where they are already uncertain of potential growth in demand for their goods and services and have yet to see a significant pickup in top-line revenue, there is palpable angst surrounding the cost of doing business. According to my business contacts, the opera buffa of the debt ceiling negotiations compounded this uncertainty, leaving business decisionmakers frozen in their tracks.

I would suggest that unless you were on another planet, no consumer with access to a television, radio or the Internet could have escaped hearing their president, senators and their congressperson telling them the sky was falling. With the leadership of the nation – Republicans and Democrats alike – and every talking head in the media making clear hour after hour, day after day in the run-up to Aug. 2 that a financial disaster was lurking around the corner, it does not take much imagination to envision consumers deciding to forego or delay some discretionary expenditure they had planned. Instead, they might well be inclined to hunker down to weather the perfect storm they were being warned was rapidly approaching. Watching the drama as it unfolded, I could imagine consumers turning to each other in millions of households, saying: "Honey, we need to cancel that trip we were planning and that gizmo or service we wanted to buy. We better save more and spend less." Small wonder that, following the somewhat encouraging retail activity reported in July, the Michigan survey measure of consumer sentiment released just recently had a distinctly sour tone.

Importantly, from a business operator's perspective, nothing was clarified, except that there will be undefined change in taxes, spending and subsidies and other fiscal incentives or disincentives. The message was simply that some combination of revenue enhancement and spending growth cutbacks will take place. The particulars are left to one's imagination and the outcome of deliberations among 12 members of the Legislature.

Now, put yourself in the shoes of a business operator. On the revenue side, you have yet to see a robust recovery in demand; growing your top-line revenue is vexing. You have been driving profits or just maintaining your margins through cost reduction and achieving maximum operating efficiency. You have money in your pocket or a banker increasingly willing to give you credit if and when you decide to expand. But you have no idea where the government will be cutting back on spending, what measures will be taken on the taxation front and how all this will affect your cost structure or customer base. Your most likely reaction is to cross your arms, plant your feet and say: "Show me. I am not going to hire new workers or build a new plant until I have been shown what will come out of this agreement."

Moreover, you might now say to yourself, “I understand from the Federal Reserve that I don’t have to worry about the cost of borrowing for another two years. Given that I don’t know how I am going to be hit by whatever new initiatives the Congress will come up with, but I do know that credit will remain cheap through the next election, what incentive do I have to invest and expand now? Why shouldn’t I wait until the sky is clear?”

Based on past behavior of fiscal policy makers, businesses understandably regard the debt ceiling agreement and the political outcome of negotiations between Congress and the president with the suspicion akin to how the British humorist P.G. Wodehouse regarded his aunts: “It is no use telling me there are bad aunts and good aunts,” he wrote. “At the core they are all alike. Sooner or later, out pops the cloven hoof.”[2]

It will be devilishly difficult for businesses to commit to adding significantly to their head count or to meaningful capital expansion in the United States until clarity is achieved on the particulars of how Congress will bend the curve of deficit and debt expansion and the “cloven hooves” are revealed. No amount of monetary accommodation can substitute for that needed clarity. In fact, it can only make it worse if business comes to suspect that the central bank is laying the groundwork for eventually inflating our way out of our fiscal predicament rather than staying above the political fray – thus creating another tranche of uncertainty.

In the interest of full disclosure, I should add that I was also concerned that just by tweaking the language the way the committee did, our action might be interpreted as encouraging the view that there is an FOMC so-called “Bernanke put” that would be too easily activated in response to a reversal in the financial markets. For those of you unfamiliar with the expression “Bernanke put,” or more generally, a “central bank put,” this term refers to the concept that a central bank will allow the stock market to rise significantly without tightening monetary policy, but will ease monetary policy whenever there is a stock market “correction.” Given the extent of the drop in the stock market leading up to and following Standard & Poor’s downgrade of U.S. debt, combined with the FOMC’s commitment to hold short-term rates near zero until mid-year 2013, some cynical observers might interpret such a policy action as a “Bernanke put.” My long-standing belief is that the Federal Reserve should never enact such asymmetric policies to protect stock market traders and investors. I believe my FOMC colleagues share this view.

Connecting the dots

Now, how do you connect the dots between Texas’ record of economic growth and my dissenting vote?

Despite the fact that Texas has severely limited social services and an education system that faces great challenges, people and businesses have been picking up stakes and moving to Texas in significant numbers over a prolonged period.[3] It should be noted that in the last census, Texas gained population and congressional seats, while California’s population growth and congressional representation was static and New York’s was diminished. Jobs have been created for American workers in Texas in several different sectors, not just in the oil and gas and mining sectors. People have taken those jobs of their own free will, even though the jobs may not measure up to the compensation levels everyone would like. And yet Texas, like all states, is subject to the same monetary policy as all the rest: We have the same interest rates and access to capital as the residents of any of the other 49 states, for the Federal Reserve conducts monetary policy and regulates financial institutions under its

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2 *The Code of the Woosters*, by P.G. Wodehouse, New York: Doubleday, Doran, 1938.

3 See “Texas: What Makes Us Exceptional? Where Are We Vulnerable?,” speech by Richard W. Fisher before the 2010 Pre-Session Legislative Conference, Dec. 2, 2010.

purview for the nation at large. From this, I draw the conclusion that private sector capital and jobs will go to where taxes and spending and regulatory policy are most conducive to growth.

Therein lies a lesson for our fiscal policy makers as they grapple with their monumental task of reconfiguring fiscal policy and eliminating the prevailing uncertainty about their remedy.

We live in a world that, through steadfast sacrifice of the American treasure and with blood and capable diplomacy, won the Cold War, induced the Chinese to pull back the Bamboo Curtain and opened up the majority of the world to once unimaginable economic opportunity. China, the rest of Southeast Asia, Eastern Europe, India, most of Latin America and significant swathes of Africa are eager to improve the lot of their people through full participation in the global economy. In doing so, they have become serious competitors for capital, including that plentiful and affordable capital we at the Federal Reserve have created.

In a cyberized, globalized world, those with the means to create jobs will gravitate to those places that provide the best prospect for a return on the investment of the abundant capital on business' balance sheets or available to them in the marketplace or from eager bankers. Just as many people and firms within the United States have relocated to Texas from other states, investment will flow to countries anywhere in the world where it is most welcome.

Our fiscal authorities must not only figure out the way to contain the nation's runaway deficits and public debt accumulation, but they must do so in a manner that is competitive with others who seek access to our money, and do so in a manner that does not pull the rug out from under the meager recovery we are experiencing. The Committee of 12 and the president have an awesome task. Essentially, they must reboot our entire system of economic incentives and come forward with an updated tax and spending and regulatory regime that incentivizes businesses to invest in the United States and create jobs for American workers rather than gravitate to foreign shores. And they must do so in a manner that avoids engaging in a race to the bottom, but rather, puts us back on the path to ever higher achievement of prosperity.

The sooner they get on it, the better. Uncertainty is corrosive; it is hurting job creation and capital expansion when we need it most. As Margaret Thatcher would say: "Don't dawdle. And don't go wobbly on us, Congress." Monetary policy cannot substitute for what you must get on with doing. Get on with your job.

The ugly truth

I think I have made it pretty clear today that I believe what is restraining our economy is not monetary policy but fiscal misfeasance in Washington. We elect our national leaders to safeguard our country. An integral part of that consists of safeguarding the nation's fiscal probity. Pointing fingers at the Fed only diminishes credibility – the ugly truth is that the problem lies not with monetary policy but in the need to construct a modern, appropriate set of fiscal and regulatory levers and pulleys to better incentivize the private sector to channel money into productive use in expanding our economy and enriching our people. Only Congress, working together with the president, has the power to write the rules and provide the incentives to correct the course of the great ship we know and love as America. I hope you, as the voters who put them in office, will demand no less of them.

Thank you. I will be happy to do my level best to avoid answering any questions you might have.