Alan Greenspan: Receipt of the Truman medal for economic policy

Remarks by Alan Greenspan, Chairman of the Board of Governors of the US Federal Reserve System, at the Truman Medal Award and Economics Conference, Kansas City, 26 October 2005.

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I am pleased to be here today and to have the honor of being the first recipient of the Truman Medal for Economic Policy. I want to thank the Truman Library Institute for sponsoring this award and supporting the Truman Library. The Truman Presidential Library performs an important public service by promoting scholarly work and presenting the life and times of President Truman, thereby providing us all with a better basis for addressing today's challenges.

The Truman Administration marked a time of dramatic change as World War II ended and the architecture of the post-war era was put in place. In the words of Truman biographer David McCullough, that era was "the watershed time of the century and Truman stands forth now--especially now in the aftermath of the Cold War--as a figure of utmost importance."[1]

Within the realm of economic policy, part of Truman's importance derives from the fact that several key new governmental structures were established during his Administration. Among these were the Council of Economic Advisers (CEA) and the Joint Economic Committee of the Congress (JEC). These organizations were established by the Employment Act of 1946, signed by President Truman on February 20. In my remarks today, I will discuss the origins of the Employment Act and the history of the CEA and will also reflect on my time at the Council.

Two ingredients seem to have been essential precursors of the Employment Act. The first was a deep concern that the problem of peacetime unemployment had not been solved. Although employment roared back during the war, the memory of the Great Depression was quite fresh, and considerable uncertainty attended the economic outlook. Put simply, many feared that the economy would slip back into depression. The second element was the economic thinking of John Maynard Keynes. Keynes argued that the economy could get stuck at a point of inadequate aggregate demand and high unemployment and that deficit spending by the government could provide the stimulus needed to reach and sustain a better equilibrium.

President Truman's memoirs make clear that both of these strands--the fear of depression and the view that the government has a role to play in economic stabilization--influenced his request to the Congress for full employment legislation in the fall of 1945.[2] Of course, the legislative process is full of compromise and can lead to unexpected outcomes, and according to some observers, the creation of the CEA by the Employment Act was just such an event. According to Herb Stein's history of the CEA--he was Chairman during the Nixon Administration--the CEA was an accident that did not need to have happened.[3] Early drafts of the Employment Act enshrined very specific, and simple-minded, Keynesian policy prescriptions that worked backward from estimates of full employment to specific numerical targets for investment and fiscal policy. Not surprisingly, many in the Congress opposed such provisions. In the end, the numerical targets were struck from the act, and "full employment" became "maximum employment, production, and purchasing power." As Stein tells the story, the bill was seen as lacking in substance at this point. That gap was filled by creating new processes and institutions--hence, the CEA, the annual *Economic Report of the President*, and the JEC. This outcome was indeed fortuitous.

The CEA consists of a Chairman and two other members, all of whom are appointed by the President and confirmed by the Senate. In its early years during the Truman Administration, the CEA was not without controversy. The two best-known members of the first CEA--the Chairman, Edwin Nourse, and Leon Keyserling--clashed repeatedly about whether the agency should just provide private advice to

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1 See David McCullough, *Truman* (New York: Simon and Schuster, 1992).

2 Harry S. Truman, *Year of Decisions* (New York: Doubleday, 1955), pp. 491-94.

3 Herbert Stein "Fifty Years of the Council of Economic Advisers," in *What I Think: Essays on Economics, Politics, and Life* (Washington, D.C.: AEI Press, 1998).

the President or should be a public advocate for the Administration's economic program. More broadly, however, the Truman CEA marked a transition from a relatively ad hoc style of economic policy making to a more institutionalized and focused process. The groundwork was laid for an agency that would make lasting contributions to economic policy making.

These contributions have taken several forms. Over the years, the CEA has provided objective and professional economic advice at the highest levels in the White House. Remarkably, this tiny agency has asserted its influence even while filling most of its positions with economists who were on temporary leave from other professional activities. A hallmark of the ethos of the CEA is the pride that its staff members take in providing objective analysis. That devotion first and foremost to objectivity has led to the interesting phenomenon that, while the overall economic views of Administrations have swung widely, the policy advice given by their successive CEAs has undergone far smaller swings.

Even though the average tenure among members of the Council and staff economists is short--often just a year or two--there have been some sources of continuity. Perhaps the most remarkable element of continuity has been the service of Catherine Furlong, better known to her friends and colleagues as "Kitty." She recently retired after fifty-four years of service, with her tenure extending back to the earliest years of the agency during the Truman Administration. Among other important roles, Kitty was the fact-checker-in-chief at the CEA--an important position when the stock of the agency depends critically on its credibility. For Presidents on down, having your material fact-checked by Kitty meant that you were going to meet the gold standard of credibility. The type of continuity she provided is rare in the government and contributed to the CEA's success over the years.

Among its contributions, the CEA serves as an in-house research organization that can assemble, analyze, and present information relevant to an economic decision. Many of the members and staff come from research backgrounds and are uniquely positioned to play this role in the Administration. Because the CEA has retained its small size over the years, it can be quick and nimble in ways that are difficult for some larger agencies.

Moreover, because the CEA is viewed as a neutral agency without ties to any particular constituency, the CEA often has played an important role on interagency committees and working groups, ensuring that economic insights are heard at debates about key issues.

Along those lines, perhaps the most important role of the CEA has been to scuttle many of the more adventuresome ideas that inevitably bubble up through the machinery of government. In every Administration, all sorts of ideas for changes in spending, tax, and regulatory policy are developed by one agency or another and then circulated within the Administration. A few of these ideas are genuinely good. However, many of them are ill-advised and not well thought through and fail miserably the test of benefits exceeding costs. Often, it falls to the CEA to point out the flaws and derail these ideas. This role of the CEA is wholly unheralded--after all, who hears about the idea that never came to fruition--but it serves as an important check in the policymaking process.

As I mentioned, economic thinking at the CEA has been marked by important continuities. Nevertheless, the evolution of thinking at the CEA over the years has reflected the economic challenges of each era as well as continuing developments in economic research. The ideas of Keynesian stabilization that were an important motivation for the Employment Act reached their zenith during the Kennedy Administration. Since that time, the CEA has followed the economics profession away from a belief that fiscal policy can or should fine-tune the level of aggregate demand.

During the 1960s and 1970s, the economy was confronted by rising inflation pressures, a series of energy shocks, and a slowdown in the underlying pace of productivity growth. At the same time, there was considerable ferment within the economics profession, as prevailing views of the inflation process and of the government's role in economic stabilization were challenged. Successive CEAs agonized over these issues and over whether to use the new ideas emerging from the academy and, if so, how.

Since the 1980s, the CEA has focused increasingly on understanding the sources of economic growth and the supply side of the economy. The focus on international issues, too, has intensified as trade and international financial flows between the United States and other countries have grown. I should also note that, despite its overtly macroeconomic origins, the CEA has expanded successfully into the realm of microeconomics, particularly issues related to regulatory policy and market structure.

Notwithstanding these changes in focus over time, there have been important intellectual continuities. In particular, a common theme throughout the CEA's history has been a belief in the importance of market forces, and this belief stands as an important legacy of the CEA.

Of course, as chairman of the Council during President Ford's Administration, I was close to some of these debates and decisions. I was recruited to serve as chairman of the Council by President Nixon's economic team. As it turned out, I was before the Senate Banking Committee for confirmation the day that President Nixon resigned. President Ford quickly renominated me, and I began work at the CEA in September 1974. I was privileged to serve President Ford, and found him to be a very effective leader. Parenthetically, there are some interesting parallels between President Ford and President Truman. Both were serving as Vice President and became President rather unexpectedly; both men had had extensive legislative and budget experience in the Congress; and both men had belief systems anchored by strong core values.

During my years at the CEA, the focus of the economic policy team underwent a number of twists and turns. In the fall of 1974, inflation was the critical issue. Some months later, it became apparent that a recession was under way, and attention turned toward policies for recovery. Subsequently, the focus on inflation returned. It was a challenging time, and we did not solve all the problems that we confronted. Nevertheless, I found my time there quite rewarding and benefited greatly from my work with the other members and with the very highly skilled staff. I could recount much about the work of the CEA at that time, but I will only highlight three themes that recurred during my tenure.

First, economic modeling is as much art as science. Economic policy makers face enormous uncertainty. Economic models provide a set of useful tools to frame future outcomes; but as we were reminded repeatedly during our efforts to forecast the economy in 1974 and 1975, models can go off track in myriad ways. Objective and thorough analysis, as is the norm at the CEA, is the most effective counterweight to this challenge.

Second, high-quality and timely data are crucial inputs to the process of making economic policy. Because we had access to high-frequency data, we were able to see that the sharp further downturn in the economy in early 1975 reflected largely an inventory correction and that final demand was holding up. That insight provided support for the view that, so long as final demand was sustained, recovery was imminent. As it turned out, that was the right call.

Finally, as hard as this can be to achieve, economic policy should take the long view. Although pressures to use the government's tools of economic management to achieve one or another short-term aim are always present, the tools of government are, in fact, most appropriately used to create an environment in which private economic activity can flourish over the longer run.

As I indicated, the focus of the CEA has changed over the years as the economic challenges facing the nation have changed. Through all this history, the CEA has, in most cases, provided the President with the best economic advice available at the time and has, crucially, been a consistent advocate for the importance of market forces. Whether or not all of those involved in passing the Employment Act and creating the CEA realized it at the time, they created an enduring agency that has played a significant role in economic policy making. President Truman apparently had an inkling. He noted in his memoirs:

> Occasionally, as we pore through the pages of history, we are struck by the fact that some incident, little noted at the time, profoundly affects the whole subsequent course of events. I venture the prediction that history, someday, will so record the enactment of the Employment Act.

I concur with President Truman's assessment. Indeed, based on a cost-benefit test, surely the CEA must be one of the most successful government agencies in history.