GRADING THE ECONOMY

Nate Silver says we—liberals—are not celebrating the Administration's economic successes enough.

> And yet, the [financial reform] bill has received scant praise, and indeed very little attention, in liberal circles. Some of this is based on legitimate concerns that the bill did not go far enough — although it does do quite a lot. Some of it is based on a not-unreasonable assumption that although the House bill is fairly adequate, it is likely to be significantly watered-down by the Senate.
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> Even so, there seems to be extreme reluctance among the left, and particularly the online left, to praise any economic successes achieved by the Congressional Democrats and the White House.

Now, here's how Nate himself judges the Administration's accomplishments.

> **Putting out the fire.** On the first imperative — that of averting a meltdown — I would give the Democrats high marks. Not only did we avoid Armageddon, but we did so with relatively little contribution — "only" about $42 billion — from future taxpayers. At the time these interventions were undertaken, this would have been regarded as an exceptionally good outcome. And with the advantage of hindsight, objective evaluations of TARP tend to be similarly rosy, including that from the very liberal (and smart) economist Elizabeth Warren, who chaired a Senate panel on the subject.
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> The recovery. As to the second objective, we have a split between the performance of the labor market, and

> that of other economic indicators. Back in February, when the stimulus was passed, the Wall Street Journal forecasting panel projected 3Q GDP growth of 0.7 percent; the actual figure, after revision, was 2.9 percent. They predicted 1.9 percent growth in the 4Q; the actual figure is likely to be closer to 4.0. On the other hand, they projected December unemployment to be 8.8 percent; November's figure was 10.0 and December's is likely to come in somewhere close to that.
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> Certainly, I think that the stimulus package ought to have been both larger and more focused on infrastructure-type programs that would have led to more direct creation of jobs. The stimulus, however, passed the Senate with just one extra vote (the tally was 61-37), suggesting that there may have been very little additional wiggle room. I think that is actually somewhat too narrow a reading of the political conditions in place at the time; more persuasion on the part of the White House (which was very popular then) might have moved the needle some, as might have the tactical gambit of throwing out a higher number rather than counting on the Congress to do the heavy lifting. Nevertheless, there probably wasn't *much* room for improvement; an extra $100 or $150 billion, perhaps, which if directed toward infrastructure might have led to an unemployment rate that was 0.3 to 0.4 points lower than it is now. Moreover, some of the shortfall has been made up for with post-facto mini-stimuli like cash-for-clunkers and the unemployment benefits extension, and the forthcoming jobs bill.
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> In any event, such as it was, you have a stimulus that has tended to exceed expectations in terms of GDP growth. It

would appear, on the other hand, to have fallen short in terms of jobs growth. But that conclusion is debatable. If the CBO's estimates are to be believed — that the stimulus has reduced the unemployment rate by 0.4 to 1.1 percent — that would be in line with both the White House's estimates (which had forecast an 0.7 percent improvement in unemployment through the 3Q as a result of the stimulus) and the CBO's expectations in March.

Yes, the *systemic* conditions in the job market have been somewhat worse than most (though not all) private forecasters anticipated, and much worse than the White House seemed to anticipate. Certainly you can fault them for failing to frame the public's expectations adequately, and also for aiming for too small a stimulus — although, again, it's not clear that aiming higher would have substantially improved what actually came out of the Congress. But subject to those admonitions, the White House's efforts at facilitating a recovery would seem to deserve a grade of somewhere between adequate and good, on the basis of the objective evidence.

Financial sector reform. Here, there is no grade that can be given other than incomplete — the Congress has yet to pass any substantial regulatory reform effort, and the systemic risk in the financial sector very much remains and could cascade at any time. Nevertheless, the bill that the House just passed has been a reasonably good start. The White House and the Senate will lay their cards on the table sometime early next year. Perhaps the most robust criticism of the White House is that it should have tackled regulatory reform before health care — a course of action that

> most liberals would have been very upset about.

Now, unlike me, Nate has a degree in economics, so maybe I'll be busted for making the following observation, but it seems to me Nate is measuring the Administration's economic success by measuring a collection of symptoms: Meltdown, B+; GDP, A-; Jobs, D; Financial sector reform, INC.

My thinking on the issue is somewhat different. Our finance system melted down about 15 months ago, bringing down the rest of the economy, and how have we responded to it? As I understand it, we have simply addressed symptoms, while showing a fundamental unwillingness to address the larger imbalance in our economy. So my thinking would go something like this:

Putting out the fire. Yes, the Obama Administration (and the Bush Administration) prevented a meltdown of our financial system. But they did almost nothing to make sure that their efforts to prevent that meltdown at the same time prevented the follow-on effects; they did almost nothing to make sure that–after spending billions–the financial system would still serve the function that was the underlying rationale for saving it for in the first place. That is, we "had" to save the financial system because it provides capital that feeds the productive parts of our economy. But Geithner and Bernanke et al focused largely on whether the system remained intact, and not whether appropriate loans were going to to appropriate borrowers (which is one of several reasons why the auto industry proceeded to meltdown). We saved the financial system as a system, but did nothing to save the financial system as provider of capital.

In fact, I'd say that a key mistake that Geithner and Bernanke made was in reifying the role of the Masters of the Universe, rather than using the rescue to forever deprive the MOTUs of their claim to being MOTUs. AIG was different,

Rattner said, because it operated at the "nerve center of our financial system," and as such, it couldn't be put through a bankruptcy process that would allow the government–in funding that bankruptcy–to demand concessions from all parties involved. So rather than saying, "AIG is a company offering some valuable insurance products attached to a giant cancer that is not only unnecessary, but which has infected the nervous system of our economy, and therefore we must excise it," the government said, "AIG is our central nervous system and we can't do without it."

The recovery. And once you reinforce the false claim that a bunch of common banksters are MOTUs, then you trap yourself into the problem that Nate describes, in which GDP performs better than expected, but, even with a sizable but too small stimulus, jobs perform far worse. That, to me, is a testament to the fact that our GDP is still measuring all the unproductive foaming that our economy has relied on for the last twenty years, and that as GDP recovers without creating jobs, the focus on that foam will continue to get worse.

We discovered that our emphasis on finance and bubbles was unsustainable. But we did nothing to change that emphasis.

Two policy approaches embody this to me.

First, the Democratic Congress is getting further away from being able to pass cramdown legislation. In March 234 Reps voted to support cramdown; on Friday just 188 did. It seems to me there are two main arguments to vote against letting bankruptcy judges redefine the terms of a mortgage–including lowering interest rates and/or principal. One is the belief that people who bought into these mortgages made poor economic decisions and therefore must pay the price. This suggests, of course, that the moral hazard of bailing out individual homeowners is bigger than the moral hazard of bailing out AIG and Goldman Sachs and Citi. It also pretends that the mortgage industry wasn't inflating

appraisals to allow for increased profits at every level of the mortgage bubble. It pretends, too, that banks didn't use asymmetrical information to push consumers into products they had no business being in. In other words, this logic assumes all the blame belongs on the homeowner, and none on the mortgage industry, so as a result the homeowners must pay all of the price.

The other argument, though, is that banks—particularly in their still-fragile condition—cannot afford to write down the principal on these mortgages, so the homeowners are just going to have to suck it up. (This ignores, of course, that the banks will lose just as much putting the properties through foreclosure, but whatever.) In other words, one of the reasons to vote against cramdown (aside from the lobbyist cash involved) is because the banking industry—and its current practices—must be protected, because we have to ensure the banking industry remains profitable.

There's a similar logic to the health care debate. What the Senate bill, especially, has done is craft a way to give health care to a lot more Americans without touching the profitability of the health care industry. There has been no discussion of whether, by tolerating—or even encouraging—exorbitant profits at each stage of the health care delivery process, the legislation will ensure that other productive parts of our economy will suffocate under the much greater health care costs they pay in the US than they would in any other country. Instead, people like Mary Landrieu and Joe Lieberman insist we have to do it this way—we can't have a public option—to ensure that the health care industry remains one-sixth of our economy, if not becomes a larger share of our total economy.

Congress and the Administration have—at every stage of the game—worked to maintain the balance between FIRE, health care, defense, and the rest of the economy remains what it is if not becomes

even more whacked out. The only segment the Democrats have tried to change—with investments far too small to do the job—is in green industries.

So Democrats are not really trying to change the problem that we don't make anything anymore. Even in an area—pharmaceuticals—where we do export to the rest of the world, they're sustaining a system in which American consumers pay more of the drug development costs, and to hell with whether that policy will make it much less likely that that American consumer will have a job that pays enough to pay for those drugs.

And the result, it seems to me, is the condition Nate describes, in which on paper, measuring GDP, our economy is turning around. But in which the balance within the economy leaves average American further and further behind those making profits from a resurgent bubble economy.

Financial sector reform. Which all influences the way I look at financial sector reform. Had the financial sector not been treated like "the nerve center" of the economy, it would have had reform forced on it in September 2008, along with taxpayer monies. Now, frankly, the fact that financial service reform is being driven, slowly, by Congress will result in a better outcome than if Hank Paulson had (ha!) imposed reform along with the bailout. Disempowering the Fed by having a group of entities serve as the regulator and by auditing it will slowly begin to change the balance of power within our economy (though the notion that we ought to have banks that are banks and brokers that are brokers and insurers that are insurers is still a quaint old-fashioned idea).

But the fact that reform is discussed in the absence of the larger question about the structure of our economy—about what Americans will make in the future to prevent the country from sinking further and further behind—is one of the reasons I'm not applauding Democrats' performance.