THE FOUNDRY THEATRE

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Guest speakers: Dean Baker, Doug Henwood

Seth Ackerman: So first I guess I ought to welcome our speakers. On my left is Dean Baker, who is the Co-Director of the Center for Economic & Policy Research in Washington, which is perhaps the best think-tank churning out studies and commentary and analysis on the economy in Washington. On my right is Doug Henwood, who is the founder, editor, publisher, layout designer, and so on for *Left Business Observer*, which is a fortnightly newsletter on economics, politics, and more. So I think everybody has already got the article, the *New York Times* article that we passed out. This was actually a piece that came out in January. It was on the December Jobs Report that the Labor Department put out. It's a little bit out of date because we had a new Jobs Report, I believe, on the February employment situation, and that had it's own front page article in the *Times* the other day, which was even worse. But we can always update what we have here, and I think that since this article really does delve into the details of our current economic downturn, we might want to back up for a second and ask the question, now that we're in this downturn or recession, if it is that, how did we get here, and how did it grow out of the bubble, the boom, that we had in the nineties? I think that's a good place to start. So, I think everybody here remembers and is familiar with that boom, and I would like to ask the question, where did that boom come from? And how did it lead to where we are now? So, let's start with Dean.

Dean Baker: The boom we had in the late '90s... I'm a habitual pessimist on the economy, people would say I'd find the cloud in any silver lining. But in the late '90s – '96, '97, '98 – you had to look at the economy and go, you know, good things were going on. The unemployment rate was getting down. In the early '90s and the '80s, the conventional wisdom was the unemployment rate could not get below 6%. And I had a lot of arguments with economists who told me I was a fool, because I thought you could get below 6% unemployment without runaway inflation. Well, in the late '90s, the unemployment rate fell below 6%, fell below 5%, and for a year in 2000 was 4%, which looked really, really good, 'cause we hadn't seen that since the '60s. And 4% unemployment as opposed to 6% unemployment makes an incredible difference – those aren't just numbers in space. A lot more people had jobs, and disproportionately, the people who get jobs when the unemployment rate falls that low are the most disadvantaged. As a rule of thumb, the unemployment rate for African Americans is twice the overall average, so if you're looking at 4% unemployment overall as opposed to 6%, for African Americans that means 8% unemployment as opposed to 12%. And to carry it a step further, for African American teens, the rule of thumb is 6 to 1. So at 4% unemployment you're talking about 24% unemployment for African American teens – pretty high but an awful lot better than 36%. So, the late '90s, 2000, was a pretty good period that way. Also, you saw real wage growth up and down that income ladder, which was something we hadn't seen really since the '60s, a period of sustained real wage growth even for low-end workers, workers without college degrees, workers without high school degrees. So it was a very good time. So what was pushing that? Well, to my mind, there are two things. One was the Fed wasn't stopping that. To back up for a second, the Federal Reserve Board, it can't always make the economy go, but the Federal Reserve Board can make the economy stop. And what they've done in that past is when the unemployment rate has gotten below 6%, they've deliberately slowed the economy by raising interest rates.

SA: In the past like when?

DB: In the past like '94, like '89, like non-ancient past, so in the very recent past. They deliberately raised interest rates to slow the economy and keep the unemployment rate from falling. So what was great during this period, and Alan Greenspan deserves credit for this, was he saw the unemployment rate go through barriers that, as I say, most economists didn't think it could get through. They let it get through 5 and a half, it got through 5, it got through 4 and a half, they let it go down to 4%, and he did not raise interest rates, did not deliberately throw people out of work. So that was part of the story.

SA: **I just want to stop for a second and try to explain why it is that so many economists had said for so many years that if unemployment dips below 6%, that's a disaster. What was their reasoning? What was the logic behind that?**

DB: Good question. There wasn't very good logic behind it. What you could point to were statistical models that had pretty good predictive value, that you'd run regressions where you could show that when the unemployment rate got below 6%, there was some statistical evidence that that would lead to higher inflation, more rapid inflation. So we'd go from 3% to 4% to 5% if we had, let's say, 5% unemployment rather that 6% unemployment. And conversely the other side of this story was that if the unemployment rate was high, if the unemployment rate was 8%, then inflation would fall. So there was some statistical evidence to support that. There wasn't very much of a theory behind this. There wasn't anything that someone could say as to why it would be the case. I mean lots of people have ideas on this, but there was no...

Doug Henwood: Sure there is.

DB: Excuse me?

DH: Sure there's a theory. It's class struggle.

DB: You won't find that among neo-classical economists.

DH: No, but you'd certainly find it among central bankers. And in Alan's Greenspan's public statements throughout the late nineties, he frequently would look at, and said this very explicitly in Congressional testimony and such, he would say he was encouraged by the fact that workers were not acting militant as a result of a low unemployment rate. The reason they don't like low unemployment rates, and it's very hard to put an exact number on it, but the political point is that if the labor market gets too tight, it's too easy to find a job, then workers get bold – they're not so easily pushed around by their bosses. And Greenspan was looking at surveys that showed that workers, even despite an unemployment rate 5% or approaching 4%, were acting like it was 6 or 7 or 8 and in constant fear of losing their job, and he was encouraged by this, which is one of the reasons why he didn't push up interest rates from '96, '97, '98 and let the unemployment rate drip lower. It's because workers we're scared. And it wasn't until late in the decade when things started getting really tight and the wages started rising too much that Greenspan finally got nervous and pulled the trigger.

SA: If Doug was talking about the political ramifications of these debates about full employment, how low the unemployment rate can get... Dean, why is it, as an credentialed, certified economist, why is it that when you read the paper and you read an article about unemployment – is it too high, is it too low, what should the Fed do about it... First of all, do you see this political subtext to the unemployment rate, and if so, why don't we see it in the newspapers?

DB: In terms of the implications for wages? It's a mixed story. One of the issues, I mean Doug's right about Greenspan certainly, but you know, one of the forces you would have found back in the late '90s…you would have found the National Association of Manufacturers yelling at Alan Greenspan, you better not raise interest rates, because we want to have a demand for our products. They weren't that worried that wages would rise; they cared more about the demand for their products. So it's a little more complicated than, just…I mean I'm not going to try to pick Greenspan's mind, but in any case I'd just say there's not a simple relationship between profitability and the unemployment rate. Now in terms of how this is reported, you do have some very good reporters that do try to look at these things and do report the impact of unemployment on wages. Lou Chitelb), who's a reporter for the *Times*, being one example. But most of the reporters, I think, have relatively little idea what they're doing, so when they report on, you know, this point about 6% unemployment, they just treated this as something they'd read in the Bible, and they were fundamentalist, and it says 6% unemployment so therefore the economy can't get below that. They weren't in a position to assess either the evidence for that view or assess any theories behind it. So they just sort of repeated that as a mantra.

Audience: Can I ask something? Is there any reality to the idea that the more people are employed, the more people can, you know, the more products can be sold, the more people can raises their prices, and that's why inflation, that's why there is some relationship between them?

DB: It's part of the story. There's an important distinction to be made. When you have low unemployment, almost definitionally you're going to have a more inflationary environment. I mean, when are workers best situated to raise their wages? Well, when there is 4% unemployment as opposed to 8% unemployment. When are firms best positioned to raise prices? Well, when every one has a job, and there's a lot of demand as opposed to right now when there's very slack demand. So you have a more inflationary environment, there's no doubt about it, in a period of low unemployment. But that raises a different question than the way this theory was posed. This is referred to, among economists, as the Non-Accelerated Inflation Rate of Unemployment theory. And the point is not that you might get somewhat higher inflation at a low unemployment rate, but that you'd have ever-accelerating inflation. And it's a very important distinction, because right now the inflation rate is 2, 2.5%. And if we said, well, maybe if the unemployment rate fell to 4%, the inflation might go up to 3.5%. People could weight that and go, well, if a lot more people that would have jobs, then so what? Prices would rise 3.5 rather than 2.5, who cares? But NAIRU, the Non-Accelerated Inflation Rate of Unemployment says it wouldn't stop there. It would keep going. You'd have 4.5, you'd have 5.5, you'd have 10.5, and then you'd have German-type hyperinflation where you have to get wheelbarrows full. That was the view they were pushing, and that's an argument. If you really believe that it just goes right through the roof, that's a good argument not to have low unemployment.

DH: Well, there's also an unusual conjunction of events in the late '90s in that the U.S. economy was strong, and the rest of the world wasn't. The rest of the world was either stagnant or worse, and this kept pricing very weak. So business people were constantly complaining that despite what looked like a strong economy there was no pricing power, they couldn't raise prices. But at the same time, the U.S. labor market was very tight; wages were rising. The real value of the real hourly wage declined in the United States from 1973 to 1995, it fell about 16% in real terms. It started rising again in 1995, and it's actually still positive now although much less so than it was a year ago. So after 22 years of falling real wages, they started rising, and partly this was explained by the alleged productivity revolution, but part of it was just old-fashioned, when the unemployment rate gets low, wages rise. Since companies didn't have any pricing power, because the rest of the world was in such weak shape, this put a bite on profits.

SA: Explain why the rest of the world's bad economic shape cut into companies' pricing power.

DH: Well, there's a lot of excess capacity around the world. A lot of Asian exporters could afford to just run their factories, export cheap products. Also basic commodity prices were weak, oil prices were low, there was not an environment friendly to raising prices. Business people perceived that the competition was so intense that if they raised prices they'd lose business very badly, but they were facing higher costs, so the profit rate peaked in 1997 and started heading down, curiously just at the time that the stock market was leaving the earth and heading into the stratosphere. You can say that for the first 15 years or so, the great Bull market in stocks, it was pretty rational.

SA: Which began in…

DH: In 1982. You could say that after the 1970s when – I'll resume my class-struggle theory of inflation here – in the late sixties and throughout the '70s labor markets were pretty tight, unemployment rate was pretty low. There's also this sense among the ruling class that things are just out of control. Workers were getting bad attitudes. There was a time in the early '70s where wildcat strikes…workers were getting high on the job and sabotaging car production. There's the famous Lordstown plant in Ohio where working-class hippies were getting high and messing up the production line. And then you had a bunch of rebellions in the Third World, nationalist revolutions, commodity price cartels coming together, OPEC coming together, the United States lost the Vietnam War, so by the mid-seventies there was this sense that things were just out of control from an elite point of view. And one of the economic symptoms of things being out of control is a rising rate of inflation, so there's this political or psychological side to inflation. It's just like, the ruling class thinks the workers have a bad attitude, and we're losing our control of things. So you had, starting in the late '70s, Paul Walker took over the Federal Reserve, raised interest rates to very, very high levels.

SA: Paul Walker who was nominated by...

DH: By Jimmy Carter, Democrat, yes. But Carter had no idea what he was doing, and Burt Lance said, if you nominate this guy, you can kiss your re-election goodbye.

SA: And he did it anyway.

DH: And he did it anyway. And so the rest is history. But and then you had Thatcher coming into office, and then Reagan took over in the United States January 1981. So it's this real elite assault. It was a very successful class war prosecuted by one side, and the other side, the working class, lost completely. But from the point of view of the elite, this was wonderful. Profits started rising, almost exactly in the end of 1982, and headed pretty much straight up through the '80s, took a little break in the recession of the early '90s, and then resumed their increase. So you could say that the great bull markets in stocks ran from '82 until 2000, and the first part of it was indeed a rational exuberance in response to this great political and economic triumph. But then things started getting out of control; the exuberance got irrational; the speculation got wild; the public started getting into the financial markets in a big way, just about the same time wages were rising and profits were falling. So although that was a really good time to be a worker, it was not such a good time, or it was becoming a less good time, to be a capitalist. That was one of the reasons that the boom ended, was because there was too much, too many good times going around and it couldn't be sustained. And that's when Greenspan moved in and started tightening in 1999 and that brought the bull market to an end and brought the boom to an end as well.

SA: **Well, that brings us to the current situation. We had that mania and a strong economy with low unemployment in the late '90s, and now we are where we are. Was it the Fed? Was it the pricking of the stock market bubble? What was it that brought us to where we are now?**

DB: It was definitely the pricking of the stock market bubble. Very little investment is financed through issuing stock, as much as you hear celebrations about the stock market and it being reported like it's the central feature of the economy. It's actually pretty peripheral to the economy for the most part. But in the late '90s, when you had price turning ratios getting more than twice their historic average, and in the case of tech companies, over 100 to 1, and even more than that in companies that never made a profit, that could sell their stock for billions of dollars…at that point you actually were getting investment being financed by issuing stock, and a lot of it. And that disappeared when the bubble burst. So when you had the NASDAQ fall from a peak of over 5000, which I guess was almost exactly 3 years ago, to its current level, twelve or thirteen hundred today. When was it, I don't follow too closely?

DH: Tomorrow's the anniversary. March 10.

DB: Okay, so I know it was close to 3 years. Anyhow, that knocked out a huge chunk of investment, particularly in the tech sector, telecommunications being the largest chunk of that.

SA: **Was there any particular reason why it burst on March 10, 2000?**

DB: I don't know anything about that date, but basically you had investment that made no sense. People were investing, they were saying stuff that was just idiocy.

Audience: **And it made no sense for so long, and it kept on rising. I mean, why?**

DB: It's one of these things that's characteristic of any bubble. It doesn't make sense, but at some point you run out of gas.

DH: There's a theory in financial economics called the Rational Bubble, which is that you may know that a bubble is underway, but if you think you can unload your stock tomorrow for a price greater than you paid for it today, it makes sense. So...

SA: But that theory doesn't tell you why it ends.

DH: No, but these things always end, and they almost end because of higher interest rates. So at some point, you can't say what exactly what hour it's going to end, but once you start seeing the interest rates rise, you can say the end is in sight.

SA: Do you buy that, where it was higher interest rates that...

DB: Well, the interest rates certainly brought it on sooner. I mean it would have ended if Greenspan had never raised interest rates; it would have gone higher and would have ended. Greenspan, I think, he did want it to end; it wasn't the most clever way to do it; he let it go on way too long, but that certainly contributed to it ending.

DH: Well there's also a psychology during the bull market too. I mean it's very difficult to be a skeptic…Dean and I are running around saying, this market is insane; this is not going to last; bad things are going to happen, and nobody wants to hear you; nobody wants to believe you, and people will say, oh, this time it's different because...And so this time it was different, because there's this technological revolution that meant that productivity is going to be rising forever, and people like Greenspan embrace this argument. 30 years ago or a little more than that, really, in the mid to late 1960s, then-chair of the Federal Reserve, William McChesney

Martin, was alarmed by talk of a new era. People were saying this is a new economy, people were saying it then too, and Martin saw that as almost sufficient evidence in itself that things were out of control and getting very dangerous. 35 years later, Greenspan himself as the Chair of the Federal Reserve was endorsing it and cheerleading it onwards, so he really helped promote the thing and let things get wildly out of control.

SA: We have a question?

Audience: Yeah, I guess **I want to back up a little bit, see if we can go back to economics 101 and unpack a couple of terms. I guess I want to understand more specifically the relationship of interest rates, inflation rates and unemployment rates, and the rise of profits, and understand how these are being measured. 'Cause I remember at the first roundtable series, hearing how the unemployment rate is being measured was really a surprise to me.**

SA: Well how is the unemployment rate measured?

DH: It's a monthly survey of 60,000 or so households in which enumerators from the census bureau, under contract from the bureau body for statistics, go around and ask people, were you working last week, were you looking for work? And if you were working just an hour, well they ask about the week of the month in which the 12th falls, so were you working in that week? If the answer is yes, you're employed, and if the answer is no, the next question is, were you actively looking for work? And if you weren't actively looking for work, you're not counted as unemployed. You have to be out there sending out resumes, reading the want ads, making phone calls, just making some effort to find a job. If you're not actively looking for work, you're counted as not in the labor force.

A: Contract counts?

DH: Yeah, anything you are paid for self-employed work, just as long as you're working an hour in the reference week than you're counted as employed.

A: 60,000 households, that's it?

SA: That's a very good sample

DH: That's a very, very large number. Yeah, a standard poll that like Gallup will do is only 1200 people, or, you know, a big poll will be 3000 people so 60,000 is a really, really large sample.

DB: You're going to be within the ballpark.

DH: It's very, very accurate. I mean, you can complain about the definitions, it's a very liberal definition of employment to say if you're working just an hour, you're employed, and if you're not actively looking for work then you're not unemployed, so there are not what people consider ideal definitions of either employment or unemployment, but they're very, very accurate on the basis of…When you can see what they're trying to measure, they do a very good job of it, and the people who do it, you know, I talk to these people on the phone, and they are all very serious, honest public servants. It's almost inspiring. They really take their work very seriously. So they're not...The tendency is…

DB: That's important, because there have been battles over the statistics they've produced, and I'd say the statistical agencies in general try to be very, very honest in producing straight statistics.

DH: But they're also very open, they'll talk to you. It's not like, even in other countries like Britain they won't talk to you. So you know one of the amazing things about American life is how open it is in so many ways, and we all know that there are terrible things that go on, and nobody cares, and we've got exact measurements of how poor people were, and how many there are, how far their incomes are below the poverty line…We know all this stuff in great detail, but nobody really seems to care.

SA: But speaking of the statistical agencies, the Bush administration recently killed one the series that they put out, isn't that right?

DH: They did actually, I had to say I was not…I didn't care that much, because what they killed was…There's a series of mass layoffs where they measure layoffs of more than fifty…Actually Bush Senior had killed the same series. I guess for some reason they have it out for that series. I mean, as an economist, I'd rather have more data than less data, but this is one series that I had actually very little occasion to ever make use of. And the reason from their vantage point, it didn't seem like that good of an idea, there's a private firm Gray & Challenger that regularly reported every month the number of layoff announcements. Now, from a statistical vantage point, it's not nearly as good as what the Bureau of Labor Statistics does, because they're actually measuring the number of times people were laid off. They're getting into how many cases there were of more than 50 people getting laid off this month. Whereas announcements, you could have AT&T announce, we're going to lay off over 50,000 people somewhere over the next two years. They may do that; they may not do that. They may contract out; we don't know what that means. But as a practical matter from the politics of it, that was what got widely reported. I can't recall when I've seen that mass layoff number in the newspaper.

SA: But it must have been a political decision to kill…

DB: Well it was because the Bureau of Labor Statistics' budget was being not cut, but not keeping up with their needs, and so they cut what they thought what was the least essential program, and that was very non-essential, and it also came out with a considerable delay. And people who follow this stuff in the market particularly want up-to-the-minute new, and statistics that are 2 or 3 months old are, you know, who cares?

SA: Okay, enough of the inside baseball.

Audience**: I want to back to go what Bonnie asked, which is the relationship between the rising of interest rates and the burst of the bubble. I don't understand the relationship.**

DH: I think he wanted to burst the bubble...

Audience: But how did it burst...?

SA: When exactly are we talking about, first of all?

Audience: This is '101.'

DB: Okay, let me back up a little bit. Doug might back me up on some of the dates here…

DH: Greenspan actually was restrained – I was giving a short quick story, and maybe a little too much credit to Greenspan, but he was being somewhat restrained in his raising of interest rates. He had wanted to raise interest rates through '97,'98,'99. He was prevented from doing that in '97 by the East Asian Financial crisis. 'Cause again he saw the unemployment rate getting low. He did make some comments about the stock market. Greenspan was very good at playing both sides of this, he made…

SA: **"Irrational exuberance"**

DH: Irrational exuberance.

DB: In December of '96, he said that, and got hammered and never said it again.

DH: Right, he backed away from that. But he wanted to raise interest rates in '97, in fact he did begin raising it, and then you had the East Asian financial crisis, with first a run on the Thai currency and spreading to Indonesia, South Korea, all the East Asian economies. There was a world crisis. Greenspan responded by restraining himself in terms of raising interest rates.

Audience: Then how does it affect it…

DH: They way it would affect it is if you're holding stock, what you're doing is comparing the return you expect to get on that stock from alternatives, and one alternative is to put the money in some sort of interest bearing note. So when Greenspan raises interest rates, I'm going, well instead of putting my money in the NASDAQ, I could get a short term treasury bond that is absolutely rock solid and going to pay me 6% interest. So what happens is people pull their money out of the market and put it in these interest-bearing notes, 'cause it's a better deal.

DB: There are some other things that happen too. A lot of people who operate in the stock market operate in borrowed money, so if interest rates rise, then the cost of speculating rises, and so they're less likely to speculate. Higher interest rates also tend to slow down economic activity, and it's more expensive to do business; it's more expensive to pay a mortgage; its more expensive to get a credit card; it's more expensive for a corporation to borrow, to expand, or even just to do its regular business. So it has an effect on the real sector. And people on Wall Street are always like – this is one of the things that always confuses people who watch Wall Street, is that today's news is often shrugged off, and they're trying to figure out what tomorrow's news or next week's news is going to be. And when eventually they see the Federal Reserve pushing up interest rates, they say the Fed is turning hostile; they want to slow the economy down. So, I want to get away from this; let me do something safe.

SA: Don't fight the Fed.

DH: **"Don't fight the Fed" is a common Wall Street saying. And in that case, when interest rates started rising, there was a complex psychology in the bubble, 'cause when a lot of people know that something's wrong, they'll say, oh this looks like a bubble, but it sure is a lot of fun. So there's this kind of internal dialogue that goes on – I'll worry about that tomorrow. If you're out late drinking, you'll still have another drink. I know I'm going to feel terrible tomorrow, but you know you'll do it anyway. To some degree speculation is like that. It's a very, very psychological thing. The short term, medium term movements in financial markets are much more psychology than fundamental economics. And when they see interest rates rising, it's a bummer man.** Uh, Martin, the Federal Reserve Chair I mentioned earlier, in the '50s and '60s was famous for having said that the job of the Federal Reserve is to take away the punch bowl just when the party was getting going. Greenspan wasn't doing that – he was spiking the punch bowl for a good bit of the late '90s and then took it away. But when people see the interest rates rising, they say the Fed is turning hostile. So...

DB: **...If you think about the NASDAQ, there were some people who were true believers. You know, they thought Amazon was going to be worth more than the whole U.S economy in 10 years. But there were also a lot of people who knew Amazon was worthless, you know, but fine, who cares? I don't care if it's a totally worthless company if the stock price is going up. And those people, as soon as they saw things turning, they were running. And that's why the NASDQ fell from 5,000 on March 10th, it was down to 3,000 three weeks later. 'Cause there were a lot of people who knew the stuff was worthless, and they were very quick to dump it.**

DH: Yeah, I interviewed a portfolio manager, this was like 1998 or something like that – he ran something, a little fund, called the Net Net Fund, which was just highly speculative Internet ventures, and I said, how do you value a stock that has no earnings? These are companies that not only didn't make a profit, they never had a prayer of making a profit, which is very unlike earlier bubbles. In the '20s, things got out of control, but we're talking about companies like RCA and Ford that were powerful and made lots of money. This rampant speculation in companies that weren't making money and didn't have a prayer of making money is almost without historical precedent. So I asked this guy, how do you value these stocks? And he said, well, actually, that's a good thing, not to have earnings.

[Laughter]

DH: How's that? He said one, you can't plug them into conventional evaluation models and find out that they're worthless. And two, when you have no earnings you can't disappoint Wall Street's profit expectations. So it's a good thing to have stocks with no earnings. And this guy, he wasn't kidding. I was doing this little story for *Wired*. So there was an audience he wanted to talk to, the readers of *Wired*. And I thought, my God, this is insane.

SA: And he was right for a few years, he made money that way for a few years.

DH: Yeah.

A: He made money, whether he was right or not...

DH: Now they're all gone of course. Amazon is still around…Does it have a prayer of making money? Pets.com was a pretty insane idea.

SA: We have a question?

A: Well, you just tied together this relationship between inflation and the money available to companies for investing. Could you also talk about how the huge inflow of pension plan money that created a lot more capital available to companies at the same time you talk about interests?

DH: Well that's one theory**. It's also unusual for the stock market to provide a lot of investment. That's certainly the case in most periods of history, the stock market... The floatations of new stock don't really provide much in way of investment funds. The funny thing about the late '90s was that there was a period, an exception, when initial public offerings did provide funds to companies, several went to their real operations, several went to their investors, and didn't have anything to do with funding their business operations. But most of the things that got money in the late '90s shouldn't have. There were companies, in normal times, they wouldn't have been able to get a bank loan, you know, and here they were selling billions of dollars worth of stock. It was a case where these entities just didn't deserve the money they got, so it was all wasted. Spent on advertising, dot-coms were advertising each other's sites. But there was no actual production of value. It was just the equivalent of just burning the money.**

SA: I think this is an interesting point to dwell on. In contradiction to what every TV pundit and local libertarian seem to say all the time, you're saying that the market was misallocating funds.

DH: Profoundly misallocating funds.

SA: Misallocating capital. In other words the market mechanism, not some government bureaucrat but the free market – the stock market as a way of channeling funds to companies

– just made the wrong decisions, it sent the money to things, o places, where the money would get wasted. Now you're an economist. Don't economists tell us that that doesn't happen?

DB: They do their best to hide it. You'll find few, if any, economists... There's a very rightwing economist at Stanford, a very prominent economist, Robert Hall who likes to defend the market all the time. I remember I saw him on a panel in January of 2001, so the bubble is partially deflated, and the NASDAQ had just gone up about 5% based on Greenspan having cut interest rates the prior day. And he's going, well that was rational, because that meant Greenspan was going to fight a recession, and he was telling the markets that he's going to do whatever is necessary, and they were actually just rationally responding to that. I mean, the fact was, movements we saw in the late '90s made no rational sense, and as I say, you have to be some kind of real nutball ideologue to try to explain that as being entirely rational. The implication is exactly what Doug was saying, that you had companies that shouldn't have been allowed money, that were getting billions of dollars basically to throw in the garbage. The implication then is, yes, the market really blows it. It blew it there. You have all sorts of other situations. The DOW is hugely out of line, that's a misallocation of capital. I've been writing about the housing bubble, that's a misallocation of capital. We're having huge overbuilding, we actually saw this with commercial real estate, and we'll see it with the residential very shortly. The market misallocates all the time. Anyone who's not so ideological that they just rule that out as a possibility has to acknowledge that. The bubble we saw in the late '90s... If we had conversations with economists in the late '80s or even the early '90s about that, they would have told you it was impossible. But there it was, right in front of our faces.

SA: And have they admitted the error of their ways?

DB: Never! Never.

[Laughter]

DH: There were some benefits, of course, to that bubble moment, because it did provide... Semiotics graduates at Brown could get jobs in Silicone Alley, and it turned Avenue B into Avenue Bistro. But providing jobs for people is better than building weapons.

DB: It's a benchmark, though. Having been in on these debates on how low the unemployment rate can go in the early nineties, and having been laughed at because I said the unemployment rate could get well below 6%, and then we saw it. A full year, it was 4%. That's an important benchmark that I think sets something up that we can fight for in the future, and when the Federal Reserve Board tries to clamp down on the economy and says the unemployment rate is getting too low, we can point back to 2000 and go, no, it got to 4% and things were fine.

SA: I don't want to get too much into inside baseball, but I'm fascinated by this point. So they've now seen, they've now proved, that unemployment can get as low as 4% for a whole year without generating constantly rising inflation. What have they done, these economists who peddled these theories in the past, what have they now done? Have they got their phone numbers unlisted?

DB: I grew up in Chicago with the Dailey machine so I'm used to corruption, but no matter how corrupt you think it is, it's always worse. It doesn't matter; it's just amazing; it really doesn't matter. The same people are still saying the same thing; they can ignore what is right in front of their face. **During the bubble, Doug was saying that we both had the experience of going, this doesn't make sense. I was on panels with many prominent economists, and I'd just go, if this makes sense, if price-to-earnings ratios of 30-to-1 – the historic average was less than 15-to-1 – if this makes sense, write it down for me...what is the path of stock price growth, what is the path of dividend yields that makes sense of this? And there was no way you could do that, because you'd have to have people getting very low returns on their stock. Either that or the bubble goes 40-to-1, 50-to-1, 60-to-1. Those were the two choices; there was no way around it. None of them would do it. I'd challenge them; I'd do my best to humiliate them. I'd go, come on, we write things down – that's what economists do. None of them ever took me up on it. I'm sure in their spare time, some of them sat down, and they knew I was right – they had to know I was right. But it wasn't as though any of them suffered anything for it. They never acknowledged they were wrong. And this was a colossal mistake. I keep thinking about this. We have an economy where the busboys, when they break the dishes, they get fired. The truck drivers, when they're in an accident, they get fired. People working normal jobs, they're held accountable. But these people who control billions of dollars, make huge decisions, and there's no accountability. They could fuck up as big as you could imagine, and no accountability. No one holds them accountable.**

DH: Keynes said once that it's better for your reputation to fail conventionally than to succeed unconventionally. I think that's further proof that "failing conventionally" is okay.

Audience: We often hear about the economy as a psychological measure to people feeling confident or insecure, and what we're seeing is the changing of the composition of the investor. The investor is no longer the wealthy individual, but it's also all these people that have pension money, and their pensions are evaporating because of misallocation of funds. That would have to generate a lot of insecurity.

SA: This is the wealth effect. You're talking about individuals who are seeing their pension money evaporate and not spending. Yeah, we should get to that in a second when we talk about following the course of the burst bubble downward. But before that we have one question here.

Audience: In the first half of this century, it seems to me, that the idea was more widely accepted that capitalism allocated resources through a series of crises. You have a period of rising productivity, followed by a period of open investment, followed by a failure, followed by a gradual economic recovery. This was so well known that it was called, in fact, the Ten Year Cycle. A five-year period of depression followed by an abrupt, 5 to 7-year repudiating boom. Now what is surprising about the quarter century after World War II is the relative

absence of these cyclical movements, and they are occurring again, and seem to us unfamiliar but that were much more familiar to people in the past. But maybe what needs to be accounted for is their relative absence for a quarter century.

SA: So could you explain what the question is?

DH: Okay, for example, in the second half of the nineteenth century, booms and busts are about equal in length. About half of the late nineteenth century was spent in periods of recession or depression or panic or whatever quaint names they used then. Now, in recent years since World War II, the booms have been about 4 times as long as the busts or even longer. In the '80s, we saw expansion that lasted almost the whole decade, and in the '90s we saw the same thing. The formal parts of the recessions were actually quite short. The recession of the early nineties, in formal terms, was like 7, 8, 9 months long. Although, most of the Bush I years were spent in a pretty stagnant flat economy, so the formal part of the recession was short, but the economy stank for 3 or 4 years. And I think we're seeing something very similar now. The formal part of the recession, you could say, lasted most of 2001 and may have ended then, but the recovery since has been terrible. So we're just in this long period again of flat, grinding stagnation or slightly worse. But I think part of the reason is big government, as we have much more active and skilled central banks that know how to manage cycles better than they used to, and the fact that we have very large government spending now, compared to even after the cuts of the Reagan-Bush-Clinton years. We still have a big government and most other countries do as well, and that kind of puts a floor under economic activity, so it makes it that nineteenth-century-style collapse impossible. It doesn't necessarily guarantee that you're going to have quick recoveries and endless prosperity, but it makes a complete implosion very, very unlikely. This is what we've seen in Japan for the last 10 or 12 twelve years, that they had a bubble of their own in the eighties that broke very dramatically, and their economy's been pretty much stagnant since 1990. If it had been 60 years ago before there were large governments, it probably would have been a depression. But because there's big government to keep a floor under economic activity, that's how you have this long stagnation instead.

SA: You referred to the formal part of the recession in the '90s and today. I think a lot of people wonder, how do they figure out when a recession starts and when it ends? How do we know we're in one? And actually the answer isn't as scientific as it may seem.

DB: Yeah, actually I just learned something new about that the other day. We have a little commission of people from the National Bureau of Economic Research, which is chaired by the chief economist in the Reagan years...

SA: This is a private agency.

DB: It's a private agency, that's right, and they are responsible for dating business cycles. And what I just learned was that the economy was very different than we thought, because there are larger visions. As good as the statistical agencies are, the fact is, it is hard to know exactly what the economy is doing today. One of the things that just came out was in the employment report, issued Friday, they found that there were 300,000 fewer jobs created the prior year, in 2001, than we had thought. What often turns out to be the case is that you revise data, and the world looks somewhat different, sometimes very different, than what you had originally thought. The dating commission, the National Bureau of Economic Research's dating commission, they actually never go back and revise their dating. So ironically if you look now, they dated the beginning of this most recent recession in March of 2001, but the economy had stopped growing back at the beginning of the year. So if they were going back and looking today, with the data we have now and they were dating it, they would probably say December or January – they would have to look carefully to see what would make the most sense, but they wouldn't put it at March. But they would never re-date that. Now they haven't said the recession had ended. And there's not a fixed time for that. What they usually look for is when they think the economy is back on a sound growth path, but they've not yet said that and with good cause – I think we're going to see a second dip to this recession. But in any case, they haven't put an ending on it. That doesn't mean that they're going to end it some time in the future. They might sit down next month and say, oh, it actually ended in November of 2001. They might say that. So it doesn't mean that they're going to say it ends next year, but they haven't yet put an end to it, so we don't have any official dating of the end of the business cycle.

Audience: I have two questions that lead up to the third one, which is, who lost the most? The first is, there was all this talk of the broad ownership of stock – there were more stakeholders in the stock market, so the percentage of institutional investors was smaller. The other is, was there a change in the percentage of stock, which were non-dividend-paying stocks? Because that's the common idea of stock ownership, that you're paid dividend and can live off of them, but a large percentage of stocks don't pay dividends.

DB: There was a huge increase in stock ownership in the course of the '90s, and this is largely because of the spread of 401(k)s and the ending of traditional defined-benefit pensions. To my mind, it is an unfortunate development in the economy, but there's been a huge shift over from defined-benefit pension plans, where you're guaranteed that you'd get 50%of your average wage or whatever, to these defined contribution 401(k)s and 413(b)s, where you get whatever you happen to put in there, that's what it does. It's gotten to the point where defined-benefit programs are dwindling so fast they're almost dead. Still, a lot of people have them but they're clearly going quickly.

DH: But the companies that have them, their pension funds are woefully under-funded, so that may be cutting people's pensions.

DB: That's right. We've seen some examples of that with bankrupt companies. Yeah, there some other big issues in there also. Anyhow, so there was a huge growth in stock ownership primarily because of that, although the median stock ownership as of 2000, and roughly 50% of households had any stock at all, including through 401(k) and mutual funds. The median ownership at that point was $25,000 – I don't know the exact number. Even then, a way to think of it is 75% of the people in the country still had less than $25,000 in stock. You asked about the dividends. There were always some stocks that didn't pay dividends, but with the surge in the NASDAQ people began to think, who cares about dividends? What do you care for dividends that are 2 or 3% of the share price, and we're looking at stocks that go up 20 or 30% a year, sometimes more. So you did have a lot of companies that didn't pay dividends in part because of that mentality, in part because they didn't profit. It's pretty hard to pay dividends when you don't have profits. So you did have a proliferation of companies who didn't pay dividends. I think we're seeing an end to that, though, because a lot of those are now out of business, and I think of the ones surviving there is pressure. Even Microsoft just announced a dividend. I think there is going to be a lot of pressure on those companies so that we might be reverting back to the old dividend-paying routine.

DH: Microsoft is an interesting example because it, unlike the dot-coms, makes a lot of money. I think the last time I looked, Microsoft had 42 billion in cash that they didn't know what to do with.

SA: 42 billion?

DH: 42 billion dollars that's been sitting in treasury bills and short-term securities. And now they've started playing with very notional, tiny dividends, so they're not distributing very much of it. They apparently lose money on everything they do except Windows.

SA: Is that true?

DH: Every X-Box they sell, they lose like a hundred bucks. MSNBC loses money. I think they barely make money on the Office software. So they make a ton of money on Windows because of their monopoly position, and they accumulate all this cash. They've got $42 billion they don't know what to do with. I have plenty of ideas what they can do with it, but they're not about to spread the wealth. But it's an interesting example of what happens. They've accumulated so much cash that they can't possibly reinvest it – there's nowhere they can put it in their underlying business. This is the most successful company of all time, a monopoly that's failed at everything that they do that isn't a monopoly.

SA: I have one small question. What is the point of owning a share of stock if it doesn't pay you dividends?

DB: Well, there is an underlying value there. In the case of Microsoft, they could never pay dividend, the point is there's 42 billion is cash plus ongoing profit...

SA: Right, but the vast majority of people who own Microsoft stock are never going to own a controlling interest, so they'll never have a say in how that 42 billion gets allocated.

DB: They don't care. The point is, it has value because it is one-millionth of that – I don't know how many shares they have, probably over a million – so one ten-millionth of it.

Suppose I had a claim to one ten-millionth of the gold in Fort Knox, I could always sell that and that's worth, presumably, one ten-millionth the value of the gold in Fort Knox.

DH: And presumably the profits are going to rise every year, so you have a claim on that rising steam of profits and that's what gives a stock its real value. Dean was saying that it used to be that dividends were a very important part of the return of owning stocks. About a third of the long-term returns over the last decade of owning stock come from dividends. But dividends just got, in the '90s, people thought, how boring, how old-fashioned, dividends... yawn. Now people are looking with a little more fondness on dividends, but then it was just like buggy-whips to them.

Audience: I wanted to pick up where he left off, which is, who lost the most? Who suffered the most? And where are we now? What are the indicators that we use for...Where do I look to assess where we are?

DB: In terms of who lost the most, in percentage terms, you could find some dot-commers who were in their twenties who worked for 4 years for stock options, and they have nothing. The company's bankrupt, the stock options are paper, and if they really want to rub it in, maybe they bought a home in Silicon Valley and paid twice what it's worth today. So they lost the most. I'm not too worried about those people, though. I mean, a) there weren't too many of them, and b) most of them will land on their feet.

Audience: But where do we…where does the average person…

DB: Well, ok let me go on a little bit with who I think did get hurt a lot, and is a bigger issue and that's, you know, with the 401(k)s you did have a lot of people that did have much of their money, maybe most of their retirement money tied up in the stock market, and weren't looking to make a fortune; it's just that's what they told you to do – you don't have a defined benefit pension, so you have a defined contribution, that's the only thing you can do. I had one at, actually I'm getting a new one now, but I had one at my old job and, you know, I'd always love to have these people call me up, 'cause I put all my money in bonds back in '98, 'cause the markets crazy, and I have these people call me up and harangue me and go, well you're still a young guy, you should be able to go, why? And you know this is my area of study, so I want to hear what they're going to tell other people.

SA: They didn't count on talking to an economist on the other end of the phone.

DB: So, you know most of the people who had their money in the 401(k)s,they put large shares of it in the stock market, thinking that its gonna give a real return of 7, 8, 9% a year, and that's a sure thing, and they're nailed. And you have a lot of people, you know, who are in their fifties; they don't have too many more years until retirement; they don't have necessarily secure jobs, because these are the people most vulnerable to downsizing, to getting laid off. And they're going to have very little to retire on. So those people, I think, are the ones who are hit hardest. Now, there are secondary effects – what does the economy look like when we come out of this, and that's very much up for grabs. It's not good now, is it gong to get better? I think the immediate prospect is worse rather than better – that means a lot of unemployed people. So there's a lot of secondary impacts. But the people who I worry about the most is the older people who had a lot of money in their 401(k)s, who might not get a chance to make that up.

Audience: Plus there's so many baby boomers, getting raped by…

DB: Again, you know, one of the things in Washington - I just want to strangle some of these people - 'cause you know, I don't know how many times I'm with people and they're talking about the burden on the government 10, 15, 20 years out. And I go, fine but what about the private sector, and people won't have that conversation. So in other words, yes social security is going to cost more in 20 years from now than it does today, no doubt about it, but the point is you have a lot of people with their private savings – this is again when I try to get them in a discussion of the stock market – isn't this something that concerns you? Blank faces. So you know we have a very large generation of baby boomers, many of whom are already in their fifties, most of whom are already in their fifties, they have very little saved for their retirement. They're going to be dependent on social security, and that's better than nothing - I'm gonna spend a lot of time defending their program, it's a great program, but its not much to speak of if that's going to be your whole retirement.

DH: I also want to say that one of the strange things about this cycle though, is that people kept buying houses and cars throughout it. Retail spending, consumption didn't decline anywhere near as it did in earlier recessions, what really happened was on the business side. Businesses stopped hiring as much, they stopped investing in a big way, so there's been really a collapse in capital spending on gadgetry and buildings and things like that, that are things that make economy grow over the very long term. But people kept buying houses; they kept buying cars.

SA: They're still buying houses and cars.

DH: Yeah, there's these things, well the car market is slowing down, and the housing market shows sometimes maybe it's about to turn, but it kept going and it was very strange. And people report they're anxious about the job market, the consumer confidence numbers or any number of surveys have measured how people feel about the economy, those numbers are terrible. But they keep spending anyway. So you could look at that as one of two ways - that they're just sort of riding – they're being courageous and looking at the long term and riding out this temporary rough spot or this is really the last aspect of the bubble that hasn't quite burst yet. But the rise of unemployment has certainly not been as bad now as it was in earlier recessions.

SA: The unemployment rate now is what, 5.8%?

DH: Yeah like a 5.8. Yeah and you know earlier recessions…

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DH: I'd say there are several things that are unusual and uh, kind of scary about this cycle which, aside from the fact that some of these indicators don't look as bad as they did in earlier recessions. One is that the economy is just refusing to recover. In a normal cycle you'd have maybe a twelve-month recession, and then it would come back, often very strongly. That hasn't happened. We've had probably some of the most aggressive easing of interest rates in the history of the Federal Reserves since they opened in 1913, and the economy has not responded. The stock market has continued to decline even though the Federal Reserve has been very, very indulgent. That, the only kind of precedent for that, that kind of non-response by the stock market is the 1929-32 period, so that's a little scary. Um, I really don't like to wheel out the heavy artillery, but that's the case. Uh and the other thing that's really, really bad is state and local governments are in just dire shape.

SA: This is what we talked about two weeks ago.

DH: And New York City is particularly bad, New York City is particularly bad because what happens on Wall Street is very, very important to what happens in the NYC economy. Our city has never been so dependent on Wall Street as it is now, and it's a disaster, and nobody in the political sphere talks about this dependency, and nobody talks about trying to use the city's government to diversify away from this dependency. You know, our mayor is a Wall Streeter, and he's certainly not going to be the one to think boldly about alternatives to Wall Street. But it's also other state governments and local governments around the country are in dire shape, much worse than in any other earlier recessions, and Bush, of course, is talking about more tax cuts. And most state tax codes sort of mirror what the Federal code does, unless the legislature comes in and explicitly undoes that. So the risk is, if the Federal Government comes in and cuts taxes more, the states are going to be hit even harder – it's just, no one in America likes to raise taxes, so we can't even talk about that. So that even though tax cuts at the Federal level would seem to have some kind of economic stimulus effect, the composition of the tax cuts is terrible; they're skewed to rich people, and don't provide any relief to working class or poor people. That also is not very good news for a stimulus effect, because rich people don't spend as much of their money as poor people do. It's not going to happen for another year or two, so we're not going to see a good Federal fiscal stimulus, and at the same time state and local governments are cutting spending. So whatever stimulus is coming out of Washington is being undone and maybe more than undone by what's happening at the state and local level. So, you know, you can separate two aspects of government spending, one is just the economic stimulative aspect of it and the other is the good things the government sometimes does, and we're losing on both of those counts. We're getting the government sector now as a drag on the economy, and things the governments do, like providing education and healthcare, are being cut. So that's really one of the worst aspects of the current cycle, is what's happening now.

Audience: Do you think Bush or anyone around him is even thinking about relief in terms of the assistance to states?

SA: Not Bush.

DH: Some people in the democratic party are talking about it but not very loudly, and it'll never get through a Republican congress and not get signed by a Republican president.

DB: Let me just say, there's one more layer to Doug's balloon and that's just the housing bubble. We've had a housing bubble in the last seven years, which is very similar to what happened in Japan where they had a stock bubble and a real-estate bubble.

SA: I just want to point out one thing. Doug mentioned earlier that autos and housing are two of the things that are propping up the economy now. Both of those are very interest rate sensitive sectors. The amount of money that it costs to buy a car or a house depends in large part for the consumer on what the interest rate is. We have very low interest rates.

DB: You know, actually, one of the things that's the economy too, is that when people refinance their mortgages, which they've been doing a lot of, they've been taking cash out because out of the appreciated value. So that has been a tremendous kick in the, not kick in the ass, but chop in the arm for the economy. You know, that's really kind of reckless, people are adding to their debt. But it's kept the things going, so like I said, it's going to look like a wise thing to do if the rest of the economy recovers soon. But if the rest of the economy doesn't recover, it's going to look really, really stupid.

SA: Explain the housing bubble.

DB: Housing prices, and there's a great index that tracks re-sales of the same homes, so we don't have to worry that we're comparing, you know, that we have new homes that are bigger or better than the old ones. We're comparing the resale price of the same home, so that index shows that home prices have gone up about 33-34% points more than the overall rate of inflation since '95. And again, this is when I like to have economists have fun with it, go, okay what do you think, people just fell in love housing in '95 – it's never happened before - so they just fall in love with housing in '95 or is this a spin off from the stock bubble, as we had in Japan? And the idea of it being a spin off is that people, when they're buying a house, they're not looking and going, well, you know I could spend $200,000 on that house or you know, this will be money for my retirement, or whatever. They're thinking, well I'll spend $200,000 on this house today, but in five years I'll sell it for $300,000. And I'm absolutely convinced it's the later, if you look at it, it's hard to believe otherwise. So, what are the implications of that? It's helped sustain the economy; we've had a lot of home building, people are building new homes; they move into a home; they get furniture and all these other things, and they borrow against it. As Doug said, and one of the scary numbers to me is, if you look at the ratio of equity to value, you know what percent of the home do you have paid off it's near a record low – it's about 55%. If you go back to the '60s the '70s the '80s it's been around 67%, so were way below…

SA: That number measures the percentage or the value of somebody's house they actually own – they don't owe that money to the bank.

DB: That's right, and there are two reasons why that's so low right now. One is as soon as you have a rise in value, that adds to the numerator. So if I have a $200,000 home, and it just goes up 10%, that's raised my numerator. Flip it over, it goes down 10%, and the numerator falls. So in other words, when the bubble corrects, you'll have a lot people that have very little – some might even have negative equity. They might owe more than the value of their home. The second one is just again the demographics…You know, we have a very old population right now. It's certainly much older than it was in the '70s and '80s. You know at that time, the baby boomers were in their thirties, now they're in their fifties, many of them. So if you're in your fifties, and you don't have very much equity in your home, you don't have a pension, you're not in real good shape for your retirement. So those are not good numbers.

Audience: To incorporate what someone said before, it seems like we're in this culture of denial. The spending keeps going and people are borrowing. I don't know if there's something about the lending that's changed; I don't know if that's true, but it feels like it has. Like people used to have maybe one credit card, and it was an American Express, and now people have 10 credit cards, and I can walk into a bank and walk out with $7,000 worth of credit and I earn nothing. So why is that, and what does that have to do with this kind of spending?

SA: Credit cards are, I believe, the most single profitable financial business that the financial sector has.

DB: Yeah it's about twice as profitable as other lines of businesses for banks. I mean, the economics of it are very simple. You know, they borrow the money at say 5%, and they lend it to you at 20%, and sure you get some defaults, so maybe if they lost 5% of the money that they lend to people who default or go bankrupt – then you know they're still 10 percentage points ahead. So from a bank's point of view, unless crisis comes, they're printing money. But now that they've tightened, they're trying to get the bankruptcy code. There may be some problems, but the one piece of personal financial advice I would give people is, if you've got a lot of credit card debt, you should really, really consider going bankrupt, it's really a good thing to do.

DH: It's a really important point, because this hasn't passed yet, and it's been held up cause of real idiocy, idiotic things, but fortunately it hasn't passed yet. The bankruptcy law – they intend to tighten it up in a really big way. I mean it really is outrageous, because these companies are making a fortune now, so this is just pure gravy to tighten up the bankruptcy law. And the fact is, the vast majority of people who are going bankrupt, it's not because they ran out and bought everything in sight. The vast majority of people had divorces; they had personal illnesses; they lost their job, and that's the vast, vast majority of cases. And the idea that you're just going to squeeze them to get every last pound of flesh out – it's really pernicious.

SA: Well, what was the change in the bankruptcy laws?

Audience: It hasn't changed yet.

DH: It hasn't changed yet, but the fundamental proposal is, that the people with incomes below the average, below the medium would not be allowed to…People rather above the medium would not allowed to wipe out their debts completely – they'd be forced to go into repayment schemes. Right now, there are two choices in the bankruptcy code, you can just go, what is it chapter 7?

SA: Seven.

DH: Where they just wipe out your debt. And I sat through a day of these hearings some years ago at the Manhattan bankruptcy court, and it's just amazing. You know, people would come in with $30,000 of credit card debt; the banks wouldn't even be there; they wouldn't even question it; there would be a five minute hearing; the examiner would say, okay, discarded, and the next person would come. I watched, like, forty of these in one afternoon. But they want to make it so that people have to go through what's called a chapter 13, which is that the court puts you on a budget, and you're supposed to pay off their debt, and people can do that voluntarily now if they want to, but most of them don't work out very well. Most people who are at the verge of bankruptcy just can't pay off their debt, and it's pointless that they should even be forced to try, but this bankruptcy reform bill which is literally written by a law firm for the credit card industry – Morrison and Forester, which is a San Francisco law firm. They literally wrote the language of this bankruptcy reform bill, and they want to force people with above average incomes into these repayment plans and make it much, much more difficult to have your debts wiped out.

SA: And this was, wasn't it Tom Dacshle's number one priority for the session that ended in…

DH: Yeah when he briefly became majority leader, when Jefferts changed parties, he said he wanted to get that bankruptcy bill approved, so there are um…and thank god for the abortion nuts – they're the ones who stopped this from going through, because there was a fight over whether people who caused trouble at abortion clinics were going to be able to declare bankruptcy so they could avoid paying their fines. And we can only thank the religious right for having stopped the bankruptcy bill going through.

Audience: What is the median…

SA: The median income? What is the median income these days?

DH: For a family it would be about $46-$47,000.

Audience: For a family of four?

DB: For the average household?

DH: For a family that means two or more related individuals living together. For a family of four it would be a little higher. It would be about $50,000.

Audience: Can I ask you something? It's interesting that you say that the credit card business is the most lucrative in the financial sector. Is it dangerously weighted in that direction? In other words, in the same way that we, NYC, has be so reliant on a kind of mono-industry with Wall Street, is the financial industry overly…

SA: The regulators have put some constraints on how much of a bank's holdings can be credit card debt, I believe. It's a relatively small percentage. And I think it would be bigger if it weren't for the fact that the banks are prevented from loading up on credit card assets.

DH: The big discovery of the late '90s is what's called sub-prime credit in the industry, and that's poor people or people who've had credit problems in the past, and the great growth in credit cards in the late '90s was among people with…lower income people, and people with…you see in your mail, almost everyone gets like, one a day, at least, I can't remember the number of billions of solicitations they send out every year, but its an enormous number.

Audience: And every company sends…

DH: My favorite factoid about credit cards is that if you charge say $3,000 on a credit card and pay off just the minimum payment every month, it would take you 35 years to pay it off, so that's why they love credit cards so much.

SA: And you would end up paying a total principle and interest or some huge multiple…

DH: And there was actually a bill in congress at one point to require the credit card people to print on the bill how long it would take you to pay off your bill, just that minimum, and they went ballistic, you know, they just didn't want that to appear on the bill, and so they wrote a lot of campaign checks and the move died.

Audience: Do you think that's how some of the baby boomers will live out their old age, I ask hopefully?

DH: Well you can only go so far with it, because you can borrow for a period of time, but after awhile, your interest is, you know, exceeding what you borrow, so that won't get you too far. It would get you through, a year or two or three, but, you know, if you really don't have enough to retire on…

Audience: What don't you switch it around…these are people who produce theatre.

DH: Yeah, and then file for bankruptcy, but I can't counsel that, because it's counseling bankruptcy fraud. So I'm not advising to do that.

Audience: You can only declare bankruptcy so many times in your life?

DH: Yeah there's a seven-year interval.

Audience: Oh you could do it every seven years.

[Laughter]

DH: The average credit card… Do you have any…

DB: It's not very large; it's a few thousand dollars.

DH: If you restrict it to people that had debt, 'cause a lot of people do pay off their credit card every month, I think it might be more.

DB: Yeah, I mean the credit card problem is really concentrated among a minority of people with very high debts. Most people don't have, you know, serious credit card problems, but some people have really serious credit card problems, and that's what's driving the average number up so much.

SA: Well here's a question. We're talking about credit card debt and debt in general. Well who's loaning the money, who's lending the money, providing the funds, providing the savings for people to borrow. Globally in macro-terms, the U.S economy is borrowing money abroad.

DB: The U.S is a huge importer of capital right now, and you know, in Washington people start to say things. They repeat everything, and one of the mantras is the strong dollar **– everyone's supposed to like a strong dollar. I figure it's a kick me sign, so when someone says I support a strong dollar it's a code for saying, I have no idea what I'm talking about. Uh, what does a strong dollar do? Well its made our goods non-competitive – you know Doug was talking about why firms have no pricing power, and one of the reasons is that the dollar has risen about 20-30% in the last five years against other major currencies. So what does that mean, if you're a Korean steel producer or car producer, or whatever – you're selling your stuff for the same price in Korean currency today as you did in '97, we'll ignore inflation, you're selling it for the same price. Okay, well in U.S dollar terms it's 30%less; okay, so we get all our imports really cheap. The flip side of that, we're trying to sell our products, you know our computers or whatever it is we produce here, it's not 30% more for someone looking to buy that in Korea. So as a result of that we now have this huge trade deficit; our trade deficit is, taking in 4th quarter numbers, it's 480 billion at an annual rate. And then we have some other, you know, we have other outflows of money, so currently we're borrowing at an annual rate of about 550 billion a year. And this is a first approximation – we could think of that the same way we would a government budget deficit of that size.**

Audience: What do you mean we're borrowing 550 billon dollars?

DB: Okay, we're selling off assets in effect. What's happening is that foreigners are financing this trade deficit by buying up different types of financial assets.

SA: Lending us money.

DB: One thing they do is that they buy short-term certificates of deposit or buy treasury notes; they buy stock; they buy bonds; they might buy real-estate. Okay, but in total they're buying 550 billion more than what people in the U.S are buying abroad. And we could do that for a year with a huge economy; we could do that for two years, but you try and project that out, and, say, suppose we did this for ten years? Well carry that out and pretty soon we've sold off the whole stock exchange; we've sold off all our homes; I mean it's a little more than ten years out, but not too much more. I mean it's…you just can't drop that for very long. We're at a level of borrowing that simply cannot be sustained, and the only way to correct that is that the dollar has to fall. It has to fall by 20-30% possibly more, but that's something that will have to happen; it's better if it happens sooner rather than later, 'cause if it happens later, we're more indebted, and it will have to fall further.

Audience: How are you lowering the value of the dollar?

DB: I'm a big fan of talk. I said that Greenspan, if he wanted to have brought down the bubble when he made his irrational exuberance comment, that alone brought down the market for that day, and then he backed away from it. I have all these charts that showed how the stock bubble was impossible, Greenspan had all the same charts, he could have gone on CNN or testified before Congress, here are my charts. Same thing with the dollar – this doesn't make sense; the dollar has to go down; here's why. I think that would go very long way towards bringing it down. There's other things the Fed could do; the treasury could do, but first and foremost I think just calling attention to it, and saying this doesn't make sense, it's unsustainable.

Audience: And who could do that?

DB: The treasure secretary could do that.

DH: The treasury secretary is officially the one that's supposed to run dollar policy.

SA: And just the other day he made a statement that set a run on the dollar.

DH: And it seemed to be inadvertent.

SA: Right, it was inadvertent…they have a habit of this.

DH: [Robert] Rubin and [Larry] Summers kept saying things like, Dean's mantra, you know, the strong dollar is in the interest of the United States…

SA: They said that thousands of times.

DH: They said that thousands of times. Rubin must have said it in his sleep. We're in this kind of vicious circle, where the United States runs this very large trade deficit – needs foreign money to come in and fund it. We're essentially living beyond our means as a nation, and this is not…people in the mainstream and to the right say all this money is coming in, because it's the strongest economy in the world, and we have the brightest future around, and so it's just natural that everyone wants a piece of the action. That seems rather Pollyanna-ish to me, but it's bubble thinking. And this is part of the bubble that has not yet burst. But we need that money to keep coming in. And as the money comes in, it pushed up the value of the dollar higher – people are selling foreign currency to buy dollars, to buy these U.S dollar assets. So as long as the money keeps coming in, the dollar keeps rising, and it's also psychologically comforting to people who buy U.S. assets to see their value keeps rising, because the dollar keeps rising. Unlike most ordinary markets, with financial markets, it's very often the case that rising markets increase demand instead of decrease demand. It's like the stock market, because when the prices are rising, people buy. Because the dollar is rising, people want to buy U.S. assets.

SA: It's not like that for cars or clothes.

DH: No, no it doesn't work for normal products. But for financial assets, 'cause they're just so wrapped up with crazy thinking. So we need this high dollar to keep the money coming in, but the high dollar suppresses the demand for our exports, 'cause who's going to buy U.S. dollar-denominated computers, because you can buy Korean-denominated computers much more cheaply. So that worsens the trade deficit, and you get in this vicious cycle where the trade picture worsens; our current account picture worsens; so we need even more money to keep coming in. So at some point this is very much like the stock market – the bubble will burst, and things are going to happen that are not too pleasant. Now the dollar has come off its highs; it's off 10-15% in the last several months, so it may be that we're about to enter the next phase of whatever that's going to be. **How the United States adjusts to this arrangement is the big question for the next few years.**

SA: It's a big question all over the world.

DH: Yeah it's a big question for the rest of the world – our trade deficit really has been great stimulus for the rest of the world's economy. We're buying all this stuff from other countries, and we're borrowing from them to pay for it. It's a pretty good deal while it lasts. It's kind of like running up a credit card – it feels nice while it lasts, until the bill comes, and the bill is maybe about to arrive, or maybe in the mail now, or maybe waiting downstairs – we haven't picked up the mail yet. So that is the big question of the moment. So the United States also has a great bonus in that the dollar is effectively the world's currency. Most foreign central banks keep their reserves in U.S dollar assets – important commodities are priced in dollars; oil is priced in dollar. If that ever changes and serious competition comes from say the Euro, the

United States is going to have to learn to live in a very different world. In a lot if ways the U.S resembles Thailand in early 1997 – this is a country that was running account deficits; had over valued financial markets, and Thailand of course led Asia into this financial crisis. The United States is not Thailand; United States is not a normal country. If the United States were a normal country, it would have the IMF on our doorstep imposing a structural adjustment. The United States, of course, runs the IMF, so it's not about to do that to itself. So how does the United States adjust? I don't know, but I think we're about to find out.

SA: I think it's politically interesting that just at the moment when our government believes deeply that the United States doesn't need the rest of the world's permission for anything it does, we're more dependent than ever just for the basic functioning of our economy on the savings provided by the rest of the world. There was an article in the *Financial Times* just the other day, where they said that fund managers, you know the people who make these decisions about whether to hold U.S assets or not, think that a war in Iraq without Security Council approval is bearish for the dollar. Not for any particular mathematical reason, but because what does it say about the future direction of the US economy if we're going to be going into a war the rest of the world disapproves of, that we're going to have to pay the cost of? So it's sort of an interesting political moment now, because we get to find out whether you can sort of bully the world around while borrowing their money, while being in hawk to them.

DH: Yeah all these people who live in Old Europe as Rumsfeld called them, are the ones who are writing the checks to fund our excesses, so let's see, they don't have to. Yeah, especially now that the Euro is maturing as a currency, European financial markets are going to be redenominated in the Euro so there will be a very large place indeed to put a lot of money. I don't think anybody in the Bush administration is thinking about this. Are people in Washington really talking about this?

DB: You can't get anyone to have that conversation. Um, they just don't think about it. I mean as a practical matter, if you have the war,that increases the dollar outflow, because a lot of it is for buying weapons back here. But some of that's going to be for buying things. You know, we're occupying Iraq – that's US dollars going out, paying for services in Iraq.

SA: They try to ship as much of it as possible from the States.

DB: They do but they will be getting some there, but the other point to be made about this…

Audience: Did you just say that the dollar value will rise?

DB: No, you know, the dollar outflows, you know, we will have to borrow more, because there are more outflows also for bribes. But the other part of this, the point Doug was making, you have people actually taking a beating by holding dollars rather than Euros, because if you're a smart investor you go, I want the best return of my money. You're holding a three month treasury bill that now pays an interest rate of 1.25, something like that. You'd be getting *that* rather than if you were holding the Euro three-month bill; then you'd be getting 2.5 percent interest. But more importantly, your Euro has appreciated by about 10% against the dollar over the last six months – you just threw a lot of money in the garbage. So it's not clear how much longer investors will be happy to throw money in the garbage in order to hold dollars.

SA: But there are artificial reasons, aren't there, why people who might otherwise not choose to hold dollars and fund our trade deficit do so anyway, because they sort of have to because if they need to buy oil; they need to keep reserves for foreign currency intervention.

DB: The amount that they have to hold for those reasons is very small compared to the stock of dollars out there. So that contributes to the demand for dollars, but that's very small compared to the stock of dollars.

Audience: In terms of whether anybody is actually better in a so called boom economy…What is the figure that used to come up…household income of people working more hours, fewer dollars, so that kind of a rise itself in calculation, and then within the inflation calculation you have certain grades of product like technology and long distance phone calls, but the life and death things, healthcare and housing and rent, the prices go up astronomically, so there's these two kinds of mirages built into the whole sense of how our economic well being is conveyed to us. I mean you would think that in terms of factoring in inflation, has there ever been a point in history where there was such a dramatic…where the calculations of people who made the same…dropping and one going up like that, and is that a big change?

DB: Well it's not that uncommon to have relative prices to move in different directions. It's extraordinary when you look at some of the high tech items that have just plunging prices. Some of that's just a measurement issue, though. I think it's…you have people at the basement of the Bureau of Labor Statistics, and it's not anything you see in the world, computer prices. If you're going to buy a computer, it's not 40% cheaper this year than it was last year – you may be getting a better computer, but you're not going to make 40% less. But you look at – to me the best indicator, just sort of quick glance indicator, if you know how people are doing – is the median hourly wage. And that rose fairly rapidly in the late '90s; it rose about as rapidly, maybe a bit less than it was doing in the '60s, but 1.5% a year from '96 to 2001.

Audience: In real terms?

DB: Real terms, adjusting for inflation, that gets you about back to where you were in the end of the '70s, you know, because we had a long period of decline. So, you know, we made up some good ground in the late '90s; it would have been great if that continued. For now at least, it doesn't seem that it is – whether it does or not once the economy gets back on its feet, or maybe it depends on how long the economy is off its feet, we'll have to see. I think the late '90s were a good period, but we had a lot of bad times to make up for and we really didn't go very far into doing it. It was a step in the right direction.

DH: Even during the good years, people were working harder and longer, the number of hours of work it takes to make the average household income keeps rising. More people working, more people working longer hours, and we heard constantly about this productivity revolution in the late '90s. You think you could take some of the productivity pay-off in chilling out a little bit, but it's not working that way – people just keep working harder and longer hours. And now the recession – people are working shorter hours, because the boss doesn't want him to work, so there's this kind of enforced leisure in a recession, but the U.S economy is in most times a workhorse economy. We have some of the longest workdays, workweeks, work years in the world. We're only beaten really by…I think Japan's actually fallen back because of their recession, so Korea, they're below us now. Korea, I think, is about the only country with a longer work year.

DB: I think even that might be changing 'cause they're going down, and we're staying the same or going up.

SA: And that's interesting, because before we were talking about, is it in the interest of employers to have a low unemployment rate or a high unemployment rate? People were saying if the unemployment rate is low, people have a lot of money to spend on our products; if the unemployment rate is high, then wages won't rise as fast, which is better for them. I guess the real answer is, the best thing for them is to have people who weren't in the labor force to begin with before coming into the labor force to work for them.

DB: But they're perceived as low quality.

SA: Is that right?

DB: Yes.

DH: Firms always want to pay their employees absolutely as little as possible; they complain like crazy whenever, I accept that, if you want to call it "class warfare," I don't have a problem of calling it that, but the thing is that firms live with that. They complain, but they lived with that; they lived with that in the sixties; they lived with that in 2000. I mean one of the things I do, I write a report on the Federal Reserve Boards beige book – this is the report they – remember there's twelve federal reserve banks, there's one in New York, there's one in Boston, there's one in Richmond, they're scattered across the country, and every six weeks they write up this statement about how the gross economy looked in their area. And back in '99-2000, when the unemployment was getting down to 4%, the accounts – they mostly talked to employers, every now and then, very, very, little talk to unions, but mostly they were talking to employers – so all these accounts – we have to accommodate our workers demands for childcare; we have to go into inner cities and bus people out; we have to hire people with disabilities; they're very unhappy about that. They'd rather just hang up a sign and get hundreds of people there, and they'd pick the ten best. But the fact was that they were doing fine – they were making profits; business was good. So to answer, would they rather pay their workers less; would they rather have it easier? Of course. Does that mean that they can't survive in those circumstances? Absolutely not they're doing fine.

Audience: I have a question then. I have a sense that the economy is in a mess; I don't know what the indicators are beyond unemployment for me, which I consider a major indicator. I don't understand where or how to look to say 'oh its getting better, or it's getting worse.' Because, I mean, you don't want to rely on the stock market – that would be ridiculous. So where, what are the indicators that you in particular suggest that we keep an eye on?

DB: The best conventional measures are the monthly employment reports – first Friday of every month the Bureau of Labor Statistics releases it – it's got a numbers on the amount of jobs that are created or destroyed in the economy. They have two surveys: one they serve the employers, the so-called establishment survey, and the other serves a household. And the survey for employers, this is the one that tells you we lost 308,000 jobs last month. Employers file these reports; the Bureau of Labor Statistics compiles these numbers every month to produce this. That's also where they get figures of what's happening with hourly and weekly wages. So you can get a sense from that of how many people were working; whether their pay was rising or falling; how long the work week was, etc. And on the other side the households report on unemployment, whether people were having multiple jobs; whether people were working part-time, but they'd rather work full time…That report, I think, is the single best picture of what's happening on a human level, where the economy connects with peoples real lives. It's very timely; it's available every few weeks, and it's high quality. So that's the best single thing to look at. There are also all kind of subjective indicators to… For example, in the late '90s, the economic indicators looked as good as they get, but are people stressed; are people alienated; can they pay for healthcare – there are all sorts of much more subtle things that the conventional indicators can't always answer. We supposedly have this economy that was the envy of the world – you walk into a bookstore, and you see shelves full of self-help and recovery books. There's something wrong – even when the economy is working well, it doesn't necessarily make people happy. So there's often a very big gap between what the indicators are saying and what people are feeling.

Audience: A lot of statistics…particularly when it comes to employment…

DB: You can get all those numbers – if you know where to look for them, they're there. Very often in a recession, self-employment rises, because people get laid off, and then they said, well I'm a consultant. So they may not be working, but they're pretending to be working. So they're a consultant – you see those sorts of things. Getting back to indicators, one thing that is hugely misrepresented in the media on this is GDP growth is often used as sort of an all purpose measure of the economy. And it's valuable; I'm very glad we have GDP. It's a useful measure for many purposes, but it's not measuring how society is doing, and it doesn't necessarily give you a good indicator of the economy.

SA: First explain what GDP actually measures.

DB: Okay. GDP in principle is supposed to be the value of all goods and services produced over a period of time. Typically they do it on an annual basis, so we're just adding up all the cars that were produced and all the services that were provided – things like restaurant services, airplane rides, healthcare services. Everything the economy is producing over that period of time, you just sum it up. The point I was going to make, some of these things [….??...] bombs at the GDP if were spending another hundred billion on the militarily well that's part of the GDP just as if we were spend it on schools or education, in principal I doesn't, cause we'll all feel safer and supposedly better off, but that may not be the case, but there's a lot of things in GDP that may be not be helping us that much but the other side of it is that GDP is we need a denominator to the equation that is gets back to Doug's point about how much people work. In Europe in Japan as the economies have gotten more productive over the last 2 or three decades they've taken the gains of that productivity to a very large extent in the form of less work time, so its absolute standard in Europe that people get 4,5 6 weeks a year of vacation, in fact to join the RU, I want the U.S to join the EU cause then you get 4 weeks a year of vacation at least, bare minimum.

SA: Is that a EU requirement?

DB: Yeah, it's an EU requirement. So if we can get the U.S. to join, we'd be cooking- Old Europe. And people talk about how they have no growth. I don't know how many times I've seen in the *Times*, I'll do a pitch for a weekly commentary, online commentary, on economic reporting in the *Times* and the *Post*. You can get in on our website, CEPR.net…

SA: That's the *Washington Post*.

DB: *Washington Post* not *New York Post,* but **I don't know how times I've seen references to Europe's slow growth, and they talk about how this is a bad thing; they take long locations; they have you know a 35 hr work week in France. Well if someone wants or work 50, 60 70, hours a weeks and some of us do, good, but for a lot of people that's not their goal in life and you know that every bit as legitimate a way for people to take the benefits of higher productivity as getting more money and buying another SUV, its often misrepresented but its not a bad thing people in Europe choose to do that, people in Japan choose to take more leisure time, and no economist has a right to tell them that's the wrong thing, that's their option.**

DH: There's a very funny piece in the *New York Times* I think it was 1997 by Alan Cowell about, there one of these almost everyday, lecturing Europe on how tired and old they are this was specifically about Germany, it was complaining you know Germans like all this time off, he actually said they need to get in touch with the American way, and this is a direct quote, "working harder for less", and this was a selling point apparently.

Audience: …I just wonder how long it will take for this information to really filter into mainstream media and for the economy to become alive…for Bush…the …2004 these numbers, the administration now says a balanced budget is a priority, what in the *Times* in the *Washington Post*…I feel this information is hidden again and again and again every day, it's certainly not in mainstream network news, we don't hear these stories they sort of get glossed over I don't remember why with Bush one the economy sort of become a liability, if the economy came alive for him, what has to happen in the next…

DH: I think you have to separate certain things, I mean, to go back to my Chicago background we had a mayor, the one who immediately followed Daily, the Senior Daily, when he died, who lost for reelection, because there was this huge snowstorm that they were completely unprepared to deal with, and anyhow a week or so after the storm, he had a press conference and someone said, how come the side streets still aren't clear? And he said, what do you mean? The side streets are cleared. And anyone could go outside and see…And there's an aspect to that in the economy where people know if they don't have jobs, so if we're still sitting around a year and a half from now in October, and the unemployment rate is still relatively high, they'll know that.

Audience: Well what about the tax cut? The tax cut is this sort of bizarre thing that the administration wheels out, because people don't pull it apart and see who's going to benefit.

DH: Well they may or may not know about that, but what I'm just saying is he can promise all the tax cuts he wants, but it's his economy come November of 2004. But as far the long term issues, none of that will ever get in the media, because the people writing on it have no idea what they're talking about, with very few exceptions. So in fact, I mean, I actually think the budget, well his deficits are getting very large, but the way that it was talked about has been 99% idiocy when it was Clinton and when it was Bush. When Gore was running the mantra was "lock box" – save the Social Security surplus. Stupidest thing I've ever heard anyone say. It was impossible; it was not desirable. You know, it's one of the things that scares me to death – suppose Al Gore had been elected; we would have a deficit; the only way he could prevent that would be to have spending cuts and tax increases in a recession. Would Al Gore have done that? Well, with Tom Delay jumping up and down and yelling and showing the videotapes, "I promise you," Al Gore might have done that, the man with no backbone. And this was talked about at a level of idiocy you can't believe.

SA: And Gore during 2000, during that campaign, he was specifically asked about that, in a *Wall Street Journal* piece…

DH: He said he would raise taxes.

SA: They said, well okay, we're in a boom now, but what if we were in a recession. Would you still raise taxes or cut spending to cut the deficit? And Gore said just like a business does when you run into hard times, you gotta cut back when your revenue falls off, which is…I doubt you could get even the dumbest economist to say that.

Audience: Are you saying that, that's just a purely cynical ploy because they can say that something that people don't understand? Or are there other schools of thought?

DH: Totally focus groups. I've been in conversation with these people – it's totally focus groups. They couldn't care less whether it makes sense. He has advisors who understand completely that that's idiocy, but if they'll be able to carry the day…Let's imagine we're in an Al Gore residency – we're in a recession; we're looking at a 200 billion dollar deficit, and you have all of his advisors saying it would be the stupidest thing in the world, but you have his political people saying, you're going to get skewered, you said you'd save the Social Security surplus.

SA: But you have to ask where the focus groups come from. Where did all these people get the idea that balancing the budget and putting the Social Security surplus in a lock box and all these other crazy ideas, where did they get the idea that this was sound policy? I mean these people aren't experts.

DH: It's homey analogies. You know, we're sitting around the kitchen table doing our financing, and if the income comes down, we have to cut our spending.

SA: But they're selective, I mean they don't do that w ith the trade deficit

DH: No.

SA: As if you're a household sitting around the old hearth.

DB: But the Democrats played into this going back to '98. We owe Monica Lewinksy – she saved Social Security. Clinton was going to privatize it, 'cause the dynamics changed completely, and he decided that the most clever thing in the world was to say, oh we're going to save Social Security, and that eventually got built into this lock box thing, so that got repeated a lot. Again we think about this very differently than they think about this. There's somewhere we want to go – we want to get to a better society; we want more equity in jobs and healthcare – these are things we care about. They care about the next election. So they're going out there saying the smartest thing our focus groups tell us is to save Social Security. It's not really in danger, but we don't care – put it in the lock box. So they start saying that and then this is self-reinforcing.

SA: But what I was trying to get at before is that these idiotic clichés about what the correct sound thing to do with the economy is – you gotta balance the budget all the time, put social security surplus in a lock box and so on, it doesn't just come from focus groups and political consultants, those focus groups and political consultants have this message reinforced when they read the *New York Times* and the conventional wisdom that the reporters put forward is if you have a deficit, that's a bad thing.

DB: A generation ago the conventional wisdom was you need pump priming – that was the homey phrase that would come to mind. Prime the pump if the economy is weak, and that was a holdover from the '30s New Deal, Keynesian thinking of the '30s, through the moment when Richard Nixon said we're all Keynesians – now that was the end of it.

SA: The contrary indicator.

DH: And then there was this big shift in the economics profession, but it also reflected a shift from the elite, going back to what I was saying earlier about that sense that things were out of control – the masses were rebelling; the working class had a bad attitude; the third world was getting rude, all these things. And the response to this was a strong dose of discipline. One of the forms of discipline was budget cutting, and so the elite came to think that what was needed was austerity, and that meant cutting spending and eliminating from peoples' minds the idea that they were entitled to anything – no benefits, no entitlements, you are out there on your own. So there's this big change in elite thinking, from worrying about the system falling about in the '30s into the earlier decades after WWII. There was still this lingering anxiety that depression would lead to the economic and political collapse of capitalism as we know it. They stopped thinking about that and really wanted to have a big class warfare crack down, and that I think it's the origin, the ideological origin of this big shift in the conventional wisdom was from the necessity of having the government being the protector and guarantor of full employment to you're out there on your own.

Audience: Isn't it also true that from about 1966 on, there was a big decline in the rate of profits which, began to register…

DB: 1969-82

Audience: …in the '70s began to register with the oil companies and that only began to recover to pre-1966 levels at the peak of the boom…

DH: The '66 numbers were somewhat inflated by the war so if you look at the '60s, what happens is it peaks at '66, so if you go back, if your standard is 1962-1963, we're up there by the '90s, by the mid '90s – '94, '95, '96…

SA: But we surpassed it.

DH: We surpassed it; we didn't quite surpass '66, '67, I forget which year was the peak…

DB: '66 was the peak profit year.

DH: We didn't quite surpass that, but we surpassed the early '60s.

Audience: I wanna go back to what Dean was saying which is – my eyes are crossed – it seems there's a lot of people out of work, but there's going to be more people out of work. Unemployment is rising, am I correct? The number of people out of work and the number of jobs being created…

DH: It's probably going to rise.

Audience: So if that's the trend, it doesn't take rocket science to understand that, and so when Bush says tax cuts, how is it that the average person doesn't say, I don't understand how there can be tax cuts when the economy is in the shit.

DH: Well in principal, a tax cut when the economy is in a bad place isn't a bad idea. You just don't want to give it to the richest people. He's being dishonest about that, so if you listen to what he says on it he goes, my tax cut gives an average of 1200 bucks to 92 million families, and it's a true statement. Suppose he gave it to Bill Gates and brought in 91 million other families in there, that's almost literally what he's doing. It gives a lot of money to a very small number of people; it gives a few crumbs to everyone else. And then you go, there's 92 million people who benefit from this. So you and I know this, people who follow this stuff closely understand that, but the media doesn't make a big point of going, this guy is lying.

DB: Paul Credner is the only one who'll say, this guy is lying.

Audience: We have an opposition party, and nobody is standing up in congress and saying, this guy is lying?

SA: But even with the opposition party, I mean, one of the few things that the Democrats are willing to stand up and say is that the Bush tax cuts give most of their benefits to the richest people. But even in that example, when you do, in this case, finally have the Democrats willing to say something critical, but the mentality of the reporters is that it's not their job to figure out what's true – it's their job to simply report what both sides are saying. And there are these reporters who are famous within the industry within the Washington press core for being these eccentric mavericks who don't follow that example, and the famous example of that is Dana Milbank from the *Washington Post*. He's a White House correspondent, I think, and among the press core in Washington, he's sort of famous. People will actually say, oh that's daring, because he'll actually say, the President said this yesterday, and explain why it's not true. That's eccentricity; that's not the way you're supposed to do it.

DB: That's not the way to get promoted.

SA: That's certainly not the way to get promoted. I don't know what Milbanks…who he's related to. He gets away with it, but most people don't do it. So I think that's the thing. I mean, most Americans are incredibly disengaged from politics, and if they happen to catch a snippet on the evening news, where they have Bush with his sound bite and Daschle with his sound bite, and one of them is saying that the benefits are going to go to Joe Sixpack and the other is saying it's going to go to the rich, who can tell? I'm not an expert – I think that's the way a lot of people think about it.

DB: A lot of people think too that they're richer than they really are. There's a poll that's been slightly misquoted, but it was done after the 2000 election in *Time* magazine, and the question was, do you think you're in the that top group that's going to benefit from the presidents tax proposal? Really, it's only a few percentage points of the population that are going to benefit, but 20% of them thought they were going to benefit immediately and another 20% thought they were going to benefit eventually. So you have 40% of the population that's deluded into thinking they're part of this elite that's going to get tax cuts from Bush.

SA: I don't buy that, because the poll didn't say, do you think you're part of the top group, it said do you think you're part of the group that will benefit from the tax cut?

DB: No it did say the top group.

SA: The top group? Who knows how they're interpreting that question. My understanding is, people who are in the upper middle class think they're in the middle class in the country - it goes the other way.

DB: But people did think they were going to benefit from the tax cut.

SA: I think that's because they misunderstood the tax cut, not because they misunderstand their income – that's my interpretation. It would be an interesting thing to do an academic study.

Audience: What seems to be happening is that there's this big disparity, which is growing, between most people and the very rich, and that's been going… that's still going on. Nobody seems to know why or how that's happening. What can we do to reverse that?

DB: Well, they know why. You know our trade policy has been oriented to undermine the position of manufacturing workers; anti-union policies make it almost impossible to unionize; the real value of minimum wage – we did have a rise back in '95, '96 but none since – it's well below the peaks back in the '70s, even though productivity is 30-40% higher. So we can find a lot of reasons as to why that is the case, but the bottom line is that the people setting the policies are being put in office primarily by the ones who benefit from them – those are the ones who make the campaign contributions. So you know, we could figure out answers, it's just that they're not going to solve the people in office.

DH: And the major thing is that the very elite are doing very well – even the upper middle class didn't do anywhere near as well as the top 1 or 2% of the population, so it's people with incomes of $400,000 or more that are really making out like bandits. It's just amazing – it's never become a big political issue. Uh, and I think part of it is it's just deeply rooted in American culture. We're all out in this world on our own, and you're paid what you're worth, and you just have to write a better resume, and work harder, and if something goes wrong it's not the fault of the system – it's your own fault.

Audience: The rich vote with for their pocketbooks, the poor vote for their aspirations.

DB: Yeah, but I just want to point something out, because it's often very affirming, and I'm not accusing Doug here of doing this, but somehow we want the government and they want the market. And I just really think that's totally wrong, 'cause they don't want the market any more than we do. They want to shape the rules so that rich people come out ahead, so autoworkers in the U.S have to compete with autoworkers in Mexico, Malaysia and China. Doctors in the United States do not, they deliberately wrote rules so that it's very difficult for a foreign educated doctor to come and practice in the United States. Quite deliberate, quite deliberate.

Audience: They have changed it recently.

DB: It must have been very recent.

Audience: Very recent, within the last two weeks. Doctors no longer have to do a year of study and rewrite their thesis.

DB: Well we'll see how much impact that has.

SA: That's Canadian doctors?

DB: Oh well, that's just one group then.

Audience: I happen to know because I am Canadian…

DB: Well if might be part of NAFTA.

DH: I though NAFTA allowed professionals to work with either country?

DB: You have to meet licensing requirements.

SA: Explain what the importance of this is, this distinction between the manufacturing workers and the doctors.

DB: Okay, the point here is that our trade negotiators in the WTO and NAFTA, they want to make it as easy as possible for General Motors, General Electric to open a factory in Mexico and hire workers for a buck and hour. Which means that any worker here has to compete with a worker in Mexico, who's willing to work for a buck an hour. 'Cause that's a good wage there. Our doctors don't do that because our trade negotiators are not trying to standardize education and licensing requirements; they're not sitting down and saying okay, how do we make it so that a smart kid in Mexico can get educated as far as necessary in Mexico, maybe they complete their education in the U.S, and then come and practice medicine in the United States? They have never done that – they've done the complete opposite. They've actually taken steps in '97 to make it more difficult for foreign doctors to come and practice in the United States. Same with law, same with accounting, same with academia. We could have negotiated so that we said that state universities cannot discriminate against foreign academics, and they have to have a standard hiring practices so that our PhDs have to compete with PhDs from India, China, etc. on equal footing.

SA: If they had done this what would the result have been?

DB: The result would have been that wages for those groups would have plummeted. Instead all these groups think they're just real smart and they just benefit from the global economy. That's bullshit, they benefit from the global economy 'cause they rigged the rules.

DH: And of course when something goes wrong, they're the first to turn to the government for a bail out.

SA: The airlines…

DH: The one experience I even had in mainstream media where I actually didn't feel like I was speaking Martian was uh, on the Charlie Rose show after the Mexican crisis, and I was surrounding by editorialists from the *Wall Street Journal* and someone from Goldman Saks, and they were saying, we need to get the government to give a rescue package, blah, blah, blah. And I said, well you guys are always talking about the beauty of the market and competition and discipline, and you're always complaining about welfare, and here you are – you run into trouble and are running to the government for a handout! And Charlie Rose liked that he said, yeah, yeah what about that? And so it was the first time I really felt like I had managed to set the agenda for a mainstream event – most of the time I feel like I'm speaking Martian. But it is amazing – whenever these guys run into trouble, they are the first to turn to the Federal Reserve for a bailout or to the Exchange Stabilization Fund for a bailout. But if you're a poor mother and your welfare check runs out, it's your own fault.

SA: There's something that you said earlier about the American tradition, American culture that has these deeply rooted individualistic ideas that prevent people from thinking about inequality. There is a counter-narrative, a New Deal narrative that was pretty widely understood and shared by a lot of people.

DH: Well it took a 25% unemployment rate for that to happen.

SA: But it lasted for a while, it lasted for several decades, and I do think that…I think your point is you can't just blame the Democrats for not bringing it up, because they're sort of reflecting a deep-seated, cultural phenomenon in the American psyche. But I do think you can blame the Democrats a lot – they could be making the point that you made on Charlie Rose every night. I think that's a point that a lot of people will respond to, and they don't do it.

DB: What about trade agreements? How many people knew that we had restrictions on foreign doctors to make it more difficult for them to come in the country? How many people knew that? I don't know many economists that know that, because in '97 when this was going on the debate was an incredible debate, because on the one side there were people who said, no this is good that these people come here, because you have these foreign doctors that come and serve underserved areas – you know, they work in inner cities they work in rural areas. And then the other side was, no they're lowering our wages. There were no economists there saying, this is good; that means cheaper medical services, greater efficiency; they weren't there. They're there when you want them to get down the price of autoworkers – they're there then, but when it came to doctors they're nowhere to be found.

SA: There was a great quote from a guy who I think at the time was Goldman Sachs' Germany chief, Thomas Meyer. He was quoted by Bill Geider, the reporter in one of his books, and he was in Frankfurt, and he was complaining about, as you were saying they lecture the Europeans day after day about their unreasonably high wages and vacations and generous pension benefits and healthcare, and **this guy Meyer, who is quoted all the time in the American press** – I'm sure Dean runs through quotes from his twice a day about the German economy and how you've got to lower wages there. And this guy, he writes op-eds in the *New York Times* and so on, and he told Greider, Greider said well what does Europe do? And Meyer **said, well when I look out there on the trading floor, I don't see any need to get the wages of the traders down – that's beside the point. What you need to do is lower the wages of the janitors and widen the spread between them, and then we'll get more growth. That's almost a direct quote – I've quoted it so many times in print I know it almost word for word. That's exactly what he said. And this is a guy who was regarded as an authority and actually quite a reasonable, moderate, sane authority by the people who sort of shape opinion on economics in this country.**

DB: Well, he would defend that by saying that the reward for being a janitor is too high and if you're paid crappy then you're going to either live with the consequences of that or work harder and improve yourself and then the economy will be better off so poor, as George Gilder and such argued in the early eighties when they were promoting the end of welfare the poor need the spur of their poverty, I think is the phrase that Gilder used, and any attempts to soften that with welfare measures or higher wages are really detrimental to the economy.

SA: There's the John Kenneth Galbraith quote about how poor people need to have less money so they'll work harder and rich people need more money so they'll work harder. I butchered that…

Audience: With the tax cuts…what truly is the incentive for doing it? I have probably very cynical opinions about doing this, but…

DB: Those are probably correct.

DH: One thing in terms of whether it will stimulate the economy that will just show you how horrible the economic reporting is, go and read it – it used to be on their website, its probably still there – they never called it a stimulus package. They never even claimed it would stimulate the economy.

SA: They were defending is against the accusation that it would stimulate the economy too much.

DH: Stimulus is old discredited Keynesian crap – what we need is long term incentives for growth.

DB: So they don't claim it will stimulate the economy – that's something that people…

Audience: Who writes that then?

DB: The media had to make it sound like a credible proposal, so they had to say, you know, talk about a stimulus. And the Bush people didn't make a point of correcting them and saying, no, it won't do that. But it wasn't intended to do that…

Audience: What's it intended to do?

DB: Well, I think Doug's exactly right. It gives money to rich people, but I mean, if you try to be as generous as possible to them, and say what's the story, how would this help the economy? The argument would have to be something like this – that because you're increasing the rate of return on savings, you know I can put my money in a stock and never pay a penny on it, a penny of tax on the dividends.

SA: You're talking specifically about the dividend tax?

DB: The dividend tax. But the others as well, you're lowering the tax rate so that…What that will do is encourage me to save more, but its really hard to understand this fully, because the government is saving a lot less because it has a larger deficit. Now in the way new classical economics works, it's just one big pool of savings. So if the government's putting in less, I have to save an amount that's even larger that the tax cut. Not me cause I'm not that rich, but the folks that are getting it have to save an amount that's even larger than the tax cut. I don't know anyone who thinks it's going to happen; it's such a far-fetched notion. So it's almost impossible to tell the stories of how this would promote that.

DH: They would also argue that governments waste money, so when you take money out of the government hands and put it in the private sector, it's going to be allocated more effectively, more productively. And there are people who would argue, the *Wall Street Journal* is arguing now, that this fiscal crisis for state and local governments is a good thing, because it'll force them to cut spending. They'll be more efficient in what they do spend, with what's left in their spending, and that will allow the private sector to take over.

DB: Okay, but I want to be very careful, because we should never give them more credit that what they deserve in what they're putting forward. So if they're saying tax cut, just tax cut – that increases the deficit. The only way that could increase growth in the standard models is if people save an amount that's in excess of the tax cut; if they're getting a hundred billion tax cut, they have to save a hundred and twenty billion. Now Doug's saying they'll do better with the money than the government would, but the government's spending just as much. How many of them think – and it's probably true – if the government doesn't have the money, then you will see cuts in spending. So behind there is an agenda that they want to have all these spending cuts, but that's not on the table. So what is on the table right now is the tax cuts. So we're comparing the world where, we have a hundred billion additional tax cuts, the governments still spend just as much, and in that world the only way they can get additional growth is if somehow people increase their savings by an amount more than a hundred billion.

DH: These guys are completely incoherent and dishonest, so I'm providing some kind of theoretical clarity to what they're doing that they wouldn't provide themselves, 'cause this really is a gang of liars and hacks.

Audience: Would you say that the liar and hack index is higher than in the past?

DH: There are a lot of Democratic hacks and there was a lot that was dishonest about Clinton's budgets. For example, the pros that went with the budgets during the Clinton years was, we're investing in people. The level of dishonesty is much, much higher with this gang. I mean, the budget estimates, just the technical budget estimates – they're not doing ten-year projections anymore; they're doing five-year projections, because the ten-year ones would look too bad.

DB: It's even worse, because the rationale for doing five-year rather than ten-year is that the ten-year budgets are very…they get very fuzzy, this and that. That's the official rationale. But what they're actually doing is they're deliberately front loading their tax cuts, so some of the changes –
I won't get into all the technicalities of this – but some of the changes in their IRA proposals will increase tax revenue over the next five years at the cost of tax revenue in the second five years. So they're taking advantage of that, 'cause I would be on the one hand, sort of sympathetic to saying, okay, five years we can know, but ten years? But they're deliberately stacking the deck and taking advantage of that.

Audience: We run theatres we know exactly what that's about.

SA: Question back there?

Audience: If there are instances like that, how would you inject that into the discourse?

DB: There's a standard measure that economists use the Gini Co-efficient that takes, uh I can't think of a simple way to describe.

DH: Well it's a number between zero and one – the higher the number, the more unequal the society is. If we have a society where one person had all the income, the Gini would be one; if we had a society in which every one was equal it would be zero. In practice, Sweden is around a .25 the United States is a .5. It's just a way of saying society X is more equal than society Y, and the United States has gotten more unequal anyway.

Audience: Does that become an economic indicator in any way?

DH: No, almost never; people don't talk about it.

DB: It's a good indicator, but there are other ones. I tend to look more directly at wages. You look at the gap of, say, wages at the 90th percentile, and someone, their wage is above 90%, and compare that to the middle level workers, and someone at the tenth level. So there are different things you could look at. I tend to focus on that more. But in reality – Doug talks about this; I talk about this; there's a few other economists, but it's really buried in terms of economic debates – it doesn't get out much.

Audience: Say a CEO or a waitress…What's the difference in wages between workers and CEOs? Is there a recent thing that you could point to…

DB: Well on and off, their wages are controlled by higher management, and how is top management controlled? Well, it's controlled by the major shareholders, where were they? They were totally out to lunch, so what happened was they let these guys take over the companies; run them for their own interest; make out fortunes, and in many cases bankrupt the company, even if they did a good job. Who says they deserve two, three, four hundred times the wage of the average worker? They tend to, usually…it might be in every case, they have compensation committees that are usually appointed by the board, but in practice the CEO usually has a very large say in who sits on the compensation committee, and very often they're their friends. So they go, well I want to get double what I got last year.

DH: There's also a big change in the way CEOs are paid. Back in the '50s for example, I think the highest paid exec in the *Business Week* annual roundup was the CEO of General Motors, who was paid in 1950 what would be the equivalent of 2 millions dollars today. Obviously that's what some CEOs make in a day or a couple of hours now, and the big change was moving away from paying just straight salaries to paying them in stock or options. And the rationale behind that was that the stock market is so wise that if the stock is going up, they're doing well, if the stock is not going up, they're not doing well. The CEOs will do everything they can to reward the stockholders, and if they're not then they'll get punished, because their pay will suffer. Clearly the stock market is not very wise. It's kind of a foolish thing, and it rewarded a lot of people who didn't deserve to be rewarded, and that's the main reason why these compensation packages got so huge. Because they were so oriented towards the stock market, and we had this great Bull market – the CEOs cashed in, and you know like Dean said, the board who sets pay for the top execs went along with it. Bernie Ebbers at World Com actually got bonuses, like retention bonuses, just so he'd keep showing up for work.

SA: But it also created perverse incentives in other ways, because once their compensation got tied to the stock price, suddenly it became very attractive for them to have the company borrow huge amounts of money to buy up shares of stock on the market to drive the price up. And that's one of the reasons why when this recession started, we had a large stock of debt that corporations were holding that forced them to stop their investments and fire people. I think that was one of the contributing factors to the recession.

DB: Yeah it certainly gives them incentive to buy back shares, drive up the stock price rather than pay out dividends.

DH: And cook the books too.

DB: Yeah, it gave them huge incentives to cook the books, and one thing to keep in mind, some people have flipped over the causation – they talk about the accounting scandals as having led to the collapse of the stock market, and really the dam runs the other way. It was the bubble that created the environment in which you could have the ENRONs, World Coms, just putting down nutty numbers. I mean World Com – two thirds of their profit from 1999-2001 was invented. You know how could that be – you're supposed to have stock analysts that get paid 6 and 7 figure salaries to figure out what World Com is doing, and yet two thirds of the profits were made up. You could only do that in a nutty bubble environment in which you could put down anything and go, oh that's okay.

SA: The one question that I have, 'cause I don't know that much about corporate governance is, it seems to me that you hear shareholders complaining, sometimes, about CEOs' salaries and executives' salaries and executive compensation. They say, they're using our money to pay these lavish salaries for the executive, but on the other hand, it doesn't seem that they get as mad at money wasted on executives as they get about money wasted on workers at the company, or is that just the illusion of class solidarity that I'm imagining? But it really does seem like if a big company hires 10,000 workers, Wall Street will get madder than if they spend the same amount of money lavishing their executive with perks.

DB: Well, I think it is an issue of class solidarity – it's somehow whatever you spend on your CEOs, if you gave them 200 million and maybe they should have gotten 2 million, it's, well maybe that was a little excessive but no big deal. But if you gave 10,000 workers a thousand too much, which is actually less money, then that is a big deal. So I really do think it's a class thing, because in principle what they should be looking at is the costs of the company. And they should be every bit as pernicious that they're giving, from the standpoint of maximizing returns to the shareholders – also, one other point, Doug's exactly right about the stock options, but one of the points that's just to me sort of remarkable, if you bought that thing about stock options tying the interests of the CEO to the interests of the shareholder hook, line and sinker, the one thing that I would want to say as a shareholder is that I want my CEO to be compensated for doing something that makes my stock do particularly well, and not just cause the stock market went up. Very simple thing to do, you just index it, you just index the options to say, okay, you're in the auto industry, so if GM stock does better than the other auto company stock, then you get a bonus based on that. We may or may not like that, but that would at least make some sense. But instead they just say if the stock price goes up, you're rich. And basically in the late '90s on the Bull market, unless you're doing something really incredibly bad in running your company, your stock price went up.

Audience: Are there ever governments that try to moderate that or legislate that?

SA: Yeah why are CEO salaries lower in Germany?

Audience: But is there any governmental ruling, or legislature or relationship that…I mean, it's not going to come from the corporation.

DB: In Europe there's much more of a tradition. Banks hold large chunks of corporate stocks in continental Europe, this isn't true in England, and they wouldn't have put up with that. Now that is changing, although the change maybe reversed. They're trying to emulate the American model in 1999, 2000. They may no longer be trying quite the same way but that, to some extent, put a real brake on CEOs salaries, 'cause they'd look at these and they weren't about to hand them the store, you know, they weren't going to let them walk off with 50 million or 200 million dollars – there are some norms about it. They have stronger unions there, a somewhat more responsible press – it would be considered really outrageous for someone to walk away with those sort of salaries, and the people that did in these companies really became sort of pariahs. The guy at the Venda in France – which is now in major bankruptcy – he was paying himself tens of millions. He's now out; that was really an outsider, actually. There were institutional structures and norms that prevented the sorts of runaway salaries in Europe, and they were weakening in the late '90s. I don't know where it stands now. I think the blowing up of the stock bubble here probably has strangulated the forces in old Europe.

SA: You have friends among economists in Europe. You used to complain that they have this sort of foolish faith in the American model back in the '90s. Has that changed in their eyes?

DB: Yeah, I mean, I remember I was at a conference at the Brookings Institute in Washington in '99, and we were sitting around with a group of Europeans and they were saying, we really wish we had something like your NASDAQ.

DH: Germany had this…but the flip side is, a friend of mine used to be correspondent for the Dow Jones in Amsterdam – this was in the mid '90s – and Phillips, which of course dominates the Dutch economy, was on hard times. And the CEO was giving a press conference about their restructuring plans, and she's taking notes and the CEO says, we're going to have layoffs and she continues taking notes. And then she looks up, and all the other reporters in the room were like, layoffs! And she's an American used to the American environment, and just kept writing and didn't even miss a beat, whereas all the reporters were stunned. All the Europeans were stunned that they were going to have this mass layoff in order to improve the stock price, so it's a very, very different structure; very, very different mentality.

DB: Just to add one more thing about that. Daimler-Benz bought Chrysler for about 50 billion back in '99, and Chrysler immediately reported multi-billion dollar losses for the next two or three years. Why on earth would you spend 50 billion buying a company that seems to mostly produce losses? One explanation, I hear, I don't know this to be true, but it's an interesting thing to think about, is that the executives want to pay themselves U.S. type salaries. So in other words, they can be sort of a U.S. company – if they bought up Chrysler, they'd be on a different pay schedule. I don't know that to be true, but its sort of an alternative to they threw 50 billion in the toilet.

Audience: So, you actually think it's a more active press?

DB: Its not just press – you do have unions, you have norms, you have banks that own shares in the companies. They aren't going to let the CEOs…

Audience: Yeah, but our banks own shares in the companies.

DB: No, they don't. There's a different structure there. They have investment banks that hold, you might have an investment bank that holds 15-20% of major companies there, the single bank.

SA: But in theory, why would an investment bank be any more vigilant about CEOs' salaries than a pension plan that holds shares?

DB: They should be, but they've had a tradition of doing it where, as the pension funds sort of fall into it, and they really have an attitude. Remember, I actually did this from personal experience, NTIA crap. You could get anything you want on ballot there, so I said, why didn't we have something to say we're going to work to limit CEO pay to 3 million dollars, they should be able to make ends meet on that. And they were completely hostile; they were like, what does this have to do with us? Why would you? So they don't think of really running the companies as their responsibility, whereas the banks do.

DH: There's a big difference of, even a very large pension fund won't own more than 1% of the company. If you're a big bank, like a German bank that owns 15% percent of it, you feel a lot more…It's a lot more intimate an issue for you.

SA: Yeah, but pension funds have been increasing their activism, and how they micromanage the businesses for a long time. And yet, CEO salaries doesn't seem to be one of the points that they…

DH: Well some of them do, I mean CalPERS is doing it now…

SA: About CEO salaries?

DH: …But its considered kind of maverick thing to do, it really is a issue of class solidarity, the pension fund managers themselves are paid enormous sums for running money, and most of them can't even be as well as the market averages, but they're still paid enormous sums of money. So they figure the CEOs should be too. And while the bull market was going on, who wants to ask any questions? If the CEO is making a hundred million, but the stock market is going up 20% a year, who cares?

SA: We are running out of time so let me just get the last questions that people have. Right over there.

Audience: Is oil a rationale for pushing the drive to war?

SA: That's a big question.

DB: I don't really think it can be explained that way. I mean, I think first and foremost, it was Bush's politics that…He's plunging in the poles last summer, and it's a clever way to pull victory out of defeat in the November election. He does have some friends who will profit – Halliburton already has some big contracts, so there are some people who will make a lot of money on it. But it's hard to see that that's the main motivation, 'cause they could just funnel that money to them in another way.

SA: Yeah, I tend to agree. I think people talk about, people on both sides of this debate talk about oil, and I think there's a lot – when you hear people talk about the significance of oil in the war, you have to ask for specifics, because I've never really gotten a straight account from anybody of how the Bush administration and its allies could in a realistic way profit from what going to happen to Irag's oil or the other oil in the region. Some people say, well maybe they'll privatize the oil. I have to say I seriously doubt that even the craziest fringes of the administration would try to do that and try to implement that. Now, I could always be wrong about the craziness of the fringes of the Bush administration, but I remember there was a conference on the future of the post Saddam Iraqi oil industry at the American Enterprise Institute, which is a very prominent neo-conservative think tank that Dick Cheney is a figure in, and they've been pushing for a war in Iraq for a long time. And on the panel on oil in Iraq after the war, there was a guy on the panel named Patrick Clauson, who was from the Washington Institute for Near East Policy, sort of a right wing pro-Israel hawkish guy, who used to be the IMF representative in Iraq. And so of all these people in the audience and on the panel, he was the expert on the Iraq economy, Iraqi oil, and he's very much for the war. And people were saying, yeah once we get into Iraq shouldn't we privatize the oil – shouldn't we just dole out contracts to foreign oil companies so we can make it more efficient and reduce the role of the state, which is really strangling the political life of the Arab world etc. He said, look, I would love to privatize Iraq's oil, I think it's a great idea; I think Iraq would be better off from that. But I'll tell you that the Iraqis have built their nationalism around the oil question for 80 years, and if you go in there and try to impose privatization on them by, you know, through your influence as an occupying force, then in his words, you will walk away with your tail between you legs. Which is the kind of language that people on the pro-war neo-conservative side of the argument never use. They always say it's going to be a cakewalk, and we're going to be greeted as liberators. So this guy, who I think is in a position to know, said don't even try it. So I tend to think based on things like that, that the crazier elements in the administration, who might want to press for something like that where U.S. companies and the U.S. economy maybe in a macro sense could actually benefit, that they will be restrained by sort of the wiser heads.

Audience: The invasion, the occupation, the rebuilding of that would be done but the…those contracts are already being…

SA: Those provide sort of perverse incentive – sort of every destroyed building is another million-dollar contract.

DBL: I think that's extremely true, and those who go, oh they're friends of the Bush of administration, but it's just a little hard to imagine that being the whole rationale for this war, which is obviously going to be a risky venture for them, just to swing government contracts for Bechtel, cause as I said, they can get that to them another way.

SA: The tax cut itself is probably worth more.

DB: Another weapons system.

DH: I think it's much more about wanting to assert U.S. imperial power. These guys are real nationalists; they want to dictate things to the rest of the world. Iraq is very weak – it's not like there's no brooding doubts about if Sadaam had succeeded in developing nuclear weapons, we'd be sending him a fruit basket instead. I think they think they've got a weak target, and they can just show everyone who's boss, which I think was the whole point of the first Gulf war too. It's right after the end of the Soviet Union; there's not much certainty about what the post Cold War order is going to look like, and daddy Bush wanted to show the world who was running things. He did it in a much more collegial fashion than the younger one – this guy is dumber, more arrogant and more filled with religious fundamentalist certainty about…There's this story on the front page of the *Times* today – it's frightening. This guy – no doubt in his mind, he just knows the difference between good and evil, and he's on the side of good. This is really a terrifying character to have with his finger on the button.

SA: That brought a lot of hands up. Right there.

Audience: I was wondering if you guys have any ideas of what we can look forward to, because if we see that opposition parties are not doing their job; the press media its not doing its job; in a way, one can't help but feel helpless…

DB: You have to look at the protest that we seen. There's a lot of reasons to be pessimistic, but on the other hand, the fact that we have an anti-war momentum build up this quickly in advance of an actual war – that's really a fantastic thing.

DH: And it's worldwide. George Bush has done more to develop a world-wide anti-imperialist moment that any one of us could have done in a lifetime and…

DB: We have the Internet – that's an incredible asset, the fact that we can get so much info. Yeah, we get garbage in the media but we can get something and that's a huge...

Audience: The fact that you can get to this newsletter, we have the Internet…

DB: Those demonstrations wouldn't have happened on Feb 15.

Audience: But its still going to take some time for the media to pick up. I was at those demonstration, and they were fabulous, but the conversation is…it's just teen anarchists stomping on police horses so…

DB: In '91 during the first Gulf War, I was a reporter in Washington. I'm not bullshitting about the numbers, it was to wall-to-wall people – no beginning, you couldn't see the end. It was a huge, huge protest. I came home, turned on the TV, and CNN reports that protesters both for and against the war march in from of the White House today, which was technically true – there were about 200 pro-war nuts…As bad as the media is, it's better than it was then, because they get embarrassed. We can use the Internet; we have other means, and you look really stupid when you compare 150 to 150,0000.

DHL: Well, it's also much, much bigger and worldwide and coordinated, and it's just growing.

SA: And it reflects some of the concerns that the media themselves have about the war, not in the same language.

Audience; Also there's new stuff popping up, media outlets like Free Speech TV; there are things popping up that are in their infancy. But I think that they'll pull the attention – more people are showing up to those events that just the likes of us.

Audience: And the danger is, I think, certainly even just now, we talk about the war and the future, as far as what's going on economically, there's a certain sense of the war effort and no energy around really looking domestically at what's going on with the economy.

DH: The conventional wisdom among Wall Street types and pundits is that the war is holding back the economy, and when the uncertainty is over, which they presume will be quick, everything will recover. And the impending war and anxiety has been like this big weight, and once that weight is lifted, the economy will bounce back. Somebody on CNBC used the image of a beach ball under water – it's going to get released and shot skyward. So I think that's crazy – I don't think that's true. I think war certainly is keeping a lid on economic activity, but there are fundamental problems not going to be cured by the passage of time.

SA: But I think that what really points to the ideological difficultly for most people, opinion-shaping people, to explain why the economy is so bad…

DH: They never say it's bad. If you go back to 2000, again this comes from doing the economic reporting review every week, they kept saying when there were first signs of the fall in 2000, the economy was weakening. All these people kept saying we're just going through a soft spot in the economy. It'll rebound back in the second quarter, then the third quarter, then it became the forth corner. No one could ever say – most economists said they didn't think we were going to have a recession. Well we had a recession. No one said we would, but we did. If you go back and read the article about the jobs report on Saturday, most economists don't think we were going to have a recession. It's almost like a fraternity – you're not supposed to say things are really bad.

SA: And it's partly because they can't give an ideologically pleasing reason for why we would have a recession now, because if you listen to the rhetoric from the same people from the late '90s, we were experiencing a great economy because we had done everything right, we balanced the budget…We did all the stuff they thought we should do, and it turns out we got this nasty and difficult recession, and they have no way of explaining it. I think that's part of the reason why there's denial about it.

DH: Last year the Federal Reserve did a research paper, in which 12 staff writers from the *Economist* collaborated, so they put some resources in it, about looking at what happened in Japan in the '90s as a possible precedent for what happening in the US now it was. Reportedly the Fed had been looking too, but one of the things the paper said was in Japan, nobody really thought they had a serious problem on their hands. It wasn't just a cyclical thing or just this, you know, like little post bubble problem – it will go away in a little while – it took them 4 years to recognize how serious things were. And the message of this paper was, let's not do that here. I don't think anyone is listening to that message, beyond whatever they're thinking within the Fed. In the larger pundit community, they're not saying things like that. People are entertaining the prospect that this is more than an ordinary recession. I think by conventional indicators, it's kind of mild, but what's scary is that it's just not recovering – they could have a really long period of weakness, stagnation, even deterioration. No one is taking the possibilities of that seriously now, as far as I can tell.

DB: Just to take it a step further, nearly always when an economy is bouncing back out of a recession – Doug made this point earlier – what leads is the auto industry and homebuilding, because typically those fall 20, 30, even 40% in the recession, so as soon as things start to clear up, interest rates fall; they go zoom. That can't possibly happen because homebuilding is at record highs, auto sales had been very high – they just recently have plummeted. But there's no way they could take off and grow 20 or 30%. The idea of the beach ball underwater – that's what's underwater usually, the auto and housing sectors. And they're not – they're way above the surface.

Audience: Is there a big idea that a progressive politician can run on, that people can understand, and sell this kind of alternative vision?

DB: Well, there are lots of things you could say. In terms of getting the economy back on a sound footing, I don't think there is a single policy. The one thing that could probably come closest to being the single most important policy, in my opinion, is getting the dollar down. I don't know if that's the sexiest thing to have a campaign on. But that would be the single most important policy. National health care insurance is an incredibly important thing we didn't really talk about, but we have far and away the most expensive health care system in the world. We don't cover 40 million people. We have the worst outcomes in terms of life expectancy and infant mortality of any industrialized nation. That would be a really big issue that someone could talk about. There are a few other things we could throw out like that. But I can't think of a unifying thing that says, do this and you'll fix the economy. In that sense, I could hand it to the Republicans and their tax cuts. It's not true, but that's what they could say.

DH: I would also say that things were pretty good in the '90s for average people. Real wages rose, the poverty rate was down, the unemployment rate was down. We know now, that was the fortunate by-product of what turned out to be an unsustainable bubble, an unsustainable boom. So the structure of the U.S. economy is not given to providing mass prosperity and security. I think we need to get that idea. That's the starting idea. There's something structurally wrong with things. It's not just a business cycle; it's not just the wrong set of policies at the moment – there is something structurally screwed-up about the economy. The only way it can deliver rising wages and low unemployment is by having an unsustainable bubble. So we would have to reorient the discussion towards much more qualitative kinds of issues. We need job security. Income security. Government guaranteed jobs. You need a minimum income. You need a civilized welfare state. You need universal health care, a basic social democratic agenda. Free child-care. We need these basic kinds of things, and to stop relying on the idea that economic growth alone is going to do these things. You need positive interventions, the creation of things that provide to people, and not hope that 5% GDP growth is going to provide these things spontaneously. It's not going to happen.

SA: I think the basic idea is that people have economic rights to begin with, which is not a concept, even under a different name, that you hear as part of the mainstream political discourse. The idea that people have a right to health care, and a comfortable retirement, and a lot of other things.

DB: I'm all for economic rights and everything, but a lot of this is just holding them honest to what they're saying, because if you listen what George W. Bush says, he wants to do something about those 40 million uninsured people too. But his solution a) won't get them insured and b) will give a huge amount of money to the health insurance industry. So what I like to say is that I want the same thing that George W. Bush does. I just want it done in the most efficient possible way, which would be some sort of single-payer type national health care system. We don't have to argue about economic rights, because they don't want to hear what I have to say on that. Let's just have it the most efficient possible way, and that would be much closer to what I want than what he's talking about. I think that's true of most policies.

SA: Well I'm getting the signal to wrap-up here, so I want to thank our speakers and thank everyone for coming out.

[Applause]