Event Transcript

What should the 2023 Washington Consensus be?

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Lawrence Summers: Thank you very much, Adam. It is good to be here. My only regret is that Dick is not here to explain to me why I have said several things that were in error in the course of these remarks. Of Dick's many accomplishments, his role in stewarding the Peterson Institute into being is one of the important ones. Keynes talked about the distilled frenzy of academic scribblers. If he had been writing today, I think he would have been talking about the policy briefs and emails from Capital city think tanks as having a profound influence on the direction of policy.

And I know that he was immensely proud of everything that Fred did and everything that you have done, along with all of your colleagues, Adam to carry on the work of the Peterson Institute. As some of you know, I come from a family of economists and a family that had many economic friends. I grew up calling Art Okun, Uncle Art. And the first time I ever heard about Dick Cooper was long before I met him.

And I don't know why my father had the occasion to tell me this story. But my father had been enormously impressed because he had been one of the group of outside examiners at Swarthmore College in some year, perhaps in the late 1960s or early 1970s. And he said there were 5 or 6 economists who were involved in examining their undergraduates, but just as nothing one of them emerged as the leader of the group and kind of said when they were going to talk to each student, and kind of guided the process through.

And he remarked that that same person, Art Okun, had told him about how in the 60s, whenever there was going to be a meeting on an international economic question, everybody who was going to go to the meeting called the then very junior economist to find out what it was they were supposed to say and what it was they were supposed to think and what the conclusion of the meeting was going to be. And that economist was Richard Cooper.

And you don't, without having some quite extraordinary skills, become the provost of one of the world's leading universities when you are 37. And so, Dick Cooper had a capacity for leadership and bringing people together that supplemented his remarkable understanding of international economic issues. I learned a lot as a young professor watching him.

I saw that he never failed to support a student who was being criticized. And that he never failed to challenge an eminence who was being platitudinous. I saw that he always drove the conversation back to basic things that economists understood. But never let the executer of a mathematical exercise lose sight of the fact that this wasn't fundamental moral philosophy, that the point of making models of gold standards was to make a monetary system that worked better for people.

And so, he was an enormously influential figure in my life. And in times when things were going well for me, and much more importantly, in times when things were going poorly for me, he was always my friend. And that is something that I will always appreciate. Because he was so good at leadership, because he knew so much about so much detail, there is, I think, a tendency for people when they think about Dick Cooper to miss his capacity for abstraction.

There's much discussion these days. I've engaged in it, Dani Rodrik has engaged in it of the various tensions and dilemmas associated with globalization. We think it's good when there's more integration. We also think, though, that it's good when countries can make their own policies rather than have them imposed from abroad. And we think it's good when those policies can resist market forces.

But all those objectives are in some tension with each other. If you're Jacques Delors, you don't think it's a big problem. You think that we just need to have governance at levels above the nation. If you're Milton Friedman, you don't think it's really much of a problem if competition between jurisdiction drives all tax rates and regulatory burdens to zero, so much the better.

If you're Donald Trump or Ross Perot or Pat Buchanan, and in order to have sovereignty, you have protectionism and you cut off integration. That's really good too. But the ultimate challenge is to find ways to balance all three.

Many of us at many different points have thought we were involved in having that pretty good idea. But if you go back and read Dick's book from 1968 on the Atlantic Economic Community, roughly speaking, it is all there. He was a towering figure and one who believed very strongly in the importance of international economics and international economic integration. And who believed that, of course, there were appropriate limits and constraints. But that they better be appropriate and there better be a good reason for them.

I remember a conversation we had probably in about 2007 in which he began by saying that you should never hold somebody responsible for the sins of their relatives. And then he proceeded to offer his opinion of Paul Samuelson's now quite famous paper. Explaining that while it was true -- Paul's paper -- that free trade was good. It was not a corollary of that theorem that the greater prosperity of one's trading partner made one worse off.

That in essence, one's trading partner was both one's customer and one's competitor. And if your customer gets richer, that's good. If your competitor gets more efficient, that's bad. And so, it all depends. And Dick said that was a nice mathematical exercise that Paul had done. But David Ricardo had more or less done the same mathematical exercise. And what mattered was what was true. And I was then treated to a learned discourse on the impact of the rise of the South on the New England economy, explaining how it had been good.

The rise of Western Europe after the Second World War on the American economy and how it had been good, and a variety of other examples. He was right. He was right. And the single most important proposition on which any Washington consensus going forward has to be based is the common interest we all have in shared prosperity.

And ideas that seek to reframe international economics as a zero-sum game or even as a negative-sum game where we benefit from other nations' misfortune are an enormous danger. And yet such ideas are increasingly in fashion with the calls for a new Washington consensus. Those who speak of a new Washington consensus mostly have never heard of John Williamson.

And they mostly do not actually mean to speak about the set of propositions that John Williamson enunciated in 1989 having to do with the proper macroeconomic management of a developing country. They instead, are speaking to the broad principles that undergird or have undergirded American international economic policy since the end of the Second World War.

Renewed after the breakdown of the original Bretton Woods exchange rate system in 1971 and re renewed after the end of the Cold War when Bill Clinton famously asked the question, "Would the United States at the end of the Cold War make the mistakes that were made after the First World War or recreate the successes after the Second World War?"

He, I'm sure, imagined at that time, that by 2023, the answers to those questions would be clear. And yet think they are not completely clear. And I think the prospects that history will see us as having gotten it right are not as large as those prospects looked one or two decades ago. I would suggest six misconceptions that purveyed a great deal of the current economic debate.

First, it is supposed that the idea of economic policy is to maximize the creation of jobs rather than to maximize the availability of goods at low cost to consumers and firms. Both the officials responsible for competition policy and those responsible for international trade have explicitly rejected economic efficiency as a central guide for economic policy. This, I would suggest, is a costly and consequential error.

All the more it is a costly and consequential error at a time when the ratio of job vacancies to unemployment is higher than it has been any time in the last 40 years. And all the more it is a costly and consequential error at a time when high cost of living is a central concern of the American public.

The second misconception is that these have not been good decades. For the American economy in international perspective. I first got to know my friend Ted Truman well when he was long into his career as the head of the Federal Reserve's International Economic Section. and I was a new undersecretary of the Treasury for international Affairs. We were involved in making various long term economic projections for the world.

None of them would have believed that US GDP as a share of global GDP would have remained robust for the entirety of the next generation. And if we had been told how spectacularly China was going to do over the next 30 years, we would have been that much more pessimistic. We could not have imagined that the share of US wealth reflected heavily in the stock market would have been far higher a generation later than it was at that time.

The truth is that the United States has done extraordinarily well. It could have been argued until a few years ago that if you looked at what's probably the single best measure of an economy's performance, its GDP per person between the age of 20 and 65, that we had not done so well. But if you look up till now, we have actually done very well on that standard as well. So, there are plenty of internal issues. But as an overall economy, the United States has fared very well.

Third, the world has fared very well. Relative to the time when I was chief economist of the World Bank at the beginning of the 1990s, child mortality rates are less than half of what they were then. Literacy rates are more than twice what they were then. Poverty rates, terms of extreme poverty are less than 40% of what they were then.

And in some ways most fundamental and important, this month, we celebrate the 78th anniversary of a situation where there has been no direct war between major powers. You cannot find a period of 78 years since Christ was born when that was the case. So, the idea that we've been doing it all wrong is, I would suggest, a substantial misconception.

Fourth, the problems that we have are not due to trade liberalization. The single most misleading idea that has moved from academic economic research into the popular domain is the concept of the China shock associated with China's accession to the WTO. To start with, that agreement did not change one iota of US policy permitting Chinese goods to be sold in US markets.

The principle that China would be the beneficiary of most favored nation treatment and get the same benefits that other countries did had been well established years before. It was ritually reaffirmed annually by the Congress. Yes, China's tremendous economic progress did lead to far more sale of goods in the United States. But it is hard to imagine a less credible approach to the problem. The adding up all the losers from the imports without taking any account of the jobs created and the economic impacts of the goods we sold to China.

Of the lower cost inputs we received because of imports from China. Of the enhanced real wages and associated with greater spending caused by those lower prices. And the lower capital costs associated with the inflows of capital that we received from China. When those calculations have been done, as they've now been done by Rob Feenstra and several other teams of economists, they show that, in fact, as with NAFTA, the net benefit to the US economy has been substantial.

The fifth misconception is that domestic industrialization and some kind of renaissance of manufacturing is somehow the central issue for US prosperity going forward. This is simply not a realistic idea. In 1970, about 20% of US workers were engaged in production work in manufacturing. Today, that number is about 6%.

That number has trended downwards in countries like the United States that have tended to run trade deficits. It has also trended downwards rapidly in countries like Germany that have run manufacturing, export, mercantilist oriented economic strategies and not at very different rates. It is a consequence of the same set of phenomena that led to declining shares of workers in agriculture over time.

Rapid productivity growth, relatively inelastic demand, rapidly declining relative prices created abundance without substantial and with declining levels of employment. And there is nothing in the coming robotic revolution to suggest that these trends are likely to do anything other than accelerate going forward. I would note that the president of Ford has judged that it requires about 40% less labor input in a Ford factory to make an electric car as to make a traditional car.

I am aware that we have a much-ballyhooed increase in manufacturing plant construction going on in the United States, and that that figure has shown almost a hockey stick level of growth. I'm also aware that of the 30 categories of business investment, that category is one of the very smallest, and that it constitutes less than 2% of total business investment.

The idea that we can build an economy on growing our manufacturing sector is just not realistic and it is potentially counterproductive. I would just note that there are about 100 times as many workers in steel using industries as there are in the steel industry as evidence of the potential costs of domestic content requirements motivated by the desire to create capacity.

Finally, I would suggest that substantial. And accumulating deficits and debts are a substantial threat to national security and national power contrary to what is often believed in what sometimes seems like a post budget constraint era of economic thinking. This is not the place to rehearse the details, which I did in an earlier Peterson lecture.

Suffice it to say that a reasonable calculation would suggest that our budget prospects are vastly worse than they were at the time of the Clinton administration's successful budget actions and substantially worse than they were at the time of the Simpson-Bowles efforts. The budget deficits a decade out comfortably in double digits now seems as a share of GDP now seem a reasonable projection with primary deficits quite likely in the 5% of GDP range.

This is without the assumption of the need for vast mobilization for meeting contingencies, military or non-military. And I think it is reasonable to ask the question. How long can or will the world's greatest debtor be able to maintain its position as the world's greatest power. So, I think we are at a moment when we require what Dick Cooper gave us so often for so long. Clear questions, clear recognition of reality.

I don't know what that Washington consensus going forward will exactly be, but if it can rest on the things that Dick Cooper stood for and America committed to underwriting, underpinning and undergirding an increasingly integrated and prosperous global economy. And America always questioning of itself, but also confident in its ultimate capacity. And not seeing any need to fear the success of others.

An America concerned not with the economic activities of the past, but the potential economic activities of the future. An America in which elites do not just speak to themselves but are concerned with all of their fellow citizens. I believe we can and will find a healthy path forward. And that Dick will look down on all of us with a sense of satisfaction. Thank you very much.

Adam Posen: Thank you. Thank you so much, Larry. That was practical idealism in the same sense that [inaudible 0:33:00]. And I'm grateful for it. We're going to have a brief conversation, Larry and I. This is all, of course, on the record and the video and the tributes to Dick will be permanently on the PIIE website for all to access. And then we'll come to our audience for questions.

Let me start with what I realize you intentionally brought us to but didn't address, which is the addressing of misconceptions by the general public or by influential voices in the general public. Dick went through, as a public servant, the 60s and the 70s, which had their own moments of turmoil and lack of US confidence.

We, the Peterson Institute, among others, have published a lot of work trying to correct some of the misconceptions you've had. What do you see as the way forward for better addressing some of these misconceptions?

Lawrence Summers: I think you got to state -- you got to make the arguments clearly, strongly and non-apologetically. And you've got to be prepared not to say things just because a lot of people believe that they're true so that you can be heard saying other things. And I think there's been a tendency for many to fall a bit into that kind of trap in this moment. I think there is a lot to be said for the importance of truth telling.

I also think that we all need -- those of us who are fortunate enough to do the kinds of work you and I do, Adam -- to think about our legitimacy in a broad national dialog. That's why it's a very different subject than our subject today. But that's why I've spoken out recently on the subject of legacy admissions and a variety of other things that are going on in our leading universities.

That's why you've been engaged in some efforts to speak to audiences, not just in Washington and New York. I do think that the detachment of elites is a contributor to a variety of these kinds of phenomena. But, Adam, I think also it's probably a good idea for all of us to know their limits. And I may know a certain amount about economics, but I'm not sure that I know that much about how to communicate effectively with a vast public.

I do think it's unfortunate when people who should know better are sometimes saying things that probably don't really correspond to accurate assessments of the situation.

Adam Posen: Thank you, Larry. And I know you have other venues where you're talking about those issues. So, let's move back to some of the core things you spoke about. One of the things that was notable about Dick Cooper, as I think we mentioned, was that he was very active in national security discussions and public health, global public health when he was, of course, coming at it as an economist.

You were as sub-Cabinet and Cabinet official involved in some of those discussions. What do you think he would think about the -- or not so much he would think about -- he unfortunately is not here. Let's channel you. How should we be addressing the sense that the national security threat from China or China combined with others changes the game on economics. I mean, what specific ways do you give credit to that argument versus the non- --

Lawrence Summers: I like the phrase small yard high fences, but I'm skeptical that anybody except some people in this city think the yard we have in mind is small. And I think that's something we have to be very careful of. When I hear discussions of technology controls or technology competition of one kind or other, and the area is semiconductors, I find it much easier to relate than when the subject is some kind of green technology.

I'm inclined to think that if climate change is a central problem, we should want climate change technologies produced as inexpensively as possible. My view, which I've been expressing for some years, that has become more fashionable in the last few months, at least in some part of it, is that people, historians will look back on American views of the Soviet Union in 1960, American views of Japan in 1990 and American views of China in 2020 in quite similar ways as maximum alarm just at the moment of maximum mean reversion for the economy in question.

And I think we have to think very hard about, in the context of that possibility, what the right strategies are and strategies that are about maximum pressure can also be strategies that provoke maximally sharp responses. Every time I hear somebody talk about Britain in the 1930 with an emerging threat, I'm led to think about the antecedents to Pearl Harbor in terms of Japanese perception.

And so, I think we need to proceed with very considerable care. I'm also very alarmed anytime you have a dynamic where on any issue, it's only safe to be on half the spectrum of views for an individual. You are at risk of the outcome, moving a very, very long distance. The reason why the grade point average at Harvard University is now above 3.7. Think about it.

Adam Posen: It wasn't when Dick Cooper graded me.

Lawrence Summers: Is that no one wants to be in the hard-ass half of the grade. No one with ambition wants to be in the dovish half of those talking about policy directed towards China. And that creates a potentially very, very dangerous dynamic. So, I don't think we can ignore the national security issues posed by China at all, but roughly speaking, whenever somebody talks about jobs in Ohio, at the same time they're talking about the national security threat from China, and as an important benefit of the national security policy, I get pretty nervous.

Adam Posen: As some of you know, I've also been out there saying we may be overestimating the China threat or mis conceiving it, but I will invoke again Dick Cooper, who accompanied a group of our fellows on a trip to Beijing a few years ago, and I remember talking with him at the time. He had been part of the delegation sent by Jimmy Carter to set up the relationships and the summit that came about.

And he took great pride and excitement in the China that grew and developed since 1979 despite being a patriot who devoted a lot of his time to the US national defense questions, including as chair of the National Intelligence Council.

We have time for perhaps one or two questions from the audience. If you come to the front, Sarah, I believe, has a microphone if you're from the front. If you're near the back, it may be easier to go to the standing mic. Would anyone like to pose a question or comment to Professor Summers. Please, if you could go to the mic and identify yourself, please.

Harriet Choi: Hi, my name is Harriet Choi. I'm a reporter with the Wall Street Journal. I just wanted to go back to a point that you made about policy being more focused on job creation than on prices of goods and services and so on. Since this is quite topical at the moment, I would just be really interested in hearing your views on how high you think unemployment might have to rise for the Fed to bring down inflation from its current high levels.

Adam Posen: I'm sorry. It's our fault with the sound. We didn't hear you very well.

Lawrence Summers: The acoustics here are really not --

Adam Posen: Yeah, apologies to all, and especially to Jen and Jenny. This is our first run this fall. We'll fix it. But as our colleague from the Wall Street Journal, if you could project a bit more, please.

Harriet Choi: Okay. Sorry. In your comments you were talking about how policy has been more focused on job creation than on prices. Given that we're in a very high inflationary environment, I would just be curious in hearing your thoughts on whether unemployment is going to have to rise and how high potentially or if there are other ways that this situation might be resolved.

Lawrence Summers: Good try. I think that we all have the same desire, which is for a maximally soft landing of the US economy. We're all aware of the same history, which is that high rates of inflation in the last 70 years have not come all the way down and stayed down without significant increases in unemployment. That's why I've often said that what Samuel Johnson said of second marriage is true of soft landings. They represent the triumph of hope over experience.

But sometimes hope does triumph over experience. And so there is certainly a possibility. I believe that declaring victory at this point is premature since it seems to me there are still substantial risks of inflation remaining elevated. And it seems to me there are also substantial risks of the economy at some juncture turning down in a self-reinforcing way. So, we will have to judge. But the aspiration is, I think, entirely clear in terms of wanting to see a soft landing.

Whereas a couple of years ago, it was my view that the Fed was misunderstanding the broad dynamics of the situation in not recognizing the inflation threat. I think the Fed's current view of monitoring very carefully and seeing risks and achieving a soft landing will require very careful calibration and might or might not ultimately prove possible is, I think, that's a broadly appropriate posture for the Fed.

Adam Posen: Two notes from the facts research side, our colleagues here at Peterson, Gary Hufbauer and Meg Hogan did a short study a couple of years ago, partly inspired by Larry on the consumer side. And since the Biden administration hasn't changed its tariff policies, the numbers still count. A reduction or reversal of the tariffs since Trump would take roughly 1.25 to 1.5% of CPI.

The second factual statement about jobs and so on is Larry mentioned in his remarks the idea of Germany versus US. One had a trade surplus and merchandise goods one didn't, they both lost jobs. The last time I appeared before a congressional committee and was questioned by an Ohio congresspperson, we followed up with a chart that showed Nordrhein Westfalen had lost as many manufacturing jobs proportionally as Ohio.

That chart's on the PIIE website if someone wants to look at it in the Biden administration. One more question, please, from the audience. Yes, over here. Sarah, could you bring the microphone?

Barney Rush: Hi, I'm Barney Rush. It was my pleasure to work for Dick when he was Undersecretary of State. So very wonderful things that everyone has said about him today. Thank you very much for raising the issue of the deficit. And I just read that we now expect it to be 2 trillion this year instead of 1 trillion.

But I'm curious, when I look at the long-term rates and treasuries, maybe 1, 1.5% above the rate of inflation, who is actually buying this debt? Why isn't there more crowding out if the Fed is actually reversing its quantitative easing and pulling money in? How is this this deficit actually being financed without causing the crowding out that we all took 10 decades ago?

Lawrence Summers: Look, I think, the question in many ways is, what will the future hold as the nature of the supply demand dynamic for bonds evolves? And it's the logic of what I've said that that's going to be a difficult supply and demand dynamic. There are a variety of economic forces. I used to talk about them a lot when I spoke about secular stagnation having to do with reduced investment demand.

A law firm used to need 1200 square-feet of space per lawyer. Now it needs 600 square-feet of space per lawyer. The canonical capital good used to be a $50 Million Cray supercomputer. Now there's more computing power in my $600 smartphone. These kinds of developments reduce the demand for investment and therefore create more space than there might have been in an earlier time.

There are a set of forces having to do with higher inequality, meaning higher savings rates that are operative. For a variety of reasons, the share of national income going to corporate profits are higher than they once were, and those profits are more likely to be saved than if that income had gone in the form of salaries to workers.

So, there are many different factors at play, and markets find their equilibrium. My judgment is that the Fed's current view that the sort of neutral interest rate when you take out the supply and take out the cyclical factors, is going to settle at 2.5%, 0.5% real rate and 2% inflation. Certainly, represents a possible outcome, but that there's far more ways it could turn out to be wrong on the low side than it could turn out to be wrong on the high side.

And that's part of why I'm more alarmed about the fiscal and the debt posture. But there are forces at play. I just mentioned a couple of them. There are many more that do operate in the direction of creating room for savings to be channeled into debt securities. But it is very much a question. I'll just maybe close with this view. It's my quite high conviction belief that the day the dollar loses its major role in the world monetary system, the loss of that role will be the least of our problems.

That is to say, I am not saying that it couldn't happen. It could, but if it does, it will come with very substantial issues of US creditworthiness of US price stability, of reliance on the US system of national defense to undergird the world order. And so, if you think about Britain as a great power, by the time the pound lost its role, it was the least of Britain's major problems, not the cause of other problems.

And I have the same view about the dollar. And that's why I think we do need to be paying attention to our fiscal challenges. We do need to be paying attention to a whole set of domestic challenges.

Adam Posen: With that, let's close out today's very important, very inspiring -- and for the institute -- very proud occasion. I would like to thank again Mrs. Jin Chen Cooper and Jenny Cooper for their decision and generosity in creating the annual Richard N. Cooper lecture here at the Peterson Institute. We look forward to doing it annually.

But to thinking, as Fred Bergsten said, as I tried to say, thinking about the example as a person, as a scholar, as a policy influencer, as a public voice that Richard Cooper provided for us quite frequently. It's an inspiration to us all.

And in that regard. Thanks again to Lawrence Summers, former Treasury secretary, former director of the National Economic Council. Charles W Eliot University professor at Harvard. Normally, I would end with Peterson Institute vice chair, but long-term friend and colleague of Richard Cooper. Thank you for doing this, Larry.