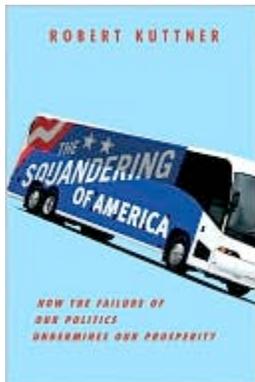




The Squandering of America: How the Failure of Our Politics Undermines Our Prosperity

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Introduction

JOANNE MYERS: Good morning. I'm Joanne Myers, Director of Public Affairs Programs. On behalf of the Carnegie Council, I'd like to thank you for joining us.

It is a pleasure to welcome Bob Kuttner, a leading political economist, to our breakfast program. Mr. Kuttner is a person who persuasively writes about what he believes in and, in so doing, conveys a message of urgency for all of us to reclaim our democratic politics and our prosperity. For decades, he has successfully pursued this theme as a writer, editor, teacher, lecturer, commentator, and public official.

Today he will be discussing two books, [The Squandering of America: How the Failure of Our Politics Undermines Our Prosperity](#) and [Obama's Challenge: America's Economic Crisis and the Power of a Transformative Presidency](#).

No one doubts the magnitude of what [Barack Obama](#) achieved in becoming America's 44th president. But moving forward, everything will depend on how he governs. This election was about many things. It was about big issues—a global economic meltdown, a massive government intervention in the financial markets, and, of course, two wars which must be resolved. Although it began with the war in Iraq as its central focus, by Election Day it was mostly about the economy.

As President-elect Obama approaches the presidency, the national coffers are virtually empty, much of our infrastructure is crumbling, the education we offer our children is falling behind, and our health-care system needs to be rebuilt. The tasks facing the new president are daunting.

In *The Squandering of America*, our speaker explores the political roots of America's narrowing prosperity and the systematic risks facing the U.S. economy. By sharing his ideas for a more balanced and managed form of capitalism, he offers clear alternatives to failed and undemocratic policies on everything from trade to entitlement. He argues for broader distribution of opportunities and more economic security for all.

In advocating a populist resurgence in which brave politicians reenergize and reconnect with the public, one might have thought that Mr. Kuttner was imagining a president who would transform politics as we have known it. Just as he was prescient in warning of the impending financial collapse, in a leap of faith before the election, he seized the moment and published the perfect companion piece to *The Squandering*

of America, entitled *Obama's Challenge: America's Economic Crisis and the Power of a Transformative Presidency*. In it he explains what President-elect Obama will need to do to redeem his own promise and the promise of America. It is not only a call for economic change, but a challenge for our next president as he takes over a nation weary of the past and wary of the future.

Mr. Kuttner leaves us with the audacity to hope that President-elect Obama can seize the moment and become the transformative leader that will help all Americans to recover a sense of optimism and to believe in limitless possibilities once again. While there is no magic wand that President-elect Obama can wave, he could take the advice of our speaker and become the transformative president we are all hoping for and, at this time, desperately need.

Now can you all join me in welcoming our speaker?

Yes, you can. Bob Kuttner.

Remarks

ROBERT KUTTNER: Thank you. Thanks so much for having me.

There is a passage in Hemingway's [The Sun Also Rises](#) where one character says to the other, "How did you go bankrupt?"

The other one says, "Two ways. Gradually and then suddenly."

If you think about that, the reason you go bankrupt gradually and then suddenly is, the "suddenly" part happens when people stop lending you money, when people take a good look at your balance sheet and realize that you are already de facto bankrupt and you can't keep up the pretense any longer.

I started writing the book that became *The Squandering of America* in 2004-2005. I was interested in the connection between two things: the widening inequality and insecurity that faced most Americans and the deregulation of our financial system and the prevalent, ubiquitous at the time philosophy of market fundamentalism, the idea that markets could do nothing wrong and that governments could do nothing right. I had explored this in an earlier book called [Everything for Sale: The Virtues and Limits of Markets](#), where I looked hard at what realms of the economy work as markets, as we study them in economics courses, where supply and demand determine price, and allocate resources efficiently, and what realms of the economy don't work as markets.

I concluded that 60, 70 percent of the economy works perfectly well as a market, but if you look at education and health and research and development, public infrastructure, financial markets themselves, you can't trust markets to allocate resources efficiently; you can't trust markets to regulate themselves. They over-invest in things that pollute. They under-invest in things that lead to growth, like education and research and development. They under-invest in things that we need as a society, like public health. In the case of financial institutions, you need the stabilizing and supervising role of government so that financial markets don't turn into casinos.

We learned this in the 30 years following 1932, and we gradually forgot it in the 30 years that began in the late 1970s.

I argued in *The Squandering of America* that this was not only creating a very unequal and insecure and unattractive society, but it was also laying the seeds of a second great depression; it was laying the seeds of a second financial catastrophe.

There was also a political feedback loop that was undergirding this; namely, the less faith we had in public institutions, the less government delivered for ordinary people, the more cynical ordinary voters became about government. If you have one candidate offering a rather faint echo of the [New Deal](#) but not delivering much and the other candidate saying, "Well, at least I'll cut your taxes," the fellow who

cuts your taxes get the vote, because it has been a long time since government has delivered ordinary Americans the kinds of things that were delivered to them in my father's generation, where he became the first person in his family to become a homeowner, thanks to a GI loan, and went to college on the GI Bill. You all know the story of that generation.

For folks who grew up, my age and older, the idea that government could improve people's lives was actually plausible, because it did. It made a huge difference in the lives of ordinary people.

But if you are 35 years old now and you start out life with college debt and you have trouble getting a job with health insurance and the price of homeownership is beyond your reach, unless you have an affluent family to give you a head start, you don't see government doing a damn thing for you, except collecting your taxes.

So in order for the economic policies to change, the politics have to change. The vicious circle has to be changed into a virtuous circle.

I remember, in writing this book—at one point I was going to call it *The Coming Collapse*, but that seemed too apocalyptic—I was very worried about the timing of the book. In between the time I turned the manuscript in, in March and April of 2007, and the time the book appeared in October of 2007, it all started to unravel.

Anyway, so I wrote that book. In the fall of 2007, I started thinking to myself that if I'm right, if this is going to be a very serious collapse, the president who takes office in January 2009 is going to face a very interesting situation. I took a good look at the Democratic field. At that point there were three frontrunners, [Edwards](#), [Hillary Clinton](#), and Obama. By conventional tests, Edwards was the populist, Hillary was a bit more liberal, Obama was a bit more centrist. A lot of my friends, as fellow liberals, which I certainly am, were backing either Edwards or Hillary. I convinced myself that of the three of them, the one who really stood a chance of becoming a great transformative president, even though he was a shade more middle-of-the-road on the issues, was Obama, because of his character, his history, something remarkable about his capacity to lead.

Since my day job is being a magazine editor, I said to myself, "Gee, that's a good article. I want to get a presidential historian to write an article about presidents who faced great crises, turned them into great opportunities, and became transformative, in the sense of changing the public's conception of what was possible, what was necessary, and rallying the public to be an active constituency for surpassing change."

So I telephoned [Doris Goodwin](#), who has written a couple of times for the Prospect before, whom I just admire immensely, and said, "Will you please do this article?" She said no, she was busy writing her book on the one president she hasn't yet written about of the great presidents, [Theodore Roosevelt](#).

I said, "Is there any way I can get you to talk about this?"

She said, "Why don't you come to my house with a tape recorder? We'll do a transcript. You can do it as an interview."

The thing about Doris is, she speaks prose. She speaks perfectly formed sentences. You don't even need to edit her. You just need to transcribe the tape.

We spent three hours, and at the end of the three hours, I said, "This isn't just an interview. This is a book. You have to write a book on this."

She said, "No, I can't, but you have to. I will help you. I will suggest sources. I'll even read your chapters."

So the book that became *Obama's Challenge* is dedicated to Doris.

Then I decided to take a couple of risks. It occurred to me that if I waited to see who won the election and then published the book, by the time it came out, there would be 50 books, 100 books. If I was right about the impending crash, then Obama would probably be elected. So I said, "What the heck, I'll blow a few months. I'll write the book and we'll get it out by Labor Day. We'll either have a bestseller or a bonfire."

It's not on the bestseller list yet, but it's doing rather well.

Here's the basic argument (and the two books, I think, can be read together): Why did this happen economically? Why did this happen politically? That's all in *The Squandering of America*. Then, what in the heck do we do about it?

In the well-known Chinese formulation, a crisis is also an opportunity. One of the things I did in researching *Obama's Challenge* was to take a good hard look at what the great transformative presidents have faced and what they have achieved. I put three of them on the Democratic side on this—an interesting Freudian slip—two Republicans, two Democrats.

[Lincoln](#), Republican: When he took office, his hope was that he would save the union. By January 1, 1863, he had issued the [Emancipation Proclamation](#). One of the things about a transformative president is that things that seem inconceivable when he takes office become inevitable, by force of circumstances, by force of leadership, by force of social movements pushing the president—in this case, the [abolitionist movement](#).

The same thing with [Franklin Roosevelt](#). There were three and a half years between the crash of October 1929 and the inauguration of Franklin Roosevelt in March of 1933. [Hoover](#) basically chased the Depression downward. It took about two years for the air to come out of the real economy after the crash of 1929. In 1930, the unemployment rate was 8.8 percent by the end of the year—not anything to be proud of, but not a depression. Yet everything that Hoover did was too little and too late. Then Roosevelt, in the campaign of 1932, criticized Hoover from the right. He criticized Hoover for spending too much money.

There's a wonderful line from [Marriner Eccles](#)' memoirs. Marriner Eccles was the populist chairman of the Federal Reserve, the only one in the history of that institution, appointed by Roosevelt—a banker from Utah. In his own memoirs, commenting on the 1932 election, Eccles wrote that if you read the transcript of the debates—there weren't formal debates, but there were a lot of joint appearances and arguments—it looked like there was a giant typographical error where Hoover and Roosevelt were each speaking each other's lines. Hoover was the one arguing for public works spending; Roosevelt was the one criticizing Hoover as a big spender. Roosevelt had been a critic of deposit insurance, had been a critic of large-scale public works spending.

It took about two weeks after he took office for him to realize that things were a lot worse than he had imagined and the remedies needed to be a lot bolder.

Just as in the case of Lincoln, there were social movements on the ground pushing Roosevelt to be still more aggressive.

The same thing with [Lyndon Johnson](#). In November of 1963, the general view was that civil rights legislation was hopelessly blocked. Those were the years when the Dixiecrats, the southern segregationist committee chairs, could tie up legislation. The country was divided. Public opinion polls showed that 50 percent of Americans felt that [Kennedy](#) was moving too fast on civil rights. [Bobby Kennedy](#) was trying to broker between the southern governors and the sheriffs on the one hand and Dr. [King](#) on the other hand. It was not going anywhere.

But when Johnson took office, he resolved that his legacy was to be the redemption of civil rights. When

the [1964 Civil Rights Act](#) passed, in July of 1964—this was before the landslide election of November 1964—it was the same 88th Congress, the same segregationist committee chairs. But the combination of Johnson's legislative mastery and the bravery of the movement on the ground, and the shift in public opinion that was created both by Johnson's leadership and by the bravery of the civil rights movement, transformed what was deemed possible.

So I think this is the situation that Obama faces. Things that were deemed inconceivable six months ago will be barely adequate six months from now. Only a president can achieve this. The president needs help from the citizenry. One of the intriguing questions is, what is going to happen to this movement of young people that came together to help elect Obama? Will this simply be an Obama club or will it take on a life of its own as a social movement, supporting him but occasionally pushing him, as the civil rights movement did with Johnson, as the industrial labor movement did with Roosevelt, as the abolitionist movement did with Lincoln? There is a kind of dance between great presidents and social movements.

Lest we forget, for every president who seized a crisis and turned it into an opportunity and became transformative, there's a president who came to power in the face of a crisis and failed—Hoover, [Carter](#), [Bush](#). Not guaranteed.

With Obama, I think many of us feel—most of us, even—that there is the raw material of greatness here. But it is all going to unfold before our eyes in the next several months.

So what does he need to do? I argue in the book and in my talks—my efforts to influence them as a friendly critic—that he needs to be much more radical as a president than he has been as a candidate, not radical in the sense of crazy left-wing, but radical in the sense of perceiving that the conventional wisdom will not solve the problem. The conception of what needs to be done has to be transformed or he, like Hoover, will chase a depression downward.

Four things, for starters:

First of all, he needs to get the financial rescue done right. Secretary [Paulson](#) has not achieved this. Paulson has been incredibly timid in extracting conditions from the banks in exchange for the \$700 billion that the public is giving the banks. Here's the argument you hear—and I have been in on some of these phone calls and some of these meetings—the argument is, "We need to get private capital to come back to the table. If we, the Treasury, tell the banks that they can't pay dividends or that they can't pay executive bonuses or that they can't use this money to underwrite mergers and acquisitions, that's going to scare off private capital. Therefore, we just have to trust the banks to do it their own way."

That's not good policy. The person I have been promoting to be secretary of the Treasury is [Sheila Bair](#). Sheila Bair is the chair of the [FDIC](#) [Federal Deposit Insurance Corporation]. She happens to be a Republican. But she's the toughest guy in the room, in the sense that when the FDIC takes over a failed bank, they don't just purge the toxic assets, they purge the toxic management. Sheila Bair has used IndyMac, a \$32 billion failed thrift institution that the FDIC took over—they were one of the perpetrators of the subprime mess, big-time—she has used this as a laboratory to do what she has pushed Paulson to do and what, thus far, the Bush Administration has refused to do. She refinances mortgages. There are 60,000 distressed mortgages either held by IndyMac or serviced by IndyMac on behalf of bondholders. She is refinancing every one of them that needs refinancing.

FDIC is one of the few government agencies involved in banking that has the technical capacity to run a bank. I think, before this is over, we're going to end up nationalizing a bank or two to show them how to do it right. If the banks that get this bailout money are sitting on the funds and refusing to lend it—Roosevelt called this "yardstick competition"—instead of just throwing money at them, nationalize one and start lending. Then maybe the others will follow.

That sounds pretty radical, doesn't it? But it may be necessary—or at least put some people on the board. That's what the Reconstruction Finance Corporation did in Roosevelt's era. They didn't just hand

out money.

We face a similar dilemma with the auto bailout. On the one hand, it's not a secret that Detroit makes cars that not very many people want to buy. On the other hand, this is a huge linchpin industry that we can't let go down the drain. What do we do? I'm not sure I have the answer, but I don't think we just hand out money with no strings attached.

There's an extraordinary documentary—if you haven't seen it yet, I recommend it—called [Who Killed the Electric Car?](#) In the mid-1990s, the California Air Quality Board passed a regulation requiring that 20 percent of all vehicles sold in California by the year 2000 be zero-emission vehicles. The only way you could meet that standard was to devise an electric car. General Motors did it.

It was a gorgeous car. People were lined up to buy it. By 1997, it was sold as a production vehicle. You could go into a showroom—they didn't sell it; they leased it. They realized after a while that they weren't making much money on it. It didn't break down. It didn't have a lot of moving parts. Enviros were lined up to buy the thing. So instead of investing in engineering or in marketing, they invested in politics. They got a new chair of the California Air—I'm not making this up. It sounds paranoid, but this is factual. They got a new chairman appointed. They created an institute that he could be head of on the side, as a way of bribing him. He got the regulation repealed, and they recalled every damn one of those cars and sent them to the crusher, so that there wouldn't be a single one left on the road.

Now, 11 years later, they are having to reinvent what was a plug-in electric vehicle via hybrids, via converting hybrids to pure plug-in cars. That is just appalling. Now these people want \$25 billion or more in taxpayer aid.

I don't know whether you take them out and shoot them and start over or what you do. It's a terrible dilemma. You have an industry that doesn't seem to learn from history. Yet how can you have no auto industry in the United States? It's one of the dilemmas that Obama is going to face.

Back to my litany of four things he has to do:

One, get the financial rescue done right, so that credit starts flowing, so that we're not just throwing money at bondholders.

Two, put a floor under the collapse in housing prices. This is what Sheila Bair has been pushing—futilely, so far. The way you do that, it seems to me, is not to bail out bondholders, bail out banks, and hope that some of it eventually trickles down to homeowners. You have 2 million or 3 million distressed mortgages at risk of foreclosure. If they go into foreclosure, the collapse in housing prices is going to deepen. We're eventually going to need to refinance a lot of those mortgages directly—hopefully, sooner rather than later. Again, Roosevelt's Home Owners' Loan Corporation used the federal Treasury borrowing rate to refinance mortgages at very low interest rates. HOLC in the 1930s eventually refinanced one mortgage in five. It saved millions of people from the heartbreak of foreclosure and succeeded in breaking the collapse in housing prices. That's what the Obama Administration needs to do.

Third, they have to re-regulate finance, so that there are no non-bank banks doing what banks do—creating credit, creating risk—but beyond the purview of the regulators. Something like 40 percent of the credit created in the United States in the last three years was created by institutions that are not subject to any kind of supervision. With the repeal of [Glass-Steagall](#), with the invention of all kinds of new, exotic securities, we really have one big financial services industry. This is what the industry wanted. Well, they got it.

Given that fact, it all has to be regulated basically the same way. It all needs capital adequacy standards. It all needs supervision. There cannot be any such thing as a derivative security that is a privately traded contract.

One of the basic concepts in standard economics is the concept of price discovery. If I put my house on the market and I think it's worth \$800,000 and no buyer is willing to pay more than \$500,000, and it sells for \$500,000, the process of supply and demand has discovered the price. Ditto with the stock market. Ditto with the ordinary bond market. Even ditto with ordinary options and futures.

But when you have an exotic derivative like a credit default swap, something that is going to cost the taxpayers hundreds of billions of dollars, and maybe more, before this is over, there is no price discovery, because it's not publicly traded. There is no transparency. You don't know what it's worth until somebody tries to sell it, and then it turns out that maybe it's worth nothing.

That, writ large, is the story of this whole financial crisis.

To give a sense of the bipartisan responsibility for this catastrophe, when [Brooksley Born](#), who was then the chair of the [Commodity Futures Trading Commission](#) in the mid-1990s—a Clinton appointee—tried to increase the regulation of derivatives and saw this coming, all the old boys ganged up on her—[Rubin](#) and [Summers](#) and [Greenspan](#)—and bludgeoned her into submission. My friend [Jim Stone](#), who was the first head of CFTC under Jimmy Carter, has been pushing for 30 years the idea that there should not be any derivative contracts traded over the counter or not traded over the counter as private contracts; they should all be exchange-traded.

So there are lots of things like this. Another one is the bond-rating agencies. The credit-rating agencies are conflicts of interest at their absolute core. They are paid by the people who create the securities to give the securities good ratings. It's exactly analogous to the accounting scandals of the late 1990s. Credit-rating agencies should either be public agencies paid for by tax dollars or they should be nonprofits, where there are no such conflicts of interest.

These are radical remedies. On the other hand, the kinds of remedies that Roosevelt proposed—and he only got about half of them through in the 1930s—were radical remedies, too. If you go back and read the history, the creation of the Securities and Exchange Commission, the Glass-Steagall Act, deposit insurance—if you listen to the people testifying from Wall Street, this was going to kill American capitalism. Of course, it saved American capitalism.

Lastly, he is going to have to spend a lot more public money than he thinks right now. There's an argument going on right now between the Obama people and the congressional leadership in the House: Should the stimulus be \$250 billion in the first year? Should it be \$100 billion?

I argue in the book that we need to increase public spending by about 4 percentage points of GDP. It just happens that that's \$700 billion. But Wall Street got the first tranche, as they say, of that \$700 billion.

Main Street needs to get the next several tranches—meaning that there are all kinds of public systems that have been undercut over the past 30 years. There is \$1.6 trillion of deferred maintenance in basic public infrastructure. Just across the river in Hoboken, where you have had a huge building boom, they have a water and sewer system from the 19th century that is so primitive that wastewater and floodwater are commingled in the same sewer system. On top of this you now have a whole row, if you look across the river, of high-rises that this water and sewer system was not designed for. You multiply that times 1,000 all over the country—bridges, tunnels, schools, public buildings, the electricity grid. You could easily have a serious program in repairing basic infrastructure. You could complement that with public spending on green energy.

One of the scandals of the last 20 years is that as intergovernmental revenue aid has dried up, state after state after state has balanced its budgets on the backs of America's great public universities. Universities that used to be 80 or 90 percent funded by the state legislatures are now 15, 20 percent funded by the state legislatures, and tuition has to make up the difference.

So instead of kids from non-affluent families being able to get an affordable education at a great public

university, these kids graduate college with debt. Then on top of that, they have trouble getting health insurance. On top of that, they have trouble affording to become homeowners. So you have a whole generation of young people who start out their lives with these financial millstones.

Spending that we need to do to prevent a classic macroeconomic collapse of purchasing power is also spending that we need to do to restore public systems that have been left to ruin and then—I say this as a good liberal—restore the ideology that the role of government is to help ordinary people and to restore the credibility of government in the eyes of voters.

So this is Obama's opportunity. If he doesn't do it, he will very much be in the same situation as Hoover was, where a recession is deepening and he is chasing it and doing too little and too late. You have all the classic signs—retail sales collapsing, layoffs increasing, credit markets being frozen, state and local governments laying off people as the recession deepens. Of course, all you have to do is write a check for about \$100 billion, and no state or local government will have to lay off anybody, no state or local government will have to have education cuts or cuts in police and fire and first responders.

The only thing holding this back is the tyranny of the conventional wisdom. The conventional wisdom is that deficits are a bigger worry than a depression. That's the view. You hear it over and over again from the media. Obama gives a speech and says we need to put X billions of dollars into infrastructure, and the shocked reporter says, "Well, my God, that will increase the deficit."

I ask you, which is the lesser evil? A bigger deficit for a couple of years or the Great Depression II?

Let me leave you with some statistics, God help us. The ratio of debt to GDP, even after George Bush's deficit spree, is only about 40 percent. Public debt is 40 percent of one year's GDP. At the end of World War II, the public debt was 124 percent of one year's GDP, and that was on the eve of a great boom. How could that be? How could a nation saddled with that kind of a debt have a 25-year boom? The answer is to look at what we spent the debt on. We spent the debt on the recapitalization of American industry during the war, the retraining of American workers during the war, the reemployment of American workers during the war, science, technology. We came out of the war as the world's industrial leader. The wartime production boom turned into a postwar consumer boom.

So the question isn't, within reason, whether we can afford more debt. The question is what we spend the debt on. If we increase the debt-to-GDP ratio from 40 to maybe 60 percent and that spares us a second great depression, it's not exactly rocket science to know which is the lesser evil.

I hope President Obama and his people have read my book. I think there are three reasons why he is more likely to succeed than to fail (one of them is not my book):

- One of them is his own character and his own capacity for leadership. This is a teachable moment.
- Another is his desire not to fail.
- But the third thing we have on our side is reality. It's very quickly going to sink in that the choice is to be bold or to fail. I think this is an impressive enough man that I think he'll be bold.

Thank you so much.

Questions and Answers

QUESTION: Two things. One is, to what extent do you blame the repeal of Glass-Steagall as one of the reasons for this debacle?

The other is, I think the most important thing that is on most of our minds is jobs. That seems to be the fundamental thing. How do you feel we can start recreating jobs?

ROBERT KUTTNER: Good questions. The repeal of Glass-Steagall in 1999 was the capstone of a kind of bipartisan crusade to let banks do whatever they want to do. Glass-Steagall had been de facto repealed, for the most part, by administrative exemptions which were permitted by the Federal Reserve before it was finally given a decent burial.

The line back then was, "Well, it's the 1990s. We don't need a 1930s system."

What actually happened was, banks kept innovating and regulators and the Congress showed no interest in keeping up with the innovations. So Glass-Steagall was one character among many. You know Agatha Christie's *Murder on the Orient Express*, where the solution is, they all did it. Glass-Steagall was one of the suspects that plunged in one of the knives, the repeal.

I was at a conference at the United Nations yesterday and one of my co-panelists was Dr. [Reddy](#), who just retired as the head of the central bank of India. I said, "How are you doing in this crisis?"

"Oh, we're doing fine."

I said, "Really?"

He said, "We're worried about the collapse of global purchasing power, but we did not permit any of these exotic investments by banks, so we have been spared this crisis."

He was so modest. He said, "We leave this sort of thing to the advanced countries."

Now, jobs. The way to get jobs is to prevent the collapse of purchasing power. It's just classic anti-recession medicine. You do this by a lot of short-term stimulus and a long-term increase in public investment. It provides jobs directly and then, when you put a floor under a collapsing economy, you don't lose jobs indirectly.

QUESTION: I too was fascinated by what you had to say. Thank you very much.

You emphasized bold and radical steps. Yet your response about jobs was very traditional. Why don't you suggest—or why don't they look at a works program, such as they had during the Depression? If we had that, we wouldn't have to help these terrible automobile companies who don't deserve my money to be kept in business for making bad cars, making SUVs at a time when everybody was talking about the quality of the air and so forth and so on. The people who would lose jobs—it would be catastrophic. But we could create jobs for them. Detroit certainly needs a green-jobs program.

ROBERT KUTTNER: I think we're saying the same thing. I was proposing \$700 billion a year of public spending for things like infrastructure and green redevelopment, green jobs. That makes me the sort of furthest out of any mainstream commentator in what I'm proposing. Much of this goes for jobs. It also goes to invent a lot of technology, repair a lot of infrastructure.

You are seen as not with it if you call it the [WPA](#). I wouldn't call it the WPA. But it's an infrastructure program.

QUESTIONER: Okay, that's great. But I'm not finished, if I may.

ROBERT KUTTNER: Proceed.

QUESTIONER: I want to know, as a liberal, which I have always thought of myself as, why has not the liberal community or the Democratic community cried out about the bad job that Paulson has done?

ROBERT KUTTNER: Oh, I think we haven't been shy in criticizing Paulson.

QUESTIONER: I haven't heard very much. We imitated [Gordon Brown](#). [Paul Krugman](#) made the suggestion that what Gordon Brown was doing was wonderful and he hoped that we would do it. We emulated him, up to the point of not insisting that they lend money, the way Gordon Brown did. Yet I don't hear people—

ROBERT KUTTNER: Certainly we all ought to be speaking with a louder voice. The good news is, this man is only going to be in office for another nine weeks. He's a lame duck.

But Congress has been fairly tough on Paulson. Paulson came in and said, "Please give me a blank check or the world will come to an end." The Democrats said, "No, we're not going to do that. We're going to change the legislation in several ways." They didn't change it enough. They gave him too much discretionary power. But that was the price of getting Bush to sign the thing.

We're in this interregnum, where the new team is ready to take over, but they don't take over until January 20. I think Obama has been very shrewd not to get pulled into Paulson's efforts to get him to put his fingerprints on Paulson's version of a rescue. He's right not to attend the global summit, which is not going to accomplish anything because it is being presided over by a lame-duck administration. Roosevelt had something of the same problem with Hoover. Hoover tried to create a kind of co-presidency during the five months between November of 1932 and March of 1933, and Roosevelt, even though things were even more dire then, said, "I want to start clean."

Congress has given Paulson a rough time. He should be given a rougher time.

QUESTIONER: [Not at microphone]

ROBERT KUTTNER: The only part of the press I can control is [The American Prospect](#), and I've sure given him a hard time.

QUESTION: I don't know if Mr. Obama's advisers are reading your book, but I am sure that the columnist who did the opinion piece in the *Financial Times* last weekend, a very brief little piece called "Obama Has a Chance To Become Another Roosevelt," certainly must have read your book.

ROBERT KUTTNER: I hope so.

QUESTIONER: His emphasis was, as I recall, the distinction between the circumstances surrounding the arrival in power of Roosevelt, Carter, [Reagan](#), and Obama, emphasizing the fact that we are now in a deflationary environment, where the cost of a radical program is absolutely affordable. When Carter came in, it was a heavily inflationary environment and catastrophic to think about doing that.

ROBERT KUTTNER: Right, exactly.

QUESTIONER: I wonder if you would expand on that.

ROBERT KUTTNER: I think that's right. When you think about the fact that people are willing to lend the Treasury money at around 4 percent for 30 years, that tells you that inflationary expectations are not exactly a problem. This means that you don't have the kinds of constraints that you had when Carter took office.

Also the crash on Wall Street was also the crash of an ideology. Obama needs to make that explicit. When an old ideology crashes, it doesn't mean that it automatically ushers in a new ideology. The new ideology has to be defined by the president. It's a modern variation on what [Joseph Stiglitz](#) called managed capitalism, what [Paul Samuelson](#) calls a mixed economy, where you let the entrepreneurial private sector do what it does well and you have the government do what the private market doesn't do well—not a new idea, but new circumstances.

He has a working majority in Congress—only the third time since Roosevelt. Only one president who had a working majority in Congress since Roosevelt—Lyndon Johnson and the 89th Congress—really used it well. Carter had a lot of Democrats in Congress, but Carter took office as an outsider and remained an outsider, and never built the necessary bridges to Congress. He squandered his majority. Clinton took office with about the same size majority that Obama now has, blew it on an ill-conceived health reform that he did not work with Congress to design, spent a lot of political capital on [NAFTA](#) [North American Free Trade Agreement], and it just got away from him.

In some respects, Obama's working majority is even bigger, because you don't have any more Dixiecrats. You only have moderate to liberal Democrats. You don't have any right-wing Democrats anymore.

The other reason that I think he is well-positioned to succeed is that the country wants him to succeed. The country can't afford to have him fail. I'm just imagining the scene—let's say it's February 1. The unemployment rate is 11 percent and Obama has sent up an emergency spending package of \$400 billion. You are a Republican congressman and your phone is ringing off the hook from mayors and county executives and small businesses saying, "For God's sake, help us." Are you going to vote against that? I don't think so.

I also think there are five or six senators—you hear a lot about the Democrats just barely falling short of the magic number, 60. You look at [Susan Collins](#) and [Olympia Snowe](#), the two moderate Republican senators from Maine, or [Arlen Specter](#), or even [John McCain](#), for that matter, who just hated the whipping that they took from the Bush White House. I don't think you are going to see very many filibusters against Obama either.

QUESTION: I'm a businessman, as you may know when I give you my question. I hear what you say about the market problems. There's no question about the market problems. But what I hear from you is that you have a lot of faith in the government, and I don't hear much other than faith about that.

One last comment on that. If it's Roosevelt you're looking at, remember—I'm sure you know (I lived through it)—by 1937, he still had 20 percent unemployment; by 1942, it got down to 8. And you know what happened to get to 8 percent unemployment there. I doubt if it was this—

ROBERT KUTTNER: One of my favorite moments on the right-wing talk show circuit, where I have been appearing to promote my books, was when a guy said to me, "You think the government is smarter than the smartest guys on Wall Street?"

I said, "Well, the smartest guys on Wall Street just lost \$2 trillion, \$3 trillion." There's \$500 trillion of derivatives out there. Nobody knows what they are worth. Nobody knows what they are.

Yes, I have a lot of faith in the government. If only the balance sheets of the money-center banks were in as good a shape as the balance sheet of Social Security, the country would be better off. This is not a conventional view.

Even Mr. Paulson, who is not exactly a Bolshevik—when it all collapses, who does he turn to? He doesn't turn to Citigroup. He turns to the U.S. Treasury.

Sheila Bair is a heck of a lot more competent than 9 out of 10 of the geniuses on Wall Street who brought us this tragedy.

So, yes, I have a lot of faith in the government. I suspect that even more people are going to have a lot of faith in the government.

I think one of the problems is that the Bush Administration argued that the government couldn't do anything right and then kept on proving the point. You need people who believe in government to run government. Otherwise, they run it into the ground.

Now, as far as the 1930s is concerned, you're right—not right on the statistics. Let me be precise on the statistics. Unemployment bottomed out at 25 percent in 1933. By 1939, it was still 12.8 percent.

That's a depression. It's very fashionable to say that the New Deal didn't cure the Depression; the war killed the Depression. Unemployment during the war was 2 percent. There were manpower shortages. That's why women and blacks got opportunities during the war that they didn't get at any other time in American history, because we needed the manpower and the womanpower.

What does that tell you? It tells you that Roosevelt didn't spend enough money. During the war, we had deficits of 30 percent of GDP. I don't think things are going to get that bad. But think about it. Even though much of the production that was created during the war was built only to be blown up, we still had record economic growth during the war, and within about a year, once we mobilized for war, unemployment melted away.

I don't know what that tells you. What it tells me is, it's better to spend a little bit too much than to spend too little if you are on the verge of a depression.

QUESTION: I want to ask you about bailing out companies and helping them. It seems to me that the basic thing is, if you give money, not only to know what it's used for, but whether it can accomplish what you are trying to do. Taking [AIG](#) as the first example, here they didn't have an end plan. From what I understand, they have \$400 billion of CDSs that they are still liable for. Once we start to put in money, are we going to stop at \$150 billion? Without visibility and knowing the endgame, I don't think we should get involved. If we have trillions of dollars of this financial dark matter floating around, I think, before we guarantee something, we should know what we're guaranteeing, what the limits are, and what the effect is.

Going back to General Motors, it would seem, if we are going to give money, we should know whether it's going to solve the problem. If not, we should structure it to know the full picture.

ROBERT KUTTNER: I couldn't agree more. There were three and a half years between the crash of 1929 and the Roosevelt Administration. Mercifully, there are only three and a half months between the crash of 2008 and the Bush Administration leaving office and the new team coming in. I think Paulson is making a complete mess of this. Their strategy is to hire other investment banks to clean up the messes created by different investment banks. You have a 35-year-old wunderkind with the wonderful Dickensian name of [Kashkari](#) throwing money at Wall Street without very many conditions. AIG is the classic case.

On the other hand, AIG is on the hook for so much insurance credit default swaps, and it's an example of the house of cards that was created by the complete laxity on the part of the regulators. Can you afford to just let it go down the drain? That's what they did with Lehman Brothers. Hey, let's let this one go down the drain. It's not named Goldman. We'll just let it go. Well, that's taking a pretty big gamble.

But I think you are absolutely right that if you are going to do these rescues, you have to be much more hands-on, you have to know what the endgame is, and you have to know what the risks are going in, to the extent that you can.

You raise another point. There's a story this morning, I guess in the *Times*, that everybody is lined up to get their own bailout. You have the people who manufacture boats, because people are not buying very many luxury boats right now. They are lined up to get a rescue. Detroit is lined up. You cannot bail out every company in America. That's why I'm a [Keynesian](#). It's much better to put a floor under purchasing power and resume a normal supply-and-demand situation—and then the household sector, which is 70 percent of the economy, buys things, and retail sales rebound and people get hired again—than it is to bail out industry at the level of bailing out individual companies.

At the same time, particularly in the financial sector, there are cases where you do need to go in and

clean up balance sheets, because the financial sector is just too important to be allowed to fail. That's why Roosevelt had a Reconstruction Finance Corporation, so that, in addition to the public works spending and the regulation and all the other stuff that he did, there were cases where government needed to infuse capital. But when the RFC infused capital, it put people on the board. It got a look at the books. It didn't just throw money away.

This is really hard stuff. But the stakes are huge.

QUESTION: One of the legacies of the last eight years may be that income disparities have greatly widened and, in this economic dislocation, will probably get worse. What will the Obama Administration be able to do to rectify that?

ROBERT KUTTNER: One of the things I proposed in my book is the idea that you take some of this additional spending that I'm calling for and you use it to upgrade, professionalize every single job in the human services. You have people taking care of our children, taking care of our aging parents, who are untrained, with 200 or 300 percent annual rates of turnover, making seven bucks an hour. In Europe these are professional jobs. They are not astronomically paid, but they are middle-class jobs. For about \$100 billion a year, you could provide that anybody working in a daycare center or pre-kindergarten or a nursing home is at least a paraprofessional with the opportunity to become a professional. These are the jobs that can't be exported.

It would also be good for our kids and good for the dignity of our parents.

I think the [Employee Free Choice Act](#), which restores the rights that are supposedly guaranteed under the [Wagner Act](#), so that unions stand a fair shot at organizing, would also help raise wages.

I think all of this public works and infrastructure and green development spending that I'm calling for—all of that creates middle-class jobs. Construction jobs are good jobs; retrofitting homes for energy efficiency, good jobs; high-speed rail, good jobs.

There are lots of beneficial side effects to outlays that he needs to have done for macroeconomic reasons in any case, and then we can get all this other benefit out of it.

QUESTION: You're absolutely correct that jobs are the underlying solution to all the problems. But you cannot just have infrastructure and green jobs by themselves, and with the government providing the funds for it. They have no funds. All they are doing is printing money, which will cause stagflation. If you want to create wealth, we have to cater to the industries where we can be successful, which are all the aspects of high technology, and get involved in the global economy, bring jobs back to this country—export goods and not jobs. They can do that with a high-tech export free zone program, a national program, for the major urban centers, which could do that kind of job.

Would you comment on that?

ROBERT KUTTNER: I guess I dispute the idea that government can't create wealth. When government makes it affordable for kids to go to college, government creates wealth. When the National Science Foundation or the National Institutes of Health puts money into research and development, and that in turn allows America's pharmaceutical companies to be the world's leaders, that creates wealth. I think in normal times you leave most of this to the private sector. But in dire economic times, the government has to step into the vacuum.

I completely agree with you that we need to rely on technology and to start exporting again, to start manufacturing in America again. I'm not sure tax-free export zones, in the absence of a whole bunch of other policies, are going to be any kind of a silver bullet.

But for 30 years, "industrial policy" has been a dirty word. Every other country practices it. But the idea

that it should matter to us whether we have an auto industry or a semiconductor industry or a high-speed rail industry—that's very controversial. That's picking winners. Government is not supposed to pick winners. Well, what is Hank Paulson doing if he's not picking winners and losers?

So we are "a little bit pregnant" here. We might as well do it right.

QUESTION: I think not enough attention has been paid to the advantage of having two members of the United States Senate become president and vice president and a leader of the House of Representatives become chief of the White House staff. In my last four years in the House as the whip, I would every other week join the other Democratic leaders of the House and Senate for breakfast with the president and vice president.

We have a Democratic president and vice president. We have Democrats in larger majorities in the House and Senate. What suggestions do you have for encouraging close cooperation between the two? Otherwise, we won't be able to attack these problems.

ROBERT KUTTNER: That's a good question. Obama has been underrated at every stage of his career. One of the very astute things he did during the campaign was to put a lot of veterans of Congress in senior positions in the campaign—[Tom Daschle](#), Daschle's former chief of staff [Peter Rouse](#), [Jim Messina](#), who used to be [Max Baucus](#)'s chief of staff. He not only appointed [Rahm Emanuel](#), a former congressman, as his own chief of staff, but as his—this just blew me away; it made my day—as his director of congressional relations, which is one of the single most important positions. He appointed a guy named [Phil Schiliro](#), who was [Henry Waxman](#)'s longtime chief of staff. Henry Waxman is probably the most effective progressive legislator in the House.

So he's being very, very astute in creating the groundwork for good relations with Congress. His people have been having meetings several times a week with Speaker [Pelosi](#). For somebody who is supposed to be not very experienced, he really seems to have a sure hand; he really seems to know what he's doing.

So I am audaciously hopeful. And I thank you all for coming.

JOANNE MYERS: Thank you very, very much.

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