Joint Economic Committee
Republicans

Representative Kevin Brady
Vice Chairman

NEWS RELEASE

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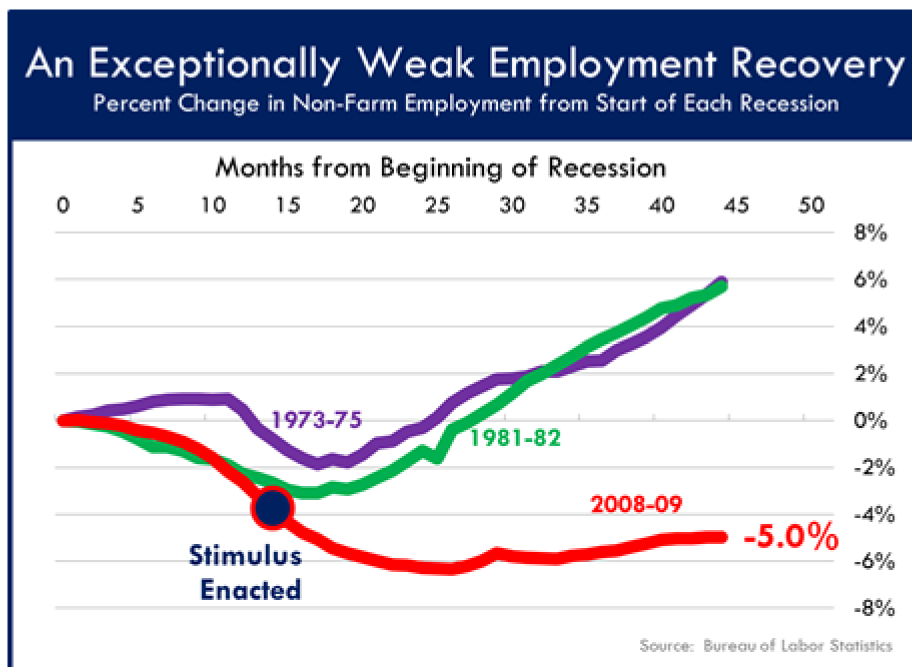
Contact: Al Felzenberg
Office (202) 226-2490
Work Cellular (202) 695-5797

STATEMENT OF
VICE CHAIRMAN KEVIN BRADY

Economic Outlook

Washington, DC – Chairman Casey, I join with you in welcoming Chairman Bernanke to today's hearing on the economic outlook.

Ominous clouds are gathering. Economic growth is nearly stagnant. We have 6.8 million fewer payroll jobs today than when the recession began in December 2007, according to the Bureau of Labor Statistics. At the comparable point during the Reagan recovery, there were 5.4 million more payroll jobs.



According to economists Carmen Reinhart and Kenneth Rogoff, recoveries from financial crises are weak and vulnerable to external shocks that may trigger double-dip recessions. Republican members of Congress recognize this. We are critical of the President's expensive economic policies because not only they have failed to spur job growth and business confidence, but also, as we feared, they have left America susceptible to a double-dip recession.

Today as we meet, America faces a growing risk from the European debt crisis.

The United States and the European Union are major trading partners. I am very concerned about the effects of contagion from the euro crisis on American financial institutions and markets, as well as the broader economy. I am anxious to hear your assessment of the euro crisis and any steps that the Federal Reserve may take to quarantine any contagion.

In response to the financial panic, the Federal Reserve took extraordinary actions to stabilize U.S. financial institutions and markets during the fall of 2008. Many of these actions were both necessary and proper, while some of them I question. Instead of rehashing the past, however, I would instead like to initiate a discussion with you on the framework for monetary policy in the future.

Nobel laureate economist Robert Mundell said, "If you want a certain policy outcome, you have to use the right policy lever." Unfortunately, too many Washington policymakers are ignoring Mundell's wisdom.

(OVER)

Monetary policy affects prices. In contrast, budget, tax, and regulatory policies affect real output and employment. While the Great Contraction from August 1929 to March 1933 proved that bad monetary policy can shrink production and destroy jobs, good monetary policy cannot accelerate economic growth or foster job creation, except in the very short term.

Washington affects business investment, production, and job creation through its budget, tax, and regulatory policies. If the prospects for a swelling federal debt, higher taxes, and additional costs from Obama-care and burdensome regulations are deterring entrepreneurs from investing in new buildings, equipment, and software and therefore hiring more workers, there is little that the Federal Reserve can do to overcome this drag.

Until 1978, the Federal Reserve's mandate regarding monetary policy was merely to provide "an elastic currency." That year, the *Full Employment and Balanced Growth* Act, known informally as the Humphrey-Hawkins Act, was enacted. This act imposed a dual mandate on the Federal Reserve that gives equal weight to achieving both price stability and full employment.

Since 1978, many countries have examined what a central bank should do and have opted for a single mandate for long-term price stability. By law, the 17 member-states of the European Monetary Union and 13 other developed and major developing countries have enshrined mandates for price stability either as the sole goal or the primary goal with the subordination of other goals for their central banks. Moreover, Australia and Canada have adopted single mandates through published statements.

The time has come for Congress to reconsider the Federal Reserve's mandate. In my view, the dual mandate should be replaced with a single mandate for long-term price stability. I will introduce legislation to make this change in the near future.

While some may mistakenly claim that a single mandate means maximizing employment is unimportant, history proves that the best way for the Federal Reserve to maximize employment is to focus on achieving long-term price stability.

Under a single mandate, the Federal Reserve would publicly announce an inflation target. The Federal Reserve would retain full operational independence from both Congress and the President to achieve the inflation target.

While I may criticize certain actions that the Federal Reserve has taken, I want to be absolutely clear. For our economy's sake, the Federal Reserve must remain independent and free from any undue political pressure in implementing monetary policy.

Congress should also reconsider the Federal Reserve's lender-of-last-resort policy. I remain deeply concerned about the precedents set in 2008 regarding clearly insolvent financial institutions, especially AIG, Bear Stearns, Fannie Mae, and Freddie Mac.

In 1913, Congress envisioned that the Federal Reserve would act as lender of last resort during financial crises. However, the Federal Reserve has never articulated a clear lender-of-last-resort policy.

As celebrated economist Allan Meltzer observed:

> *The absence of a [lender-of-last-resort] policy has three unfortunate consequences. First, uncertainty increases. No one can know what will be done. Second, troubled firms have a stronger incentive to seek a political solution. They ask Congress or the administration for support or to pressure the Federal Reserve or other agencies to save them from failure. Third, repeated rescues encourage banks to take greater risk and increase leverage. This is the well-known moral hazard problem.*

President Dwight Eisenhower said, "In preparing for battle I have always found that plans are useless, but planning is indispensable." Similarly, if the Federal Reserve were to promulgate a clear statement about its lender-of-last-resort policy, it would go far to diminish uncertainty, reduce the likelihood of political interventions, and mitigate the moral hazard problem.

Finally, many years ago, Congress gave the responsibility for exchange rate policy to the Secretary of the Treasury. This is a vestige of the long defunct Bretton Woods system of fixed exchange rates.

By controlling the money supply, the Federal Reserve directly affects the foreign exchange value of the U.S. dollar. Moreover, swings in exchange rates influence domestic prices. Thus, the responsibility for exchange rate policy should be moved from the Secretary of the Treasury to the Federal Reserve.

Chairman Bernanke, I look forward your testimony.

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